From: Marc Porter
To: Director - FASB
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FASB Technical Director:

Regarding the Exposure Draft on Accounting for Financial Instruments and Revisions to the Accounting for Derivative Instruments and Hedging Activities, my comment responses to the Board's "Questions for All Respondents" and "Questions for Preparers" (excluding those questions pertaining to core deposits and hedging activities) are set forth below.

C1 I support the dissenting view that fair value accounting should not apply to "plain-vanilla" loans held for collection. Held for collection loans are not the same as securitized financial assets where market-based values may be readily available. Since no markets or other objective measurement of fair value exist for such loans, fair value would be judged entirely on subjective inputs. Amortized cost (including imputation of interest at origination, when appropriate, and recognition of impairment thereafter) informs users about expected cash flows and approximates fair value for such loans. Recording the estimated effect of ebb and flow interest rates on individualized loans in comprehensive income is impractical and unwarranted. Entities, particularly non-financial commercial entities, should not be required to perform the fair value accounting exercise illustrated in Example 20 (Measuring and Recognizing Credit Impairment and Interest Income on Individual Debt Instruments) for "plain-vanilla" loans. Held for collection loans should be excluded from the proposed guidance and measured at amortized cost, like participant loans in employee benefit plan financial statements (per EITF Issue 10-C).

C4 Why exclude equity investments from fair value reporting when an investor has "significant influence" but not enough ownership or power to consolidate as a parent or VIE primary beneficiary? As a general rule, I believe equity investments should either be consolidated or reported at fair value; with only limited exceptions. An example of an appropriate exception might be for commercial joint ventures.

C8 I agree that a financial asset should initially be measured at fair value if subsequent changes in fair value will be recognized in net income. A financial asset to be measured at amortized cost should initially be measured at the transaction price.

C9 I do not support recognizing fair value changes in comprehensive income.

C10 I don't believe a single initial measurement principle is appropriate. The initial measurement of assets subject to fair value accounting should be measured at fair value and assets subject to amortized cost accounting should be recorded at the transaction price.

C11 Transaction fees and costs should be consistently expensed immediately for all (both equity and debt) financial instruments.

C12 The determination as to whether a difference between a transaction price and fair value is significant will require subjective judgment. Some quantitative guidance would be helpful.

C13 I disagree that fair value information should be provided in comprehensive income for financial instruments. Fair value pricing of most loans held for collection would involve incredible subjectivity as no observable markets exist for such loans. Amortized costs represent contracted cash flows and impairments of loans. Unlike traded securitized debt instruments, loans held for collection are not held for capital appreciation (lenders either collect the contracted cash flows or they suffer an impairment loss). I believe loans held for collection should be reported at amortized cost without comprehensive income adjustments.

C14 I believe that interest income, credit impairments/reversals and realized gains of all financial debt instruments should be recognized in net income.

C15 All financial liabilities on the balance sheet should simply reflect the entity's current actual obligations as of each reporting date.

C16 I agree that once an entity makes a measurement decision (fair value or amortized cost), it should be prohibited from subsequently changing that decision.

C18 All financial liabilities on the balance sheet should reflect the entity's current actual obligations of as of each reporting date.

C19 I agree with the proposed guidance for investments that can be redeemed only for a specified amount.

C20 Entities should evaluate deferred tax assets on an aggregate basis.

C21 Convertible debt should remain classified as a liability in its entirety, unless converted, and should not be subject to fair value adjustments (i.e., the recorded liability should reflect the entity's current actual obligation).

C28 For the reasons stated previously herein, I don't believe estimating the fair value of unregistered or non-securitized loans in comprehensive income is practical. Held for collection loans should be recorded at amortized cost.

C29 Liabilities on the balance sheet should only utilize fair value to the extent necessary to measure the current actual obligations of an entity. Such measurement is operational.

C30 The proposed criterion for measuring a financial liability at amortized cost is operational.

C32-34 I don't believe a change in an entity's credit standing should be recorded in the financial statements. All financial liabilities on the balance sheet should reflect the current actual amounts of an entity's obligations as of each reporting date. A disclosure that an entity's credit standing has changed would be informative to users but such change should not effect the entity's reported obligations on its balance sheet.

C37 I believe the objective of the credit impairment model is clearly stated.

C38 I agree that credit impairments (and recoveries) should immediately be recognized in net income.

C39 I agree that credit impairment should not result from changes in foreign exchange rates.

C40 The conceptual guidance for development of pooled assets loss rates is sufficient.

C41 I disagree that if an entity subsequently expects to collect more cash flows than originally expected, such gain should be deferred. If an entity expects to collect less, a credit loss should be reported in net income. Likewise, if an entity expects to collect more, a recovery or gain should also be currently reported in net income.

C42 If an individually evaluated financial asset has no indicators of being impaired, no impairment exists and no credit impairment should be recorded. While historical loss rates are appropriate for evaluating a pool of loans, application of a historical loss rate to an individually evaluated loan would not be appropriate. The impairment of an individual loan should be solely determined based on the expected cash flows of that particular loan; otherwise an entity would effectively be testing such loans on a collective basis.

C46 I agree that an entity should assume that economic conditions existing at the reporting date remain unchanged for purposes of evaluating impairment. Forecasting future events and economic conditions with consistent accuracy is impossible (and the opinions of those who do make forecasts vary greatly).

C47 I believe many entities already develop and apply custom loss rates to pools of loans based on their historical experiences. Therefore, I this wouldn't represent a significant change in accounting practices.

C48-49 If a debtor is unable to pay any portion of contractually due amounts (whether interest or principal), an impairment exists in my opinion. I believe an entity should continue to accrue contractually due interest on an impaired loan but with an offsetting entry to an allowance for credit loss (to the extent accrued interest is deemed uncollectible).

C50 I believe that interest income should be accrued and reported in net income for all financial assets.

C51 Example 20, "Measuring and Recognizing Credit Impairment and Interest Income on Individual Debt Instruments", doesn't illustrate how the fair value of the hypothetical trade note was derived. The true market sale price for a unique trade note held by a non-financial commercial entity would likely be derived from a factoring without recourse. Example 20 clearly illustrates how difficult it would be for entities (particularly for non-financial commercial entities) to record fair market accounting in comprehensive income.

C65 My comments pertaining to the disclosure requirements (referenced to paragraphs of the Update):

Paragraph 98 – I don't agree that reported financial liabilities should be adjusted to reflect changes in the entity's own credit standing. Therefore, I consider such disclosures unnecessary.

Paragraphs 99-103 – I don't agree that changes in fair value should be recognized in other comprehensive income. Therefore, I consider such disclosures unnecessary.

Paragraph 104 – I agree with the proposed disclosures for credit losses.

Paragraph 105 – I agree with the proposed disclosures of assets individually evaluated for impairment, except for the requirement to disclose fair value for a held for collection loan.

C68 I agree that a cumulative-effect adjustment transition would be appropriate.

C69-71 The effective date of the proposed guidance is irrelevant. The requirement to identify market values of unique loans for which no markets exist is idealistic and nonoperational. Delayed implementation will not change that.

I reviewed the first 160 comments submitted on this Exposure Draft and found that substantially all of the comments reflected opposition to fair value accounting for bank loans. Please keep in mind that the guidance of this proposed Update is not limited to banks, it impacts non-financial commercial entities as well.

Respectfully submitted,

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