May 31, 2013

Technical Director
File Reference No. 2012-260
Financial Accounting Standards Board
401 Merritt 7
PO Box 5116
Norwalk, CT 06856-5116
RE: Comments to Exposure Draft on Proposed Accounting Standards Update: Financial Instruments – Credit Losses

Dear Sir or Madam,

Thank you for the opportunity to provide feedback on the Proposed Accounting Standards Update referenced above. DuPont Community Credit Union is a State-charted credit union with approximately $870 million in total assets headquartered in Waynesboro, Virginia. The proposed changes concerning the methodology for recognizing credit losses on specific financial instruments appear as they will bring significant changes to the current method of calculating such losses. I will attempt to express my concerns within the following major categories:

A. Estimate of contractual cash flows not expected to be collected
B. Decision-useful information for financial statement users

A. Estimate of Contractual Cash Flows Not Expected to be Collected

I’d first like to comment on the proposed elements to be used as a basis for a financial institution making an estimate of the level of contractual cash flows not expected to be collected. The proposed rule states that information to be used for making estimates of cash flows not expected to be collected include historical experience, current conditions, and reasonable and supportable forecasts. I have concerns mostly about two of these three elements:

- Historical Experience

The current rules for recognizing credit losses when they are incurred or become probable include using historical experience as a guide for determining what losses are currently probable within your applicable financial asset portfolios. The change in the proposed rule to switch from the current ‘incurred’ model to an ‘expected’ model will require looking at historical loss experience in a completely different way. Under the proposed ‘expected’ losses model, an institution will need to have access to historical data that will allow for the assessment of losses experienced over the entire contractual term of past homogeneous asset pools. In order to have an accurate assessment of historical experience, an institution will need to be able to track static pools of homogeneous assets over their entire contractual term (which depending on the terms of the assets pools could create quite a spectrum of look-back periods) in order to know what the actual loss experience was for each pool. This will be necessary in order to set up an appropriate time value of money calculation for current pools as the timing of such things as normal principal payments, pre-payments/payoffs, and charge-offs (credit losses) ultimately have the ability to impact such a calculation significantly. We believe that in order for the calculation of ‘expected’
credit losses to supply ‘decision-useful’ information to the financial statement users, this level of detail is necessary.

We have concern as to the availability of the necessary data to do a proper assessment of historical experience. We also have concerns that the historical assessments done will only cover a limited spectrum of interest rate environments.

Lastly, we have concerns due to the inclusion of loan commitments into the proposed rule. This creates another set of challenges as to getting an accurate assessment of the historical experience concerning such things as percentage usage of lines of credit, timing of transactional activity on open-ended commitments (advances, paybacks, etc), and the average realized lives of these types of loans.

- Reasonable and Supportable Forecasts

The proposed rules concerning the use of reasonable and supportable forecasts is also concerning. There is a lot of ambiguity in the exposure draft related to this issue such as, but not limited to, the following:

- 825-15-25-5 – “an estimate of expected credit losses shall neither be a worst-case scenario nor a best-case scenario. . . . However, a probability-weighted calculation that considers the likelihood of more than two outcomes is not required. An entity is prohibited from estimating expected credit losses based solely on the most likely outcome (that is, the statistical mode).”

  This section really leaves us guessing as to what will be an acceptable ‘scenario’ for estimating our expected losses.

The exposure draft also states that an entity would consider an evaluation of both the current point and the forecasted direction of the economic cycle. This raises questions as to whether a certain level of economic qualifications will be necessary in order to have current and forecasted economic cycle factors involved in the overall forecast element of our estimate of credit losses.

The forecasting element also raises questions as to who will govern what is an acceptable forecast and/or how will the rule be regulated so that there aren’t industry-wide results reflecting too broad of a range of forecasts being accepted by various financial institutions that would create more of a challenge for the financial statement users to compare one institution to another.

B. Decision-useful Information for Financial Statement Users

It seems, in general, that the added complexity through the estimate of credit losses covering the entire contractual term and the required use of subjective forecasts, that the financial statement users will not only have more information to process, but what they are presented with will be more complex to understand and less likely to have been calculated in a similar (apples-to-apples) manner as other institutions that may otherwise be considered peers.

The desire to provide financial statement users with better decision-making information is a very worthy objective, but we believe this proposed rule will not accomplish that and, in fact, will make the financial statements less likely to aid in any decision making.

In conclusion, we are very concerned about the added complexity this proposed rule would add to the process of estimating credit losses. The burden for completing the estimate in a way that is ultimately compliant is truly unknown upon reading the proposed rule due to the ambiguity it contains. The sense of feeling like so much is open to be interpreted leaves us with a fear of the potential cost in both dollars and
time that the proposed rule, if implemented, would create. We do not believe that had such a rule been in place prior to the global economic crisis, driven by poor credit decisions, that institutions would have recognized the necessary losses as part of an estimate made before the event took place. The type of scenario that unfolded as part of that crisis likely would have been seen as a bad/worse-case scenario and therefore not prohibited in the process of establishing a reasonable estimate for credit losses over the contractual term of the applicable assets. We fear that this proposed rule is an overly conservative and burdensome reaction to what was a bad economic event.

Respectfully,

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