



October 27, 2008

Delivered via email: rule-comments@sec.gov

Ms. Florence Harmon, Acting Secretary
Securities and Exchange Commission
100 F Street NE
Washington, DC 20549-1090

File Reference: File No. 4-573 Fair Value Accounting

Dear Ms. Harmon:

U.S. Central is a not-for-profit, cooperative wholesale credit union. As a cooperative, we are owned by our members, without outside investors. We are not an SEC registrant, and yet increasingly find ourselves adversely affected by SEC actions.

My comments herein are derived from the more detailed letter (a copy of which attached) that we submitted to the FASB on October 9 in response to its request for comments for FSP FAS 157-3. Our view is similar to approximately half of the 102 comment letters submitted. It is also similar to the views expressed by Messieurs Tisch, Price and Cotton at the July 9 SEC Roundtable on Fair Value Accounting. To summarize our view:

- SFAS 157 defines fair value as the exchange price in an orderly transaction between market participants. It is not intended to represent forced sales. And yet, FASB's requirement for an excessive liquidity risk premium, as indicated by the example provided in FSP 157-3, memorializes the current distressed market conditions – and their resulting fire-sale prices – in the calculation of fair value.
- The pendulum has swung too far from entry price to exit price. There is something in-between—the holding value of a debt security as part of an asset/liability matching strategy. For longer-term investors, the highest and best use of an asset does not usually involve selling it. Marking to fire-sale prices is essentially a liquidation value which contravenes a basic premise that financial statements are prepared as if the entity is a going concern.
- SFAS 115 as written is no longer followed. Subsequent interpretations have radically changed the previous flexibility afforded by SFAS 115 to the available-for-sale (AFS) designation. Now, an investor in an unrealized loss position on AFS securities must make essentially the same representations on intent and ability as for held-to-maturity (HTM) securities. Otherwise, the investor faces draconian other-than-temporary impairment charges.

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The solution is simple. It parallels the treatment for loans, which are either held for sale or held for investment. Debt securities held for sale—whether they are classified as trading or AFS for which the investor cannot represent intent and ability to hold to recovery—should be valued at relevant market prices. In today's dislocated market, this includes the extreme liquidity risk premium in the FASB's example.

But for debt securities for which the investor has represented intent and ability to hold (either HTM or AFS as currently interpreted), using fire-sale prices is contrary to the going concern presumption. HTM debt securities should continue to be held at amortized cost. But if other-than-temporary charges are required, the write-down should be based on realizable value, not a fire sale exit price. AFS securities for which the investor represents intent and ability to hold to recovery should be adjusted for credit risk if necessary, but should not include the extreme liquidity risk premium of the FASB's example.

This change would align the accounting treatment with the underlying economics and more accurately represent the financial conditions of the reporting entity. Thank you for the opportunity to comment on this crucial issue.

Sincerely,

A handwritten signature in black ink, appearing to read "Kathryn E. Brick". The signature is fluid and cursive, written over a horizontal line.

Kathryn E. Brick
Senior Vice President and Chief Financial Officer
913.227.6159
kbrick@uscentral.coop

Attachment



October 9, 2008

Via Email: director@fasb.org

Mr. Russell G. Golden
FASB Technical Director
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5166

File Reference: Proposed FSP FAS 157-d

Dear Mr. Golden:

U.S. Central Federal Credit Union (“U.S. Central”) appreciates this opportunity to comment on the proposed FASB Staff Position No. FAS 157-d, *Determining the Fair Value of a Financial Asset in a Market That Is Not Active* (the “Proposed FSP”).

U.S. Central is a wholesale corporate credit union providing investment and financial products and services to its 26 member corporate credit unions. U.S. Central and its corporate credit union members comprise the Corporate Credit Union Network, which provides investments and financial products and services to the nation’s more than 8,000 natural person credit unions. U.S. Central, as a primary liquidity provider to the Corporate Credit Union Network, manages a balance sheet of approximately \$40 billion, with a higher proportion of assets invested in marketable debt securities than most financial institutions of a similar size. With sizable holdings of non-agency residential mortgage-backed securities, we are particularly interested in the discussions surrounding the determination of fair value for these instruments in today’s illiquid market.

The examples included in the Proposed FSP are helpful in understanding mechanically how the FASB views the determination of fair value pursuant to SFAS No. 157. However, given the unprecedented market conditions of the last 15 months, simply clarifying the mechanics of fair value determination is not enough. In summary, the Proposed FSP should address the following suggested changes to the definition of fair value:

1. For available-for-sale (AFS) securities where the investor has demonstrated the intent and ability to hold to recovery, the FSP should allow the severe liquidity risk premiums of the current market environment to be adjusted to levels observed during periods of normal market activity for the determination of fair value. Credit risk premiums should continue to be based on the best available information from market participants.

2. The FSP should amend the definition of fair value for held-to-maturity (HTM) securities to approximate realizable value. This is of great importance when determining the amount of potential other-than-temporary impairment (OTTI) charges. Such a change would place investors in HTM debt securities on equal footing with entities that hold loan portfolios for investment. Securitized loans should not be treated differently than unsecuritized loans when the intent and ability to hold to maturity is present in both cases.
3. If suggestion 2 above is viewed as unacceptable by the Board, the FSP should, at a minimum, allow the severe liquidity risk premiums of the current market environment to be adjusted in the determination of fair value for HTM securities to levels observed during periods of normal market activity – as discussed in proposal 1 above for AFS securities for which the investor has the intent and ability to hold to recovery.

In light of the unprecedented market conditions that currently exist, it is imperative that FASB adopt these or similar revisions for the calculation of fair value. Our rationale for the requested changes is set forth below.

Are current severe liquidity risk premiums reflective of fair value?

Paragraph 5 of SFAS No. 157 defines fair value as “...*the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.*” Paragraph 7 continues as follows: “*A fair value measurement assumes that the asset or liability is exchanged in **an orderly transaction** between market participants to sell the asset or transfer the liability at the measurement date. An orderly transaction is a transaction that assumes exposure to the market for a period prior to the measurement date to allow for marketing activities that are usual and customary for transactions involving such assets or liabilities; **it is not a forced transaction (for example, a forced liquidation or distress sale).** The transaction to sell the asset or transfer the liability is a hypothetical transaction at the measurement date, considered from the perspective of a market participant that holds the asset or owes the liability. Therefore, the objective of a fair value measurement is to determine the price that would be received to sell the asset or paid to transfer the liability at the measurement date (an exit price).*” (Emphasis added.)

Based on the SFAS No. 157 definition of fair value, it must be determined whether or not a transaction conducted at a price that includes a severe liquidity risk premium, such as is the case in the current dislocated market, represents an “orderly transaction.” While it may be true that the price a seller would receive under current market conditions would include such a liquidity risk premium, a seller would only accept such a liquidation value if it had no other options (*i.e.*, it was a forced sale). To sell at such a level willingly, when the amount the investor would expect to collect if it held the security was significantly higher, would not be logical. Therefore, sales at levels that include the severe liquidity risk premiums present in the current illiquid market do not represent “orderly transactions.” As a result, unusually high liquidity risk premiums in an inactive market represent liquidation values, not fair values.

When is exit price an appropriate reflection of fair value?

For investment securities classified as trading under SFAS No. 115, exit price represents the most appropriate indication of fair value. Given that trading assets may very well be sold in the near term, the financial statements of the investor should reflect the best available estimate of what would be received upon sale – even though such a determination is a highly judgmental process in today’s environment. However, for securities classified as AFS, exit price is not always the most appropriate indication of fair value.

Under the current consensus interpretation of the OTTI guidance, investors with securities in unrealized loss positions must demonstrate their intent and ability to hold the positions to recovery, which in some cases, may be maturity. Otherwise OTTI charges must be recorded. If an investor has demonstrated such intent and ability to hold the security, an exit price that incorporates a severe liquidity risk premium resulting from unprecedented market inactivity is not relevant. Certainly liquidity risk premiums in active markets are appropriate components of fair value determinations and vary depending on the particular asset class. However, it is unreasonable to reflect the dramatic increase in these risk premiums under completely illiquid market conditions – particularly if the entity has demonstrated the intent and ability to hold the related assets.

Accordingly, AFS securities should be separated into two groups: those for which the investor has demonstrated its intent and ability to hold to recovery and those for which the investor has not. AFS securities for which the investor has not demonstrated its intent and ability to hold to recovery should be valued at the best available estimate of exit price, similar to trading securities. For those AFS securities with respect to which the investor has demonstrated its intent and ability to hold to recovery, an adjustment should be made to the liquidity risk premium to reflect more normal market conditions. In both cases, fair value should continue to incorporate the best available estimate of credit risk premium.

The concept of exit price presents the same distortion of fair value with regard to securities classified as HTM. While HTM securities are not carried on the balance sheet at fair value, when an unrealized loss is considered to represent an other-than-temporary impairment, it must be written down to fair value. In the current illiquid market environment, there is a material difference between realizable value - based on expected principal and interest cash flows - and an exit price determination of fair value. Overstating losses using exit value, only to later recognize gains as the securities pay their expected cash flows, does not result in “fairly presented” financial statements. A portfolio of loans held-for-investment similar to those underlying the security would be accounted for at realizable value through the process of loan loss reserving. As such, investors in debt securities are penalized relative to holders of unsecuritized loans.

At an absolute minimum, the extreme liquidity risk premium in today’s market must be adjusted to more normal levels when determining the fair value of HTM securities for OTTI recognition.

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Summary

The Proposed FSP should distinguish between assets for which the investor has demonstrated the intent and ability to hold to recovery or maturity (some AFS and HTM) and those for which the investor has not (remaining AFS and trading). Where the investor has not demonstrated such intent and ability, exit price represents an appropriate representation of fair value. Where the investor has demonstrated the intent and ability, changes in the determination of fair value are required for a fair presentation of financial statements. The extreme liquidity risk premium must be removed from the determination of fair value for AFS securities while fair value for HTM securities should approximate realizable value.

If you would like to discuss any of the points we have raised, please feel free to contact Chief Financial Officer Kathy Brick (913-227-6159) or Director of Finance Doug Hoelscher (913-227-6091).

Sincerely,

A handwritten signature in cursive script, appearing to read "Francis Lee".

Francis Lee
President & CEO