



December 13, 2010

VIA ELECTRONIC FILING

Leslie F. Seidman
Acting Chairman
Attention: Technical Director
File Reference No. 1880-100
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-6116

Re: *Clarifications to Accounting for Troubled Debt Restructurings by Creditors, File Reference No. 1880-100*

Dear Mrs. Seidman:

The Commercial Real Estate (CRE) Finance Council appreciates this opportunity to provide comments on the proposed Accounting Standards Update, *Clarifications to Accounting for Troubled Debt Restructurings by Creditors* (the “TDR Exposure Draft”). The CRE Finance Council is the collective voice of the entire commercial real estate (“CRE”) finance market, including investors such as insurance companies, pension funds, and money managers; portfolio and CMBS lenders, ratings agencies; accounting firms; servicers; and other service providers.

Because our membership consists of all constituencies across the entire CRE finance market, the CRE Finance Council has been able to develop comprehensive responses to policy questions which promote increased market efficiency and investor confidence. Our members provide practical advice to policymakers at all levels on measures designed to restore liquidity and facilitate lending in the commercial mortgage market and have been extremely influential in helping to develop programs such as the Term Asset-Backed Securities Loan Facility. CRE Finance Council members have frequently been called on to testify at Congressional hearings on the state of the CRE market, financial regulatory overhaul measures, and proposed accounting standards.

Thus, we have a distinct perspective on the challenges facing the \$3.5 trillion market for commercial real estate finance and the need to craft policy measures that support, rather than

undermine, the recovery of the commercial real estate sector and that of the nation's economy as a whole.

To that end, the CRE Finance Council has played a leadership role in the development of standardized practices and in ensuring transparency for the commercial real estate finance industry, such as through our Investor Reporting Package (IRP), which we independently developed and implemented. The Securities and Exchange Commission recently acknowledged the extensive work done by CREFC on the IRP, through its proposed revisions to Regulation AB. The IRP provides a wealth of standardized information to investors and has been so successful in the commercial space that it is now serving as a model for the residential mortgage-backed securities market. Importantly, CREFC is currently working with market participants to make further improvements to the IRP which will provide a mechanism for reporting on troubled loans which are modified. Furthermore, and in light of the recent economic crisis, CREFC has set up three task forces that are working to create increased transparency and disclosure to commercial mortgage backed securities (CMBS) investors, enhanced mortgage loan underwriting standards and industry standards for representations and warranties pertaining to mortgage loan sales.

Given our unique perspective on both the challenges facing the commercial real estate market and our commitment to policy reform, our comments and observations on the FASB's Proposal will remain focused on our core competency, the commercial real estate finance market.

I. OVERVIEW

Approximately \$1 trillion in CRE loans are scheduled to mature over the next several years. Given the decline in CRE asset values, many of those loans will require additional "equity" contributions in order to refinance. We do believe investors are available to provide the needed funds. Further, we are starting to see a revitalization of the CRE finance marketplace. Insurance companies, community and regional banks and the GSEs have provided most of the CRE finance closed in 2010, but the marketplace has also seen \$9.2 billion of new CMBS issuance this year with up to \$35 billion in issuance projected in 2011.

In an environment where lenders, legislators and financial regulators are striving to improve the quality of loan underwriting and information transparency, we suggest that the absence of certainty in our regulatory and accounting frameworks would create a significant obstacle to the return of a healthy real estate capital market.

Therefore, although we welcome the FASB's efforts to create a comprehensive approach to identifying restructurings that constitute troubled debt restructurings, we are concerned that the TDR exposure draft does not achieve this objective but will instead cause additional confusion and diversity in practice.

CRE Finance Council strongly believes that the FASB and IASB's efforts to converge accounting standards should be the FASB's focus prior to enhancement of guidance on troubled debt restructurings. We note that the TDR exposure draft is being circulated by the FASB, while it is not currently on the IASB's agenda. At the same time, we note that the FASB and IASB are working on an updated impairment model, which may either conflict with or override the TDR exposure draft. We believe that in this age of global markets and investing, a single, high-quality standard for

accounting is critical to facilitating the cross-border movement of capital. We do not support a non-converged approach as we believe this will only create confusion in the marketplace. Therefore, we would request that FASB and IASB complete their work on an impairment model prior to enhancing guidance for troubled debt restructurings.

However, if the FASB deems it necessary to move forward with the TDR exposure draft, the following are our specific comments and recommended enhancements to the proposal as they relate to commercial real estate:

II. Market Rate Focus

The CRE Finance Council is concerned that while the TDR exposure draft's market rate focus for identifying troubled debt restructurings may work for more homogeneous asset classes, it causes significant challenges for the commercial real estate finance marketplace. Specifically, while the Council agrees that the inability to access to funds at a market rate may be one indication of a debtor's financial difficulty, we do not believe that a specific market rate focus will be able capture what is significant in both understanding and determining a commercial real estate troubled debt restructuring for financial statement users and preparers. Furthermore, due to the heterogeneous nature of commercial real estate assets, it would be nearly impossible to compare one market rate to another since they may vary significantly depending upon the nature, location and age of the real estate.

The commercial real estate marketplace is made up of diverse and heterogeneous loans, such as office buildings, hospitals, retail centers, hotels and industrial complexes as examples. Additionally, commercial mortgages have different terms (generally 5-10 year "balloon" loans) than more homogenous asset classes, and they are, in the vast majority of cases, non-recourse loans that allow the lender to seize the collateral in the event of a default. Furthermore, unlike consumer borrowers, commercial borrowers are highly sophisticated businesses with cash flows based on business operations and/or tenants under leases. The leases are with tenants of differing credit quality, operations, terms, etc. thus adding different credit risk considerations for each property.

The Board clarified in the Proposal that 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 below a market rate, and thus would be considered a troubled debt restructuring.

For CRE lenders, an increase in rate to market on a loan extension to a borrower is less significant than having the flexibility to manage the terms of the restructure to best reduce credit exposure due to the fact that most, if not all, debt is non-recourse. From this perspective, CRE lenders are focused more on the value of the assets collateralizing the loan and the creditworthiness of the tenants rather than on the borrower itself. Therefore, CRE lenders restructure loans in order to reduce their credit risk exposure throughout the term of the loan extension.

More specifically, CRE lenders work to ensure that they remain whole financially on the debt by taking into consideration **all** terms being changed. Recently, CRE lenders have worked to reduce credit exposure with debtors by means other than cash pay-downs. Specifically, CRE lenders may, for example; require a debtor to provide additional collateral and/or implement capital improvements

in a property in exchange for extended repayment terms at a rate that may be considered lower than a market. These restructurings allow the CRE lender to remain whole from a fair market value perspective by maintaining if not reducing their credit exposure over the extended term.

Accordingly, the CRE Finance Council would recommend that the FASB consider that the TDR guidance in ASC 310-40-15-8A be revised to allow commercial real estate lenders the flexibility to use not only market rate but also allow lenders to consider other structure added to the loan such as more collateral, improved collateral, cash flow sweeps, etc. This recommendation would also be consistent with Federal Regulatory guidance on prudent CRE loan workouts.¹

III. Debtor and Creditor Symmetry in Identifying a Troubled Debt Restructuring

The FASB noted that there is diversity in practice in identifying restructurings that constitute troubled debt restructurings, and therefore; the purpose of the Proposal is to create consistent application of Generally Accepted Accounting Principles (“GAAP”) for debt restructurings. While the CRE Finance Council agrees with FASB’s goal of creating more consistent application of GAAP, including for debt restructurings, we are concerned that the preclusion of the creditor from using the debtor’s effective rate test will create more diversity, not less.

To determine if a concession has been granted by a creditor, a debtor performs an “effective rate” test that compares the effective rate on the debt before and after a restructuring. In the Proposal’s comments, the Board decided to preclude the creditor from using the debtor’s effective rate test in its evaluation of whether a restructuring constitutes a troubled debt restructuring, acknowledging that the identification of a troubled debt restructuring need not be symmetrical between a creditor and a debtor. At the same time, the FASB noted that there is diversity in practice in identifying restructurings that constitute troubled debt restructurings.

The CRE Finance Council believes that, by precluding a creditor from using a debtor’s effective rate test, the TDR exposure draft would create further diversity in identifying troubled debt restructurings, as a debtor and creditor may well come to opposite conclusions on the same receivable.

At the same time, there are many entities, such as insurance companies and financial institutions; that are both lenders and debtors in commercial real estate transactions. The preclusion would cause divergence within an entity that would be able to look at the effective rate test in the case where it is a debtor, but not in the case where it is a creditor. Therefore, the preclusion would not only cause diversity between entities, but within an entity itself.

Unfortunately, these circumstances would make it more difficult for users of financial statements to compare troubled debt restructurings across periods and entities. Furthermore, the Board recognizes that the preclusion will cause asymmetry between lenders and debtors.

Accordingly, we recommend that the FASB remove the preclusion of the creditor using the debtor test in its evaluation of whether a restructuring is a troubled debt restructuring.

¹ Policy Statement on Prudent Commercial Real Estate Loan Workouts, October, 2009, at <http://www.federalreserve.gov/boarddocs/srletters/2009/sr0907a1.pdf>

IV. Insignificant Delays

The Proposal states that a restructuring that results in an insignificant delay in contractual cash flows of the original receivable may still be considered a troubled debt restructuring if the restructuring is considered a concession. Furthermore, the Board noted that the concept of an “insignificant delay” should be used in assessing when a receivable is impaired under Section 310-10-35 rather than assessing when a restructuring constitutes a troubled debt restructuring.

The CRE Finance Council is concerned that such an approach will cause many commercial loans to be classified as troubled debt restructurings when, in fact; the “insignificant delay” was caused not by a troubled loan, but by the complexity of the commercial real estate lending process.

Specifically, the complexity of commercial real estate loans allow for longer lead periods in processing loans. While a residential mortgage may be turned around in a matter of weeks, the typical time frame for a commercial loan refinancing is 3-6 months. Due to the heterogeneity and complexity of commercial loans, the appraisal alone, which is necessary for a refinancing, can take up to three months to complete. Furthermore, while a residential loan may involve as few as three parties, a commercial mortgage loan financing may involve many parties. In short, the complexity of commercial real estate loan refinance can lend itself to longer timelines than other asset classes. These timelines can lead to delays that are due to process issues, and not necessarily a debtors’ financial situation or ability to pay. It is not unusual for lenders to allow a debtor to extend the payment of principal while servicing the debt in order to allow enough time for the completion of a refinance.

In another example, a commercial mortgage may have temporary cash flow issues and a lender may permit a temporary modification to allow the borrower to restabilize the property’s operation by, for example, replacing a tenant. Lenders would only do this if they believe that the collateral value will be adequate to secure the debt balance. As such, an impairment should not be placed on the loan. The proposed guidance could result in labeling these limited modifications as TDRs although there is no ultimate impairment. This process does not provide meaningful information on the financial statements and would create an operational burden for the lender without improvement of reporting. Additionally, we are concerned that there is no mechanism for a loan to fall out of TDR status even if, like the performing loan described above has no real impairment issues.

Accordingly, we do not see the need for insignificant delays to be included in the TDR analysis and the inclusion of it is a conflict with ASC 310-10-35-10 which states that ‘a credit or need not consider an insignificant delay or insignificant shortfall in the amount of payments...’ when assessing impairment.

V. Prospective Implementation for Financial Statements, Retrospective for Disclosures

In the Proposal, the Board decided to require prospective application from a financial statement perspective and a retrospective application from a disclosure perspective. The goal of the implementation guidance is to improve comparability across entities and consistency in information across periods. Furthermore, the Board noted that the information required to apply the proposed guidance for purposes of calculating impairment may be difficult to obtain.

The CRE Finance Council is concerned that a retrospective approach for disclosures will be difficult, if not impossible, for the industry to implement. We agree with the Board that information will be difficult, if not impossible; to obtain retrospectively to determine whether past changes meet the criteria for troubled debt restructurings.

While the Proposal may be easier to implement retrospectively for homogeneous asset classes, such as residential mortgage backed securities, it is extremely difficult for commercial mortgages. Due to the unique structures of commercial mortgages, it is very hard to retrospectively substantiate a market rate. For example, a lender may have increased the interest rate in the past in order to modify a loan, believing that the increased rate was a market rate at that time. However, under the new guidance, it is unclear whether this would be considered a troubled debt restructuring.

Finally, the time and cost associated with implementing the guidance retrospectively, especially if information is incomplete or unobtainable, will neither provide useful nor consistent information for preparers, and more importantly, users of financial statements, who will find it difficult to compare troubled debt restructuring decisions over periods and across entities.

Accordingly, we recommend FASB remove the retrospective requirement, and implement guidance prospectively both from a disclosure and financial statement perspective.

VII. Conclusion

The CRE Finance Council recognizes and appreciates the efforts of both FASB and IASB to converge accounting standards internationally. However, we strongly encourage FASB to delay work on troubled debt restructurings until a single converged standard for an impairment model is completed. At that point we question the real need for TDR guidance when the impairment models and disclosures would provide the pertinent information needed by financial users. If this cannot be achieved, we urge FASB to consider the Council's recommended changes to the Troubled Debt Restructuring Proposal outlined herein, and we stand ready to provide any additional assistance that may be helpful.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "John D'Amico". The signature is fluid and cursive, with a large initial "J" and "D".

John D'Amico
Chief Executive Officer
CRE Finance Council