April 3, 2012

Ms. Susan M. Cosper
Technical Director
Financial Accounting Standards Board
401 Merritt 7
Post Office Box 5116
Norwalk, Connecticut 06856-5116

RE: File Reference No. 2011-230 – Proposed Accounting Standards Update (Revised) - Revenue Recognition (Topic 605)

Dear Ms. Cosper:

The staffs of the four federal regulatory agencies (the Agencies) responsible for supervising the safety and soundness of U.S. financial institutions appreciate the opportunity to comment on the proposed Accounting Standards Update (Revised) - Revenue Recognition (Topic 605) (Proposal). The Agencies support the continuing efforts of the Financial Accounting Standards Board and the International Accounting Standards Board (collectively, the Boards) to improve accounting standards and move toward convergence between U.S. generally accepted accounting principles (GAAP) and International Financial Reporting Standards.

The Agencies’ comments respond to Question 6 of the Proposal, which addresses the transfer of a nonfinancial asset that is not an output of an entity’s ordinary activities. More specifically, our comments focus on gain recognition for seller-financed sales of other real estate owned (OREO)¹ by financial institutions, particularly in situations where the financing is provided to a buyer who has made little or no initial investment in the real estate.

The Agencies do not agree that an institution should apply the proposed control and measurement guidance to seller-financed OREO sales. Sales of OREO are intended to be the final step in a financial institution’s loss mitigation activities associated with its collection of troubled receivables. Unlike other real estate holdings where owners can choose whether and when to sell, financial institutions are constrained by federal and state laws restricting their ability to hold OREO by requiring its disposal within specified time limits. Additionally, financial institutions are motivated to take actions to reduce the reported amount of these nonperforming assets from their balance sheets to improve various regulatory and analytical ratings and ratios. As a result, we recommend seller-financed OREO sales be explicitly excluded from the scope of the final update, and the Boards instead apply or simplify existing U.S. GAAP on gain recognition for real estate sales.

¹ OREO is real estate acquired for debts previously contracted, including through foreclosure or repossession.
If the Boards decide to apply this proposed revenue recognition guidance to seller-financed OREO sales, the following comments present the Agencies' views on recommended changes that should be part of the final update to address our concerns about inappropriate acceleration of gain recognition on such sales.

The revenue recognition criteria in the Proposal include a requirement that each party to the contract be committed to perform its obligations (paragraph 14(b)). The Agencies urge the Boards to provide practical guidance on how a buyer's initial cash investment, if any, should be assessed when determining, for purposes of meeting the paragraph 14(b) criterion, whether the buyer has demonstrated a commitment to perform on its loan obligation in a seller-financed OREO sale.

Under the Proposal, an asset is transferred when the customer obtains control of that asset, which enables the entity transferring the asset to recognize revenue. Paragraph 37(d) states: "The transfer of the significant risks and rewards of ownership of an asset to the customer indicates that control of the asset has been transferred." In the Agencies' experiences, the seller has not fully transferred the ownership risks associated with seller-financed OREO until the purchaser has made a sufficient investment in the real estate. Thus, we recommend the concept of transferring control as evidenced by the transfer of significant risks and rewards of ownership be clarified by emphasizing that the risks of ownership do not transfer to the purchaser of seller-financed OREO until the purchaser has made a sufficient investment in the property.

The Agencies also recommend clarification of paragraph 69 regarding income statement presentation. As written, this presentation guidance does not appear to recognize the differing income statement presentation practices currently followed by different industries, such as financial institutions. In typical financial institution income statements, net gains (losses) on sales of OREO are presented in other noninterest income (or expense) below net interest income after provision for loan losses, whereas credit losses on the related loans are included in the provision for loan losses.

Lastly, we note limited amendments are slated for Subtopic 310-10 even though paragraph 9 of the Proposal states that the revenue recognition guidance does not apply to contracts within the scope of Topic 310, Receivables. Because of these proposed amendments, we reiterate the Agencies' support for a general nonaccrual principle in which accrual of interest income ceases on a financial asset when full payment of principal and interest in cash is not expected. Further, we recommend the Boards clarify that the amendments in this Proposal do not change the existing interest income recognition model for financial instruments, including the nonaccrual concept as applied currently by financial institutions.
We would be pleased to discuss any questions the Boards may have regarding our comments.

Sincerely,

Kathy K. Murphy
Chief Accountant
Office of the Comptroller of the Currency

Steven P. Merriett
Assistant Director & Chief
Accountant - Supervision
Board of Governors of the
Federal Reserve System

Robert F. Storch
Chief Accountant
Federal Deposit Insurance Corporation

Larry Fazio
Director, Office of Examination and
Insurance
National Credit Union Administration

cc: Ms. Leslie Seidman, Chairman
     Financial Accounting Standards Board
     Mr. Hans Hoogervorst, Chairman
     International Accounting Standards Board