

May 31, 2013

Financial Accounting Standards Board

Dear Members of the Financial Accounting Standards Board,

The Proposed Accounting Standards Update regarding Proposed Accounting Standards Update, Financial Instruments—Credit Losses (Subtopic 825-15) (herein after “Update”) as proposed will have a disproportionate and highly adverse effect on community banks.

The definition of community banks for purposes of this comment letter are banks localized in a specific geographical area with less than \$1 billion in total assets. Community banks unlike its larger counterparts, the regional and money center banks do not have the size to make the law of large numbers to average out fluctuations in income and losses that the Update proposes to measure with respect to financial instruments.

As you may know the basic concept of banking is that depositors with demand deposits and other deposits will generally leave their money in the bank for a term longer than the term of the deposit. This allows the bank to lend money for a much longer average term than the average term of the demand deposit. The Update runs against this basic concept as it anticipates near real-time reporting of credit losses which fluctuate during the long period of the average credit. In other words, the credit is not due until its due date and not on any of the dates in between, and while the credit may be impaired before the due date there is no realization of loss until it can be “accurately” measured. The Update is a method to try to “precisely” measure and recognize credit impairment, but that is not the same as to “accurately” measure and recognize impairment.

For example, if a borrower with a home loan were to lose his or her job, and the CCR’s for the borrower’s home provided that there could be no letting of homes in the borrower’s tract, then the lending bank would likely have to record an immediate loss on the loan until he or she was employed again in a job that covered the loan payments. Does this really make any sense, for the bank to have such volatility in its income measurement and reporting. While the law of large numbers will even this out for large banks, the community bank does not have this luxury because it is subject to geographically localized events.

Keep in mind that every industry has in its chart of accounts, accounts, including estimated loan losses that can not be “accurately” measured. GAAP has thorough carefully thought out accounting standards endeavored to smooth out the volatility that would be detrimental to reporting wildly fluctuating income results.

Another important concept of the community bank is character lending based on past relationships. If the objectivity intended in the Update were used to measure the impairment of such loans which may

be made without collateral, these loans may require immediate charge off, which totally disregards the importance of what is intrinsic to every community.

Lastly, and possibly most important is that the Update unduly empowers the federal and state banking regulatory agencies to enforce the Prompt Corrective Action laws and regulations against community banks. While community banks were equally guilty in being too slow to recognize credit losses in the recent financial meltdown, there is no valid reason for community banks to be singled out for punishment by empowering these regulatory agencies to shut them down on a faster track.

Sincerely,

Thomas Kwan  
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