May 31, 2013

Ms. Leslie Seidman
Chairman
Financial Accounting Standards Board
401 Merritt 7, P.O. Box 5116
Norwalk, CT 06856
director@fasb.org

RE: Don Cohenour – Comments on Proposed Accounting Standards Update: Financial Instruments—Credit Losses; File Reference No. 2012-260

Dear Ms. Seidman:

On behalf of the 1.3 million credit union members, the Missouri Credit Union Association (MCUA) would like to take this opportunity to express our views regarding the Financial Accounting Standards Board's (FASB) Proposed Accounting Standards Update on "Financial Instruments – Credit Losses (Subtopic 825-15)."

MCUA has reviewed FASB's proposal in detail, and opposes the proposal in the strongest terms. We believe the proposal would harm the credit union system as a whole and impose unintended and serious consequences on credit unions, credit union members, and the wider economy. Further, we believe the current system of reporting is functional, cost-effective, and delivers meaningful information to all stakeholders in the credit union system.

Credit unions are different and distinct from other financial institutions. They are not-for-profit financial cooperatives owned by their member-depositors. Credit unions promote thrift, provide credit, and offer other consumer and small business financial services to their members and communities at a favorable cost or rate of interest. We highlight these distinctions to illustrate our belief that credit union financial statements and financial reporting should reflect the unique characteristics of credit unions. If forced to conform to accounting standards that are more appropriate for publicly-traded banks and other investor-owned companies, those standards will impose significant costs and hardships on credit unions and their communities with no offsetting benefit.

Proposal Overview

Most credit unions generally recognize credit losses when such a loss is considered "probable." Credit unions maintain reserves in their allowance for loan and lease losses (ALLL) accounts based on historical loss data, cash flow calculations and qualitative and environmental factors, reflecting expectations of losses and losses that have been incurred and will be charged-off during the next 12 months after the last reporting period.

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FASB's proposal would require an estimate of the present value of cash flows associated with all loans and other assets that are not expected to be collected over the life of the loan or asset. To formulate the estimate, past events, current conditions, historical loss experiences, the borrower's credit worthiness, forecasts of expected credit losses and predictions about the economy would be calculated and evaluated. Credit loss reporting could not be based solely on the most likely outcome, even though financial reporting on that basis seems to be reasonable and rational.

We believe credit union members and regulators are not interested in credit loss estimates based on subjective projections of cash flows. In fact, such projections may raise the legitimate question (among members) of why the credit union is making the loan in the first place if the credit union projects that payments will not be made! Credit union members and regulators (and management) are interested in and fully familiar with reasonable analysis of the performance of loans and investments based on analytical components, such as under the current incurred loss model, and the extent to which the credit union has provisioned its ALLL account to reflect loan nonperformance.

The rationale for the proposed changes is that the current impairment methodology does not allow for the timely recognition of credit losses. We are not aware of empirical evidence to support this concern for credit unions generally. The vast majority of natural-person credit unions have been able to deal with credit impairment using the present incurred loss approach. NCUA's Inspector General's material loss reviews support a conclusion that there was a misapplication of the current incurred loss methodology by those credit unions which experienced losses in connection with the recent financial crisis, not a need for a new approach for credit unions.

The recent financial crisis and its fallout were and are extreme events. Mainstream financial professionals did not adequately forecast such events. We are unconvinced the proposed changes will be effective at preventing credit losses in credit unions resulting from such circumstances. Accounting practitioners will be involved in or responsible for preparation of reports that comply with the proposed approached. Accordingly, we raise the following question: are accounting practitioners able to predict the extent and timing of the type and scope of credit and other events that lead to losses, extreme or otherwise, in loan and investment portfolios?

Potential Impact of Proposal

Credit unions would be required to recognize current loss expectations in their ALLL accounts on the balance sheet. Thus, the proposed changes would likely cause an immediate and drastic increase to the ALLL accounts of credit unions. This increase could double or even triple current ALLLs, and would result directly in a reduction of retained earnings for many credit unions.

Decreased retained earnings could lead to a lower net worth ratio, which could trigger prompt corrective action (PCA) implications for numerous credit unions that currently do not have PCA concerns.

The MCUA is also concerned that the proposed current expected credit loss (CECL) approach could result in more volatility in reported earnings due to quarterly adjustments in expected loss projections. Credit unions could take large one-time charges at the first sign of distress in their loan portfolios, and then look for opportunities to smooth earnings over time through reserve releases or reverse provisions.

Ultimately, the proposed changes could result in consolidation of credit unions for those that have difficulties in complying with these changes. Obviously, such a result would affect not only the members of those credit unions directly involved, but would reduce consumer financial options in the larger financial services marketplace.

Unfortunately, no one knows if these concerns would materialize; the problem is that no one knows for sure that they will not.

However, one certain result of the proposed changes is that credit unions will have to expend extensive financial and technical resources to even begin to comply, particularly to be able to forecast future credit losses. The costs of any such expenditure will be borne by credit unions' member-owners.

Additional Challenges & Impediments to Compliance

The CECL model requires credit unions to predict the extent and timing of future impairments. Making such loss predictions with any degree of accuracy will be extremely challenging, even for those credit unions with adequate data sets and modeling capability. Inherently, credit loss predictions for the life of a loan will be affected by the assumptions made by and the subjectivity of credit union management.

Credit unions maintain data similar to what will be necessary under the proposal, but most do not have access to data with sufficient detail to forecast future events. Static statistical models cannot be used per the proposal, so credit unions will not be able to apply a statistical process to loan portfolios to estimate future expected losses. Thus, at the end of a month or quarter, a credit union must look at its portfolio at that time and attempt to determine how its loss projections will vary in the future.

Most credit unions (and in particular, smaller credit unions) use models that involve homogenous loan pools and application of historical loss ratios and environmental loan factors. The models considered in the proposal are much more complex; they will therefore require significantly more resources for purchase/development and ongoing operation. This will have a major impact on smaller credit unions that are pressed to meet their internal reporting deadlines under the current credit losses standards.

We expect audit fees to increase. The proposed changes will require credit unions to obtain costly core enhancements. Finally, we do not believe these added costs will result in a commensurate benefit.

The proposed CECL model is inconsistent with the accounting principle of matching. The proposal requires expected future loan losses to be recorded immediately.

Potential Impacts Beyond Credit Unions

MCUA is very concerned that the proposal will have a chilling effect on lending in general. The proposed changes could result in credit unions overestimating losses and over-reserving ALLL accounts, at least initially. To avoid the appearance of increasing losses and having to unnecessarily maintain increasing ALLL accounts, credit unions may tighten their loan standards and may even be encouraged to do so by examiners. Such a result could discourage credit unions from providing loans to borrowers that are marginally risky and reduce availability of credit in the economy.

MCUA Urges FASB to Withdraw the Proposal

The FASB proposal has raised numerous concerns within the credit union system. These proposed far-reaching changes will likely severely impact all financial institutions, but especially credit unions. We do not believe FASB intended that negative outcomes for credit unions and beyond to their members and communities would result from these proposals; accordingly, we respectfully request that FASB withdraw the current proposal as issued.

As always, we appreciate the opportunity to respond to FASB. We will be happy to discuss our concerns with the proposal and respond to any questions regarding these comments.

Sincerely,

Don Cohenour
President