1810-100 Comment Letter No. 1594



Headquarters

tel 310.966.1444 B. Riley & Co., LLC fax 310.966.1448 B. Riley & Co., LLC 11100 Santa Monica Blvd. Suite 800 Los Angeles, CA 90025 www.brilevco.com

September 30, 2010

Mr. Russell G. Gorden Technical Director Financial Accounting Standards Board 401 Merritt 7 P.O. Box 5166 Norwalk, CT 06856-5116

File Reference No. 1810-100 – Accounting for Financial Instruments and Revisions to the Accounting for Derivative Instruments and Hedging Activities

Dear Mr. Golden:

I am a Senior Equity Analyst with B. Riley & Co. LLC is a FINRA member firm providing research and trading ideas to institutional clients and high net worth individuals and investment banking services to a wide range of private and public companies. I have been involved in the financial markets for 26 years and have spent the last seven researching financial institutions. I currently publish research on 19 of the 38 banks and thrifts the firm covers. As active users of financial statements, we appreciate the opportunity to express the following concerns regarding the Financial Accounting Standards Board's Exposure Draft: Accounting for Financial Instruments and Revisions to the Accounting for Derivative Instruments and Hedging Activities.

- We disagree with the concept of expanding fair value accounting to loans held for investment. We fail to see how the marking of assets that banks intend to hold until maturity would benefit users of financial statements. We are also concerned about the accuracy of fair value information given that loans are generally level three assets with no active market. As a result, the valuation process would be highly subjective and institutions would like report very different fair value estimates for similar loans, thereby inhibiting comparability.
- For similar reasons, we are opposed to fair value accounting for deposits and debt.
- We believe that fair value accounting would understate liabilities in unfavorable credit cycles.
 In such environments, credit spreads on the debt of financial institutions would widen and the
 present discounted value of these liabilities would decline. We believe that amortized cost is
 more reflective of the true underlying liability.
- Fair value accounting would substantially increase the operating costs of financial institutions. Banks would have to overhaul their accounting systems to maintain fair value and amortized cost data. In addition, they would likely be forced to engage outside consultants to determine fair value marks and the associated accounting would have to be audited. With fair value accounting providing little benefit to users of financial statements, while adding costs at a time when bank profits are already being constrained by mounting regulatory burdens, we believe that its implementation is unwarranted from a cost-benefit perspective.



Headquarters

tel 310.966.1444 B. Riley & Co., LLC fax 310.966.1448 11100 Santa Monica Blvd. Suite 800 Los Angeles, CA 90025 www.brileyco.com

- Deriving fair value estimates is a time consuming process. Consequently, fair value accounting
 could impede the ability of public companies to provide financial information to investors in a
 timely manner.
- Fluctuations in fair value marks would increase the volatility of reported capital positions and tangible book values per share of financial institutions. Given that investors are generally averse to volatility, fair value accounting would tend to increase the cost of capital for the sector.
- Recognizing the need to limit such volatility, banks would be incentivized to extend only
 variable rate or short duration loans. Given that some borrowers may be reluctant to absorb
 interest rate risk, fair value accounting could negatively impact consumers, businesses and the
 economy.
- The exposure draft proposes that interest income on loans should be determined by applying the effective interest rate to the amortized cost net of any allowance for credit losses. This would tend to distort the net interest margin, a key metric for the sector, and reduce its usefulness to users of financial statements who, in our opinion, prefer to evaluate the net interest margin and credit risk separately
- Impairment measurement under the exposure draft would be based on "all available information relating to past events and existing conditions". As a result, the proposal does not provide flexibility to allow for the impact of economic cycles. The preponderance of bad loans are made in good times given that loan demand is slack and underwriting standards are tighter during economic downturns. We believe that disallowing financial institutions the flexibility to establish appropriate reserves during favorable economic cycles is in violation of the matching principle. It appears counterintuitive that banks are effectively required to under-reserve in strong environments and then be forced to catch-up in bad times when capital is scarce.

Again, we thank you for the opportunity to comment on the exposure draft.

Regards,

Andrew W. Stapp Senior Equity Analyst

andrew W Steps

Financial Institutions Group