Comerica Incorporated

VIA ELECTRONIC MAIL (director@fasb.org)

June 7th, 2013

Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116
Attention: Ms. Susan Cosper, Technical Director


Dear Ms. Cosper:

Comerica Incorporated (“Comerica” or “we”) appreciates the opportunity to comment on the Financial Accounting Standards Board’s (the “Board”) Exposure Draft of a Proposed Accounting Standards Update – Financial Instruments–Credit Losses (Topic 825-15), dated December 20, 2012 (the “Exposure Draft”). Comerica is a financial services company headquartered in Dallas, Texas. As of March 31, 2013, we are among the 50 largest U.S banking companies, with total assets of approximately $65 billion, total deposits of approximately $52 billion, total loans of approximately $45 billion, and total shareholders’ equity of approximately $7 billion.

Comerica supports the Board’s efforts to determine appropriate measurement of impairment and provide users of financial statements useful information regarding an entity’s exposure to credit losses while decreasing unnecessary complexity in accounting literature. We appreciate the challenges involved with developing a standard that appropriately addresses the perceived weaknesses of the existing incurred loss model following the most recent global economic crisis. Comerica takes pride in the fact that we have successfully endured this most recent challenging economic cycle and believe that the current credit loss model, though prone to pro-cyclicality, served us well. We believe that the model could be improved with better timeliness in measuring exposure to credit losses. We further believe that accounting guidance developed for credit losses needs to be: (a) based on sound accounting principles which include the matching principle, reliability and representational faithfulness, (b) easily understood by investors and other stakeholders while consistently applied across entities and (c) operationally feasible.

While we recognize the amount of thought and consideration that went into the Board’s latest Exposure Draft, we are generally concerned that the proposed Current Expected Credit Losses (“CECL”) model contradicts basic accounting principles, requires entities to make assumptions beyond what is reasonably estimable, introduces significant operational complexity, and ultimately will result in less meaningful information for users because credit losses will be too disconnected from the very business performance they are trying to evaluate and less comparable across entities.
General Observations Regarding the Proposed Credit Impairment Model for Loans

Matching the recognition of revenues with that of related expenses (the “matching principle”) is a fundamental accounting principle. A credit loss model developed in an ideal world would recognize such losses over time, for example as a yield adjustment. This would require all credit losses to be recorded and tracked at a loan level. Such a model would perfectly reflect the matching principle. However, since the vast majority of reserves are comprised of estimated losses for pools of loans, loss rates are not contractually driven (unlike contractual interest rates and fees used to calculate effective yields), and loan systems are not built to handle such a credit model, Comerica (and we believe many others) does not believe such a credit model to be operationally feasible. Because the matching principle cannot be operationally achieved, other alternatives or proxy models that result in both a match of the timing of recognition of income and related losses and an appropriate loss estimate should be considered. Models under discussion vary considerably and include the following:

1. The current incurred loss model (record the best estimate of losses for the near-term future in accordance with ASC 450)
2. Modify the current incurred loss model to reduce the probability threshold to “reasonably possible,” thereby increasing the loss emergence period and the level of losses that are considered to be incurred
3. Record an estimate of expected losses over the foreseeable future
4. Record an estimate of all expected credit losses using CECL
5. The “3 bucket” approach proposed by the IASB

CECL would by far be the alternative that would be most misaligned with the matching principle because it would require all expected losses to be recorded up front, resulting in a full acceleration of loss recognition. Our analysis of historical loss recognition indicates that credit migration patterns may serve as a good proxy for the timing of loss recognition aligning with income recognition. When losses are recognized on the basis of a sound credit migration analysis, the result is a gradual pattern of recognition of losses as they emerge over the life of the loan proportionate to its credit risk.

CECL would require entities to make assumptions beyond what is reasonably estimable. Any organization that prepares forecasts will agree that the further you project into the future, the less reliable the quality of estimate will tend to be. Since companies will need to incorporate economic and other assumptions over a very long period of time into their credit loss estimates, CECL will significantly increase the subjectivity and judgment involved with the reserve process of financial institutions to uncomfortable and unauditable levels. In our opinion, the accuracy of expectations decreases the further out the life of the instruments go into the future. At a certain point into the future, these types of calculations simply cease to be reliable estimates.

Under the current incurred loss model, provisions to build the allowance for loan and lease losses (“ALLL”) and credit quality indicators of the performance of a loan portfolio (e.g., past due and nonaccrual statistics) are correlated and move in the same direction. Therefore, as credit quality declines during a downturn, provision levels within financial statements indicate that incurred loan losses have increased. Similarly, the ALLL decreases in times of economic expansion. It is easier for investors and stakeholders to understand our financial results when the changes in the level of the ALLL are directionally consistent with changes in macro-economic factors, taken as a whole. While many have looked to the accounting model to solve the
problem of pro-cyclicality and provide soundness in the levels of reserves at financial institutions, we believe that these goals should be left to the regulators to address through capital rules.

We believe a better operational alternative is one that leverages and builds upon existing best practices. In general terms, existing credit loss models employed by the larger banks are based on probability of default and loss given default factors derived using historical trends, such as statistical migration analysis, as predictors of what banks can reasonably expect their losses to be over generally a 12-month period. In addition, qualitative adjustments may be overlaid by management to ensure reserve levels are considered sufficient based on current conditions. We think the Board should consider this as a good starting point with the following improvements:

a) We recommend the Board establish guidance regarding the loss emergence period based on a threshold of reserving for losses when they become reasonably possible. We believe that this will result in a measurement that is reasonably estimable and, for many types of loans, will be a period of time greater than twelve months. For funded loans with a stated term, we recommend the Board considers establishing this requirement as the shorter of the loss emergence period or the average expected life of the portfolio (adjusted for prepayment expectations) with a minimum requirement of twelve months of loss estimates. For demand-type loans and unfunded commitments we recommend a strict 12-month requirement. Standardizing the period of time for which to estimate credit losses for demand-type loans and unfunded commitments will improve comparability among entities that may have differing assumptions and reduce complexity for users of the financial statements. In addition, we consider extending the probability of draw (and consequently estimating losses) on unfunded commitments too far into the future akin to forecasting new loans in future years for reserve consideration. To ensure comparability and transparency, preparers should be required to disclose the time horizon used to develop reserve estimates by portfolio type.

b) Incorporate the use of supportable forecasts about the future\(^1\) as proposed in the Exposure Draft. We recommend the Board considers limiting adjustments made to historical experience based on supportable forecasted information to the time horizon the allowance is intended to cover. We believe availability of forecasted information will vary depending on the type of loans and therefore would also support emphasizing that forecasted information should be limited to “what is available without undue cost and effort” and what can be reasonably estimated.

We believe these recommended improvements will retain some of the directional consistency of credit quality indicators with the movement of the ALLL so users can better understand credit impairment. In our opinion, this model will also provide a higher quality of the loss estimate than CECL since there are fewer assumptions extending further in the future. At the same time, the recommended improvements will result in a reserve coverage that extends beyond what the existing incurred model allows for today; hence, a better estimate of what entities will suffer in losses as a result of credit deterioration.

**Specific Concerns Regarding the Proposed Credit Impairment Model for Loans**

We have other more specific concerns we would like to highlight before the Board finalizes its decisions based on our understanding of the Exposure Draft.

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\(^1\) Paragraph 825-15-25-3


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**Estimating Credit Losses over the Contractual Term of Loans**

The use of *contractual term*\(^2\) in the Exposure Draft to describe the period of time over which credit losses should be estimated presents operational issues. As a primarily commercial bank, a large portion of Comerica’s portfolio is comprised of demand loans and revolvers for which *contractual term* may not be the best representation of the credit exposure horizon. We do not believe it is clear from the Exposure Draft how these types of instruments should be considered with regard to future expectations.

We are supportive of a forward looking model that would project losses over a time horizon that is reasonably estimable, but not so far into the future that would jeopardize the ability of management, auditors and regulators to ascertain the reasonableness of the allowance estimates. We believe a contractual term requirement in a significant number of cases would exceed the time horizon over which entities could reasonably estimate credit losses.

**Incorporating Time Value of Money into Allowance Measurement**

The proposed guidance is built on the premise that net amortized cost\(^3\) represents the present value of expected collections when discounted at the original effective interest rate. Further, this premise also includes the assumption that the allowance for credit losses reflects the present value of contractual cash flows (both principal and interest) not expected to be collected. This premise does not function well in the context of the nonaccrual framework. It is well-established practice and broadly-understood concept that U.S. banks stop accruing revenue for loans that have credit deterioration. Because of this, investors and analysts view loan reserves in the context of principal losses. Likewise, charge-offs are understood to represent the amount of principal not repaid by a borrower, and not a combination of forfeited interest revenue and uncollected principal.

To enhance user understanding, as opposed to furthering a theoretical concept, credit loss measurement should be based on principal losses and not forfeited interest revenue for loans. We believe including a time value of money element into the reserve estimate introduces unnecessary complexity for the following reasons:

a) Generally, credit deterioration resulting in losses “shortens” the time frame needed to be evaluated as banks employ their resources to maximize collections. For example, a bank may move forward to foreclose on the collateral for a mortgage loan. Although foreclosure is not an immediate process, it is something that can be achieved in a matter of months. This action by the bank shortens the time frame over which to estimate losses from the contractual term of the mortgage to how long it takes to foreclose and liquidate the collateral. Because banks take similar actions with other types of loans in order to maximize collections, the typical collection period is about 18 months. Therefore, we believe a larger portion of the allowance pertains to losses that are expected in the near-term decreasing the relevance of time value of money.

b) Such a requirement will burden preparers to evaluate whether or not their reserve methodology appropriately gives implicit/explicit consideration to the time value of money. In the Exposure Draft the Board explains that allowance methods loss-rate methods, roll-rate methods, probability-of-default methods, and a provision matrix method using loss factors implicitly reflect the time

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\(^2\) Paragraphs 3 and 19 of section 825-15-25, 19, 23 and 24 of section 825-15-55, BC18 and BC24

\(^3\) As used in paragraphs BC 16 and 17, net amortized cost represents amortized cost net of allowance for credit losses
value of money.\textsuperscript{4} Further, the Board has stated that an entity would not be required to prove that the results would be the same using an explicit versus implicit method.\textsuperscript{5} However, we are concerned that auditors and regulators will ultimately challenge the “implicit” reflection of time value of money of an entity’s allowance methodology.

c) Typically, other areas of accounting which require preparers to estimate the impact of time value of money incorporate guidance as to the subsequent treatment of the present value discount, including whether to separately recognize interest expense. However, it is unclear from the proposed guidance how the time value of money will be de-recognized (i.e. accreted) in subsequent periods. We believe that it will be extremely difficult for entities to roll forward allowance balances for the effects of passage of time if they use models which implicitly reflect the time value of money.

d) The existing accounting model for purchase credit impaired (“PCI”) assets incorporates a time value of money element into the reserve calculation. However, users of financial statements are more comfortable with the reserve and nonaccrual concepts for “traditional” loans than they are with the existing PCI model. We believe that incorporating the impact of time value of money into the allowance measurement will increase complexity for investors and other users of the financial statements.

Therefore, we are not supportive of the Board’s proposal to include time value of money into the allowance calculation. We support an impairment model that is principal balance based and incorporates nonaccrual treatment for loans as a method of reducing future credit loss exposure. This approach is consistent with the business practice of financial institutions, and is therefore a more relevant measurement in our opinion.

**Nonaccrual Guidance**

As previously discussed, the banking industry and its stakeholders are long-accustomed to the nonaccrual framework with respect to loans that are held for investment and contractual cash flows. We generally support inclusion of this guidance in the Exposure Draft, with two recommendations: (a) clarification regarding what instruments meet the scope and (b) clarification regarding the treatment of cash payments for nonaccrual assets.

a) **Clarification Regarding Scope:** The Exposure Draft says that interest income should not be accrued “when it is not probable that the entity will receive substantially all of the principal or substantially all of the interest.”\textsuperscript{6} In contrast, regulatory guidance states that interest should not be accrued on “(1) any asset which is maintained on cash basis because of deterioration in the financial position of the borrower, (2) any asset for which payment in full of interest or principal is not expected, or (3) any asset...in default for a period of 90 days or more.”\textsuperscript{7} In order to avoid inconsistencies and eliminate operational concerns, we recommend the Board makes changes to the final guidance to conform to the regulatory language.

Regulatory guidance includes a scope exception for PCI assets which we believe should be retained. As proposed in the Exposure Draft, we believe application of the nonaccrual guidance

\textsuperscript{4} Paragraph 825-15-55-3  
\textsuperscript{5} Response to question 16 of the Board’s FAQ on the Exposure Draft  
\textsuperscript{6} Paragraph 825-15-25-10  
\textsuperscript{7} FR Y-9C Glossary, *Nonaccrual Status*
will result in nonaccrual of interest income for all PCI loans. This contradicts the fact that in the preceding paragraph (825-15-25-9) the Exposure Draft provides guidance regarding how to recognize interest income for PCI financial assets. We disagree with the inability to recognize accretible yield on PCI loans that are performing at least as well as initially expected. Therefore, we ask the Board to clarify the scope of paragraph 10 to exclude PCI instruments unless cash flow expectations have deteriorated beyond the original expectations used to establish the value of the instruments at acquisition.

b) **Clarification Regarding Treatment of Cash Payments:** Paragraph 825-15-10b states “Cash receipts that exceed the amount of interest income that would have been recognized in the period had the asset not been placed on nonaccrual status shall be applied to reduce the carrying amount of the asset.” In contrast, regulatory guidance states that an entity may choose to apply contractual interest cash payments received as “income, reduction of the recorded investment in the asset, or recovery of prior charge-offs…consistent with its accounting policies.” To avoid inconsistencies and operational concerns, the Board should consider making cash basis recognition of income an accounting policy choice and requiring entities to disclose the method of recognition.

However, if the Board chooses to include specific guidance regarding the treatment of cash payments received while an asset is on nonaccrual status, the final guidance should be modified. We believe that the Exposure Draft has the unintended consequence of giving priority to interest recognition over principal recovery. Because we believe that maximizing recoverability of principal (an entity’s investment) should take priority over income recognition, we recommend the Board revises the language to state, “Cash receipts that exceed the amount of principal scheduled to be collected in the period had the asset not been placed on nonaccrual status shall be recognized as interest income.”

**Purchased Financial Assets**

We support the Board’s efforts to simplify the accounting for PCI assets. The proposed guidance in 825-15-25-9 requires entities to establish an allowance at acquisition for the embedded discount in the purchase price that is attributable to the expected credit losses. Unlike existing guidance, under the proposed rules such credit discount is not recognized as interest income even if expectations improve in the future. Rather, changes in estimates of cash flows expected to be collected would be reflected through the allowance for loan loss. We believe that requiring entities to establish an allowance at the time of acquisition and eliminating yield adjustments for improvements in cash flow expectations are both improvements over existing guidance.

We agree that the recognition of interest income should be different for PCI and non-PCI assets and support the income recognition guidance under 825-15-25-9 to be limited to PCI assets. However, we are not clear why recognizing a credit allowance at acquisition should be limited to assets that meet the PCI definition. Having a different set of rules for the establishment of an allowance for acquired non-PCI assets creates an unnecessary inconsistency prolonging, rather than eliminating complexity. Both PCI and non-PCI assets acquired at a discount have some element of credit risk associated with their acquisition price. Perhaps an unintended consequence of the Exposure Draft is that it reintroduces an “incurred” notion by distinguishing how assets are going to be treated from an allowance perspective based on the level of experienced credit.

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8 FR Y-9C Glossary, *Nonaccrual Status: Treatment of cash payments and criteria for the cash basis recognition of income* section of the
deterioration. Not only do we believe this contradicts the very premise of the CECL model proposed by the Board, we also believe it is erroneous to have a different reserve methodology for assets that are not deemed to be PCI. Therefore, we recommend the Board eliminate the distinction and require entities to establish an allowance for all acquired assets equal to the embedded discount in the purchase price that is attributable to the expected credit losses.

The Board should also consider transition guidance for PCI loans currently accounted for under ASC 310-30. We believe a reasonable and simple approach would be to record an allowance upon transition for the amount of remaining principal cash flows not expected to be collected concurrent with reversing any remaining non-accretable discount. Interest income recognition can then follow the guidance in 825-15-25-9.

**Collateral-Dependent Financial Assets**

The Exposure Draft defines collateral-dependent financial assets as those “for which the repayment is expected to be provided primarily or substantially through the operation (by the lender) or sale of the collateral.”\(^9\) This change from existing guidance will greatly limit the current use of the practical expedient of measuring the loan at the fair value of the collateral under ASC 310-10-35-19. Although we agree with the Board’s substitution of the term *solely* with *primarily or substantially,* we disagree with the limitation that the collateral must be operated by the lender in order for a loan to be considered collateral-dependent. Often, the process that must take place to assume control of the underlying collateral is costly, and there are legal ramifications to a lender being in operational control of collateral which financial institutions may want to avoid. Therefore a financial institution may only assume control of the collateral as a last resort when collectability is significantly uncertain. We believe requiring the lender to be in control of operations is inconsistent with the Exposure Draft’s emphasis on expectations. If management expects the repayment of a loan to be primarily or substantially through the operation or sale of the collateral it should be able to apply the practical expedient proposed under 825-15-55-4.

**General Observations Regarding Instruments Measured at Fair value with Changes in Fair Value Recorded through Other Comprehensive Income ("FV OCI")**

We believe that the existing guidance for measuring impairment losses for debt securities based on other-than-temporary-impairment ("OTTI") is well understood and effective. Therefore, the OTTI model should be retained and applied to all FV OCI instruments.

Whether or not the Board chooses to retain OTTI for FV OCI instruments, we recommend that the Board change the criteria in 825-15-25-2 from “both” to “either” in order to maximize what we believe to be the intended use of this practical expedient. In our opinion, assets with insignificant credit losses should not be unnecessarily subjected to more rigorous quantitative analysis. Even very highly-rated securities such as U.S. Treasuries may be valued below par in a rising rate environment without significant credit deterioration. However, as proposed, entities would not be able to make use of the practical expedient. Entities should also be allowed to avail themselves of the practical expedient for instruments whose fair value exceeds their respective amortized cost basis. If the instrument’s fair value exceeds the amortized cost basis, presumably any credit deterioration that may exist has been overcome.

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\(^9\) As defined in the Glossary section on page 12 of the Exposure Draft
Disclosure Requirements

We also have significant concerns with what seems to be an unbridled approach to disclosure requirements. As the Board may be aware, disclosure requirements result in a significant amount of effort for preparers who must comply with them. Therefore, we ask that the Board would consider the balance between added costs and additional benefit before finalizing the proposal. In this regard, we recommend that the board ask users how additional disclosure information will be used and what purpose it will serve — if for no other reason, then to avoid disclosure overload.

In our opinion, whatever small benefit may be garnered by providing users of financial statements with a roll forward of debt instruments as required by the proposed guidance\(^{10}\) is not commensurate of the additional operational burden that will be placed on preparers. Accordingly, we ask the Board to eliminate this requirement. Likewise, if fair value has been determined to be the most relevant and appropriate measurement attribute under the Recognition and Measurement guidance, we fail to understand the necessity for requiring a reconciliation between fair value and amortized cost for FV OCI instruments.\(^{11}\) We recommend this requirement also be eliminated.

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We thank you for the opportunity to express our concerns regarding this proposal, and we respectfully request that the Board consider the points we have raised. Should you require further information or have any questions, please do not hesitate to contact me (telephone 214-462-6684; email address mscarr@comerica.com; facsimile no. 214-462-6810) or Mauricio Ortiz, Vice President - Accounting Policy (telephone 214-462-6757; email address maortiz@comerica.com; facsimile no. 214-462-6810).

Sincerely,

Muneera S. Carr
Executive Vice President and Chief Accounting Officer

cc: Karen Parkhill, Vice Chairman and Chief Financial Officer
    John Kilian, Executive Vice President and Chief Credit Officer
    Mauricio Ortiz, Vice President - Accounting Policy

\(^{10}\) Paragraphs 12 and 13 of section 825-15-50

\(^{11}\) Paragraph 825-15-50-15