



VIA Electronic Mail (director@fasb.org)

December 10, 2010

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

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Dear Board Members and FASB Staff:

The Mortgage Bankers Association<sup>1</sup> (MBA) appreciates the opportunity to comment on the Proposed Accounting Standards Update, *Receivables, Clarifications to Accounting for Troubled Debt Restructurings* (Proposed Update). The stated objective of the Proposed Update is to provide additional guidance to assist creditors in determining whether a restructuring of a receivable meets the definition of a troubled debt restructuring (TDR) both for purposes of recording an impairment and for disclosure of TDRs.

MBA notes that the exposure draft for the Proposed Update is being circulated only by the FASB and not the International Accounting Standards Board (IASB). Although TDRs are not on the IASB's agenda, the IASB and the FASB are working on a converged standard for impairment measurement of financial instruments. As discussed more fully in our response to Question 3 (below), some elements of the Proposed Update conflict with the FASB's current proposal on impairment of financial instruments. Therefore, MBA recommends that the TDR exposure draft be withdrawn and re-considered after the converged guidance on impairments has been developed. This would prevent preparers from converting to guidance which may ultimately conflict with the converged international standard on impairment.

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<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, Wall Street conduits, life insurance companies and others in the mortgage lending field. For additional information, visit MBA's Web site: [www.mortgagebankers.org](http://www.mortgagebankers.org).

## Background

Under the amendments in the Proposed Update, a creditor would be precluded from using the debtor's effective rate test in its evaluation of whether a restructuring constitutes a TDR. In addition, the following would apply:

1. If a debtor does not otherwise have access to funds at a market rate for debt with similar risk characteristics as the restructured debt, the restructuring would be considered to be at below a market rate and therefore should be considered a TDR.
2. A restructuring that results in a temporary or permanent increase in the contractual interest rate cannot be presumed to be at a rate that is at or above market.
3. A borrower that is not currently in default may still be considered to be experiencing financial difficulty when payment default is considered "probable in the foreseeable future."
4. A restructuring that results in an insignificant delay in contractual cash flows may still be considered a TDR. That is, that factor should be considered along with other terms of a restructuring to determine whether a TDR exists.

## General Comments

### Exacerbating Diversity In Practice

The reason for the Proposed Update, as stated on page one of the draft, is:

"Several stakeholders have raised concerns about diversity in practice related to identifying troubled debt restructurings. Those stakeholders suggest that additional guidance may be necessary to assist creditors in determining whether a restructuring of a receivable meets the criteria to be considered a troubled debt restructuring . . ."

MBA notes that the FASB guidance for creditor TDR accounting has been supplemented by the AICPA's Center for Audit Quality issued *Application of Statement 114 to Modifications of Residential Mortgage Loans That Qualify as Troubled Debt Restructurings*, issued in December 2008, as well as guidance from the bank regulators. From the Proposed Update's purpose statement, we presume the FASB intends to enhance, not change, existing TDR guidance. We note, however, that some proposed statements are inconsistent with existing guidance as well as guidance

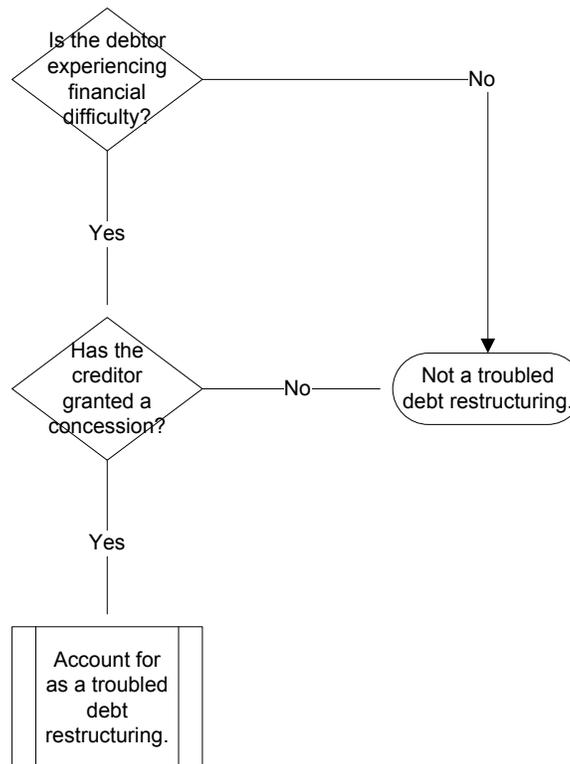
Technical Director of FASB  
December 10, 2010  
Page 3 of 8

issued by the AICPA and the bank regulators. Further, we believe the proposed guidance may increase diversity in practice for TDR accounting. Additionally, MBA believes that the Proposed Update may create additional situations in which there are zero reserves for modified loans as, under the Proposed Update, loans may be classified as TDRs but not require an allowance for credit losses.

Alternatively, if the FASB intends to change TDR accounting guidance, we do not agree with some of the proposed changes.

### The Proposal May Impact the Ability to Apply the Two-Step Decision Process

Existing guidance calls for a two-step process in determining if a loan modification is a TDR. The chart below depicts that process under current accounting rules:



We believe the two criteria: 1) a debtor experiencing financial difficulties, and 2) a creditor granting a concession, adequately capture the principles which should be applied in determining a TDR. Furthermore, these principles can be applied regardless of the terms under which a loan is restructured. We believe most creditors understand how to assess a borrower's status for financial difficulties and understand the nature of a concession.

Technical Director of FASB  
December 10, 2010  
Page 4 of 8

We agree with the proposal to include within creditor TDR guidance the indicators of TDRs described in *Determining Whether a Debtor's Modification or Exchange of Debt Is within the Scope of FAS Statement No. 15* (the former EITF 02-4). The proposed paragraphs 310-40-55-10A and 310-40-55-10B have been used by creditors as examples of conditions under which a TDR may or may not occur. However, as discussed below, we disagree with several of the other provisions in the Proposed Statement.

### **Proposed Changes That Do Not Aid in the Determination of a TDR**

We disagree with the proposed paragraph 310-40-15-8A which states: "If the debtor does not otherwise have access to funds at a market rate for debt with similar risk characteristics as the restructured debt, the restructuring would be considered to be at below a market rate and therefore should be considered a troubled debt restructuring." As stated, this appears to introduce a new criterion in determining a TDR requiring that a creditor determine a debtor's ability to obtain a market-rate loan from another party and, absent evidence of the debtor's ability, a TDR exists. MBA agrees that access to funds at a market rate may be one indication of a debtor's financial difficulty; however, we do not agree that this criterion alone is compelling or determinative of a TDR.

A debtor may not be able to obtain a market rate loan due to constriction in the credit market or due to the perceived value or liquidity of the loan or underlying collateral. For example, few lenders are currently originating Alt-A, subprime and jumbo residential mortgage loans. So, there is no "price list" to access to determine a market rate for these new residential loans. The absence of an observable market rate for a loan product is not indicative of financial troubles on the part of the debtor; rather it is the result of current market conditions. For commercial mortgages, creditors generally focus on the underlying collateral, not the debtor, so it would be impossible to determine the commercial market's assessment of a debtor-focused rate. Also, a commercial loan is priced based on a creditor's individualized assessment of adequate compensation for the credit risk associated with that specific collateral, and what one creditor requires as a market rate may differ from another creditor. Again, a possible difference in market rates among creditors is not an indication that the debtor is experiencing financial difficulties.

MBA also believes that the proposed statement would not be operational. Although a creditor may be able to assess whether a debtor is experiencing financial difficulties and determine that a concession has been granted, the creditor may not be able to provide evidence of a specific market rate for the loan. Alternatively, if a creditor has lowered the rate on the restructured loan, the creditor may have given up economic value and may, as a result, have granted a concession. A focus exclusively on market rates ignores other available evidence in determining whether a concession has been granted and is also inconsistent with existing impairment guidance in ASC 310-10

Technical Director of FASB  
December 10, 2010  
Page 5 of 8

which requires that impairment be measured based on a loan's effective rate, not its market rate.

We propose that the statement in paragraph 310-40-15-8A be revised to: "One indication of a troubled debt restructuring is a debtor's inability to access funds at a market rate for debt with similar risk characteristics as the restructured debt." We further propose that this statement be included in the list of financial difficulty indicators in the proposed paragraph 310-40-55-10A as it is one possible indication of financial difficulty which must be assessed along with other factors. An available market rate would be considered in conjunction with other factors in determining a TDR. In addition, the guidance should state: "If the effective rate on the restructured loan is commensurate with the credit characteristics and risk for that loan, taking into consideration all relevant factors including, but not limited to, additional collateral, guarantees, loan covenants and other factors, the modification of the rate is not considered a concession by the creditor."

MBA also disagrees with the proposed 310-40-55-10C which states: "A restructuring that results in an insignificant delay in contractual cash flows may still be considered a troubled debt restructuring. That is, that factor should be considered along with other terms of a restructuring to determine whether a troubled debt restructuring exists." MBA strongly disagrees with this proposal. Rather, MBA believes TDR guidance should be consistent with the other existing guidance, particularly ASC 310-10-35-10 which states: "...a creditor need not consider an insignificant delay or insignificant shortfall in amount of payments..." and disagrees with the Board's analysis in the Proposed Update paragraph DC 7 which discounts the need for consistency in accounting standards. An insignificant delay in cash flows should not scope a loan into a TDR evaluation. This approach is consistent not only with other FASB guidance but with industry practice and with the Office of Comptroller of the Currency guidance which allows short-term modifications to not be considered TDRs. Further, guidance which requires that a creditor examine each loan with insignificant delays in cash flows would create a tremendous operational burden.

### **The Consequences of the Proposed Statement**

We acknowledge that the language of the proposed 310-40-55-10C does not require that a loan experiencing only an insignificant delay in cash flows be classified as a TDR. However, discussions among industry participants, subsequent to the issuance of this proposal, indicate that many participants, including some auditors, regulators and users, believe that the proposed statement must be interpreted as any insignificant delay in cash flows, regardless of the existence of other factors, must be classified as a TDR. We believe clarification of the FASB's intent on this point is necessary. If the FASB intends that an insignificant delay in cash flows, absent other factors, indicates a TDR, we do not agree. The impact of such an interpretation would be that any

Technical Director of FASB  
December 10, 2010  
Page 6 of 8

payment plan, late payment, or any other very minor difference between the contractual terms of a loan and its actual performance, would result in a TDR.

The consequence of classifying a restructured loan as a TDR is that the loan must be measured for impairment under the current ASC 310-10-35 even though, in some circumstances, the restructured loan is not impaired. MBA points out that a loan with zero reserves under ASC 310-40-50 would not be subject to impairment measurement under ASC 450-20 and, as a result, would have no reserves.

Requiring insignificant delays in cash flows to be classified as TDRs exacerbates the non-impairment result as ASC 310-10-35-10 states: "...a creditor need not consider an insignificant delay or insignificant shortfall in the amount of payments..." when assessing impairment. As a result many loans could be classified as TDRs and, perhaps, would be accruing with no impairment reserves. MBA believes impairment measurement under ASC 310-10-35-10 should only occur if the loan is impaired and that the determination of a TDR should be de-linked from the impairment requirements. This approach would be more consistent with the IFRS approach which requires disclosures about modified loans and has separate guidance for the measurement of impairment. In addition, MBA recommends that the proposed guidance state that "a creditor need not consider an insignificant delay or insignificant shortfall in amount of payments when assessing whether a restructured loan is a TDR".

### **Transition Rules Are Flawed**

For purposes of measuring impairment of a receivable, the Proposed Update would be applied on a prospective basis. MBA agrees with this treatment. However, for purposes of identifying and disclosing TDRs, the Proposed Update would require retrospective application. Applying the proposed guidance to past transactions would be an extremely onerous and expensive task. For many preparers, it would be impossible to apply retrospectively, as preparers did not previously track or have access to market rates for loans such that they would not be able to evaluate historical restructurings under new standards. Furthermore, MBA does not believe the retrospective disclosure provides any useful information to financial statement users and MBA questions the cost/benefits of the retrospective proposal. Preparers are already required to disclose the amount of receivables and associated impairment allowance. Because the retrospective application proposal is only to identify TDRs, there would be no comparison between that proposed TDR information and any other amounts, such as allowance balances, within the financial statements. Therefore, MBA does not agree with the proposed retrospective disclosure requirement because it would provide no additional useful information to users of financial statements. MBA believes that the TDR-related disclosures included in ASU 2010-20 should be delayed to coincide with the implementation of any final guidance that results from the Proposed Update. See the MBA's letter submitted November 23, 2010 for further discussion on this point.

### Reponses to FASB's Specific Questions

**Question 1:** Would precluding creditors from applying the guidance in paragraph 470-60-55-10, create any operational challenges for determining whether a troubled debt restructuring exists? If yes, please explain why.

**MBA's Response:** Yes. See general comments, *Proposed Changes That Do Not Aid in the Determination of a TDR*, above for details of the operational challenges posed by the Proposed Update.

**Question 2:** Do you believe that the proposed changes to the guidance for determining whether a troubled debt restructuring exists would result in a more consistent application of troubled debt restructuring guidance? If not, please explain why.

**MBA's Response:** No. As discussed above, MBA believes several of the proposed statements are inconsistent with existing accounting guidance and, if issued, would serve to create additional confusion and diversity in practice.

**Question 3:** The Board decided that a creditor may consider that a debtor is experiencing financial difficulty when payment default is considered to be "probable in the foreseeable future." Do you believe that this is an appropriate threshold for such an assessment? If not, please explain why.

**MBA's Response:** MBA believes that evaluating whether a payment default is "probable in the foreseeable future" (emphasis added) is inconsistent with existing accounting guidance which requires that impairment is determined based on whether a loss is probable as of the reporting date and does not permit entities to consider future possible events. Likewise, the criterion of "probable in the foreseeable future" is inconsistent with the FASB's recent Financial Instruments exposure draft which proposed to eliminate the probable threshold and also to restrict preparers from considering future events when measuring impairment. For these reasons, MBA does not agree with the proposed criterion and recommends that the FASB reconsider the Proposed Update to TDR accounting guidance after converged criteria for impairment recognition and measurement has been developed in conjunction with the IASB.

**Question 4:** Are the proposed transition and effective date provisions operational? If not, please explain why.

**MBA's Response:** MBA believes that the proposed transition rules with respect to disclosures are not operational. See general comment *Transition Rules Are Flawed*, above for further details.

Technical Director of FASB  
December 10, 2010  
Page 8 of 8

**Question 5:** Should the transition and effective date be different for nonpublic entities versus public entities? If so, please explain why.

**MBA's Response:** MBA supports reducing the burden of onerous new accounting rules on small businesses, including non-public companies.

**Question 6:** Should early adoption of the proposed amendments in this Update be permitted? If so, please explain why.

**MBA's Response:** MBA is not opposed to permitting early adoption, but we believe it is unlikely that many reporting entities would elect an early adoption.

The MBA appreciates the opportunity to share these comments with the Board. Any questions about MBA's comments should be directed to Jim Gross, Associate Vice President and Staff Representative to MBA's Financial Management Committee, at (202) 557-2860 or [jgross@mortgagebankers.org](mailto:jgross@mortgagebankers.org).

Sincerely,



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