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237 Park Avenue, Floor 9
New York, N.Y. 10017

September 28, 2010

Mr. Russell Golden
Technical Director
Financial Accounting Standards Board

(Via electronic mail)

Re: Proposed Accounting Standards Update *Accounting for Financial Instruments and Revisions to the Accounting for Derivative Instruments and Hedging Activities*.

Dear Mr. Golden:

Thank you for the opportunity to comment on your Proposed Accounting Standards Update *Accounting for Financial Instruments and Revisions to the Accounting for Derivative Instruments and Hedging Activities*.

I take a particular interest in the changes you have proposed. I run a hedge fund that invests *solely* in banks and financial services companies, so your proposals figure to have a direct effect on the returns I generate for my limited partners. Prior to starting my fund in 2000, meanwhile, I was the top-rated bank analyst on Wall Street for ten years, for Smith Barney, PaineWebber, and Donaldson, Lufkin, & Jenrette. I am therefore precisely the sort of investor your proposal is supposed to help.

And yet, respectfully, I oppose your proposals vigorously. They will make bank accounting less transparent rather than more so, and thus will make it harder for me to do my job. In particular, your proposals will have the effect of emphasizing metrics I don't care about as an analyst (random near-term price movements of fixed-income instruments) at the expense of those I do (loan delinquencies, say, and loss provisions). What's more, they'll exacerbate future credit cycles rather than diminish them. Nor, for that matter, am I even convinced that market prices always provide an appropriate basis for determining an asset's true value in the first place. I urge you in the strongest possible terms to not approve the standards as currently proposed

As a bank analyst, I simply don't care about the "market value" of an illiquid asset sitting on a bank's balance sheet, if the bank intends to hold that asset to maturity. The information isn't merely of little value to me. It's of *no* value. All sorts of factors go into determining the price of a fixed-income instrument at any given moment, from the level of interest rates, to the width of credit spreads, to the number of available buyers and sellers. These numbers are inherently volatile and, as I say, irrelevant to my work as an analyst trying to understand an individual company's balance sheet and income statement. Alternatively, I *do* want to know about changes in the value of a given asset on

Mr. Russell Golden

September 28, 2010

a bank's balance sheet—if the change occurs as a result of possible credit impairment. Under the current reporting regime, I get information related to credit quality, via disclosures regarding (among other things) reserve additions, delinquencies, and asset writedowns. There are certainly ways to improve such disclosures, but adding a mark-to-market overlay isn't one of them.

From a practical standpoint, meanwhile, the effect of your proposals could be disastrous. If the proposals are put into effect, banks will surely be more reluctant than they are now to write long-term loans, and will surely demand higher interest rates for any such loans they do write. Credit creation will thus be stunted and economic growth will slow. What's more (as we've all already experienced, often to great distress) the pro-cyclical effects of the FASB's existing policies on loss reserving and marking securities portfolios to market are clear and undeniable. During the credit crunch of 2008-2009, banks were forced to take huge mark-to-market-related losses as the fixed-income markets froze and investor fears caused the value of fixed-income instruments to plummet. Those losses further undermined investors' already-shaky confidence in the system, which in turn led to additional mark-to-market losses. The cycle fed on itself, to devastating results. Should banks also be forced to mark their loan portfolios to market, as well, that pro-cyclicality will only become more extreme.

In the fullness of time, furthermore, we now know that the collapse in prices during the credit crunch *was* largely irrational and the attendant charges to capital pointless. There's no shortage of examples to illustrate this, but one that stands out is State Street's experience after it reported its earnings for the fourth quarter of 2008. In the report, the company disclosed additional losses of \$3 billion in its fixed income portfolio. The losses arose entirely from the credit panic, not from credit issues in the portfolio itself. Still, speculation immediately arose that the company would have to do a big capital raise to shore up its financial ratios, which in turn put enormous pressure on its stock. The more the stock fell, the larger the estimate became of how many new shares the company would have to issue, which in turn pressured the stock even further. Result: thanks to the bogus "loss" State Street had to report, its stock dropped by 59% *in a single session*. All because of a misguided accounting rule. Since then, we now know that the company's fixed-income portfolio encountered no undue credit problems. As the credit markets have recovered, the company has reversed that entire fourth-quarter charge. What, exactly, is the point?

Finally, I am at a loss to understand the FASB's seeming fetishization of market prices as an all-season, unerring indicator of an asset's inherent value. One of the main lessons of the credit crunch that we've all just endured is that market prices are *not* always reliable indicators of an asset's true value. Sometimes they're not even close. Forcing banks to tie their financial statements to such prices makes no sense. The reason I became a professional investor in the first place is that I'm skeptical enough of the ability of even liquid, supposedly efficient markets to reliably reflect the true value of a given asset. The past ten years worth of bubbles and busts in the equity markets, supposedly the most liquid and efficient markets of all, ought to provide more than enough evidence to even the most hardened efficient-market-hypothesis believer that perhaps market prices aren't

Mr. Russell Golden

September 28, 2010

as all-informative as they're cracked up to be. And now investors are supposed to take seriously financial statements based on the "market values" of assets for which there is no active market? I can't see why they should.

My understanding is that the FASB moved toward its mark-to-market approach in order to provide a systematic way to establish the value of assets, and in turn narrow management's ability to unilaterally assign (and possibly fudge) them. That's a worthwhile goal. But now that we've seen the devastating effect mark-to-market accounting can have in the real world, it's clear the tradeoff isn't worth it. By all means devise standards that impede management's ability to publish misleading results. I'll be all for them. But if the choice is a set of accounting rules that, when properly applied, can help push the financial system to the brink of collapse, or having to put up with some occasional accounting shenanigans, I, for one, would rather put up with the shenanigans.

Again, with respect, do not approve these standards.

Sincerely,

/s/ Thomas K. Brown
CEO and Portfolio Manager