September 16, 2013

Ms. Susan M. Cosper
Technical Director
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, Connecticut 06856-5116
director@fasb.org

File Reference No. EITF – 13E, Reclassification of Collateralized Mortgage Loans Upon a Troubled Debt Restructuring

Dear Ms. Cosper:

The Mortgage Bankers Association\(^1\) (MBA) appreciates the opportunity to comment on the Financial Accounting Standards Board’s (FASB) Exposure Draft, *Reclassification of Collateralized Mortgage Loans Upon a Troubled Debt Restructuring* (Proposed Update). The following are MBA’s general comments and responses to FASB’s specific questions.

**Background**

Weakness in the housing market in recent years has resulted in a record number of vacant or abandoned residential real estate properties. Generally accepted accounting principles (GAAP) provides accounting principles for troubled debt restructurings, like loan modifications, and on situations in which the creditor obtains one or more of a debtor’s assets in satisfaction of all or a part of the debt. This guidance indicates that a creditor should reclassify the asset from a mortgage loan to real estate owned (REO) when there has been an *in substance foreclosure*. The trigger for such a

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\(^1\) The Mortgage Bankers Association (MBA) is the national association representing the real estate finance industry, an industry that employs more than 280,000 people in virtually every community in the country. Headquartered in Washington, D.C., the association works to ensure the continued strength of the nation's residential and commercial real estate markets; to expand homeownership and extend access to affordable housing to all Americans. MBA promotes fair and ethical lending practices and fosters professional excellence among real estate finance employees through a wide range of educational programs and a variety of publications. Its membership of over 2,200 companies includes all elements of real estate finance: mortgage companies, mortgage brokers, commercial banks, thrifts, REITs, Wall Street conduits, life insurance companies and others in the mortgage lending field. For additional information, visit MBA's Web site: [www.mortgagebankers.org](http://www.mortgagebankers.org).
reclassification is when the creditor receives physical possession of the debtor’s assets regardless of whether formal foreclosure proceedings take place.

Apparently, diversity in practice has developed because GAAP does not define in substance foreclosure and physical possession. The Proposed Update would clarify in substance foreclosure as the moment the creditor is considered to have physical possession of a residential real estate property collateralizing a consumer mortgage loan upon (1) the creditor obtaining legal title to the residential real estate property or (2) completion of a deed in lieu of foreclosure or similar legal agreement under which the borrower conveys all interest in the residential real estate property to the creditor to satisfy the loan.

General Comments and Questions

MBA Supports the Proposed Update

MBA believes that the majority of reporting entities already apply the proposed rules in determining an in substance foreclosure. MBA believes that the Proposed Update should be limited in scope to residential mortgage loans to consumers and not extended to commercial real estate loans or to auto loans. In the case of commercial real estate loans, the laws and practices are different. For example, frequently a lender can exercise protective rights but not take legal custody because of lender liability laws. In some cases a lender may put a deed in lieu of foreclosure into escrow in return for a concession made but cannot execute unless there is triggering event like an event of default. Further, legal possession and ownership involves more legal precedent and case law for commercial real estate loans. MBA’s members believe that there is no diversity in practice in the commercial real estate lending area and it should remain scoped out from the Proposed Update. Likewise, auto loans should be excluded from the Proposed Update since physical repossession in many jurisdictions constitutes legal ownership.

In Substance Foreclosure Within a Consolidated VIE

Page 10, paragraph BC5, states, “The Task Force further noted that commercial real estate loans may involve structured financing arrangements that are beyond the scope of this Issue, such as use of special-purpose entities.” It appears to carve out structured financing arrangements, although that is not apparent in the ASC marked-up version.

If a reporting entity is the Primary Beneficiary of a Variable Interest Entity (VIE) requiring the VIE to be included in the reporting entity’s consolidated financial statement, should the Proposed Rule apply to in substance foreclosures within a securitization trust? MBA recommends that the final rule clarify this issue.
Proposed Roll-forward of REO

The Proposed Update would require reporting entities to disclose in the notes to financial statements a roll-forward reconciling the changes from beginning to end of period for residential real estate owned (REO). MBA points out that increasingly the FASB, in proposed and new accounting pronouncements, requires roll-forward analysis of various line items on the balance sheet. MBA further points out that the statement of changes in financial position is designed to show users the material changes in the respective balance sheet line items, and doing roll-forwards of specific accounts or line items in the notes to financial statements is redundant. MBA further points out that REO is not a material asset for most financial institutions and often rolls up under “other assets” in the balance sheet. MBA recommends that the final rule require a roll-forward only if the beginning or ending balances for REO are material or if the activity in the account during the period is material and the material roll-forward data is not otherwise disclosed in the statement of changes in financial position.

Impact of New National Servicing Standards

MBA notes that the Consumer Financial Protection Bureau (CFPB) issued a new national servicing standard (NSS) earlier this year. It specifies certain timetables and action steps servicers must take prior to commencing or completing foreclosure. Some of these rules conflict with state foreclosure laws. MBA notes that page 12 of the Proposed Update states, “The determination of whether a loan is in the process of foreclosure should be made by reference to local requirements of the applicable jurisdiction.” MBA recommends that FASB write this section in a more general fashion, especially taking out the reference to “local requirements” and substituting “applicable laws and regulations.”

MBA appreciates the opportunity to share its observations with you. Any questions about the information provided herein should be directed to me, Vice President Financial Accounting and Public Policy and Staff Representative to MBA’s Financial Management Committee, at (202) 557-2860 or jgross@mortgagebankers.org.

Sincerely,

James P. Gross
Vice President of Financial Accounting and Public Policy
Appendix A – Responses to FASB’s Specific Questions

**Question 1:** Should the scope of the proposed amendments about the timing of reclassification of receivables to foreclosed residential real estate properties be extended to commercial real estate mortgage loans? If yes, please explain why, including a discussion on any special considerations related to reclassifying commercial real estate mortgage loans.

**MBA’s Response:** No, the scope should not be extended to commercial real estate loans. See general comment above titled *MBA Supports the Proposed Update.*

**Question 2:** Should the scope of the proposed amendments about the timing of reclassification of receivables to foreclosed assets also be extended to loans collateralized by nonfinancial assets other than real estate (for example, auto loans)? If yes, please explain why, including a discussion on any special considerations related to reclassifying loans that are collateralized by nonfinancial assets other than real estate.

**MBA’s Response:** No, the scope should not be extended loans collateralized by nonfinancial assets such as auto loans. See general comment above titled *MBA Supports the Proposed Update.*

**Question 3:** Do you agree that a creditor should be considered to have received physical possession of residential real estate property collateralizing a consumer mortgage loan upon (a) the creditor obtaining legal title to the residential real estate property or (b) completion of a deed in lieu of foreclosure or similar legal agreement under which the borrower conveys all interest in the residential real estate property to the creditor to satisfy that loan, even though legal title may not yet have passed? If not, please explain why.

**MBA’s Response:** MBA agrees.

**Question 4:** Do you agree that the recurring disclosures of (a) the recorded investment in consumer mortgage loans secured by residential real estate properties that are in the process of foreclosure according to local requirements of the applicable jurisdiction and (b) a roll-forward schedule reconciling the change from the beginning to the ending balance of foreclosed residential real estate properties provide decision-useful information and should be required to be provided in interim and annual financial statements? If not, please explain why and what disclosures, if any, you would propose.

**MBA’s Response:** MBA notes that depository institutions already disclose consumer mortgage loans in the process of foreclosure in their quarterly call reports, and questions how useful such a disclosure would be for non-depositories. MBA does not agree with the proposed roll-forward schedule for REO. See MBA’s general comment above titled *Proposed Roll-forward of REO.*
Question 5: If the scope of the proposed amendments is extended to commercial real estate mortgage loans and/or loans collateralized by nonfinancial assets other than real estate (for example, auto loans), should different disclosures be required for these loans? Please describe how and why you think the disclosures should be different.

MBA’s Response: MBA does not agree that the Proposed Update should be extended to commercial real estate loans and/or loans collateralized by nonfinancial assets other than real estate and believes that no additional disclosures are deemed necessary for these asset classes.

Question 6: Do you agree that the proposed amendments should be applied to both collateralized residential mortgage loans and foreclosed residential real estate properties existing at the date of adoption by means of a cumulative-effect adjustment as of the beginning of the annual reporting period for which the guidance is effective? If not, please explain why.

MBA’s Response: MBA agrees.

Question 7: If an entity is required to reclassify foreclosed residential real estate property to consumer mortgage loans upon transitioning to the proposed guidance, at what amount should those loans be recorded at the date of adoption? For example, (a) should the recorded investment in such consumer mortgage loans at the date of adoption be the initial recognition basis of the foreclosed residential real estate property and (b) should any difference between the carrying amount of the foreclosed residential real estate property at the date of adoption and its initial recognition basis be recorded as an allowance for loan losses for such consumer mortgage loans? Please explain the reasons for your view.

MBA’s Response: MBA believes that the recorded investment as an REO should be the amount expected to be recovered, net of estimated marketing costs. Any difference between the basis of the consumer mortgage loan and the new REO basis at date of adoption should be recorded as a loss charged against the allowance for loan losses.

Question 8: Do you agree that the proposed amendments should apply to both public entities and nonpublic entities? If not, please describe how and why you think they should be different.

MBA’s Response: MBA believes that the Proposed Update should be applied to both public and nonpublic entities.

Question 9: Do you agree that an entity should be permitted to early adopt the proposed amendments? If not, please explain why.

MBA’s Response: Yes, early adoption should be permitted.
Question 10: How much time would be needed to implement the proposed amendments, and should the effective date differ for nonpublic entities versus public entities? Please explain why.

MBA’s Response: MBA does not believe that implementation should take longer than one year.