

November 14, 2008

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



LETTER OF COMMENT NO. 31

File Reference No. 1610-100

Dear Mr. Golden:

Discover Financial Services ("Discover") appreciates the opportunity to comment on the Exposure Draft dated September 15, 2008, of the proposed amendments to FASB Statement No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishment of Liabilities ("Statement 140"). Discover is one of the six largest U.S. credit card issuers as measured by receivables outstanding as of December 31, 2007. As of August 31, 2008, Discover had approximately \$48 billion in total credit card receivables outstanding, including \$27 billion in securitized receivables that we had originated and continue to service. Discover conducts its credit card issuing business through its subsidiary, Discover Bank, a Delaware state-chartered bank.

Discover has been active in credit card securitization since 1990. Since 1993, when we began using a master trust structure, we have securitized approximately \$82 billion in credit card receivables through more than 100 separate transactions. Our structure was expanded to include a note issuance trust in 2007. Our securitizations involve transfers of all of our right, title and interest in specified credit card receivables to a credit card master trust, and the transfer of a collateral certificate representing an interest in that master trust to a note issuance trust. Today both trusts are recognized as qualifying special purpose entities ("QSPEs"). These trusts are variable interest entities ("VIEs") that would likely have to be consolidated by Discover Bank under the proposed amendments.

We appreciate the Board's ongoing efforts to reconsider the appropriate accounting for transfers of financial assets, which have culminated with this Exposure Draft and which led to certain of the proposed amendments to Interpretation 46R, on which we have provided comments in a separate letter. We support the Board's stated objectives for this project, but we believe that certain clarifications are needed to ensure proper application of the amended sale accounting analysis that the Board has proposed.

Our specific comments on the Exposure Draft are outlined below.

Amendments to paragraph 9

As proposed, paragraph 9 will require that all of the conditions for sale accounting be satisfied by both the transferor and its consolidated affiliates included in the financial statements being presented in order for the transfer to be recognized as constituting a sale. It is unclear whether "consolidated affiliates" is meant to include a VIE of which an enterprise will be determined to be the primary beneficiary under an amended Interpretation 46R. The transferor in a typical credit card securitization is likely to be determined to be the primary beneficiary of the credit card master trust once the OSPE scope exception from Interpretation 46R is eliminated. As the primary beneficiary, the transferor would then have to consolidate the credit card master trust under Interpretation 46R. On a consolidated basis, we understand that there will be no recognition of a sale for accounting purposes between the transferor and the credit card master trust. However, we believe there is a critical distinction between a transfer being deemed to satisfy the conditions for sale accounting and a legal sale to a consolidated affiliate. While we recognize that the guidance in amended paragraph 9 is written to apply only to those affiliates "included in the financial statements being presented," we are concerned that this might preclude the evaluation of the transfer on its own - for purposes of a legal isolation determination - in situations where the transferor does not present financial statements on an unconsolidated basis.

This result would be inconsistent with the traditional analysis of what constitutes a "true sale" under applicable insolvency law. Under U.S. bankruptcy law, for instance, it is well established that a parent can transfer assets to a wholly owned subsidiary in a transaction that legally isolates the transferred assets from the parent, even where the consolidated enterprise does not meet the requirements for sale accounting treatment. This intermediate outcome — where the parent achieves a sale as between itself and its subsidiary but then consolidates the subsidiary — is permitted under the current version of Statement 140 and would appear to yield a reporting result consistent with the transparency goals of the proposed amendments. In such circumstances, the parent's consolidated financial statements would typically indicate that the assets, though consolidated, have been transferred to a subsidiary and are not considered available to the parent's creditors. In our view, financial statements such as these that both reflect the sale of the financial assets at the parent level *and* consolidate the VIE would provide clearer information to investors in the parent entity than a financial statement that continued to treat the assets as if they were controlled by the parent, especially where parental control would not as a matter of law be recognized in an insolvency proceeding.

Although the Board has specified that bankruptcy remote entities are not to be considered consolidated affiliates for applying the provisions of paragraph 9(a), the draft does not include a corresponding exclusion in paragraph 9(c). Satisfaction of the condition for sale accounting treatment in paragraph 9(c) would require that the transferor and its consolidated affiliates "not maintain effective control over the transferred financial assets." But if the assets have been transferred to an entity that is then consolidated – even a bankruptcy remote entity such as a special purpose subsidiary, a master trust or a note issuance trust for which the legal isolation prong in paragraph 9(a) is satisfied – this condition seems impossible to meet, and presumably no transfer to a VIE for which the transferor is the primary beneficiary would ever be treated as a sale if the transferor did not issue unconsolidated financial statements. This seems to us to be the wrong result, and one that will ultimately make financial statements less transparent rather than more transparent. We believe that the failure to recognize the transfer as a sale ignores the

economic reality of the underlying transaction: that through the process of securitization, the cash flows of specifically-identified assets have been effectively sold to unrelated third parties.

For bank transferors, there is additional importance to achieving sale accounting treatment on a nonconsolidated basis even though such a transferor would not likely have a reason to issue unconsolidated financial statements. The FDIC rule, Treatment by the Federal Deposit Insurance Corporation as Conservator or Receiver of Financial Assets Transferred by an Insured Depository Institution in Connection with a Securitization or Participation, requires that the transfer satisfy the conditions for sale accounting treatment under U.S. GAAP (other than the legal isolation condition itself) to be recognized by the FDIC as legally isolating the transferred assets. It is our understanding that the FDIC rule was negotiated with the Board and promulgated based on concerns the Board raised as to whether the FDIC would be able to reclaim securitized assets in a receivership of the transferring bank. We further understand that since the adoption of the FDIC rule, it has become the market standard to achieve legal isolation for bank transfers by satisfying the rule's conditions, and it is not clear to us that the law relied on prior to the rule's adoption would continue to be accepted. As a result, if it becomes impossible for a transfer to a consolidated VIE to be recognized as a sale to a consolidated affiliate, it may similarly become impossible to achieve legal isolation of the assets—and legal isolation has been a fundamental aspect of securitization since even before it became important under Statement 140. Although we appreciate this is a problem that the FDIC may need to address as well as the Board, we believe an FDIC solution becomes much easier if sale accounting treatment can be achieved between the transferor and the VIE prior to consolidation.

We urge the Board to preserve the fundamental construct under which the securitization industry now operates with respect to legal isolation. To that end, we suggest several clarifications. First, we believe that paragraph 9(a) should be written to clarify that any special purpose entity that is designed to legally isolate transferred assets is not considered a consolidated affiliate. Second, we believe that the carve-out for such entities from the consolidated affiliate definition should be applicable for purposes of applying any part of paragraph 9, rather than simply applying that carve-out to paragraph 9(a). In addition, we do not believe it is necessary or appropriate to limit the carve-out only to those special purpose entities used in multiple-step transfers, as legal isolation is recognized today under certain circumstances with single-step transfers, particularly as a result of the FDIC rule.

Participating interests

The Board has proposed under paragraph 8B that a transfer of a portion of a financial asset is eligible for derecognition as a sale only if the transferred portion meets the definition of a participating interest. For a transfer to meet the definition of a participating interest, all cash flows received from the asset must be proportionately divided among the participating interests and must remain pro rata over the life of the original financial asset. In addition, the rights of each participating interest holder must have the same priority.

In a typical credit card securitization, whole receivables are transferred to a trust, which then issues beneficial interests to the transferor and investors. The interest in the trust which the transferor retains represents a fractional undivided interest in the securitized pool, but it is legally a beneficial interest in a trust rather than a participating interest in receivables. Given that credit

card securitization vehicles typically issue beneficial interests consisting of a senior class and one or more subordinated classes, if the transfers were treated under paragraph 8B not as the transfer of a group of financial assets in their entirety but as a transfer of a portion of each individual financial asset, it is unlikely those portions would satisfy the description of a participating interest.

For the avoidance of doubt, we suggest that the determination of whether a transaction involves the transfer of a portion of a financial asset or the entire financial asset should be based on a consideration of the legal characterization of the transfer. In particular, a transfer of "all right, title and interest" in a financial asset should always be treated as the transfer of that financial asset in its entirety, whether or not the transferor has equity or other interests in the transferee.

If you would like to discuss any of the comments made in this letter, please contact Kevin Killips, Senior Vice President, Controller and Chief Accounting Officer of Discover Financial Services at 224-405-1101.

Sincerely,

Roy A. Guthrie Executive Vice President and Chief Financial Officer