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1890-100
Comment Letter No. 91
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January 31, 2011

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

Via email to director@fasb.org

Reference: File Reference No. 1890-100, Discussion Paper, *Effective Dates and Transition Methods*

Dear Sir or Madame:

Freddie Mac appreciates the opportunity to comment on the Discussion Paper, *Effective Dates and Transition Methods* (the "Discussion Paper").

Freddie Mac was chartered by Congress in 1970 to increase the availability of funds for home ownership by developing and maintaining a secondary market for residential mortgages. We participate in the secondary mortgage market principally by providing our credit guarantee on the mortgage-related securities we issue, and investing in mortgages and mortgage-related securities. As of September 30, 2010, our total assets were approximately \$2.3 trillion, which is comprised primarily of mortgage loans and mortgage-related investment securities.

We appreciate the Board's efforts to solicit feedback from stakeholders to develop an implementation plan for the multitude of projects currently under deliberation. We believe that careful consideration needs to be given to the magnitude of the effort involved to implement the changes to the accounting models contained in the multiple projects discussed in the Discussion paper ("the proposed standards"), as well as the cost of implementation relative to the benefits derived from the implementation approach ultimately taken by the Board.

Three of the ten proposed standards subject to this Discussion Paper will have a very significant impact on our accounting, financial reporting, systems and operations. Those standards are Accounting for Financial Instruments, Fair Value Measurements and Disclosures, and Financial Statement Presentation.

We believe that the adoption of the proposed standards covered by the Discussion Paper should be on a single effective date - preferably January 1, 2015, with prospective application of the standards that impact accounting and retrospective application only for the standards that impact financial statement presentation.

Included in the Appendix to this letter are Freddie Mac's responses to each of the individual questions posed by the Board in the Discussion Paper.

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The views expressed in this comment letter are solely those of Freddie Mac, and do not purport to represent the views of the Federal Housing Finance Agency, as Conservator.

Freddie Mac appreciates the opportunity to provide our comments on the Discussion Paper. If you have any questions about our comments, please contact Timothy Kviz (703-714-3800).

Sincerely,



Timothy Kviz
Vice President – Accounting Policy

cc: Mr. Ross J. Kari, Executive Vice President - Chief Financial Officer
Mr. Robert D. Mailloux, Senior Vice President - Corporate Controller and Principal
Accounting Officer
Mr. Nicholas Satriano, Chief Accountant, Federal Housing Finance Agency

Appendix

This Appendix includes our responses and comments to the specific questions that were raised by the Board in the Discussion Paper.

Question 1: Please describe the entity (or the individual) responding to this Discussion Paper.

For example:

- a. *Please indicate whether you are primarily a preparer of financial statements, an auditor, or an investor, creditor, or other user of financial statements (such as a regulator). Please also indicate whether you primarily prepare, use, or audit financial information prepared in accordance with U.S. GAAP, IFRSs, or both.*
- b. *If you are a preparer of financial statements, please describe your primary business or businesses, their size (in terms of the number of employees or other relevant metric), and whether you have securities registered on a securities exchange.*
- c. *If you are an auditor, please indicate the size of your firm and whether your practice focuses primarily on public companies, private entities, or both.*
- d. *If you are an investor, creditor, or other user of financial statements, please describe your job function (buy side/sell side/regulator/credit analyst/lending officer), your investment perspective (long, long/short, equity, or fixed income), and the industries or sectors you specialize in, if any.*
- e. *Please describe the degree to which each of the proposed new standards will likely affect you and the factors driving that effect (for example, preparers of financial statements might explain the frequency or materiality of the transactions to their business and investors might explain the significance of the transactions to the particular industries or sectors they follow).*

Response: Freddie Mac is primarily a preparer of financial statements. However, in our role as a creditor and an investor, we are also a significant user of financial statements in our monitoring of counterparty credit risk. Therefore, Freddie Mac both prepares and uses financial information prepared in accordance with U.S. GAAP.

Freddie Mac operates in the mortgage finance industry. Our operations consist of three business segments, which are based on the type of business activities each segment performs – Single-family Guarantee, Investments, and Multifamily.

The Single-family Guarantee segment purchases single-family mortgage loans originated by our customers in the primary mortgage market. We use the mortgage securitization process to package the purchased mortgage loans into mortgage-related securities and guarantee the timely payment of principal and interest on the issued securities in exchange for a management and guarantee fee. In our role as a securities administrator and guarantor we pay close attention to the creditworthiness of our counterparties. For example, we continuously evaluate our servicers performance, and ability to continue to pass through funds collected from loans they service to us (i.e., in our capacity as securities administrator and guarantor). We also use financial statements to assess the ability of our sellers/servicers to perform under their obligations to repurchase mortgage loans that do not meet our underwriting criteria and violate the representations and

warranties made to us. Additionally, we review the financial statements of mortgage insurers to evaluate their ability to perform on the policies (i.e., primary mortgage insurance, mortgage pool insurance, etc.) when we are the beneficiary.

The Investment segment performs investing, funding and hedging activities. We are a fixed income investor, principally investing in mortgage-related securities. This segment funds these investment securities, as well as the assets of the Single-family Guarantee and Multifamily segments, through the issuance of debt. Additionally, this segment manages interest rate risk across the entire company using, among other things, derivative financial instruments. This segment is a user of financial statements in the evaluation of investment securities for impairment (e.g., considering whether a bond insurer of an investment security we hold will have the ability to perform under the terms of their insurance) and management of counterparty credit risk with our derivative counterparties. We also consider whether issuers of mortgage-related securities that we hold have the ability to perform upon repurchase requests under seller representations and warranties for loans underlying the securities.

The Multifamily segment purchases multifamily loans originated by our customers in the primary mortgage market. We use the mortgage securitization process to package the purchased multifamily mortgage loans into mortgage-related securities and guarantee the timely payment of principal and on the issued securities in exchange for management and guarantee fees. The Multifamily segment engages in various other guarantee activities (i.e., guarantees of tax-exempt bonds issued by municipalities, liquidity guarantees, stand-ready obligations, etc.) to increase financing and credit availability for multifamily properties. This segment also invests in multifamily mortgage-related securities (e.g., CMBS). Our Multifamily segment uses financial statements to assess the performance of individual properties underlying multifamily loans in evaluating which loans are considered impaired.

We owned or guaranteed approximately 23% of the outstanding single-family mortgages in the U.S. at September 30, 2010. As of September 30, 2010, our total assets were approximately \$2.3 trillion, approximately 97% (\$2.2 trillion) of which are financial assets. Freddie Mac is registered with the U.S. Securities and Exchange Commission, and our equity securities are traded in the over the counter markets. We have approximately 5,300 employees.

The degrees to which some of the proposed standards covered in this Discussion Paper will affect Freddie Mac are described below.

Accounting for Financial Instruments

As noted earlier in our response, most of our balance sheet is comprised of financial instruments. This proposed standard would have a very significant impact on most aspects of our accounting, financial reporting, systems, and operations (please refer to our comment letter to the Board on this proposed standard dated September 30, 2010, which described these impacts in greater detail).

Fair Value Measurements

The proposed standard primarily affects our disclosure of Level 3 fair value measurements. We believe that the impacts of this proposed standard will be significant to us due to the sizeable number of financial instruments we hold that we classify within Level 3 of the fair value hierarchy, the number of valuation models/techniques that would likely require modification as a result of the proposed standard, and the number of third party pricing services that we employ in determining our Level 3 fair value measurements (please refer to our comment letter to the Board on this proposed standard dated September 7, 2010, for more information).

Financial Statement Presentation

This proposed standard will have a significant impact on our financial statements due to the major changes to both our financial reporting processes and supporting information systems that will likely be required for its implementation.

Revenue Recognition and Leases

These two proposed standards will have a minimal impact on our financial statements and financial reporting because they impact an insignificant number of transactions, which are immaterial to our consolidated financial statements.

Accounting for Insurance Contracts

This proposed standard may have a significant impact on our operations and financial reporting depending on the ultimate transition method selected. If the proposed standard is to be applied retrospectively, the impact will be significant to us for two main reasons. First, due to interaction with the transition methods of this proposed standard and other relevant accounting literature, such as ASU 2009-17, *Consolidations (Topic 810): Improvements to Financial Reporting by Enterprises Involved with Variable Interest Entities*, we may be required to reflect insurance contract accounting for our financial guarantees issued prior to the effective date of ASU 2009-17, and then extinguish insurance contract accounting upon consolidation of the securitization trusts to which we issued our guarantee upon the effective date of ASU 2009-17. Second, we lack the necessary information and data for retrospective application of this standard (i.e., expected future cash flows at inception of the guarantee arrangement that may have been entered into over twenty years ago). In addition, retrospective application of this proposed standard is further complicated by our re-securitization activity and our historical practice of making a market in the mortgage-related securities that we issue (i.e., potentially triggering extinguishment or partial extinguishment of insurance contract accounting upon acquisitions of our mortgage-related securities, with the subsequent re-establishment of insurance accounting on the sales of such securities).

Other Comprehensive Income (“OCI”)

This proposed standard impacts presentation of OCI in the financial statements only. Therefore, it will have a minimal impact on our financial statements and will not require significant preparation or implementation time.

Netting of Financial Instruments

This proposed standard impacts the presentation of financial instruments in the statement of financial position (i.e., whether multiple instruments will be presented on a gross or on a net basis). A change to this presentation in and of itself is not overly complex; however, there may be impacts to the valuation of derivative financial instruments subject to master netting arrangements if netting of the derivative positions subject to these arrangements is prohibited for financial statement purposes. If all derivatives are presented gross, the credit value adjustments applied to the instruments may be different (i.e., credit of the counterparty for asset positions and our own credit for derivative liability positions, as opposed to the credit of the party in a net liability position for derivatives subject to master netting arrangements). Changes to our systems and processes may be necessary if gross presentation is required.

Consolidation: Investment Companies and Financial Instruments with characteristics of Equity
These proposed standards are not applicable to us.

Question 2: Focusing only on those proposals that have been published as Exposure Drafts (accounting for financial instruments, other comprehensive income, revenue recognition, and leases):

- a. How much time will you need to learn about each proposal, appropriately train personnel, plan for, and implement or otherwise adapt to each the new standard?***
- b. What are the types of costs you expect to incur in planning for and adapting to the new requirements and what are the primary drivers of those costs? What is the relative significance of each cost component?***

Response:

Accounting for Financial Instruments

As discussed above, the proposed standard on Accounting for Financial Instruments will have a very significant impact on our accounting, financial reporting, systems, and operations as detailed in our comment letter to the Board dated September 30, 2010. Based on our preliminary evaluation of the proposed new standard and our current systems and operational capabilities, we estimate that it will take us approximately three years from the issuance of the final standard to adopt it in a controlled fashion. This length of time takes into consideration the analysis of the final standard, the determination of the relevant accounting policy conclusions, the programming and testing which must be undertaken to implement necessary changes to systems, models, and operational processes, an overhaul of the applicable internal controls, and appropriate training of our Audit Committee, Executive Management, and other personnel.

Based on a preliminary evaluation of the proposed standard and our current systems and operational capabilities, we estimate that over 50 systems would require either partial modifications or complete overhaul and hundreds of models would require significant changes. The most significant cost component of the implementation of the proposed standard will be driven by pervasive changes required to our current systems, models, system interfaces, processes, and the procedures that need to be planned, designed, implemented, tested and executed. We will also incur additional costs for training of personnel and for the revision of our internal controls for the implemented changes. Our preliminary cost estimate of adopting this

proposed standard is approximately \$150 million (assuming prospective application). If this proposed standard were to be applied retrospectively, these cost estimates will increase significantly, and the amount of time necessary to implement this proposed standard will be extended by approximately two years.

Additionally, fair value information is typically among the last information to be obtained during the financial reporting close process. Therefore, mandating fair value as the measurement attribute for the majority of financial instruments may have the unintended consequence of delaying an entity's closing of the books and the subsequent preparation of financial statements, ultimately resulting in a compressed financial reporting preparation timeline. To release our financial statements timely, we may need to increase our headcount to complete the close in a compressed timeframe.

Other Comprehensive Income

We believe that the time required to implement the proposed standard on Other Comprehensive Income will be minimal as the proposal only requires a change in the format of presentation of existing information.

Revenue Recognition and Leasing

These proposed standards, while very complex, would not affect our accounting, financial reporting, systems, or operations in a meaningful way. Therefore, we believe our adoption of these proposed standards would not involve significant time and cost.

Question 3: Do you foresee other effects on the broader financial reporting system arising from these new standards? For example, will the new financial reporting requirements conflict with other regulatory or tax reporting requirements? Will they give rise to a need for changes in auditing standards?

Response: We foresee two potential effects on the broader financial reporting system arising from these proposed standards. The proposed standard on Accounting for Financial Instruments will result in increased differences between financial reporting and tax reporting, which will necessitate additional system changes to accommodate multi-basis accounting. Additionally, federal regulatory agencies have just begun the process of implementing the provisions of the Dodd-Frank Act. Implementation of the rulemakings legislated by this Act are still in their early stages. Therefore, it is very difficult to determine the extent to which new regulations and the proposed accounting standards may conflict.

Question 4: In the context of a broad implementation plan covering all the new requirements, do you agree with the transition method as proposed for each project? If not, what changes would you recommend and why? In particular, please explain the primary advantages of your recommended changes and their affect on the cost of adapting to the new reporting requirements.

Response: We believe, given the magnitude of changes required by the proposed standards, the implementation of these standards will be incredibly complex. Furthermore, the data and

information required for retrospective application of the proposed standards on Accounting for Financial Instruments and Insurance Contracts may not be available or may be impractical for us to obtain. It is not operationally feasible to derive fair values or expected future cash flows for prior periods, which may be necessary to retrospectively apply the proposed standards to many of our transactions, such as our securitization and re-securitization activities.

While we realize that comparative financial statements are the most meaningful for users, we are concerned that the increase in operational complexity and cost resulting from retrospective application of the proposed standards outweighs the benefits gained by users of financial statements. As a result, we believe transition methods for the proposed standards covered by this Discussion Paper should be prospective application of standards that impact accounting and retrospective application only of standards that impact financial statements presentation. While an entity's financial statements may not be comparable year-over-year for a short period of time, we believe the users are better served with convergence to high quality global accounting standards that can be implemented in the most cost effective and time sensitive manner possible.

Question 5: In thinking about an overall implementation plan covering all of the standards that are the subject of this Discussion Paper:

- a. Do you prefer the single date approach or the sequential approach? Why? What are the advantages and disadvantages of your preferred approach? How would your preferred approach minimize the cost of implementation or bring other benefits? Please describe the sources of those benefits (for example, economies of scale, minimizing disruption, or other synergistic benefits).***
- b. Under a single date approach, what should the mandatory effective date be and why?***
- c. Under the sequential approach, how should the new standards be sequenced (or grouped) and what should the mandatory effective dates for each group be? Please explain the primary factors that drive your recommended adoption sequence, such as the impact of interdependencies among the new standards.***
- d. Do you think another approach would be viable and preferable? If so, please describe that approach and its advantages.***

Response: We believe the single date approach with the effective date of January 1, 2015 and prospective application of the standards that impact accounting and retrospective application only for the standards that impact financial statements presentation is preferable for adoption of the proposed standards. On adoption, we would propose recognition of a cumulative effect of the changes in accounting principles as an adjustment to opening retained earnings on January 1, 2015. The advantage of such an approach is that the massive changes to financial statements are implemented and explained once versus "perpetually" implementing changes required by the adoption of the proposed standards based on a timeline of staggered effective dates.

Additionally, as a preparer, we would have to implement the changes to the systems, models, processes, and financial statements only once, which would minimize disruption to our operations and financial reporting. Furthermore, a single effective date approach allows us to coordinate systems updates for all standards concurrently, minimizing the risk that interaction between the standards, systems and data may not be properly considered, which decreases the

chance of error in processing these changes, and reduces time for testing the implemented changes. This approach results in gained economies of scale and decreased cost of implementation efforts.

We estimate the implementation of the proposed standards, considering the magnitude of the changes and pervasive impacts these standards will have on entities' accounting and financial reporting, will require approximately three years. Entities will most likely be required to implement additional system changes to accommodate multi-basis accounting functionality due to increased differences between financial and tax reporting (please refer to our response to Question 3 above). Therefore, the resulting implementation period with the effective date of January 1, 2015 will allow companies to implement the mandated changes in controlled, coherent, and cost effective manner.

If users believe that comparable financial statements are an absolute necessity, then we would propose adoption on January 1, 2017, with retrospective application to January 1, 2015. While this approach would require running two sets of books in parallel during 2015 and 2016, we believe this is the only way for us to present comparative financial statements upon adoption of the proposed standards. Because it would be expensive to operate with two sets of books for a two-year period, we believe that prospective adoption, as described above, is the most cost effective approach.

Question 6: Should the Board give companies the option of adopting some or all of the new standards before their mandatory effective date? Why or why not? Which ones? What restrictions, if any, should there be on early adoption (for example, are there related requirements that should be adopted at the same time)?

Response: We believe the option of adopting some or all of the proposed standards covered by this Discussion Paper before their mandatory effective date would not provide any benefits to stakeholders or investors because financial statements would lack comparability not only from year to year but also between entities. Therefore, the Board should not permit companies to adopt some or all of the proposed standards before their mandatory effective date.

Question 7: For which standards, if any, should the Board provide particular types of entities a delayed effective date? How long should such a delay be and to which entities should it apply? What would be the primary advantages and disadvantages of the delay to each class of stakeholders (financial statement preparers, financial statement users, and auditors)? Should companies eligible for a delayed effective date have the option of adopting the requirements as of an earlier date?

Response: As a significant user of financial statements, we appreciate the comparability of financial information presented in financial statements. Nevertheless, we understand that some smaller private companies (i.e., private companies with total assets less than a certain threshold) will not have the same resources or expertise to implement the aforementioned proposed standards by the same effective date as larger public companies. Furthermore, smaller private companies may be at a disadvantage in attracting experienced personnel needed to implement the

proposed standards. Therefore, we suggest that the Board provide smaller private companies with two year deferral of the effective date.

Question 8: Should the FASB and IASB require the same effective dates and transition methods for their comparable standards? Why or why not?

Response: We believe the FASB and IASB should require the same effective dates and transition methods for their comparable standards. This approach would provide the benefit of advancing comparability of accounting standards and similar accounting and reporting for similar transactions across different jurisdictions along the same timeline. In addition, such financial statements will provide a more transparent picture of the impacts of adopting comparable standards globally.

Question 9: How does the Foundation's ongoing evaluation of standards setting for private companies affect your views on the questions raised in this Discussion Paper?

Response: Freddie Mac is not best placed to respond to this question. We will defer to those respondents who are directly impacted by the private company standards setting process.