

MEMO# 7622

February 8, 1996

INSTITUTE COMMENT LETTER ON FASB SECURED ASSET TRANSFERS EXPOSURE DRAFT

February 8, 1996 TO: ACCOUNTING/TREASURERS COMMITTEE No. 7-96 INDEPENDENT
ACCOUNTANTS ADV. GROUP No. 2-96 SEC RULES COMMITTEE No. 11-96 RE: INSTITUTE
COMMENT LETTER ON FASB SECURED ASSET TRANSFERS EXPOSURE DRAFT

The Institute submitted the attached comment letter to the Financial Accounting Standards Board on the Exposure Draft Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities. The Exposure Draft is intended to provide consistent standards for distinguishing transfers of financial assets that are sales from transfers that are secured borrowings. Among other things, the Exposure Draft will affect the manner in which investment companies recognize income earned on securities lending transactions. In particular, the Exposure Draft would require income earned on cash collateral received, and fees or rebates paid to borrowers in a securities lending transaction to be reported separately in the statement of operations. Under current industry practice, fees or rebates paid to borrowers are offset against income earned and the net amount is reported as income in the statement of operations. Under the proposed treatment, fees paid to borrowers would be reported as "interest expense" and would increase the funds level of expenses. Since funds would report the "gross" amount of income earned on the investment of cash collateral, there would be no change in the amount of net investment income. However, the funds expense ratio would increase due to the separate reporting of interest expense. The Institutes comment letter strongly opposes separate reporting of income and expense associated with securities lending transactions. The comment letter indicates that securities lending is an investment strategy that seeks to profit from a temporary shortage of physical securities and should not be characterized as a "borrowing" with associated interest expense. Further, the comment letter notes that the proposed accounting treatment would distort fund expense ratios and may cause funds to curtail their securities lending activities. Gregory M. Smith Director - Operations/ Mutual Fund Accounting Attachment

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