October 21, 2013

Russell G. Golden
Chairman
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116
Via email: director@fasb.org

File Reference: FASB No. 2013-290 Insurance Contracts

Dear Chairman Golden:

Union First Market Bankshares, Corporation (Union) appreciates the opportunity to comment on the exposure draft, *Insurance Contracts* (ED). Union is a $4 billion single bank holding company, headquartered in Richmond, Virginia. Our 1,200 employees serve a wide variety of small to medium sized companies with an array of loan and treasury management products. In early 2014, Union will acquire StellarOne Corporation, becoming a $7 billion financial holding company.

The ED redefines an insurance contract and requires new methodologies for measuring insurance liabilities. Both the new definition and the measurement differ from those that are commonly in use today among insurance companies as well as other companies, including banking institutions whose products would now fall within the scope of the ED. Wherein current insurance generally accepted accounting principles (GAAP) is generally based on industry practice, the ED prescribes guidance on a product-by-product basis. As noted in more detail below, we disagree that certain common banking products are, under the ED, defined as insurance contracts and would require accounting procedures that are significantly different from other similar debt instruments. These products do not contain the risk of an insurance contract and requiring insurance accounting will not only confuse investors, but also needlessly require more operationally complex systems to administer them.

The ED defines an insurance contract as one that transfers significant insurance risk to the entity from the policyholder. Insurance risk is “fortuitous, the possibility of adverse events occurring is outside the control of the insured” and is distinguished from financial risk, which results from possible future changes in interest rates, financial instrument prices, commodity prices, foreign exchange rates, index of prices or rates, credit rating or credit index, or other variable.

The ED asserts that various products and services commonly offered by banking institutions are considered by the Financial Accounting Standards Board (FASB) to be insurance products. Among them:

- Financial guarantees
- Standby letters of credit
- Guarantees related to trust preferred securities
Further, transactions involving recourse and indemnifications, certain guarantees related to representations and warranties on mortgage loan sales and regarding mergers and acquisitions (affecting not only those in the banking industry but all companies) are also included and appear to be considered insurance products.

Most guarantee (non-contingent) liabilities are currently accounted for in conformity with Accounting Standards Codification (ASC) Topic 460 (also widely known as “FIN 45”). They are measured at fair value at inception and subsequently adjusted to recognize the release of risk over the period of the guarantee. Contingent losses under the guarantee are recognized and measured in accordance with ASC Topic 450 (also known as “FAS 5”), the same standard that guides the accounting for losses for most other bank products (including impairment on loans). As proposed in the ED, the banking and guarantee products listed above appear to generally be subject to the “premium allocation approach”, whereby the present value of net cash flows related to the guarantee would be maintained as a liability, calculated by a probability-weighted method. Changes to the liability based on a change in discount rate would be recorded to Other Comprehensive Income, whereas all other changes in the liability would be recorded to net income. The ED also eliminates the availability of the Fair Value Option for products that are within the scope of the ED.

The Scope of the ED Must Exclude Credit Risk-Related Banking Products and Transactions

The ED states that comparability will be enhanced by requiring contracts that transfer significant insurance risk to be accounted for in a similar manner. We support the notion that comparable insurance products should be accounted for consistently. However, as we noted above, the ED includes many common banking products and transactions within the definition of insurance contracts that are not, in fact, insurance products or transactions—they are credit products and transactions. Including these products as insurance is not only inappropriate because of the nature of these products; it will also reduce comparability of credit risk-related products within the banking industry. Currently, contingent losses (and related administrative costs) on these products are recognized and measured consistently with other banking assets, but will be required to be accounted for under arbitrarily different, yet more operationally complex, accounting methods.

As a result, Union recommends that credit risk be wholly included within the definition of financial risk (we note that changes in credit ratings or a credit index are already within the definition), thus excluding the vast majority of banking products from the scope of the ED. Overall, credit risk does not represent an insurance risk, which is defined in the ED as being “fortuitous…” with “the possibility of adverse events occurring being outside the control of the insured.” In the vast majority of cases in which performance on a financial guarantee is required, there are systematic—not fortuitous—events that occur over a period of time that contribute to the “adverse event”. Further, in many of these cases, if not indemnified, the insured is able to avoid the “adverse event” by merely selling the financial instrument that contains the credit risk.

We believe banking products based predominately on credit risk do not fit into the Board’s overall definition of insurance risk. We note that financial guarantee contracts are excluded from the scope of the IASB exposure draft on insurance contracts, unless the issuer has previously asserted explicitly that it regards those contracts as insurance contracts and has used accounting applicable to insurance contracts. While we believe that banking products should not be included within the scope of the ED because credit risk is a financial (and not insurance) risk, the IASB’s explicit scope exception is acceptable. Our detailed conceptual reasons are discussed below.
The Decision Framework to Determine Product Scope Must be Refined

The ED lays out a framework in evaluating whether there is sufficient insurance risk in a product or instrument to determine whether insurance contract accounting is appropriate. However, the guidance (mainly that included in the table on pages 76 through 88 of the ED) is insufficiently clear and often seemingly contradictory, due to apparent inconsistencies in descriptions of specific terms and of instruments. Clear descriptions would allow for a more deliberate analysis of insurance risk. For example, the distinction between the insurer, the insured, the policyholder, and the beneficiary of a product is often vague. We believe these relationships are important within such an analysis. Further, more guidance is needed in distinguishing financial risk from insurance risk.

The following examples will assist the Board in understanding these comments, as banking products that appear to be captured in the scope of the ED are significantly different from other insurance products.

**Standby letter of credit (SLOC)**

A SLOC is significantly different from standard insurance contracts that are described in the ED.

- The typical insurance agreement has two parties: the insured (with a related beneficiary) and the insurer. The insured/beneficiary have a common insurable interest in the insured item/person (and, thus, should be considered as related parties) and pay insurance premiums to the insurer. A SLOC is an instrument created in a transaction among three unrelated parties: a bank, a bank customer, and an investor. In contrast to the insurance product, in a SLOC, the party with the ultimate insurable interest (the investor) does not pay an insurance premium (in this case, the premium would be the loan commitment fee). It is the bank customer that pays a commitment fee, and the presence of a SLOC normally results in a lower credit spread in the bond issued to the investor. The “insurance transaction” is basically a private transaction between the bank and the bank customer and can be thought of as collateral by the bond investor. The “policyholder” is the bank customer, not the investor.

- Insurance claims normally result in a cash payment recorded as a loss (or loss payment) by the insurer with no required continuing involvement by the insurer. In contrast, the claim arising from the contingent event in a SLOC results in a loan by the bank to the banking customer – an asset by which the bank earns interest.

- Insurance losses (or loss payments) are typically the cash used to settle a claim and are contractually defined. A SLOC is often fully collateralized, with no expected loss to be realized.

In other words, the SLOC is effectively a loan commitment between a bank and its customer. Draws on an SLOC result in recording an asset (and not in recording a loss). While the table on page 85-86 of the ED notes instances in which a SLOC may be considered outside the definition of an insurance contract, the distinction between what is in scope and out of scope is confusing.

**Guarantees related to trust preferred securities (TPS)**

Guarantees made by bank holding companies related to TPS are normally to ensure that the available amounts that have been placed into the related trust for the payment of dividends are, in fact, actually paid to shareholders. Such guarantees of the TPS structure are necessary from a tax and regulatory aspect, and connect the bank holding company to the TPS holder. In practice, however, they amount to the standard guarantee that a company makes when issuing debt or preferred stock. If it is the intent that such
guarantees are to be considered insurance contracts, we recommend that this issue be addressed comprehensively within a separate project on promises to pay made within debt and equity instruments.

Loans sold with recourse or indemnification provisions

It is common for financial institutions to sell loans with a recourse or indemnification provision in the sales agreement. If specific loans experience default or other adverse events, recourse provisions require the loans to be purchased back by the seller, while indemnification typically requires certain payments to be made. Though not included in the table on page 76-88, under the guidelines of the ED, it appears that within these transactions, a third-party (the seller) is making a guarantee to the policyholder (the buyer) on the credit of the borrower. Therefore, such sales would apparently qualify as insurance contracts.

To include recourse and indemnification provisions within the definition of an insurance contract would require changes to Topic 860-20 (Sales of financial assets) and we do not believe that it is the intent of the Board to make such changes. Consistent with our discussion above, these provisions are credit risk-related and, thus, more appropriately considered to be financial risks.

Merger and acquisition guarantees

The majority of merger and acquisition transactions have some kind of contingency in which future payments are required by either of the parties. As described in the ED, it is not clear that such guarantees are sometimes provided by the acquirer or a third-party, and are not limited to sellers. In the event the guarantee is provided by the acquirer, such a guarantee would appear to be out of the scope of insurance risk, as it relates to “own performance.” In the event this represents a third-party guarantee, it appears to be equivalent to a standby letter of credit, which (as noted above) does not transfer “fortuitous risk”, does not transfer risk between the policyholder to the guarantee provider, and merely represents a loan between the acquirer and the guarantor.

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In summary, we strongly recommend that credit risk, which does not result in fortuitous events, be considered a financial risk within the ED, disqualifying most banking products from the definition of an insurance contract.

Thank you for your attention to these matters and for considering our views. Please feel free to contact me (robert.gorman@bankatunion.com) if you would like to discuss our views.

Sincerely,

Robert M. Gorman
Executive Vice President and Chief Financial Officer