

March 26, 2013

Ms. Susan M. Cosper Technical Director Financial Accounting Standards Board 401 Merritt 7 P.O. Box 5116 Norwalk, Connecticut 06856-5116 director@fasb.org

Project: Transfers and Servicing – Effective Control for Transfers with Forward Agreements to Repurchase Assets and Accounting for Repurchase Financings (File Reference No. 2013-210)

## Dear Ms. Cosper:

The Mortgage Bankers Association<sup>1</sup> (MBA) appreciates the opportunity to comment on FASB's exposure draft (ED) *Transfers and Servicing – Effective Control for Transfers with Forward Agreements to Repurchase Assets and Accounting for Repurchase Financings* (Proposed Update). The Proposed Update is to address certain practice issues on the application of effective control guidance related to transfers of financial assets with an agreement that both entitles and obligates the transferor to repurchase or redeem the financial assets. The specific objectives are<sup>2</sup>:

1. Clearly identify repurchase agreements, securities lending transactions, and other transactions that involve a transfer of a financial asset and an agreement that both entitles and obligates the transferor to repurchase or redeem the transferred asset that should be accounted for as financing transactions.

<sup>1</sup> The Mortgage Bankers Association (MBA) is the national association representing the real estate finance industry, an industry that employs more than 280,000 people in virtually every community in the country. Headquartered in Washington, D.C., the association works to ensure the continued strength of the nation's residential and commercial real estate markets; to expand homeownership and extend access to affordable housing to all Americans. MBA promotes fair and ethical lending practices and fosters professional excellence among real estate finance employees through a wide range of educational programs and a variety of publications. Its membership of over 2,200 companies includes all elements of real estate finance: mortgage companies, mortgage brokers, commercial banks, thrifts, REITs, Wall Street conduits, life insurance companies and others in the mortgage lending field. For additional information, visit MBA's Web site: www.mortgagebankers.org.

<sup>&</sup>lt;sup>2</sup> FASB, Transfers and Servicing – Effective Control for Transfers with Forward Agreements to Repurchase Assets and Accounting for Repurchase Financings, January 15, 2013, page 2.

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2. Improve the accounting and disclosures for those transactions.

## **Background**

The Proposed Update would require that a transfer of an existing financial asset with an agreement that both entitles and obligates the transferor to repurchase or redeem the transferred asset from the transferee to be accounted for as a financing if the transaction has the following characteristics<sup>3</sup>:

- The financial asset to be repurchased at settlement of the agreement is identical to or substantially the same as the financial asset transferred at inception or, when settlement of the forward agreement to repurchase or redeem the transferred assets is at the maturity of the transferred assets, the agreement is settled through an exchange of cash (or a net amount of cash).
- 2. The repurchase price is fixed or readily determinable.
- 3. The agreement to repurchase the transferred financial asset is entered into contemporaneously with, or in contemplation of, the initial transfer.

The Proposed Update would also clarify the characteristics of financial assets that are "substantially the same," eliminate the requirement to determine whether repurchase agreements entered into as part of a repurchase financing should be accounted for separately or linked with the initial transfer for accounting purposes, and would require certain new disclosures.

The following are MBA's general observations and comments and our responses to specific FASB questions contained in the ED.

#### **General Comments**

# **Definition of a Repurchase Agreement**

ED page 15 (Master Glossary) defines a repurchase agreement as follows:

An agreement under the transferor (repo party) transfers a financial asset to a transferee (repo counterparty or reverse party) in exchange for cash and concurrently agrees to reacquire that financial asset at a future date for an amount equal to the cash exchanged plus a stipulated interest factor. Instead of cash, other financial assets or letters of credit sometimes are exchanged. Some repurchase agreements call for repurchase of financial assets that need not be identical to the financial assets transferred.

We suggest changing the wording from "for an amount equal to the cash exchanged plus a stipulated interest factor" to "for an amount equal to the cash exchanged, **including an** interest factor". The word "plus" implies the repo counterparty is paying interest. There are points in time where certain repurchase transactions trade on "special" and there is a negative interest rate associated with them.

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<sup>&</sup>lt;sup>3</sup> Ibid, FASB, Page 2.

# **Conceptual Inconsistency**

ED pages 29 (ASC 860-10-55-51A item c.) states:

Repurchase agreements—repurchase-to-maturity agreements. If a financial asset is sold under a contemporaneous agreement with the same counterparty to repurchase it at a fixed price, and settlement of the forward repurchase agreement is at the maturity of the transferred financial asset resulting in an exchange of cash equal to the redemption or settlement value of the initially transferred financial asset and the fixed repurchase price (or the difference between those amounts), the agreement maintains the transferror's effective control over the transferred financial asset.

In contrast, ED page 30 (ASC 860-10-55-51A item e.) states:

Cash-settled repurchase agreements. If a financial asset is sold under a contemporaneous agreement with the same counterparty to repurchase or redeem it before its maturity at a fixed repurchase price or a price equal to the sale price plus a lender's return and the agreement requires the transferee to settle the agreement in cash, the agreement does not maintain the transferor's effective control over the transferred financial assets.

This comes across as conceptually inconsistent. If you settle one agreement in cash on the maturity date, you account for it as a financing agreement. In contrast, if you settle an agreement the day before maturity, you account for it as a sale. This inconsistency could result in a structuring opportunity and may provide undesirable results that the FASB did not intend. MBA recommends that FASB clarify or fix this issue in the final pronouncement.

# **Consistent With International Standards Convergence?**

FASB notes in the ED that the IFRS model is different from the Proposed Update on a conceptual basis since it considers whether the transferor retains the "risks and rewards" of ownership whereas the Proposed Update is based upon whether the agreement both entitles and obligates the transferor to repurchase the transferred asset. FASB concludes that the two methodologies will "generally" result in a "converged outcome." In what situations would the outcomes differ, and would those situations be frequent enough and material enough that a converged conclusion is inappropriate with respect to accounting for repos?

MBA suggests that FASB provide examples where the conclusions would be the same and where the conclusions would differ.

MBA also notes that there is no convergence yet on derecognition as a whole, and MBA urges FASB and IASB to work together to come up with a single model to be used worldwide.

"Substantially the Same" Criteria Not Operational

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Page 26 of the ED (ASC 860-10-55-35c.) would require a reporting entity to consider the prepayment characteristics of the security sold as compared with the anticipated prepayment characteristics of the security to be repurchased in order to determine if the securities are substantially the same. How would the reporting entity be able to identify or estimate the prepayment characteristics of the security to be repurchased since that is not known until the transferee presents the substituted security for repurchase at a later date?

The inputs used to calculate the yield include prepayment speeds. The new language in ASC 860-10-55-35c is unnecessary since it implies that additional analysis would be required but this information is already captured within the yield. MBA suggests removing the new language.

## **Collateral Disclosure May be Proprietary**

Several of MBA's members believe the disclosures required under 860-30-50-3(a) on page 36 of the ED would require transferors to disclose proprietary information because of the level of disaggregation required. For regulated bank holding companies, this type of data is provided to the Federal Reserve and is not available to the public due to the proprietary nature. Also, the proposed disclosure requirement is more related to liquidity risk and not accounting for transfers. If the transfers are to be accounted for as a borrowing, then the general disclosures for borrowings should apply.

# Disclosure for Transfers that Fail "Substantially the Same" Not Scoped Appropriately and Not Operational

MBA is not supportive of the disclosure proposed in 825-30-50-3b on page 36. The scope of the requirement is very broad and may require disclosure of transactions where the substantially the same criteria are not evaluated. Every financial asset transfer that is accounted for as a sale could be within scope of 825-30-50-3(b). However, even if the scope could be narrowed or clarified, it would be operationally challenging to obtain this information.

The disclosure is also not compatible with the MBS pair-off process at the Mortgage Backed Securities Division (MBSD) of the Fixed Income Clearing Corporation. We are uncertain how to implement and operationalize the disclosure requirements based on the broad scope and the settlement process that occurs in the market.

#### **Transition Guidance**

Page 4 of the ED contains the transition guidance, "For transfers with forward repurchase agreements that settle at the maturity of the transferred financial asset and repurchase financings that involve such agreements, an entity would apply the proposed amendments by means of a cumulative-effect adjustment to beginning retained earnings as of the beginning of the first reporting period in which the guidance

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is effective. For all other transactions, the entity would apply the proposed amendments prospectively to transactions entered into or modified after the effective date."

MBA members believe that the guidance for repo to maturity transactions would require a huge effort on the part of preparers of financial statements to calculate a cumulative effect adjustment. The reporting entity would have to go through years of transactions, determine which transactions would not qualify as sales, calculate the gain to be reversed, calculate the cumulative interest income and expense, and estimate the net tax amounts. Several of our members likened the proposed transition rules efforts to the burdensome transitional efforts required under FAS 167.

MBA recommends that the entire transition be done on a prospective basis.

MBA appreciates the opportunity to share its observations with you. Any questions about the information provided herein should be directed to me, Vice President Financial Accounting and Public Policy and Staff Representative to MBA's Financial Management Committee, at (202) 557-2860 or jgross@mortgagebankers.org.

Sincerely,

James P. Gross

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Vice President of Financial Accounting and Public Policy