May 3, 2021

Mr. Richard R. Jones
Chairman
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116

Via email: director@fasb.org

RE: ESG Issues and Related Agenda Request

Dear Chairman Jones:

The American Bankers Association\(^1\) (ABA) appreciates the FASB Staff addressing Environmental, Social, and Governance (ESG) Issues through its Educational Paper issue in March 2021.\(^2\) We are disappointed, however, that the Paper omitted instances when accounting standards impact “financial inclusion” activities in the banking industry. Financial inclusion is a “social capital” issue that pertains to expanding the access and affordability of financial products and services, particularly to those of lower and moderate income levels. While the Educational Paper notes that “Financial accounting standards are not intended to drive behavior in any way…,” below are three instances in which they do. In the first two instances, due to regulatory expectations to minimize volatility in reported capital, FASB accounting standards updates (ASUs) issued in 2016 discourage financial inclusion activities. In the third instance, however, a 2014 FASB ASU encouraged financial inclusion activities:

- Loan performance of borrowers with lower or moderate incomes exhibit more volatility throughout an economic cycle compared to other borrowers. The CECL accounting standard (ASU 2016-13), which requires lifetime loss provision expenses at the time of origination without recognition of the corresponding interest income, thus discourages lending to these individuals. This problem existed prior to the adoption of CECL. CECL, however, magnifies the problem.

\(^1\) The American Bankers Association is the voice of the nation’s $21.9 trillion banking industry, which is composed of small, regional, and large banks that together employ more than 2 million people, safeguard more than $17.8 trillion in deposits, and extend $11 trillion in loans.

• Community development investment funds invest in securities whose proceeds are designed to positively impact community development. Investments in community development investment funds – even those that invest in debt instruments – are marked to fair value with the changes in fair value being recognized in net income. ASU 2016-01 (Recognition and Measurement of Financial Assets and Financial Liabilities) eliminated the previous “Available for Sale” classification, which allowed entities with long-term investments to reduce volatility in their earnings (and, thus, regulatory capital). Volatility in the fair value of these funds, often caused by changes in market interest rates and not by repayment performance, discourages investment in the related communities by regulated entities.

• Low-income communities suffer from a lack of capital, which makes progress and community development difficult to achieve. In response, various programs have been implemented to address these communities, some granting tax credits for specific projects. Prior to 2014, accounting for most investments in tax credits related to affordable housing projects distorted key performance metrics. This discouraged such investments because investing entities were made to appear less profitable (through pre-tax income) with greater overhead (through efficiency metrics). ASU 2014-01 (Accounting for Investments in Qualified Affordable Housing Projects) greatly mitigated this confusion by adjusting the criteria to qualify for accounting that effectively streamlines both the recognition and presentation of such activities within the income statement.

By effectively aligning the accounting and presentation with the economics of the investments, ASU 2014-01 was a definite improvement for all stakeholders: bankers, investors, and especially the people served through such housing projects. With this in mind, ABA is submitting this agenda request for the Board to add a new project to its technical agenda to consider expanding the qualifications for this accounting treatment to tax credit investments other than qualified affordable housing project investments. During the 2014-01 deliberations, FASB and its staff considered applying the principles in 2014-01 to other tax credit investments, but the scope was left narrow for expediency purposes. ABA believes that now is an appropriate time to expand that scope and we specifically believe that terms of “New Markets Tax Credits” projects can immediately qualify under the 2014-01 principles if permitted.

Attached is our Agenda Request for this project. If you need additional information or have questions, please contact me (jstein@aba.com; 202-663-5318).

Sincerely,

Joshua Stein
AGENDA REQUEST: EXPANSION OF THE PRINCIPLES OF 2014-01 TO OTHER TAX CREDIT INVESTMENTS

Background

Banking institutions are significant participants in tax credit investment programs. Bankers generally believe such programs encourage capital investments in disadvantaged communities. Accounting for Low Income Housing Tax Credits (LIHTC) was amended in Accounting Standards Update 2014-01: Investments—Equity Method and Joint Ventures (Topic 323) Accounting for Investments in Qualified Affordable Housing Projects (“2014-01”) to better align it with how economic decisions in such investments are made.3 With this in mind, other investment programs with financial inclusion objectives exist, including the New Markets Tax Credit Program (NMTC). These programs are often similar in structure and subject to similarly available tax advantages as LIHTC. Further, each has substantially similar economics and is subject to similar decision-making processes. However, these program investments are subject to different accounting standards.

ABA believes accounting for tax credit investments should be consistently applied, be driven by a principle-based approach and not be based on the specific type of tax credit program. The current inconsistency in accounting for tax credit investments negatively impact users of financial statements, preparers, and ultimately those who are served by the underlying projects.

Current accounting for participants in non-LIHTC tax credit investments requires the use of these tax credits to be presented as an expense in pre-tax income line while presenting the corresponding economic benefit as a reduction to income tax expense. This distorts the pre-tax income and other key performance metrics of the tax credit investor and, as a result, further effort must be made by them to explain these accounting complexities to the users of their financial statements. In addition, the timing of the recognition of this expense and the associated tax credit benefit are often misaligned, exacerbating the distortion.

Request: Consider Expanding the Scope of ASC 323-740

ABA recommends expanding the scope of ASC 323-740 to include all investments that are made for the primary purpose of receiving tax credits and other tax benefits based on satisfying the conditions in ASC-740-25-1. In a letter to FASB dated February 2, 2021, PNC Financial Services Group, Inc. (“PNC”) made a request to simplify the accounting specifically for NMTC investments. In the request, PNC details how current NMTC investments often otherwise meet the conditions in ASC323-740-25-1 and ABA concurs with PNC’s analysis and conclusion that expanding the scope of ASC 323-740 would be an improvement for financial statement users. ABA also refers to the basis for conclusions in 2014-01 where the need for exploring adding other tax credit investments was recognized and recommended by FASB’s Emerging Issues Task Force, as noted in ASU 2014-01 paragraph BC11:

3 ASU 2014-01 is documented within the Accounting Standards Codification within Topic 323-740.
“The Task Force also recommended that the Board consider adding a separate project to the Task Force’s agenda to assess the applicability of the guidance in this Update to other types of tax credit investments.”

ABA believes expanding the scope to be an accounting improvement for all stakeholders and requests the Board add a project to address the accounting for other tax credit investments.