



Via Electronic Mail (director@fasb.org)

October 30, 2008

Technical Director
Financial Accounting Standards Board
401 Merritt 7, P. O. Box 5116
Norwalk, CT 06856-5116



LETTER OF COMMENT NO. 2

File Reference: No. 1610-100

Dear Board Members and FASB Staff:

The Mortgage Bankers Association¹ (MBA) appreciates the opportunity to comment on the Proposed FASB Statement, *Accounting for Transfers of Financial Assets, an amendment of FASB Statement No. 140* (the Proposed Statement). The Proposed Statement would eliminate the concept of a qualifying special-purpose entity (QSPE) from FAS 140 and effectively eliminate the exception from applying FASB Interpretation No. 46, *Consolidation of Variable Interest Entities* (hereby FIN 46(R)), to QSPEs. The Proposed Statement would also amend the derecognition requirements for transfers of financial assets, revise the initial measurement of beneficial interests that are received as proceeds of a sale, and expand the disclosure requirements for parties to financial instrument transfers. MBA's general comments on the Proposed Statement are described immediately below, followed by some more specific comments. MBA's responses to some of the questions for which the FASB solicited responses can be found in the appendix to this letter.

I. General MBA Comments

MBA's position on the Proposed Statement is necessarily predicated on the implications to mortgage securitizations of the guidance in the related FASB Proposed Statement, *Amendments to FASB Interpretation No. 46 (R)*² (the FIN 46 (R) Proposed Statement) which, as proposed, would require many existing and future mortgage securitization trusts (that would otherwise be exempt from consolidation as QSPEs under FAS 140) to be consolidated by a party to the securitizations. In that regard, MBA believes the

¹ The Mortgage Bankers Association (MBA) is the national association representing the real estate finance industry, an industry that employs more than 370,000 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 2,400 companies includes all elements of real estate finance: mortgage companies, mortgage brokers, commercial banks, thrifts, Wall Street conduits, life insurance companies and others in the mortgage lending field. For additional information, visit MBA's Web site: www.mortgagebankers.org.

² MBA's comments on related changes to that Interpretation are conveyed in a separate letter.

proposed elimination of the QSPE concept in combination with the proposed new consolidation guidance for variable interest entities (VIEs) could require parties to many mortgage securitizations to recognize assets they do not own and liabilities they do not owe. In those circumstances, the Proposed Statements would not meet the Board's objective of improving financial reporting.

For this reason, MBA recommends that the Board undertake a FASB study, similar to the study now being undertaken by the SEC on fair value reporting,³ on the potential implications of the Proposed Statements. MBA believes the results of a study could help the Board determine whether constituents would be best served by allocating its resources to finalizing the Proposed Statements or to advancing the Joint FASB/IAS Convergence Project.

Among other things, the study should:

- assess the costs/benefits to businesses of changing their systems and procedures to comply with potentially three different accounting models (i.e. the FAS 140 and FIN 46(R) model, the FAS 140 and FIN 46(R) Proposed Statements model, and ultimately a GAAP/IAS convergence model) for financial asset transfers within a relatively short period of time;
- determine if newly consolidated information would provide users with more useful information than would be provided through enhanced disclosures;
- consider the extent to which the Proposed Statements, as drafted, would discourage securitization transactions and thereby reduce the availability of credit and increase interest rates.

In the near term, MBA recommends that the Board issue principles-based enhancements to the disclosure requirements for financial asset transfers, consistent with the recommendations in MBA's October 9, 2008, letter to the Board on the proposed FASB Staff Position (FSP), *Disclosures about Transfers of Financial Assets and Interests in Variable Interest Entities* (the Proposed FSP).

If the Board decides instead to release the Proposed Statements in the near future, MBA strongly recommends that the Board adopt the changes recommended in this letter, and in MBA's letter on the FIN 46(R) Proposed Statement.

II. Specific MBA Comments

A. Elimination of QSPE Concept

MBA believes the prescriptive nature of the QSPE concept has fostered a "check-the-box" approach to accounting for financial asset transfers (e.g. Is this servicer activity permitted? Is this activity entirely specified in the governing documents?) which, over time, has misdirected attention from judgments about ownership of cash flows to concerns about activities designed to preserve and protect the cash flows. Consequently, MBA supports this change to FAS 140 *provided* the change is

³ See SEC press release at <http://www.sec.gov/news/press/2008/2008-242.htm>.

accompanied by significant improvements to the FIN 46(R) Proposed Statement, as will be discussed more fully in MBA's separate comment letter.

B. Legal Isolation Requirement under Paragraph 9.a.

Paragraph 9.a. of the Proposed Statement sets forth a requirement that a transfer of an individual financial asset in its entirety, a group of financial assets in their entirety, or a participating interest in an individual financial asset must be legally isolated from the transferor or any of its consolidated affiliates (with the exception of bankruptcy remote entities in multiple step transfers) to qualify for sale accounting. The requirement to consider whether the transferred asset is beyond the transferor "or any of its consolidated affiliates" is confusing because it can be interpreted to mean that a transferee (that is not a bankruptcy remote SPE) that is subject to consolidation by the transferor should cause a transfer to that transferee to fail the legal isolation requirement. Some attorneys, for example, might believe that assets that have been transferred to a transferee that is subject to consolidation are not legally isolated from the transferor.

Similarly, some accountants may believe that regardless of the attorney's decision, the fact that the transferee will be consolidated by the transferor under relevant consolidation guidance after the sale renders the sale moot because sales between affiliated entities must be eliminated in consolidation. In either case, the questions raise doubt as to the purpose of legal isolation as a requirement for sale accounting. To eliminate these questions, MBA recommends that the Board exclude the transferee itself from the legal isolation analysis under paragraph 9.a. of the Proposed Statement.

In addition, MBA would like to confirm our belief that the FAS 140 legal isolation analysis of a transfer of an asset to a transferee would precede any consolidation analysis of the transferee. Thus, a determination would have to be made that a transferred asset is beyond the reach of the transferor and its consolidated affiliates before the transferee is analyzed for consolidation by the transferor. This only makes sense because if the FIN 46(R) consolidation analysis preceded the FAS 140 sale analysis, it would not be known what assets are held by the trust, which may change the consolidation analysis under FIN 46(R).

C. Restrictions on the Transferor Maintaining Effective Control under Paragraph 9.c.

1. Consolidated Affiliates' Control over Transferred Assets

MBA recommends that the guidance in paragraph 9.c. be amended also to eliminate reference to any "consolidated affiliates included in the financial statements" of the transferor. As discussed above, the reference to "consolidated affiliates" suggests that the consolidation analysis of the transferee should precede the sale analysis, rather than vice versa. If that were the Board's intention, however, the references to "consolidated affiliates" in paragraph 9 would be pointless because any consolidated affiliates that would be subject to consolidation would already be consolidated prior to performing the legal isolation and effective control analyses of a 'transfer' to them.

To clarify that the sale analysis must precede the consolidation analysis, MBA recommends that references to "consolidated affiliates" be eliminated from 9.c., as well as 9.a.

2. Transferee's Right to Pledge or Exchange Transferred Assets

MBA also notes that most transfers to securitizations would not achieve sale accounting as a result of applying paragraph 9.c.(3), which precludes sale accounting if the transferor maintains effective control through "a restriction on the transferee's right to pledge or exchange the transferred financial asset it receives unless such constraint is designed **primarily** to provide the **transferee** with a benefit." [Emphasis added] Further, paragraph 54.A. of the Proposed Statement explains that such a restriction on a transferee "...enhances the transferee's ability to market the issuance of securities backed by the transferred financial assets to prospective beneficial interest holders."

The MBA finds it difficult to assert that the transferee gets the primary benefit of such a restriction in most securitizations, because the transferee is primarily a conduit for the transferor to maximize its proceeds on its transferred loans. In most cases, the transferor (or an agent of the transferor) is the party marketing the securities and receives an initial benefit (in the form of higher proceeds). In addition, in the case of an agency securitization, the restriction may be deemed to provide the agency with a benefit, because it is paramount to its ability to market its program. Subsequent to the transfer, the primary benefactors of the restriction are the beneficial interest holders that are promised a pass-through return of a *static* pool of loans. Consequently, the MBA believes the condition described in 9.c.(3) should be removed in its entirety, because, in the current framework, it should not be relevant whether the transferee can sell or pledge; rather, it should only matter that the transferor cannot regain control.

If the FASB does not delete 9.c.(3) in its entirety, MBA recommends that it be changed to require that the beneficial interest holders have the ability to pledge or exchange their interests similar to the concept currently in FAS 140 for QSPEs.

D. Removal of Exception for Guaranteed Mortgage Securitizations

In its deliberations, the Board decided that the reclassification of loans to securities, and the recognition of servicing rights related thereto, is inappropriate if the transfer is not accounted for as a sale, as follows:

"A.30...The Board notes that the decision to not permit a change in the measurement attribute following a guaranteed mortgage securitization is consistent with the Board's decisions to require fair value measurement for new assets and liabilities received as proceeds and to not permit remeasurement for participating interests that continue to be held by the transferor..."

MBA observes, however, that certain agency guaranteed mortgage securitizations⁴ (in which loans are 'swapped' for agency guaranteed mortgage-backed securities) would meet the sale requirements of paragraph 9 of the Proposed Statement if condition 9.c.(3) were eliminated or changed per MBA's recommendation in II.C.2. In that case, MBA

⁴ Those sponsored by the secondary market agencies Fannie Mae, Freddie Mac, and Ginnie Mae.

believes sale accounting for such swap transactions would be appropriate because (1) control of the loans has been transferred, and (2) the substantive third party guarantee has transformed the character of the loans into securities that are readily tradable in the marketplace representing an economic event that should be given accounting recognition in the transferor's financial statements.

E. Measuring Beneficial Interests at Fair Value

MBA believes that the proposed requirement to measure all assets obtained and all liabilities incurred, including servicing assets or servicing liabilities, from a sale at fair value would simplify the accounting for transfers that are sales. Current guidance is a hybrid model that requires transferors to distinguish between interests that continue to be held (which must be recognized at allocated carrying value) and interests, including servicing assets, which are proceeds from a sale (which must be measured at fair value). Consequently, MBA supports the proposed change in measurement.

F. Elimination of Footnote 10

MBA believes the focus of a transferor's disclosures when their only continuing involvement in transferred assets is servicing should be the risks associated with the servicing assets and liabilities. As that information would be disclosed under subparagraphs 17.e, f, and g, of the Proposed Statement, the additional disclosures that would be required under subparagraph 17.h.(6) regarding the status of transferred assets would greatly expand the amount of information that would be required to be disclosed for little, if any, additional benefit to users. MBA recommends therefore that the Board reinsert footnote 10 which provides an exception from the disclosure requirements in subparagraph 17.h.(6) for securitized assets that an entity continues to service but with which it has no continuing involvement other than servicing. At the least, the Board should allow servicers to disclose much less information about transferred assets for which servicers have no other continuing involvement beyond the servicing.

G. Transferor Regaining Control of Financial Assets Sold and Subsequent Consolidation of an Entity Involved in a Transfer

The Proposed Statement would require transferors to apply the relevant consolidation guidance to an entity that was involved in a transfer that was previously accounted for as a sale (see paragraph 55.A.). In contrast, the Proposed Statement would require transferors to recognize assets that it regains control of subsequent to a sale by recognizing the assets and related liabilities at fair value as if the assets had been purchased and the liabilities had been assumed at that time. MBA questions why separate models are appropriate for regaining control and for consolidating and why the Board believes it could be appropriate for income to be recognized in the first case (regaining control) but not the second (consolidation).

H. Miscellaneous

Paragraph 52 – The sentence added at the end of the paragraph reads: “Additionally, depending on the price and other terms of the call, a call that provides the transferor with the unilateral ability to cause an **SPE** to return to the transferor or otherwise dispose of

specific transferred financial assets at will, for example, in response to the transferor's decision to exit a market or a particular activity, could provide the transferor with effective control over the transferred assets." Should the reference to SPE be transferee since the statement would be applicable regardless of whether the transfer was to a SPE?

Paragraph A23 – The first sentence states that many QSPEs hold financial assets that do not appear to be passive in nature. This is troubling because it suggests that many QSPEs are not in compliance with the literature. Because the guidance is unclear, as evidenced by the many practice questions that the QSPE concept has raised, the FASB should soften this statement by indicating that *it is ambiguous whether FAS 140 contemplated such assets being passive.*

III. Conclusion

MBA believes that the Proposed Statement and the related FIN 46(R) Proposed Statement, as drafted, would require parties to many mortgage securitization transactions to recognize assets they do not own and liabilities they do not owe. As the *financial reports of those parties would not be improved*, MBA recommends that the Board undertake a FASB study on the potential benefits and costs of the Proposed Statements before proceeding further. If the Board decides to proceed to release the Proposed Statements, MBA urges that they be revised in keeping with the specific recommendations in this letter and our separate letter on the FIN 46(R) Proposed Statement.

Again, MBA appreciates the opportunity to comment on this important document. All questions regarding this letter should be directed to Jim Gross, MBA's Associate Vice President of Accounting and Tax Policy and Staff Representative to MBA's Financial Management Committee at jgross@mortgagebankers.org or (202) 557-2860.

Sincerely,



John A. Courson
Chief Operating Officer
Mortgage Bankers Association

APPENDIX

1. *Will the proposed Statement meet the project's objective to improve the relevance, representational faithfulness, and comparability of the information that a reporting entity provides in its financial statements about (a) a transfer of financial assets, (b) the effects of a transfer on its financial position, financial performance, and cash flows, and (c) a transferor's continuing involvement in transferred financial assets?*

MBA Response: MBA believes the Proposed Statement could only meet the above-mentioned objectives through changes to the guidance as recommended in this letter and in the forthcoming MBA letter on the FIN 46(R) Proposed Statement.

2. *Do you agree with the Board's decisions to eliminate the qualifying SPE concept and to require that all securitization entities be evaluated for consolidation under applicable U.S. generally accepted accounting principles? If not, why not?*

MBA Response: Yes, provided that the guidance in FIN 46(R) is amended to ensure that the economic substance of mortgage securitization transactions is accurately captured in the financial statements of parties to securitizations, as described more fully in MBA's letter on the FIN 46(R) Proposed Statement.

3. *Certain financial statement users suggested that the Board adopt a no continuing-involvement model (that is, if there is any continuing involvement, sale accounting would not be permitted). The Board decided to continue to permit derecognition of financial assets with continuing involvement as long as the conditions in paragraph 9 of Statement 140, as amended by this proposed Statement, are met, with the addition of enhanced disclosure requirements about a transferor's continuing involvement (see paragraph A28 of this proposed Statement). Do you agree with this decision? If not, why do you disagree and what approach would you recommend to meet the needs of financial statement users for additional information on transferred financial assets?*

MBA Response: A no continuing involvement model would be unjustifiable because it would produce inaccurate financial reporting results for the vast majority of transfers of assets in which transferors retain the right and obligation to service the transferred assets. The risks associated with those rights and obligations should be captured in valuations of the servicing rights, and in disclosures regarding the assumptions that went into their valuations. A requirement to require the serviced assets to be recognized on the servicers' balance sheets would severely distort their financial positions for no purpose.

4. *What costs do you expect to incur if the Board were to issue this proposed Statement in its current form as a final Statement? How could the Board further reduce the costs of applying these requirements without significantly reducing the benefits?*

MBA Response: Any cost would be too much cost unless the proposed Statement produced financial reporting results that were superior to current reporting results. MBA recommends that the FASB conduct a study to assess the costs/benefits of the proposed Statement, in combination with the related proposed FIN 46(R) proposed Statement.

5. The Board decided to establish specific conditions for reporting a transfer of a portion of a financial asset as a sale. A transfer of a portion of a financial asset as a sale is eligible for derecognition only for a pro rata portion that meets the definition of a participating interest. Do you agree with this decision? If not, why do you disagree? If you agree with the Board's decision to limit the portions of a financial asset that are eligible for derecognition, do you agree with the definition of a participating interest? If not, what alternative definition do you recommend and why?

MBA Response: It is not clear why the threshold for de-recognition is higher for a transfer of a portion of a financial asset. The MBA believes that all transfers of financial assets, including transfers of a portion of an asset, should be evaluated under the provisions of paragraph 9 of the Proposed Statement to determine whether de-recognition is appropriate. As a result, two economically identical transactions are ensured to be accounted for consistently. If the Board elects to retain the specific conditions for a transfer of a portion of a financial asset, the Board should provide a basis for such a requirement.

6. Paragraph 9(c) of Statement 140 and the related implementation guidance, as amended by this proposed Statement, require that the transferor (a) not maintain effective control over transferred financial assets to account for a transfer as a sale and (b) provide examples of effective control. The Board decided to incorporate many of the concepts from paragraph 9(b) of Statement 140 into paragraph 9(c), which results in the creation of the additional examples that are included in paragraphs 9(c)(3) and 9(c)(4). Do you believe that paragraph 9(c) of Statement 140 and the related implementation guidance, as amended by this proposed Statement, clearly explain how to determine if the transferor maintains effective control? If not, what additional guidance or examples are necessary? Do you believe that paragraph 9(c), as amended by this proposed Statement, is operational in its entirety in its current form? If not, what changes are necessary? Do you believe these additional examples of effective control in paragraphs 9(c)(3) and 9(c)(4) are operational in their current form? If not, what changes are necessary?

MBA Response: As explained in this letter, MBA believes the condition described in 9.c.(3) should be eliminated in its entirety because transferees that are securitization trusts are not free to pledge or exchange transferred assets and nor do they benefit generally from such restrictions. This condition would therefore deny sale accounting to many transactions involving assets transferred to securitization trusts. If the FASB does not delete 9.c.(3) in its entirety, MBA recommends that it be changed to require that the beneficial interest holders have the ability to pledge or exchange its securities similar to the concept currently in FAS 140 for QSPEs.

7. Certain financial statement users strongly recommended that the Board provide disclosure principles and require certain specific disclosures for both transferred financial assets treated as sales and those that are treated as secured borrowings. Do you agree that additional disclosures about transferred financial assets are necessary and operational? If not, what changes would you make to the requirements? Do you believe that the revisions to the disclosure requirements are sufficient? If not, what additional disclosures do you believe are necessary?

MBA Response: MBA believes the Board should issue principles-based enhancements to the disclosure requirements for financial asset transfers, consistent with the recommendations in MBA's October 9, 2008, letter to the Board on the proposed FASB Staff Position (FSP), *Disclosures about Transfers of Financial Assets and Interests in Variable Interest Entities* (the proposed FSP). In addition, as explained in this letter, MBA believes the decision to delete footnote 10 of FAS 140 is inappropriate because it will impose a significant burden on servicers to disclose potentially voluminous amounts of information about transferred assets for little additional benefits to readers of their financial statements. In fact, MBA believes the additional disclosures could so overwhelm readers that they would likely not get as much benefit from the more relevant disclosures.

8. Appendix C includes significant amendments, primarily as a result of this proposed Statement, to related literature including (a) the FASB Special Report, A Guide to Implementation of Statement 140 on Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities, (b) certain Emerging Issues Task Force (EITF) Issues and Topics, and (c) certain AICPA Audit and Accounting Guides. Do you agree that the related literature, as amended, is consistent with the proposed amendments to Statement 140? If not, why do you disagree and what changes would you make?

MBA Response: MBA agrees.

9. Due to differences in financial statement user needs and cost-benefit considerations, should any differences exist for recognition, measurement, disclosure, transition, or effective date for private companies? If yes, please articulate what differences should exist and the reasons for those differences.

MBA Response: MBA suggests that this question be addressed within the study MBA has recommended that the FASB conduct on the probable costs/benefits of the guidance in the Proposed Statements.