

April 2, 2019

Russell Golden  
Chair  
Financial Accounting Standards Board  
401 Merritt 7  
P.O. Box 5116  
Norwalk, CT 06865-5116

**Re: Cumulative Expected Credit Loss (“CECL”) Impairment Model**

Dear Mr. Golden:

We note that tomorrow the Financial Accounting Standards Board (“FASB”) will be discussing the feedback they heard at the January 28, 2019 Public Roundtable Meeting to Discuss a Proposal Submitted by a Group of Banks to Consider an Alternative Approach to Presenting Expected Credit Losses on the Income Statement and Whether Gross Writeoffs and Gross Recoveries Should be Presented in the Credit Quality Disclosures Financial Instruments—Credit Losses (Topic 326) Measurement of Credit Losses on Financial Instruments.

CFA Institute,<sup>1</sup> has monitored the events leading up to the roundtable including:

- Reviewing the Fall 2018 comment letters of the Bank Policy Institute (“BPI”) and the American Bankers Association (“ABA”) to the Financial Stability Oversight Council (FSOC), FASB and SEC seeking a review of the systemic and economic risks they perceive are posed by the implementation of Accounting Standards Codification 2016 – 13 (ASC No. 2016-13 or the Standard), Measurement of Credit Losses on Financial Instruments; and
- Attending and observing the December 2018 U.S. House Committee on Financial Services subcommittee hearing, Assessing the Impact of FASB’s Current Expected Credit Loss (CECL) Accounting Standard on Financial Institutions and the Economy.

CFA Institute did not publicly comment on the aforementioned events prior to the roundtable. We are writing to reiterate our perspectives as expressed at that January roundtable

***If Impairment Approach is to Be Reconsidered, Investor Preferences Must Be Considered***

In the period subsequent to the 2008/2009 Great Recession, the FASB worked with the International Accounting Standards Board (“IASB”) to reach a converged solution to the accounting for financial instruments. As investors, we supported a converged solution because investing is global. The location of the registrant and the accounting required in the registrant’s jurisdiction does not change the economics of the underlying lending transactions being accounted and reported upon. We were extremely

---

<sup>1</sup> With offices in Charlottesville, New York, Washington D.C., Hong Kong, London, Brussels, Mumbai, Beijing and Abu Dhabi, CFA Institute is a global, not-for-profit professional association of more than 133,000 investment analysts, portfolio managers, investment advisors, and other investment professionals in 151 countries, of whom more than 162,000 hold the Chartered Financial Analyst® (CFA®) designation. The CFA Institute membership also include 151 member societies in 163 countries and territories.



disappointed by the FASB and IASB's decision to develop different accounting models for financial instruments broadly and impairment more specifically.

Our 2010 comment letter to the FASB provides a comprehensive analysis of our position in support of fair value accounting for financial instruments, rather than a mixed measurement model for accounting for financial instruments – including an impairment model. In our various correspondence at that time, we highlighted numerous investor surveys that backed our position in support of fair value.

At that time, those opposed to fair value – including those currently expressing their opposition to CECL – made the argument that fair value would create systemic and economic risks. These are the same arguments currently being made in objection to CECL. In the aforementioned 2010 comment letter, we outline our reasoning behind why fair value accounting, and accounting more broadly, do not create systemic risk. This same reasoning applies to CECL. Business decisions and economic cycles drive systemic and economic risk, not accounting standards. Accounting standards work to reflect the underlying economics in a neutral and faithfully representational manner.

We did not support the CECL model as it was being developed, because we didn't believe it reflected the economics of lending – that being that interest income is recognized, as are losses, over the risk bearing period. The CECL model, on the other hand, requires upfront recognition of losses. In our 2013 comment letter on impairments to the IASB and FASB, we noted that neither the FASB nor the IASB's proposed models (i.e. that became their final models) reflected the economics of lending and that neither were our preferred approach.

It is our view that the US GAAP model chosen was the preference of regulators not investors. When it became apparent that financial instrument fair values were only going to be disclosed, we were most supportive of the IASB's initial model that would recognize interest income and impairment losses through an adjustment to the effective yield over the life of an instrument. The IASB, like the FASB, ultimately chose a different approach.

Despite our view that neither the FASB nor IASB model reflected the economics of lending, the FASB and IASB during 2016 and 2014, respectively, issued their proposals in the Standard and IFRS 9, *Financial Instruments*, with scheduled effective dates in 2020 and 2018, respectively. The IFRS 9 impairment model has already been implemented in IFRS jurisdictions.

The FASB worked from 2009 to 2016 to develop the CECL impairment model. With nearly a decade spent developing and allowing financial institutions – and other entities with applicable financial instruments – to participate in its due process, the FASB issued this Standard in 2016 having provided ample opportunity for stakeholders to comment and present their perspectives on the CECL model. Further, the FASB has given public companies nearly four years to implement the Standard with a January 1, 2020 implementation date. Those currently opposing the CECL model, and proposing the alternative impairment approach, actively participated in the FASB's due process during the exposure period. Accordingly, it seems inconsistent for there to be a new assertion that the FASB's model is non-economic. As our 2013 letter highlights, this is not a new perspective requiring reconsideration of the CECL model. At this juncture, reconsideration of the fundamentals of the model is not productive as any change will likely require years to debate and implement.

Further it is our view, that should the FASB consider an alternative model they must reconsider the fair value model – the model we, as investors, supported at that time. The implementation of the CECL model, in our view, highlights that CECL is likely more subjective, less economically relevant and more procyclical than fair value. In fact, some organizations are considering the adoption of fair value for



certain financial instruments as it presents more value relevant information than the cost plus CECL impairment model for financial instruments.

### ***Prudential Regulation vs. Accounting Standard Setting***

Though we opposed the outcome of the FASB's due process, we respect the importance of independent standard-setting. The interests of all stakeholders, including investors, must be expressed as a part of an open and deliberative process – one best afforded by an independent standard setter such as the FASB. Ultimately, investors through the assessment of public companies pay for the FASB's standard-setting process and should have an open forum with opportunity to comment.

As the FASB has completed the due process on the Standard, and there are no new issues for reconsideration, we do not see a need for the FASB to reopen this issue and reconsider its conclusion – other than considering some disclosure enhancements as we highlight below. Further, because we respect the independent standard-setting process we do not see the need for regulators or Congress to engage in the accounting standard-setting process.

We want to reemphasize our long-held and expressed view that US GAAP financial statements – especially those of public companies – should not be the purview of prudential regulators. While investors certainly care deeply about solvency and prudential regulation, investors have an additional objective that includes determining and discovering the fair value of a company's shares. US GAAP financials are investors' predominate source of decision-useful information upon which to make investment decisions. While regulators have the authority to request and require any information necessary to meet their prudential objective, US GAAP financial statements filed with the SEC are meant for investors to make their investment decisions.

That said, we respect and recognize the implications of the CECL model on bank capital requirements – especially regional, medium and small-sized financial institutions. We believe this is an issue best addressed by the banking regulators with a solution outside of the GAAP financial statements. A proposal that requires the majority of the CECL reserves to be booked to equity for US GAAP so that it can be adjusted for prudential regulatory filings has the effect of further reducing the decision-useful information content of US GAAP financial statements for investors.

Our view is that if accommodations are needed for the capital requirements of such financial institutions, the regulators can make further accommodations in regulatory filings.

### ***Alternative Approach Considerations***

As we reviewed the alternative impairment proposal being proposed by the banks participating in the roundtable, and as we engaged in the roundtable discussion, it became apparent there are a plethora of conceptual and implementation considerations to be evaluated in deliberating this proposal, including but not limited to:

- How precisely the twelve-month impairment amount would be derived/computed;
- The movement of amounts recognized in equity into the income statement relative to the previous twelve-month impairment charge;
- The need for two allowance accounts: one allowance related to the amounts recognized in the income statement and another for amounts recognized in equity. There will also need to be a rollforward of each allowance illustrating the relationship between the rollforwards and the financial instruments to which they relate;
- The relationship between actual charge-offs and the impairments recognized in the income statement and equity;
- The income statement presentation of the twelve-month impairment versus any further credit deterioration reflected in the expected losses recognized in equity;



- The disclosures necessary to explain the amounts recognized in the income statement versus the amounts recognized in equity and the actual development of expected losses on amount recognized in equity including the relationship to amounts recognized in the income statement;
- What the amounts recognized in the income statement represent relative to the prior US GAAP incurred loss impairment approach and the IASB impairment charge.

These are just a few of the considerations that came to mind quickly during the roundtable discussion. The devil will be in the details and the relationship between amounts recognized in income and equity will likely create recycling complexities.

We know from our investor outreach that investors pay substantially less attention to amount recognized in other comprehensive income relative to amounts recognized in net income. Recent comments regarding Berkshire Hathaway's recognition of the fair value of equity securities in net income rather than other comprehensive income highlights this point. As such, an alternative impairment model that will likely recognize lower impairment amounts in net income than the existing US GAAP impairment model seems inconsistent with the ultimate objective of the financial instruments impairment project which was to address the "too little too late" aspects of the existing US GAAP impairment model – that investors and others saw play out during the Great Recession.

### ***Disclosures***

Towards the end of the roundtable there was a discussion of the need to improve disclosures regarding the development of expected losses recognized in the CECL model with cumulative – rather than current period loss amounts. As investors participating in the roundtable highlighted, we believe these are important improvements that should be made to the Standard, if not before January 1, 2020 then over the next 1-2 years.

### ***Overall***

Overall, we recognize the very real capital issues faced by regional, medium and small banks as it relates to the adoption of the new CECL model and, as our 2013 comment letter highlights, we recognize the non-economic implications of recognize all credit losses at inception. That said, we believe the bank regulators should address these issues rather than the FASB amending the impairment model in a way that will likely further reduce the decision-usefulness of US GAAP financial statements.

\*\*\*\*\*

If you or your staff have questions or seek further elaboration of our views, please contact Sandy Peters by phone at +1.212.754.8350 or by email at [sandra.peters@cfainstitute.org](mailto:sandra.peters@cfainstitute.org).

Very truly yours,

*/s/ Sandra J. Peters*

Sandra J. Peters  
Head, Global Financial Reporting Policy Advocacy  
CFA Institute

cc:

Wesley Bricker  
Chief Accountant  
Securities and Exchange Commission