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November 13, 2017

Technical Director
Financial Accounting Standards Board
401 Merritt 7
PO Box 5116
Norwalk, CT 06856-5116

RE: Proposed Accounting Standards Update, *Technical Corrections and Improvements to Accounting Standards Update No. 2016-01, Financial Instruments – Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Liabilities* (File Reference No. 2017-300)

Dear Technical Director:

We appreciate the opportunity to comment on the proposed ASU, *Technical Corrections and Improvements to Accounting Standards Update No. 2016-01, Financial Instruments – Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Liabilities*.

We support the Board's objective to improve and clarify certain aspects of the recognition, measurement, presentation and disclosure guidance for financial assets and liabilities. However, unlike the proposed changes to paragraph 825-10-65-2 (Issue 6), we believe that the unrealized gains on equity securities without a readily determinable fair value should be recognized consistently at the date of transition regardless of the measurement attribute (fair value or the measurement alternative) selected. Further, unlike the proposed changes to paragraph 321-10-35-2 (Issue 1), we believe that fair value measurement elections should be made only at (1) initial recognition (consistent with the fair value option guidance in Topic 825), (2) adoption of a new accounting standard or (3) on the occurrence of rare circumstances (e.g. those that would permit a security to be transferred from available-for-sale to trading under paragraph 320-10-35-12). Finally, we believe that certain other proposed amendments should be clarified.

Proposed amendments in Issue 6

Some entities have significant unrealized gains associated with equity securities without readily determinable fair values. The proposal would require an entity that chooses fair value measurement to treat those unrealized gains as a cumulative-effect adjustment to the opening balance of retained earnings. In contrast, an entity that chooses the measurement alternative would ultimately recognize the measurement adjustment (together with changes in fair value subsequent to adoption) in earnings. We believe that the manner in which those unrealized gains are recognized should not depend on the measurement attribute that the entity selected.

We believe that high-quality financial reporting includes measuring equity securities at fair value with resulting gains and losses recognized in earnings. However, we believe that the proposal in Issue 6 would provide an incentive for entities to elect the measurement alternative rather than fair value measurement. Specifically, entities that have unrealized gains likely would elect the measurement alternative to recognize those gains in earnings instead of as a cumulative effect adjustment.

If the Board agrees with our position, we believe that prospective recognition in earnings is the more practical transition alternative, and would not require an amendment to the transition provisions already in paragraph 825-10-65-2.

Proposed amendments in Issue 1

The proposed amendments in Issue 1 would permit an entity to make a fair value election at any time for equity securities without a readily determinable fair value. We believe that fair value measurement elections should be made only at (1) initial recognition (consistent with the fair value option guidance in Topic 825), (2) adoption of a new accounting standard or (3) on the occurrence of rare circumstances (e.g. those that would permit a security to be transferred from available-for-sale to trading). The Board stated in paragraph A12 of FASB Statement No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities*, that permitting fair value elections to be made after initial recognition would have allowed entities to recognize gains or losses in earnings after those gains and losses had occurred. Consequently, the Board decided not to permit fair value elections to be made after initial recognition. We believe that the Board should apply that reasoning in the final technical corrections and improvements ASU.

Similar to a concern that we expressed about Issue 6, we believe that the proposed amendments in Issue 1 also could provide a disincentive for entities to elect to measure equity securities at fair value. Because Issue 1 allows an entity to choose fair value measurement at a later date, an entity may prefer to defer fair value measurement for numerous reasons, including waiting to see how fair value would change after it adopted the ASU.

Additional recommendations and responses to selected Questions for Respondents are included in Appendix I to this letter and Appendix II provides an example that illustrates our concerns.

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If you have questions about our comments or wish to discuss the matters addressed in this comment letter, please contact Kimber Bascom at (212) 909-5664 or kbascom@kpmg.com, or Mark Northan at (212) 954-6927 or mnorthan@kpmg.com.

Sincerely,

KPMG LLP

KPMG LLP

Appendix I – Responses to Selected Questions for Respondents

Question 1:

The proposed amendments are intended to improve the clarity of the guidance in Update 2016-01. Would the proposed amendments clarify that guidance? If not, please explain which proposed amendment(s) would not provide clarification, and why.

We believe that the proposed amendments for Issues 2-4 improve the clarity of the guidance in Update 2016-01.

Issue 1:

Refer to our cover letter for our recommendations on the proposed amendments in Issue 1.

It appears that the Board intended to limit the flexibility to subsequently choose fair value measurement by including the requirement that the accounting policy be elected for all equity securities 'of the same type'. If the Board keeps the proposed change in the final ASU, we believe that the Board should clarify what it means by the term of the same type to prevent diversity in practice. For example, of the same type could be interpreted broadly to mean a major security type (paragraph 320-10-50-1B) or all common (or preferred) stock. Alternatively, of the same type could be interpreted more narrowly, potentially at the individual equity security level.

Issue 5:

We believe that the Board's intent in the proposed amendment in Issue 5 is to require separate presentation of changes in instrument-specific credit risk in the liability's functional currency consistent with the requirement in paragraph 825-10-45-5. However, we believe that the proposed amendment in Issue 5 could be interpreted to require separate presentation of changes in instrument-specific credit risk in the liability's currency of denomination.

To clarify the presentation requirements, we suggest the Board consider modifying paragraphs 825-10-45-5A and 830-20-35-7A.

> If the liability is denominated in a currency other than the functional currency of the entity, the change in fair value of the liability resulting from changes in instrument-specific credit risk shall be calculated separately from other changes in the fair value of the liability in the liability's currency of denomination. The component of the change in fair value of the liability resulting from changes in instrument-specific credit risk shall then be adjusted to reflect the current exchange rate in accordance with paragraph 830-20-35-2 <u>and presented separately in accumulated other comprehensive income</u>.

Issue 6:

Refer to our cover letter for our recommendations on the proposed amendments in Issue 6.

Question 2:

Will any of the proposed amendments result in substantive changes to the application of Update 2016-01 that would require transition provisions or an effective date for the final amendments other than as noted in the Summary section “When Would the Amendments Be Effective?” If so, please describe.

No. We do not believe that the proposed amendments would require additional transition provisions or an effective date other than as noted in the Summary.

Question 3:

Should other changes be made that are directly or indirectly related to the proposed amendments? Please note that the Board will conduct Codification improvements projects on a periodic basis and additional changes may be postponed to a subsequent Codification improvements project.

No. We are not aware of other changes that the Board should make to the proposed amendments.

Appendix II – Illustrative Example

Public Company A, which has a calendar year-end, holds XYZ common stock. Before Company A adopts ASU 2016-1, the XYZ common stock has a carrying amount of $100 and does not have a readily determinable fair value. At transition, Company A determines that its holding of XYZ common stock has a fair value of $250. There also was an observable transaction in the XYZ common stock shortly after the transition date that supports a fair value of $250.

If Company A elected to measure its investment in XYZ common stock at fair value, the $150 unrealized gain would be recorded as a cumulative effect adjustment on transition. As result, Company A would likely not elect fair value measurement. Instead, it would likely elect to measure its XYZ common stock using the measurement alternative so that it would recognize in earnings (not as a cumulative effect adjustment) the $150 increase in fair value over the cost basis of the equity security shortly after the transition date (when the observable transaction occurred).

After transition, under the proposed amendment in Issue 1, Company A could elect to change from the measurement alternative to fair value. This would allow Company A to (1) recognize the $150 unrealized gain in earnings and (2) subsequently measure the XYZ common stock at fair value. This outcome would be inconsistent with the transition alternative proposed by the Board in Issue 6.

Under Issue 1, Company A would be required to elect to change from the measurement alternative to fair value for all equity securities ‘of the same type’. Because there is no guidance in the proposed ASU about how to interpret of the same type, it appears that Company A could have flexibility to define that population narrowly (including potentially limiting its election to only the XYZ common stock).

This example highlights the concerns raised in our cover letter and Appendix I about Issues 1 and 6.

- Issue 6 would result in significantly different treatment of unrealized gains and losses existing at the date of adoption depending on which measurement attribute is selected.
- The transition guidance in Issue 6 likely would provide an incentive for entities with investments in an unrealized gain position to elect the measurement alternative instead of fair value measurement.
- An entity’s ability to subsequently change from the measurement alternative to fair value measurement would provide (1) a further incentive for an entity to elect to apply the measurement alternative rather than fair value measurement (because an entity could wait to see how fair values change after it adopts the final ASU) and (2) a potential ability to recognize unrealized gains in earnings while subsequently measuring the related investment at fair value through earnings (the outcome that the Board appears to be prohibiting in Issue 6).
- We believe that the Board intended for entities to have limited flexibility to make subsequent fair value elections under the guidance in Issue 1. However, we believe that the phrase of the same type could be interpreted narrowly. This could give entities significant flexibility to make these elections at the individual equity security level.