



Richard D. Levy
Senior Vice President & Controller

MAC A0163-039
343 Sansome Street, 3rd Floor
San Francisco, CA 94104
415 222-3119
415 975-6871 Fax
richard.d.levy@wellsfargo.com

May 5, 2004

Letter of Comment No: 2
File Reference: 1200-SRI
Date Received: 5/5/04

Via email

Mr. Lawrence Smith
Technical Application and Implementation Activities and EITF Chair
Setoff and Isolation
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116
lwsmith@fasb.org

Re: Request for information relating to the Isolation of Transferred Assets in Connection with its Qualifying Special-Purpose Entity Project to amend FASB Statement No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishment of Liabilities

Dear Mr. Smith:

Wells Fargo & Company (Wells Fargo) is a diversified financial services company with over \$380 billion in assets providing banking, insurance, investments, mortgage and consumer finance. We appreciate the opportunity to comment on the issues being considered by the Board in determining whether to revise U.S. accounting standards with regard to the isolation of transferred assets.

During the course of its project to amend FASB Statement No. 140 ("SFAS 140"), *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*, the Board has become aware of an issue related to the isolation of transferred assets that apparently was not explicitly considered when Statement 140 was issued—the common-law right of debtors and creditors to set off (net) amounts due to one another if one of the parties defaults, becomes insolvent, or enters into bankruptcy or receivership. Because isolation of transferred assets from the transferor is a necessary condition to report a transfer as a sale, the Board is concerned that the existence of a right of setoff may require a transferor of financial assets to retain the financial assets as borrowings on its own books rather than treating them as a sale to the transferee. The identification of setoff rights as one factor affecting isolation has led Board members to question whether there may be other unidentified legal factors or conditions that transferors and their auditors should consider in reaching conclusions about isolation of transferred assets in loan participations. Consequently, you have prepared a request for information about setoff rights as well as any other factors or conditions affecting isolation of transferred assets.

Wells Fargo is concerned about the impact revisions to loan participation accounting could have on the marketplace. Loan participations are a fundamental tool used by financial institutions to provide loans to borrowers and as an important component of ongoing credit risk management. They are a well-established practice that serves the needs of both buying and selling institutions as well as the public's interest. These arrangements were created to offer institutions the ability to meet borrowers' financing needs, maintain safe and sound loan portfolio management practices, and meet applicable legal and internal lending limits. Loan participations provide a safe and sound lending environment by reducing an institution's concentration risk and spreading credit risk among many lenders. By participating an interest in a loan, an institution can meet borrowers' financing needs without creating overexposure to a particular borrower, or the sector or geographic location of the borrower.

Credit availability in certain markets may be restricted should loan participations be effected by the rights of setoff in determining isolation of transferred assets in a loan participation. In certain markets, large institutions are not active lenders, and borrowers may look to smaller institutions for their financing needs. In other cases, borrowers with growing businesses need larger amounts of credit over time. While smaller institutions may not have the capacity to fully meet a borrower's financing requirements due to legal lending or other concentration limits, loan participations allow these institutions to provide credit they would otherwise be unable to provide.

While we are concerned about the potential effects that limiting loan participations would have on the marketplace, we also do not believe rights of setoff within loan participations have resulted in abuses in practice nor have they been designed to circumvent or inappropriately meet the sales accounting criteria specified in SFAS 140. We therefore encourage the Board to consider a scope exception from SFAS No. 140 for loan participations.

In response to your request for comments on your "White Paper", we have prepared the following responses:

Question 1: Is the information about setoff rights in this paper accurate for transferors subject to the U.S. Bankruptcy Code as well as for transferors subject to receivership by the FDIC or other regulatory agencies?

Yes, we believe the information in the paper about setoff rights is accurate for transferors subject to the U.S. Bankruptcy Code as well as for transferors subject to receivership by the FDIC or other regulatory agencies.

Question 2: How are rights of setoff currently considered in true sale analyses performed by attorneys? If they are not considered, why not?

Rights of setoff are not typically fully analyzed in true sale analyses performed by attorneys. To the extent such rights are considered, they are often assumed away (generally, the opinions assume that no set-off rights exist) and are not deemed to interfere with the isolation of

transferred assets. Attorneys, financial institutions and the markets generally view rights of setoff as independent to whether an asset has legally been sold.

Question 3: What additional information about setoff rights should the Board consider? For example,

- a. *Does a setoff right exist between the original debtor and the transferee?*
- b. *Do setoff rights exist if an affiliate of the transferor has a liability to the obligor?*

- a. No, a setoff right does not exist between the original debtor and the transferee.
- b. No, setoff rights do not exist if an affiliate of the transferor has a liability to the obligor.

Question 4: Can setoff rights be eliminated, and, if so, how can the elimination be accomplished? Are the legal aspects the same for transferors subject to the U.S. Bankruptcy Code as for transferors subject to receivership by the FDIC or other regulatory agencies? If not, what are the differences?

As a general rule, we believe that setoffs rights for loan agreements can only be eliminated through a written waiver of those rights. The legal aspects should generally be the same for transferors subject to the U.S. Bankruptcy Code as for transferors subject to receivership by the FDIC. There are very specific rules governing setoffs under the Bankruptcy Code that have not been fully integrated in receivership law. However it is expected that receiverships, when faced with the issues, will look to the rules governing bankruptcy proceedings for guidance. In addition, some offsets may be limited in receivership proceedings due to doctrines that limit a receiver's responsibility for a transferor's "side deals."

Question 5: The Board recently discussed defining isolation of financial assets to mean that the value of those assets to the transferee does not depend on the financial performance of the transferor and is not affected by bankruptcy, receivership, or changes in the creditworthiness of the transferor. Given that definition of isolation, what factors other than setoff rights are not typically considered by attorneys in rendering true sale opinions that may interfere with isolation of transferred assets from the transferor and its affiliates (except bankruptcy-remote SPEs)? Please explain why those factors are not considered.

Your proposed definition of the isolation of financial assets is much more extensive than what is currently used in practice. Generally, true sale opinions focus on the transferor and transferee's retention of the benefits and risks associated with owning the asset.

True sale opinions often assume the following facts: the parties to the transaction are independent, the terms of the transaction are made at arms-length and independent credit decisions are made by each party to the transaction. These factors, along with setoff rights, are typically assumed away by attorneys in rendering true sale opinions without any real due diligence undertaken by such attorneys. If any of these facts subsequently proves not to have been true, the transferred assets might not be sufficiently isolated.

Mr. Lawrence Smith

May 5, 2004

Page 4

We appreciate the opportunity to comment on the issues relating to isolation for loan participations. If you have any questions, please contact me at (415) 222-3119.

Sincerely,

/s/ Richard D. Levy

Richard D. Levy

Senior Vice President & Controller

CC: Donna Fisher – American Bankers Association
Gail Haas – New York Clearing House Association
Robert H. Herz, Chairman, Financial Accounting Standards Board