April 7, 2006

Suzanne Q. Bielstein,
Director of Major Projects and Technical Activities
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, Connecticut, 06856-5116

VIA E-MAIL


Dear Ms. Bielstein:

Freddie Mac appreciates the opportunity to comment on the Exposure Draft, The Fair Value Option for Financial Assets and Financial Liabilities (the "proposed Statement"). We strongly support the objectives of the proposed Statement. In our business, fair value measures provide an important perspective on our business and the related risks.

We request that you reconsider providing (a) guidance for determining interest income and expense recognition when instruments are measured at fair value, and (b) examples of acceptable documentation for electing the fair value option.

We anticipate that an implementation effort may have pervasive impacts for complex financial institutions such as Freddie Mac (depending on the extent of FVO elections). Furthermore, FVO adoption would require consideration of the impacts upon users of our financial statements, including regulators and investors. Accordingly, we request that you provide an extension of the required effective date for one year to January 1, 2008 (with early adoption permitted) to allow for adequate time to address all impacts.

These recommendations are explained further below.

Simplification Related to Recognition of Interest Income and Expense

We support the Board's objectives for this proposed Statement, including the objective of simplifying the accounting (¶A3b). We understand that the Board considered addressing the issue of how to determine interest when an instrument is measured at fair value and decided not to address it in this project (¶A15). However, we urge the Board to address this issue in the final FVO Statement, as we believe the Board has an opportunity to significantly further the objective of operational simplification in this area. Specifically, we recommend that the Board consider explicitly permitting a simplified approach to interest recognition for instruments that are accounted for under the FVO. For example, the Board could permit an accounting policy to recognize interest based on contractual interest, excluding any amortization of premiums or discounts, when such instruments do not involve a substantial premium or discount.
Discussion

SEC regulations require income statement presentation of net interest margin (including interest income and interest expense) for many financial institutions. In accordance with GAAP, companies recognize the components of net interest margin for non-trading securities on an effective yield basis, including the amortization of premiums, discounts and other deferred items as an adjustment to yield. However, when net income is determined by changes in fair value of a financial instrument, as under a FVO election, the relevance of the net interest margin presentation would be diminished. We understand that the Board previously acknowledged this diminished relevance in Statement No. 91, Accounting for Nonrefundable Fees and Costs Associated with Originating or Acquiring Loans and Initial Direct Costs of Leases. Specifically, in ¶34, the Board stated that carrying financial instruments at fair value “obviates the need for accounting guidance for recognition of . . . premiums or discounts” associated with these financial instruments.

From an operational standpoint, amortization can involve complex and costly processes. This is especially true for prepayable instruments subject to SFAS 91. Applying a simplified accounting policy might produce significant operational benefits. One simplified approach might involve the recognition of interest based on contractual interest excluding any amortization of premiums or discounts. A company might apply this simplified approach for instruments that do not involve a substantial premium or discount (e.g., amortization would still be required for zero-coupon instruments).

Given (a) the diminished relevance of the net interest margin presentation for instruments which affect net income on a fair value basis and (b) the potential benefits from operational simplification by changing amortization processes involved in net interest margin recognition, companies may wish to change their accounting principles for net interest margin recognition for instruments for which they elect the FVO. In investigating such a change, companies may decide there are instances where acceptable alternative treatments are available under GAAP. In those cases, the company would be required to apply the provisions of ¶5 of SFAS 154, Accounting Changes and Error Corrections, which require an affirmative conclusion that a change in accounting principle is to a preferable method.

However, whether a change in accounting principle is preferable is a matter of interpretation and is not always clear. Upon adoption of the FVO, a company may transfer assets subject to Statement No. 115, Accounting for Certain Investments in Debt and Equity Securities, into the trading category as permitted by ¶15 of the proposed Statement. For these new “trading” assets, SFAS 91 ¶3 does not technically require amortization. This means that there are acceptable alternatives for trading assets under GAAP: (a) amortization to produce effective yield interest income recognition or (b) no amortization. However, it may not be clear that a change away from effective yield interest income recognition would be considered preferable, as GAAP appears to favor effective yield recognition in EITF 99-20, APB 12, APB 21, and other standards.

We anticipate that the preferability determination related to changes in accounting principles related to net interest margin recognition will be complex. Companies will be challenged with preferability determinations in cases where acceptable alternatives exist and the basis of measurement of the related asset or liability is changing from historical cost to fair value. Therefore, we recommend that the Board consider explicitly permitting a simplified approach to interest recognition for instruments where the FVO is elected. Companies would benefit from the ability to simplify interest income and income expense recognition by reducing amortization processes, especially for prepayable instruments subject to SFAS 91.
Concurrent Documentation

Paragraph 6 of the proposed Statement indicates that the fair election "... shall be supported by concurrent documentation or a preexisting documented policy for automatic election." Paragraph A8 further explains that the Board decided not to prescribe specific documentation requirements.

Our understanding is that the documentation requirements would not be as extensive as what is required under SFAS 133, Accounting for Derivative Instruments and Hedging Activities, but rather similar to SFAS 115. However, the extent and timing of documentation will be subject to interpretation. Companies may find it helpful if the final standard provided examples of acceptable documentation, to be used as a general guide without dictating specific requirements.

Additionally, the proposed Statement is silent on whether the designation of the fair value election should occur on the trade date or the settlement date. We believe that the Board is attempting to address this question with the concept of allowing the fair value election "... upon an event that gives rise to new-basis accounting at fair value under generally accepted accounting principles." For example, an entity that accounts for a commitment to purchase a security as a derivative contract subject to the provisions of SFAS 133 would not be required to document its fair value election for the security until the date of settlement of the commitment contract. We recommend that the Board clarify this concept in the final Statement.

Extension of Effective Date

For companies whose fiscal year corresponds with the calendar year, election of the FVO would be required as of January 1, 2007 for existing financial assets and liabilities (as permitted by the transition provisions in ¶14), if the company wished to take advantage of the one-time transition provisions. We request that the final standard's effective date be extended for one year to January 1, 2008, with early adoption permitted. This extended effective date would allow entities the necessary time to fully evaluate and implement this proposed Statement in a controlled manner, while still being able to take advantage of the transition provisions related to the one-time election of the FVO for existing financial assets and liabilities.

Discussion

If the proposed Statement is issued in the third quarter of 2006 as currently planned, calendar-year end companies will have less than six months before initial transition as of January 1, 2007. We believe that successful implementation of the proposed Statement may require more than six months from the date of the final standard, depending on the circumstances of the entity and the planned extent of FVO elections.

The Board considered one aspect of the burden of implementation in ¶A29, where the Board noted that fair value estimates should already be readily available due to the current disclosure requirements in Statement 107, Disclosures about Fair Value of Financial Instruments. However, implementation of the proposed Statement will involve additional complexities beyond ensuring that reliable fair value estimates are available. For example, implementation efforts may include the following considerations:

- The scope of financial instruments that will be selected on an initial and recurring basis for election of the FVO
- Whether to discontinue any or all hedge accounting relationships
- Accounting policy determinations regarding the interaction of the proposed FVO Statement with SFAS 155, Accounting for Certain Hybrid Financial Instruments (an amendment of FASB Statements
No. 133 and 140; SFAS 156, Accounting for Servicing of Financial Assets (an amendment of FASB Statement No. 140); and the proposed standard Fair Value Measurements

- Ability and intent to change accounting principles related to recognition of interest income and interest expense for instruments for which the FVO is elected
- Preparation for complete and meaningful disclosure of fair value-based components of results of operations in the MD&A (for SEC registrants)
- Changes in systems and processes required for the planned scope of FVO elections, including the implementation of adequate documentation of the elections
- Design and operation of internal controls to prevent and detect potential errors related to the application of the FVO
- Implications for management reporting to support external disclosures and provide meaningful analysis for users of financial statements
- Implications for compliance with regulatory requirements (e.g., regulatory capital requirements)

The extension that we propose should facilitate greater use of the FVO, including the one-time election for existing financial assets and liabilities, by allowing adequate time to adopt the new standard in a well-controlled manner. Therefore, we believe that such an extension in the effective date (with early adoption permitted) is consistent with the Board’s objective of promoting the use of the fair value measurement objective (¶1).

We also think an extension in the effective date to January 1, 2008 (with early adoption permitted) would not represent a significant incremental impairment to comparability across companies. The Board has already anticipated concerns related to comparability among companies, and addressed these concerns with expanded disclosure requirements (¶12, ¶A14). The Board could address any comparability concerns related to the extended effective date and the ability to early-adopt through clear transition disclosure requirements.

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Senior Vice President – Controller and Principal Accounting Officer

James R. Gagen

Vice President – Assistant Corporate Controller

Mary A. Holm

Vice President – Valuation Accounting Policy & Analysis

Melissa L. Bellinger

Subject:

We appreciate your consideration of our comments. If the Board of such underlying any of the

issues we raised in this letter, please feel free to call Melissa Bellinger at (717) 382-3235.

If you have any questions, please do not hesitate to contact Scott Wilson at (717) 382-3172.

We would also be happy to meet with you at your earliest convenience.

We made home possible.

Fredrick Mac
In preparing financial statements, we use a consistent basis of presentation for our assets and
liabilities that are useful for communicating results and a consistent basis of presentation for our assets and
liabilities that are used for internal decision-making. We believe that these measures provide an important view of our business and
operations. These measures include revenues, expenses, and earnings before interest, taxes, depreciation, and
amortization (EBITDA) and net cash provided by operating activities. These measures are not
measures prepared in accordance with generally accepted accounting principles (GAAP).

We have included the following information:

1. A summary of the significant accounting policies.
2. A description of our operations and the markets in which we operate.
3. A description of the critical accounting estimates that we have made.
4. A description of the risks and uncertainties that are inherent in our business.
5. A description of our capital structure and financial condition.

We have made the following assumptions:

1. That the economic environment will remain stable.
2. That our competitors will not significantly increase their prices.
3. That our customers will continue to purchase our products.
4. That our suppliers will continue to provide us with materials.
5. That our employees will continue to work for us.

We have made the following disclosures:

1. A description of our long-term debt.
2. A description of our capital stock.
3. A description of our retained earnings.
4. A description of our earnings per share.
5. A description of our capital expenditures.

We have included the following notes to the financial statements:

1. A description of our subsidiaries.
2. A description of our joint ventures.
3. A description of our significant transactions.
4. A description of our significant events.
5. A description of our significant account balances.