



August 24, 2004

Russell Golden, CPA
Director of Technical Activities
Financial Accounting Standards Board
401 Merritt 7
PO Box 5116
Norwalk Connecticut 06856-5116
File Reference No. 1700-100

Dear Mr. Golden:

The Accounting Standards Executive Committee's (AcSEC) of the American Institute of Certified Public Accountants (AICPA) has reviewed the exposure draft of the Financial Accounting Standards Board's (FASB) Proposed Accounting Standards Update, *Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses*, and is pleased to provide these comments for the Board's consideration.

AcSEC supports the overall objective of the proposed Statement to provide disclosures that enable all users of financial statements to understand the nature of credit risk inherent in the creditor's portfolio of financing receivables, how that information is used in arriving at the allowance for credit losses and the changes and reasons for those changes, in both the receivables and the allowance for credit losses. The proposal is also intended to incorporate into GAAP information that is currently required for financial institution and securities regulators and to align U.S. GAAP with current International Financial Reporting Standards (IFRS). AcSEC is concerned however that instead of increased transparency, the excessive nature of these disclosures may be too much and may not provide the desired usefulness to the financial statements. As such, we have made some recommendations for the Board's consideration, as discussed in the attachment. In some cases, we believe that the costs outweigh the benefit of providing the additional information and in some cases we believe that there is too much information to be absorbed by financial statement users. AcSEC is also concerned, as further discussed in Issue 4, that the proposal adds requirements that are currently not part of many entities' existing credit quality review process. AcSEC observes that a draft of a proposed Statement of Position (SOP), *Disclosures Concerning Credit Losses Related to Loans*, last discussed by AcSEC in October 2005 and submitted to the Board, was not as detailed and extensive as the current proposal by the Board.

AcSEC notes that the timing of this proposal seems unusual considering the current projects of both the IASB and FASB discussed in the next two paragraphs. Although the Board has indicated that it did reach out to users when determining the proposed Standard, AcSEC believes it would be prudent to determine whether there are still concerns about the disclosures regarding the allowance for credit losses.



While the proposal may be consistent with current IASB disclosure requirements, AcSEC notes that the IASB has issued a Request for Information, *Impairment of Financial Assets: Expected Cash Flow Approach*, which the IASB intends to use in its reconsideration of IAS 39, *Financial Instruments*, and more specifically in the portion of the project related to impairment of financial assets. The IASB expects to issue a proposal related to the impairment phase in the third quarter of 2009. This project may result in a different model from the incurred loss model; in which case the Board's proposed ED may require certain disclosures that will not be consistent with the IFRS model. We also understand the Board's project, *Financial Instruments: Improvements to Recognition and Measurement*, is a joint project with the IASB. The task force recommends that the Board work with the IASB and focus its resources on the development of a consistent impairment and disclosure framework rather than changing the existing disclosure requirements which may only be relevant for a short period of time. We note that the Board has recently added a comprehensive disclosure project to its agenda. AcSEC notes that the timing of the proposed Standard should be reconsidered and the nature of the disclosures included in the overall project. That would allow entities to avoid the undue burden of adopting additional disclosures on a piecemeal basis.

AcSEC believes that the effective date of the proposed Standard is unrealistic and would pose an excessive burden, particularly on those nonpublic and non-regulated entities that currently do not have the systems in place to capture the required data. Because the final Standard may not be issued until quite close to the effective date, we believe compliance with the proposed effective date will be very difficult for most entities. We also note that many financial institutions will be forced to deal with these new disclosures for their December 31, 2009 year-end financial statements while at the same time implementing the recently issued FASB Statements Nos. 166, *Accounting for Transfers of Financial Assets*, and 167, *Amendments to FASB Interpretation No. 46(R)* as of January 1, 2010. In our responses to the issues raised by the Board (see Attachment A), we further expand on our position and offer recommended alternatives.

Representatives of AcSEC would be pleased to meet with you to discuss our comments.

Sincerely,

Sydney K. Garmong, Chair
AcSEC Credit Loss Disclosures Comment Letter Task force

Jay D. Hanson, Chairman
Accounting Standards Executive Committee

Appendix: Responses to Issues Raised by the ED and Other Comments



Issue #1: This proposed Statement defines a *financing receivable* as both loans as defined by FASB Statement No. 114, *Accounting by Creditors for Impairment of a Loan*, and lessors' investment in leases other than operating leases that have been recorded as assets in accordance with FASB Statement No. 13, *Accounting for Leases*. Do you agree with the definition used to identify a financing receivable subject to the provisions of this proposed Statement? If not, why not?

AcSEC recommends that several issues related to scope should be clarified. In particular AcSEC does not believe that the proposed Standard should apply to leveraged leases because of the mechanics of netting the debt against the expected cash flows. AcSEC notes the inconsistency of excluding trade receivables with maturities of one year or less, while including other receivables due on demand and suggests that the Board clarify this apparent inconsistency. AcSEC further questions the decision to include trade receivables greater than one year in the scope when many of the required disclosures are simply not applicable for these types of assets. AcSEC also recommends that the Board clarify the difference between accounts receivable and trade receivables as the terminology in the proposed Standard is not defined.

AcSEC recommends that "promises to give" be excluded from the scope of the proposal. Unlike other assets covered by the proposal, a promise to give is a nonreciprocal gift transaction. No financing has occurred in creating a promise to give. Non-profit entities do not make a decision to extend credit but rather they accept the terms that a donor suggests. Management has no ability to require collateral, or impose interest or penalties if a donor does not pay timely. Unlike financing receivables, a promise to give does not have contractual rights, even if some of them may be enforceable. Thus, presentation of the required disclosures provides little or no information about management's stewardship of its receivables. As such, AcSEC believes it is prudent to exclude them from the scope.

It is unclear if the proposal applies to financing receivables carried at fair value or lower of cost or fair value. Based on the requirements of paragraph 6(a), it appears the Board intends for those receivables to be included in the scope. However, AcSEC believes those items carried at fair value or lower of cost or fair value should be excluded from the scope since credit risk, which is included in the valuation, is only one attribute to consider in determining fair value. Further, there are already robust fair value disclosures requirements in U.S. GAAP.

Issue #2: This proposed Statement would apply to all creditors, including all public and nonpublic entities that prepare financial statements in accordance with generally accepted accounting principles. Do you agree with the scope of this proposed Statement? If not, why not?

The majority of AcSEC agrees that the scope of the proposed accounting changes should apply to all entities both public and private including nonprofit organizations. A minority believes there should be some exemption for smaller, nonpublic, entities. As noted in our general comments and more specifically in Issue #8, we strongly recommend delaying the effective date of the proposed accounting changes for a minimum of 12 months.



AcSEC observes that the term recorded investment may not be widely used outside of financial institutions and we suspect that is the reason the Board is changing the term to ‘carrying amount’. We believe the Board intended to define carrying amount to exclude any related allowance. AcSEC suggests that the term “carrying amount” should be clarified as such. A possible fix could be to add the phrase ‘exclusive of the allowance’ at the end of paragraph 4.

Issue #3: This proposed Statement would require a roll forward schedule of the total allowance for credit losses in both interim and annual reporting periods by portfolio segment and in the aggregate. In addition, it also would require a roll forward schedule of financing receivables in both interim and annual reporting periods by portfolio segment and in the aggregate. Do you believe those disclosures will assist financial statement users in better understanding the financial information for the total allowance for credit losses as well as the associated financing receivables? If not, why not?

The roll forward of the allowance for credit losses by portfolio segment and may not be readily available and for certain entities, particularly those outside financial institutions may require some systems changes to capture this information. However, we believe the roll forward of the allowance by portfolio segment is useful information and should be required disclosures.

However, we believe the roll forward of financing receivables is not necessary, because this does not relate to information about credit quality. It does not provide any incremental useful information and discussions with preparers indicate that gross originations and cash receipts on loans may not be especially useful information, especially for large financial institutions. We also observe this is not information that is required for the statement of cash flows. Further, we envision challenges in obtaining this information, particularly for entities who report cash flows from loans ‘net’ rather than ‘gross’.

Issue #4: This proposed Statement would require interim and annual credit quality disclosures about a portfolio by class of financing receivable, including quantitative and qualitative information about the credit quality of financing receivables. Do you believe those disclosures will assist financial statement users to better understand the credit quality for the associated financing receivables? If not, why not?

While we believe that some level of disaggregation is appropriate, we are concerned that the proposed accounting is excessive and that such a level of detail is not useful. We do not support a level of disaggregation by class because not all receivables may be graded, particularly on a continuous basis. Rather than requiring disclosure for the entire portfolio, we believe that to the extent that management is grading the receivables, and the grades are current, the results of that process should be disclosed. Further, we are concerned that the proposed accounting changes may impose additional requirements for management over and above preparers’ normal credit evaluation process. For example, in paragraph 13b2, there is a requirement to disclose consumer credit risk scores if those indicators are used by creditors. It is very common for financial institutions to obtain a credit risk score upon origination of a loan but those scores are not necessarily updated over the life of the loan. The proposal seems to require those be updated and disclosed on an on-going basis and we believe this would



add cost and add a requirement which is not part of many entities' existing credit quality evaluation process. Prior to concluding on the addition of this requirement, AcSEC suggests the Board consult with preparers.

Issue # 5: This proposed Statement would require an analysis of the age of financing receivables that are past due, but not impaired, at the end of the reporting period separately for each class of financial instruments. Do you believe those disclosures will assist financial statement users in better understanding the credit quality for the associated financing receivables? If not, why not?

Although the aging information may be a good predictor of actual losses, AcSEC believes that the required disclosures are too detailed and the aging analysis should be presented at a more summarized level and the requirement to disaggregate by class should be eliminated. Further, we do not believe that disclosure of the allowance by class is practical as many loans are evaluated as a pool and as such, the allowance may not be specifically identifiable by class. As indicated for many of the required disclosures, we question whether the level of detail actually helps the user understand the nature of the credit quality and the allowance.

Issue #6: This proposed Statement would require the fair value of loans at the end of the reporting period by portfolio segment. Do you believe those disclosures will assist financial statement users in better understanding the credit quality for the associated financing receivables? If not, why not?

AcSEC notes that credit risk is only one attribute to consider in determining fair value. FASB ASC 820 *Fair Value Measurements*, and Disclosures and FASB ASC 825 *Financial Instruments*, already provide substantial disclosures about fair value and the task force strongly recommends that the fair value disclosure requirements be deleted from this proposal. We also note that the scope of FASB ASC 825 applies to all public companies and certain nonpublic companies. This proposal would subject those entities, who currently are not required to follow the fair value disclosures of FASB ASC, 825 to provide fair value disclosures. As indicated in our other responses, we question whether the disclosures provide users with the appropriate information to understand the nature of the credit quality and the allowance given that there are other factors beyond credit which impact fair value.

Issue # 7: Do you believe it is operational for entities to disclose all of the proposed requirements for interim and annual reporting periods? Why or why not?

AcSEC notes that some public companies may have the information and systems necessary to make these interim disclosures although they significantly expand the level of current disclosures. However, we have received input that even some public companies do not have this information to make these interim disclosures. Interim disclosures will be operationally more difficult for nonpublic companies and we suggest that any requirement for interim disclosures be limited to public companies. Preparers have suggested that this would require a significant effort to create these interim disclosures. Because the composition of AcSEC is not predominantly preparer based, we strongly recommend that the Board do additional outreach with preparers before requiring these disclosures on an interim basis.



Issue # 8: The final Statement is expected to be issued in the third quarter of 2009.

The Board concluded that this proposed Statement would be effective for financial statements beginning with the first interim or annual reporting period ending after December 15, 2009. Do you agree with the Board's decision on the effective date? If not, what would be a reasonable period of time to implement the provisions of this proposed Statement? If you do not agree, please provide a description of the process changes necessary to implement this proposed Statement that would require additional time.

Under the current proposal, the amendments to FASB ASC Statement will be effective for all interim and annual reporting periods beginning with the first interim or annual reporting period ending after December 15, 2009, with earlier application encouraged. AcSEC strongly believes that the effective date should be delayed at a minimum to year-end 2010 for public as well as nonpublic entities including nonprofits. As previously discussed, many financial institutions will be implementing FASB Statements Nos. 166 and 167 for the first quarter of 2010 and the additional disclosures required by those Statements. Given that year end is generally the busiest part of the financial reporting cycle, we believe it will be difficult for entities to comply for 2009, particularly if there are system and internal control changes which need to take place to comply.

Other Comments: AcSEC has the following additional comments on the proposed ED:

- Paragraph 13(b) (1) uses the term “regulated creditor.” AcSEC recommends clarifying the definition. From the context of the paragraph it appears to mean insured depository institutions.
- If the Board decides to retain the requirement to disaggregate certain disclosures by class, AcSEC suggests providing guidance on how to determine the appropriate class if a loan has characteristics of more than one class.
- Credit quality indicators may be applied differently depending on whether those indicators are being used for underwriting purposes or calculating the allowance. The final amendments to FASB ASC should clarify the intended disclosure of the different applications.
- The tables included as examples in Appendix A are not included in the amendments to FASB ASC. We believe the examples are helpful in understanding the requirements and as such, we believe that FASB ASC should include those examples.
- Paragraph 9 provides guidance on disaggregation into classes with reference to paragraph 5 which provides guidance on determining portfolio segments. AcSEC recommends that the final standard eliminate disaggregation by class, but if that requirement is retained we are unclear why the reference to paragraph 5 is included in paragraph 9 and recommend that the Board provide clarification.