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November 23, 2016

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

File Reference No. 2016-340

Re: Proposed Accounting Standards Update, *Premium Amortization on Purchased Callable Debt Securities*

Dear Ms. Cospers:

Deloitte & Touche LLP is pleased to comment on the FASB's proposed Accounting Standards Update (ASU) *Premium Amortization on Purchased Callable Debt Securities*.

We support the FASB's proposal to amend the existing guidance on the application of the interest method to callable debt securities purchased at a premium. We believe that the proposed amendments represent a reasonable and practical short-term solution to the recognition of interest income on callable debt securities purchased at a premium.

Although we support the proposed ASU, the Board should consider adding a project that broadly addresses the application of the interest method to all interest-bearing financial assets and financial liabilities. The scope of such a project should include the measurement of interest income or expense on interest-bearing financial instruments that are recognized at fair value through earnings when an entity elects to separately report interest income or expense. The proposed ASU would require an investor to amortize premiums on purchased callable debt securities to the earliest call date, whereas under current U.S. GAAP, a debtor is generally required to amortize premiums or discounts on its issued debt securities over the contractual maturity. If the Board were to add a project to more fully address application of the interest method, it should consider whether this lack of consistency is aligned with the objectives, qualitative considerations, and concepts that guide the financial reporting of interest-bearing financial instruments. The Board may also consider how U.S. GAAP may be converged with international financial reporting standards.

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We have significant concerns about the clarity of scope of the proposed amendments. Those concerns are discussed in the appendix below, which contains our responses to the proposed ASU's questions for respondents.

* * * * *

We appreciate the opportunity to comment on the proposed ASU. If you have any questions concerning our comments, please feel free to contact Ashley Carpenter at (203) 761-3197 or Jonathan Howard at (203) 761-3235.

Yours truly,

Deloitte & Touche LLP

cc: Robert Uhl

Appendix
Deloitte & Touche LLP
Responses to Questions for Respondents

Question 1: *Do you agree that premiums on purchased callable debt securities should be amortized to the earliest call date? Please explain why or why not.*

Although we believe that the Board should consider adding a project that broadly addresses the application of the interest method to all interest-bearing financial assets and financial liabilities, we agree that the proposed amendments represent a reasonable and practical short-term solution to the recognition of interest income on callable debt securities purchased at a premium. However, we believe that before issuing the proposed amendments, the Board should consider clarifications to address the following matters:

- *Application to loans* — As written, the proposed amendments to ASC 310-20-35-33 would require premiums on purchased callable debt securities to be amortized to the earliest call date but would not require similar recognition for individual callable loan receivables¹ acquired or originated at a premium. The Board should consider whether it is appropriate for the interest income recognition guidance applicable to callable debt securities and callable loans to be different.
- *Application to asset-backed securities (e.g., mortgage-backed pass-through and similar securities)* — It is unclear whether the Board intends for the proposed amendments to apply to asset-backed securities (e.g., mortgage-backed pass-through and similar securities) whose prepayment is driven by call options held by borrowers of the underlying loans as opposed to a call option held by the legal entity that issued the debt security. The application of the proposed amendments to these types of debt securities could result in the immediate recognition into earnings of any premium paid on acquisition (assuming that the underlying assets are immediately prepayable). We suggest that the Board clarify that asset-backed securities for which only the underlying collateral is prepayable are not considered prepayable debt securities under the proposed ASU.
- *Application to debt securities that are callable at an amount other than par* — Certain debt securities are callable by the issuer for an amount other than par. For example, debt securities may be callable at fair value, at a fixed premium to par, or at an amount that includes a make-whole based on the present value of future interest payments. It is unclear whether the proposed amendments are applicable in these situations and, if so, when it is appropriate to amortize the premium to the call price. We believe that the Board should clarify the application of the proposed amendments to debt securities callable at an amount other than par.
- *Application to debt securities that are only partially callable* — Certain debt securities may be partially callable over various call dates. For example, a debt security may allow the issuer to call 25 percent of the outstanding principal amount on specified dates after the end of a “no-call” period. In these situations, the proposed

¹ That is, loans that are not part of a portfolio of a large number of similar loans for which prepayments are probable and the timing and amount of prepayments can be reasonably estimated.

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amendments could be interpreted to require an amount of the initial premium proportionate to the amount of the debt security that may be called at each call date to be fully amortized at such call date. However, the proposed amendments to ASC 310-20-35-33 are unclear. We suggest that the Board consider adding guidance to address these situations.

- *Application to debt securities that are contingently callable by the issuer* — It is unclear whether and, if so, how, the proposed amendments to ASC 310-20-35-33 apply to a debt security that is contingently callable by the issuer. We suggest that the Board clarify the application of the proposed guidance to contingently callable debt securities.
- *Application of the prepayment method in ASC 310-20-35-26* — On the basis of the proposed amendments to ASC 310-20-35-33, we believe that the Board intends to continue to allow entities to apply the prepayment method in ASC 310-20-35-26 in lieu of amortizing premiums on all purchased callable debt securities to the earliest call date. However, under the proposed amendments as currently drafted, confusion may exist as a result of the placement of the last sentence in ASC 310-20-35-33 and its reference to “loans” as opposed to “securities.” We suggest that the Board either amend the proposed edits to ASC 310-20-35-33 or include a discussion in the Basis for Conclusions that makes it clear that an entity that holds a large number of similar callable debt securities could elect to estimate principal repayments in its application of the interest method in accordance with ASC 310-20-35-26.
- *Interaction with the recognition of interest coupon payments* — The proposed amendments to ASC 310-20-35-33 only refer to amortizing premiums on purchased callable debt securities. When the stated interest coupon payments are level throughout the contractual term of a debt security, application of the interest method in accordance with the proposed amendments is relatively straightforward. However, callable debt securities may have uneven interest coupon payments during their contractual life (i.e., increasing fixed-rate debt securities, decreasing fixed-rate debt securities, or fixed-to-floating or floating-to-fixed debt securities). In these situations, we believe that if the debt security is callable at par, the proposed amendments are intended to require the callable debt security to be carried at an amortized cost basis equal to the par amount (or call price) at the earliest call date. However, we believe that to achieve this objective, the guidance should more clearly state that the debt security should be carried at the call price at the earliest call date. In addition, it is unclear how an entity would apply the proposed guidance to a debt security that is callable at other than par or has multiple call periods and is not called at the earliest call date. While ASC 310-20-35-18(a) partially addresses these considerations for callable debt securities that contain an increase in the stated interest rate during the term of the security, we believe that additional clarity is warranted to address the underlying interest income recognition principle for all callable debt securities with uneven interest coupon payments.

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Question 2: *How much time would be needed to implement the proposed amendments? Should entities other than public business entities be provided more time? Should early adoption be permitted?*

We believe that public business entities should be afforded at least a one-year period after the final issuance date to implement the proposed amendments. We also believe that it would be appropriate to allow entities other than public business entities an additional year in which to implement the proposed amendments, in a manner consistent with other recently issued ASUs. However, we refer you to the views of preparers on the estimated time needed to implement the proposed amendments.

We support allowing early adoption of the proposed amendments, especially if early adoption would be necessary for entities to apply the proposed amendments on the same date as that of initial application of FASB Accounting Standards Update No. 2016-01, *Recognition and Measurement of Financial Assets and Financial Liabilities*.

Question 3: *Do you agree with the proposed transition method and disclosures in paragraph 310-20-65-1(c)? Please explain why or why not.*

Yes, we agree with the proposed transition requirements in ASC 310-20-65-1(c).