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July 6, 2021

Ms. Hillary H. Salo
Technical Director
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116

File Reference No. 2021-002
Re: Proposed Accounting Standards Update, *Fair Value Hedging — Portfolio Layer Method*

Dear Ms. Salo:

Deloitte & Touche LLP is pleased to comment on the FASB's proposed Accounting Standards Update (ASU) *Fair Value Hedging — Portfolio Layer Method*.

We support the Board's efforts to clarify certain aspects of ASC 815, as amended, and to address implementation issues that have arisen as a result of recent amendments. We also understand the Board's objectives of simplifying the hedge accounting guidance and aligning financial reporting with entities' risk management strategies.

Although we generally support the proposed amendments, we believe that there are certain limited potential enhancements that the FASB should consider to further improve the standard. These potential enhancements are primarily related to the concept of a closed portfolio in a portfolio layer method hedge.

We agree that the addition of the term "hedged layer" to the ASC master glossary would provide clarification for entities applying the portfolio layer method guidance. However, we believe that the phrase "closed portfolio" in the proposed definition and throughout the proposed amendments may cause some confusion.

It could be interpreted that items could not be removed from a closed portfolio, which would contradict guidance included in the proposed amendments. For example, the proposed ASU would amend ASC 815-25-35-7A to explicitly refer to voluntary sales or reclassifications out of the closed portfolio that should be considered when an entity performs an analysis to support its determination that the hedged layer is still expected to be outstanding for the period hedged. It would be helpful to provide guidance that clarifies the concept of a closed portfolio as a portfolio to which items may not be added, but from which items may be removed (e.g., through sales, defaults, prepayments, or reclassifications).

We also believe that it would be helpful to clarify how voluntary removals from a closed portfolio would not trigger the dedesignation of all hedging relationships associated with that closed portfolio. Given that some may interpret a voluntary removal from the closed portfolio as a change to a critical term of the hedged item, additional clarification on how such removals from the closed portfolio should be treated could avoid varying interpretations. We note that proposed ASC 815-25-35-1(c) states that basis adjustments should be maintained on a closed portfolio basis and not on the level of individual assets in **or removed** from the portfolio, but the proposed amendments do not explicitly address how voluntary removals from the closed portfolio differ from removals caused by other factors such as prepayments or defaults that may trigger an anticipated breach or a breach resulting in dedesignation. We believe that providing further clarification related to this distinction would prevent an entity from being able to voluntarily remove items from a closed portfolio to intentionally cause a breach and thereby manage the timing of the impact to earnings. Currently, there are no repercussions affecting future hedging eligibility for entities that experience a breach under the portfolio layer method, and providing further clarification could address this issue.

For example, assume that an entity had a closed portfolio consisting of $300 million of prepayable assets and a single hedged layer of $100 million. Also assume that the portfolio level basis adjustment was a contra-asset of $5 million. If the entity had a planned sale of $100 million of the assets, it could voluntarily remove the other $200 million of assets from the closed portfolio immediately before the sale. As a result, the $5 million basis adjustment would become a component of the carrying amount of only the assets sold, and the gain on the sale would increase by $5 million. However, if the entity had not removed the assets from the closed portfolio before the sale, there would still be $200 million of assets in the closed portfolio after the sale, and the entire $5 million basis adjustment would remain at the portfolio level. We believe that the Board should consider two alternative approaches to avoid this problem. One approach would be to prohibit voluntary removals from the closed portfolio. The other approach would be to include the concept of a pattern of breaches, which would preclude an entity from asserting that it can support a determination that the hedged layer is expected to be outstanding for the period hedged (in a manner consistent with the guidance in ASC 815-30-40-5 on cash flow hedges of forecasted transactions).

In addition to our recommendations related to the concept of a closed portfolio in a portfolio layer method hedge, we also recommend the following potential enhancements to the implementation guidance included in the proposed amendments:

- *ASC 815-20-55-14F* — Consider removing the sentence, "In this scenario, designation of an amortizing-notional swap as the hedging instrument achieves results that are comparable with the multiple-layer strategy using two constant-notional swaps as the hedging instruments, as described in paragraph 815-20-55-14E." We believe that the results could differ since an entity that designates an amortizing-notional swap as the hedging instrument could not voluntarily dedesignate anything other than a proportion of the amortizing swap if it anticipates a breach in the future, while an entity that designates two constant-notional swaps could voluntarily choose a proportion of either or both of the swaps to dedesignate. In addition, an entity that designates an amortizing-notional swap as the hedging instrument would have to dedesignate the swap upon a breach, while an entity that designates two constant-notional swaps may only have to dedesignate one of the swaps upon a breach.

- *ASC 815-20-55-14M and 55-14N* — Consider adding that Entity A may redesignate a proportion of the swap that was removed from the hedging relationship in a new hedging relationship, if it qualifies.

The appendix below contains our responses to the proposed ASU's questions for respondents.

We appreciate the opportunity to comment on the proposed ASU. If you have any questions about our comment letter, please feel free to contact Jon Howard.

Yours truly,

Deloitte & Touche LLP

cc: Robert Uhl

Appendix
Deloitte & Touche LLP
Responses to Proposed ASU's Questions for Respondents

Question 1: Are the amendments in this proposed Update operable and auditable? If not, which proposed amendment or amendments pose operability or auditability issues and why?

We believe that the proposed amendments are operable and auditable. However, as noted above, we believe that there are potential enhancements that could be made to clarify whether voluntary removals from a closed portfolio should be treated as dedesignation events. Such clarification would enhance the auditability of the proposed amendments.

Question 2: As proposed, would the multiple-layer model align with entities' risk management objectives? Please explain why or why not.

While we defer to preparers' feedback on the alignment of the proposed multiple-layer model with entities' risk management objectives, we believe that the proposed amendments do provide clarity for entities looking to apply the portfolio layer method to better align financial reporting with risk management strategies.

Question 3: Do you agree with the Board's decision to limit the scope of the types of instruments eligible for portfolio layer method hedging to prepayable financial assets or one or more beneficial interests secured by a portfolio of prepayable financial instruments? Please explain why or why not.

No, we do not fully agree with the limited scope of instruments eligible for portfolio layer method hedging. Although we appreciate that and understand why prepayable assets or one or more beneficial interests secured by a portfolio of prepayable financial instruments are included within the scope, we do not fully appreciate why financial liabilities are excluded from the scope. While we defer to preparers' feedback, we would understand how including financial liabilities within the scope of the types of instruments eligible for portfolio layer method hedging could support the Board's objectives of simplifying the hedge accounting guidance and aligning financial reporting with entities' risk management strategies.

Question 4: Do you agree with the Board's proposed amendments on hedge dedesignation sequencing under the multiple-layer model? Please explain why or why not.

Yes, we agree with the Board's proposed amendments on hedge dedesignation sequencing under the multiple-layer model since we believe that the proposed amendments would provide for better consistency and comparability across financial reporting for entities applying the portfolio layer method. Further, we believe that the proposed amendments on hedge dedesignation sequencing would allow for better auditability of the application of the portfolio layer method upon the occurrence of dedesignation events. We believe that the examples in proposed ASC 815-20-55-14K through 55-14N provide useful implementation guidance for demonstrating the application of the proposed amendments on hedge dedesignation sequencing under the multiple-layer model.

Question 5: Do you agree with the Board's proposed amendments on accounting for basis adjustments and disclosure of those basis adjustments in disclosures required by other areas of GAAP outside hedge accounting? Please explain why or why not.

Yes, we agree with (1) the Board's proposed amendments on accounting for basis adjustments at the portfolio level and (2) not requiring disclosure on a more disaggregated basis than the portfolio level to meet disclosure requirements in other areas of GAAP outside of hedge accounting unless the assets included in the same closed portfolio are presented in different line items in the statement of financial position.

We believe that the proposed amendments would support the operability of the portfolio layer method. However, as previously mentioned, we also believe that potential enhancements could be made to clarify (1) the accounting for basis adjustments when items are voluntarily removed from a closed portfolio and (2) how such voluntary removals would not trigger the dedesignation of all hedging relationships associated with the closed portfolio.

Question 6: In the case of a breach, do the expected costs of identifying which assets in the closed portfolio that caused the breach justify the expected benefits of aligning the derecognition guidance with other Topics in GAAP? Please explain why or why not.

In our view, the expected costs of identifying which assets in the closed portfolio caused the breach justify the expected benefits of aligning the derecognition guidance with other topics in GAAP because we believe that identifying those assets is a rational and systematic approach for accounting for income statement activity in the case of a breach. Further, we believe that the expected costs are justified by other provisions included in the proposed amendments that simplify the guidance on portfolio layer method hedging (e.g., accounting for basis adjustments at the portfolio level rather than at an individual asset level).

Question 7: Would any of the proposed amendments require special consideration for private companies that are not financial institutions and not-for-profit entities (except for not-for-profit entities that have issued, or are a conduit bond obligor for, securities that are traded, listed, or quoted on an exchange or an over-the-counter market)? If so, which proposed amendment or amendments would require special consideration and why?

No, we do not believe that special considerations are required for (1) private companies that are not financial institutions and (2) not-for-profit entities.

Question 8: Do you agree with the proposed transition guidance? Please explain why or why not.

Yes, we agree with the proposed transition method guidance. Since the proposed amendments are related to an optional hedging method that entities may apply, we believe that adoption on a prospective basis is logical and appropriate

Question 9: How much time would be needed to implement the proposed amendments? Should the amount of time needed to implement the proposed amendments by entities other than public business *entities be different from the amount of time needed by public business entities? Please explain your response.*

While we defer to preparers' feedback on the time needed to implement the proposed amendments, it seems that the transition period should not have to be lengthy because the proposed amendments are simplifying or clarifying the existing hedging model. As indicated in our response to Question 7, we do not believe that special considerations are required for (1) private companies that are not financial institutions and (2) not-for-profit entities.