



May 30, 2013

Technical Director  
File Reference No. 2012-260  
Financial Accounting Standards Board (FASB)  
401 Merritt 7  
Post Office Box 5116  
Norwalk, CT 06856-5116

RE: Proposed Accounting Standards Update  
Financial Instruments – Credit Losses (Subtopic 825-15)

Dear Director,

I am very concerned about the impact FASB's credit losses proposal will have on credit unions. It is critical to this process that FASB understand the unique structure of credit unions. Credit unions are member-owned, not-for-profit financial cooperatives that operate for the purpose of promoting thrift, providing credit, and providing other financial services at competitive rates. In addition, credit unions are unique from other financial institutions in that their enabling statute, the Federal Credit Union Act, limits net worth to retained earnings only. Further, this statutory limitation restricts the ability of the National Credit Union Administration (NCUA) – the prudential regulator of federally chartered credit unions and insurer of most state and all federally chartered credit unions – to adjust its regulations in response to changes in accounting standards, as is possible for other federal financial regulators. Consequently, the proposed one-time adjustment to the Allowance for Loan and Lease Losses account (ALLL) to bring that account into compliance with this proposal will have an immediate detrimental impact on the credit union industry as millions upon millions of dollars will be withdrawn from capital with no possibility of near term replacement. This will certainly impair the industry's ability to meet the needs of its members. I foresee it as having a negative impact on products viewed as staples among consumer credit such as unsecured credit cards and personal lines of credit, unsecured business lines of credit, and small home improvement loans. It will undoubtedly result in increased costs to the borrower as some portion of this additional expense will have to be passed down to the borrower in the form of higher interest rates and fees.

The proposal would require credit unions to provide information that is not relevant to the primary users of credit union financial statements: the NCUA and state credit union regulators. Consequently, the users of our financial statement



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have different incentives and purposes in reviewing our financial statements as compared to those users of a bank, including either public or private entities.

FASB's stated intent in issuing the proposed changes is that the current impairment methodology does not allow for the timely recognition of credit losses. I strongly disagree with this. I also do not believe the proposed approach would have been effective in preventing the extent of credit losses experienced over the past several years. This is because I do not believe it is possible to accurately predict the extent and timing of the credit events that led to such widespread losses within the financial sector. This opinion is further supported by the fact that not even the regulators exhibited the foresight to require changes necessary to protect the financial industry as they could not accurately predict this downturn either. I am of the opinion that the increased use of subjective methods for estimating future credit losses and the de-emphasis of the use of the historical principal will serve to skew critical data, thereby reducing the effectiveness of financial statements going forward.

While I oppose the majority of the proposal, I do support the proposed changes regarding mergers and business combinations. Specifically, I agree with the proposed treatment that would bring the ALLL account of the targeted entity over to the continuing entity in a merger situation.

It is my understanding that the proposal would require credit unions to recognize on the balance sheet current loss expectations in the ALLL. Thus, as mentioned previously, the proposed change would cause an immediate and drastic increase to the ALLL of credit unions that have financial assets and liabilities in the broad scope of the proposal. It is anticipated that this increase will double or even triple current ALLLs, resulting in an immediate and sizeable reduction in the retained earnings of the credit union industry. Further, the anticipated decrease in future earnings could lead to a reduced capital ratio, which could then trigger prompt corrective action (PCA) implications for numerous credit unions that currently do not have PCA concerns. This problem is further exacerbated by the timing of this proposal, following on the heels of the Great Recession.

One result of the proposal that is certain is that it will require credit unions to expend extensive financial and technical resources to even begin to comply with the changes proposed. In other words, a whole new industry will have to be developed to ensure compliance with this proposal. The costs of such expenditures will be borne by credit union member-owners. The proposal attempts to address the problems of a few financial institutions – albeit some



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extremely large financial institutions – that misled or simply did not understand the credit quality of complex CMOs and MBSs by proposing far-reaching changes that will severely impact all financial institutions, including credit unions that did not cause the financial crisis. The credit union industry is clearly not your target audience, yet we will be forced to pay for the sins of others.

As a result of this process, it is very likely that the proposed changes will ultimately result in the consolidation of credit unions that are unable to comply with these changes. Such a result would not only affect the members of those credit unions and the communities which they serve, but would affect the larger financial services marketplace by reducing consumer financial options.

The proposed CECL model effectively requires entities to predict or forecast the extent and timing of future losses. Predicting such losses with any degree of accuracy will be extremely challenging (if not impossible), even for an entity with adequate data sets and modeling capability. Further, attempting to predict credit losses for the life of the loan will inherently be affected by the subjectivity of, and assumptions made by, the reporting entity. Obviously the credit union industry would never knowingly make loans to borrowers who do not exhibit an ability to repay the debt. It is recognized that losses obviously occur after the loan is made as circumstances change, the economy changes, and borrowers face life changing events such as divorce, death etc. that affect their ability to repay the loan. However, to be able to accurately predict these occurrences is simply not a reasonable expectation by FASB.

In regard to the data necessary to conduct such modeling, even the largest financial institutions have indicated that they do not have adequate information on this data and that it will take years (some estimate 8a four to five year timeframe) to develop or obtain. Further, since smaller financial institutions will require even more time to obtain such data, these institutions will default to relying on their larger counterparts' peer information, which will have a lag of at least six to nine months. In addition, even when smaller institutions obtain adequate data, it will take another three to four years for these institutions to become comfortable with the required modeling.

One of the most surprising, and disturbing, results of the proposed CECL model is its inconsistency with the accounting principle of matching, which states that expenses should be recorded in the same period as the revenues that relate to those expenses. The proposal is inconsistent since it requires expected future loan losses to be recorded immediately while the related income will be recorded over a number of years. In addition to its impact on the reporting



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entity, this inconsistently will likely cause challenges/trepidation within the audit community.

In closing, I believe it would be inappropriate to apply the proposed changes to credit unions, based on their unique structure as private, not-for-profit, cooperatively owned, financial institutions. As noted previously, the primary user of the credit union's financial statements is its regulator, which is not likely to benefit from the proposed changes since it already has a well-developed understanding of the operations of the credit unions it regulates. I encourage FASB to work closely with the NCUA in light of the unique structure of the credit union industry.

Should FASB elect to proceed with this proposal, I ask FASB to consider an impairment approach that uses a 12 month forecast period. I would also ask FASB to define "lifetime expected losses", a term used throughout the proposal but which is never explicitly defined. Should FASB move forward with this proposal or a variation thereof, it is crucial that there be an adequate phase-in/transition period for credit unions. Further, I urge FASB to delay the effective date of a final credit losses standard by at least three years for non-public reporting entities, including credit unions.

I appreciate the opportunity FASB has given to provide public comment on this proposal. It is not often that the banking industry and credit union industry unite in their agreement on a topic. However, this is one of those occasions. I would strongly encourage FASB to consider the message being sent with regard to this proposal.

Sincerely,

A handwritten signature in black ink that reads "Dennis G. Adams". The signature is written in a cursive, flowing style.

Dennis G. Adams  
Vice President/CFO

/dga