September 21, 2021

VIA ELECTRONIC SUBMISSION

Ms. Hillary Salo
Technical Director, FASB
401 Merritt 7
PO Box 5116
Norwalk, CT 06856-5116

**Re: File Reference No. 2021-004. Invitation to Comment: Agenda Consultation**

Dear Ms. Salo:

The Securities Industry and Financial Markets Association ("SIFMA")[1] appreciates the opportunity to respond to the invitation to comment ("ITC") on the Financial Accounting Standards Board's ("FASB's" or "Board's") technical agenda. Our Committee members have significant expertise in the accounting matters faced by a wide range of financial institutions, and are happy to share our practical experience with the FASB Staff to help drive future standard-setting that focuses on matters where: (1) there is a pervasive need for improvement with identifiable scope; (2) solutions are technically feasible; and (3) the expected benefits exceed the expected costs associated with the change.

Detailed responses to the specific questions raised in the invitation are included in Appendix I, but we would like to highlight the following key items for specific consideration:

- Hedge Accounting – Phase 2: While significant progress has been made with regard to the hedge accounting guidance, we believe there remains a number of key items that require additional consideration, many of which being particularly pressing (see our responses to Question 5 for more information). As a result, we believe this should be a top priority for the Board.

[1] SIFMA is the leading trade association for broker-dealers, investment banks, and asset managers operating in the U.S. and global capital markets. On behalf of our industry's nearly one million employees, we advocate for legislation, regulation, and business policy affecting retail and institutional investors, equity and fixed income markets, and related products and services. We serve as an industry coordinating body to promote fair and orderly markets, informed regulatory compliance, and efficient market operations and resiliency. We also provide a forum for industry policy and professional development. With offices in New York and Washington, D.C., SIFMA is the U.S. regional member of the Global Financial Markets Association (GFMA).

- Digital assets: Given the growth in this asset class, as well as increased focus by various regulators, we believe the Board should prioritize a project that addresses both classification (i.e., as a non-intangible asset) and measurement (i.e., availability of the fair value option).

- Environmental, social and governance ("ESG") related transactions: Although generally not yet material for our member firms, we expect this activity (e.g., loans or deposits with interest rates that vary based on the counterparty's performance against certain defined ESG-related targets) to increase significantly in the short-term and, therefore, believe a project aimed at mitigating the need for bifurcation of embedded derivative and fair value measurement requirement should be a priority of the Board.

- Definition of a derivative: In addition to addressing the item immediately above, we believe the Board should also prioritize clarifying the accounting for amendments to derivatives, particularly as it relates to defining the "initial investment." This is an area that creates meaningful complexity in practice.

Again, we thank the FASB Staff for the opportunity to comment. Should you have any questions or require further information concerning any of the matters discussed in this letter, please do not hesitate to contact the undersigned Timothy Bridges (tim.bridges@gs.com).

Regards,

Timothy Bridges, Managing Director, Goldman Sachs & Co. LLC
Chair, SIFMA Accounting Committee

CC: Kevin Zambrowicz, Managing Director & Associate General Counsel, SIFMA

## Appendix I – Responses to Questions

### *Overall*

**Question 1:** Please describe what type of stakeholder you (or your organization) are from the list below, including a discussion of your background and what your point of view is when responding to this ITC.

*>Response: SIFMA is a trade association comprised of private and public company preparers that operate as broker-dealers, investment banks and asset managers in the U.S. and global capital markets.*

**Question 2:** Which topics in this ITC should be a top priority for the Board? Please explain your rationale, including the following:

a. Why there is a pervasive need to change GAAP (for example, what is the reason for the change)
b. How the Board should address this topic (that is, the potential project scope, objective, potential solutions, and the expected costs and benefits of those solutions)
c. What the urgency is of the Board completing a project on this topic (that is, how quickly the issues need to be addressed).

*>Response: We believe that of the topics specifically outlined in the ITC, the following should be the top priorities of the Board:*

*#2A – Digital assets*

*The market for digital assets continues to expand, with the capitalization of Bitcoin, for example, approximately $890 billion as of August 31, 2021, an increase of approximately 325% from a year prior.[2] Further, it continues to be an asset class that is subject to meaningful price movements, with a one-year price range of approximately $10,000 - $65,000. Given the growth and volatility, we believe the current accounting treatment of recognizing such holdings as intangible assets[3] does not provide users with decision-useful information, particularly where active markets exist that would allow for rapid monetization. Specifically, when accounting for an intangible asset, an entity is only permitted to mark the carrying value of the digital asset*

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2 https://coinmarketcap.com/currencies/bitcoin/

3 Outside of entities that apply specialized industry guidance such as Topic 946, *Financial Services — Investment Companies* or Topic 940, *Financial Services — Brokers and Dealers*.

*below its initial cost (via impairment), with no ability to mark up, including previously recorded losses. As a result, users do not have the complete picture on the range of volatility and price movements, and entities may be carrying such assets at amounts significantly below the levels at which they could be readily converted to cash. In fact, we have observed instances where entities*[4] *elected to disclose the fair value of their digital asset holdings so that investors do have a clearer picture, though we believe that disclosure alone is not sufficient in most cases. As a result, we believe the accounting for direct holdings of digital assets should be a top priority of the Board.*

*A practical solution to address the shortcomings of the current accounting treatment would be to expand the availability of fair value option to such holdings. This would not only provide users of the financial statements with a more complete understanding of the value of these positions, it would also provide users with recurring disclosures regarding the valuation process (e.g., observability of inputs). In addition to measurement, we believe a classification other than "intangible assets" would also be appropriate, as this acknowledges the fungible and functional nature of these holdings, many of which are readily convertible to cash.*

*In addition to direct holdings of crypto assets, we observe expanded use of stablecoins (i.e., crypto asset pegged in value to a traditional asset) as well as increased focus by governments on central bank digital currencies ("CBDCs"), noting certain countries (e.g., China and South Korea) are currently piloting this technology. While different in nature than direct holdings of bitcoin, various accounting questions can arise, with the potential for diversity in practice absent specific guidance. As a result, we believe the Board should also consider providing guidance on the accounting for other digital asset offerings, such as stablecoins and CBDCs. For example, addressing: (1) the extent to which the nature of the underlying asset informs the accounting model for the corresponding stablecoins; and/or (2) under what circumstances CBDCs qualify as currency and/or cash equivalents. However, we do not believe providing guidance on these matters is as pressing as for direct holdings (as discussed above) and, therefore, would suggest this is covered through a separate project so as to not impede the accelerated focus thereon.*

*#2B – ESG-related transactions*

*Investing and financing activities aimed at advancing sustainable economic growth and financial opportunity have increased significantly in recent years. For example, global ESG-related assets are estimated to be on track to exceed $53 trillion by 2025, representing more than a third of the $140.5 trillion in projected total assets under management*[5] *– and a record of $732 billion in*

[4] https://d18rn0p25nwr6d.cloudfront.net/CIK-0001679788/cb843fec-ede4-4ff0-be56-a69062543e57.pdf (page 47)

[5] https://www.bloomberg.com/professional/blog/esg-assets-may-hit-53-trillion-by-2025-a-third-of-global-aum/

*sustainable debt was issued in 2020[6]. For our member firms, in addition to debt securities, it is increasingly common that loan and deposit products incorporate features that adjust the corresponding interest rates based on the achievement of ESG-related targets or metrics, which are typically specific to either of the counterparties to the transaction. Assuming such instruments are not marked to fair value in their entirety, under the current accounting rules, most believe that it is often the case that such features should be bifurcated as they both: (1) meet the definition of a derivative (including that existing scope exceptions generally do not apply) and (2) are not considered to be clearly and closely related to the host instrument. In many cases this results in significant operational complexity with regard to (1) booking and tracking of such provisions and (2) assessing the specific likelihoods that the stated targets or metrics will be achieved for each counterparty as part of the fair valuation process, particularly as these assessments involve factors that are not easily observable. For these reasons, we believe this area too should be a top priority of the Board.*

*A potential solution is to incorporate guidance similar to what currently exists under IFRS 9 "Financial Instruments" for financial liabilities (specifically, BA.5) which indicates that the definition of a derivative refers to non-financial variables that are not specific to a party to the contract, either to replace or expand upon the current derivative scope exception in US GAAP related to "specified volumes of sales or service revenues of one of the parties to the contract." This would allow such provisions to avoid bifurcation which would relieve significant operational burden for preparers. In lieu of fair value, we would expect preparers to recognize interest income or expense based on the probable outcome, which we believe still provides the user with meaningful and sufficiently transparent information. While this would still involve an assessment of the likelihood of achievement, it would be a more binary process (i.e., accrue or not) versus trying to identify the specific probability (or ranges thereof) that would be necessary to perform a more robust valuation analysis. Further, one could potentially make such assessment at a portfolio level versus evaluating at the individual transaction level. That said, we believe it would be helpful to also provide a fair value option where such provisions are executed as standalone agreements (or clarify that this option would generally apply), as this would provide reasonable flexibility to align the accounting and business models, to the extent the latter evolve as the activity develops.*

*Separately, we recommend the Board also consider adding a project related to tax credit investments. Currently, there is guidance related to low income housing tax credits. However, there is a lack of guidance related to other tax credit investments, such as new markets, renewable energy and other types. This results in investments that are substantially similar in nature being subject to different accounting standards. We believe a solution for this would be to expand the scope of Subtopic 323-740 from "qualified affordable housing projects" to cover*

[6] https://www.bloomberg.com/news/articles/2021-01-11/social-bonds-propel-esg-issuance-to-record-732-billion-in-2020

*"investments that are made for the primary purpose of receiving tax credits and other tax benefits."*

*#2C – Definition of a derivative*

*While we do not believe the definition of a derivative is fundamentally flawed, we observe there is need for refinement related to matters including the following: (1) evaluating derivatives with one or more underlying risks linked to the operations or performance of one of the parties to the contract (e.g., ESG-related transactions); (2) evaluating amendments to derivatives, particularly how to assess the "initial investment" in such cases (e.g., "blend & extend" type transactions); and (3) expanding the "regular-way" scope exception to transactions beyond the settlement of securities (e.g., spot FX, gold).*

- *For the first item, see #2B above for potential solutions.*

- *For the second item, existing guidance regarding the accounting for amendments to derivatives is limited (other than for certain freestanding equity-classified written call options). That said, we understand that current practice is generally to analogize to DIG A23 for purposes of evaluating the significance of the initial investment. Implicit in this approach is a view that the "old" contract has been settled and the "new" contract is executed with off-market terms via a deemed exchange of the contract's entire fair value at the time of modification. However, we believe this has the potential to overstate the extent of implicit financing the counterparty may receive in such cases (particularly in low interest rate environments) because it does not acknowledge that contract's entire fair value at the time of modification was generally not due immediately; rather, it would have been repaid over the remaining original maturity (all else equal). That is, only a portion of the entire value at the time of modification is being financed (i.e., being paid over a longer time horizon than originally contracted). As a result, we believe the Board should consider permitting an alternative approach that would compare only a reasonable approximation of the value being deferred beyond the original maturity to the total fair value of the trade at the time of amendment. We believe this would provide a more accurate representation of the effect of the contract modification.*

  *The concept of evaluating only the deferred amount (cash flows) was previously contemplated in the context of trades that embody an "other-than-insignificant financing element." Specifically, in paragraph A39 of the Basis for Conclusions of Statement of FAS 149, the Board viewed it as "conceptually preferable" to present only those cash flows associated with the financing element as a financing activity in the statement of cash flows, but decided against this solely as a result of cost-benefit concerns. As such, we believe this approach has merit, and providing this approach as an alternative* *(applied consistently as a matter of accounting policy) could alleviate any concerns around cost or complexity.*

*We believe this item is pressing and requires attention given the current interest rate environment; however, we believe #2A and #2B above are of higher priority.*

- *For the third item, we observe that there are a number of "regular way" transactions (e.g., spot purchase or FX of physical commodities) that technically meet the definition of a derivative, though this is not the overall objective of intent of the transaction. While this is not a particularly pressing matter, we wanted to highlight it for potential inclusion in any broader effort the Board may explore to refine the definition of a derivative.*

*#2D – FASB standard-setting processes*

*On numerous occasions, the Board has demonstrated an ability to respond quickly and effectively to emerging practice issues. For example, the refinements contemplated in Accounting Standard Update ("ASU") 2021-01 "Reference Rate Reform (Topic 848): Scope" ("ASU 2021-01"), for derivative instruments that use an interest rate for margining, discounting, or contract price alignment that is modified as a result of reference rate reform, were discussed by the Board, exposed for public comment and issued as final guidance within a few months, importantly with sufficient time to allow for application to 2020 calendar-year-end financial statements. This after the extensive relief within ASU 2020-04 "Reference Rate Reform (Topic 848): Facilitation of the Effects of Reference Rate Reform on Financial Reporting" also made it through the entire standard-setting process within a relatively short period of time.*

*That said, to relieve some of the burden related to such rapid standard-setting efforts, we believe the Board should consider a public process that would provide timely interpretations of existing US GAAP that would not require amendments to the Codification. This would be particularly helpful where US GAAP is unclear, and practice simply needs clarification and/or confirmation that a particular view is not unreasonable. For example, we believe such a forum would have been able to address the key refinements that were made via ASU 2021-01 which were understood to primarily be clarifications of original intent to address the potential for diversity of interpretations in practice. In addition to being more streamlined, we believe practice would also benefit if such a process was public, as it would provide greater insight and access to the technical analyses and related judgments associated with what would likely be some of the more complex areas of the guidance.*

*Separately, we believe it would also be helpful if the Codification included: (1) agenda materials for standard setting efforts (including for those that did not come to fruition); (2) the Basis for Conclusions associated with accounting standard updates; and (3) as an extension of above, the* *materials that support various interpretations of technical inquires. We believe enhancing accessibility in this manner would allow stakeholders to make more informed interpretations as it would provide greater context to the codified guidance, particularly for future generations.*

*#2E – Intangible assets, including software*

*More than ever before, companies are developing software for internal use ("IDS"). This reality is evidenced by the oft quoted phrase, "every company is a technology/digital company." The increased prevalence and size of expensed development costs and capitalized IDS as well as the significant changes in the methods used to develop that software (e.g., transition from the older waterfall method to agile development practices) create a pervasive need to update the accounting guidance.*

*While we believe that most companies are utilizing interpretations that align the measurement and recognition of IDS with the objectives of existing guidance, getting to a correct answer has become ever more burdensome and administratively complex due to the significant changes in the way the software is developed using Agile methods. Based on this, we believe the principles underlying the accounting model for IDS can and should be leveraged and the recognition and measurement should be consistent with that observed in practice today, but the application of these principles should be updated to reflect the new way that software is developed continuously and rapidly deployed.*

*We believe that updating the accounting guidance, especially the implementation or application guidance, for IDS would simplify and reduce the cost for preparers, and increase the transparency and usefulness of the information for financial statement users. The targeted improvement could be very much like the changes to hedge accounting in ASU 2017-12 "Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities" ("ASU 2017-12"), which sought to align the accounting guidance with risk management practices. The agile methodology is well defined and commonly understood and the accounting guidance could be updated to better reflect these practices achieving the same objectives noted in ASU 2017-12 to have accounting more accurately reflect business practices.*

**Question 3:** Are there topics in this ITC that the Board should not address as part of its future standard-setting efforts? Please explain your rationale, such as there is no pervasive need to change GAAP, the scope would not be identifiable, or the expected benefits of potential solutions would not justify the expected costs.

*>Response: We believe that of the topics specifically outlined in the ITC, the following should generally not be addressed as part of the Board's future standard-setting efforts:*

*#3A – Consolidations*

*We acknowledge that the consolidation guidance can be complex; however, we believe this is largely necessary given the complexity of the arrangements that exist in practice (i.e., it is less a function of the model itself and more a result of the nature of transactions that require analysis). Further, we believe that while the frameworks differ, the outcomes of the US GAAP and IFRS rules are largely converged. However, there are likely fact patterns around the edges where differences may exist and, therefore, convergence – either directly, or more generally through development of new single model framework – runs the risk of creating unintended consequences and/or replacing existing complexity with new complexity. Therefore, we strongly discourage the Board from exploring a project that amends the existing guidance in any meaningful way. Instead, we encourage the Board to proceed with the existing "Consolidation Reorganization and Targeted Improvements" project, which we believe will improve the usability and address the majority of concerns raised by stakeholders.*

*#3B – Disaggregation of financial reporting information*

*Our member firms do not typically receive inquiries from investors regarding further disaggregation of the topics outlined in this chapter of the ITC.*

*Generally, we agree with the findings of the FASB staff in its educational paper that ESG matters should be considered as relevant factors in applying judgment and developing accounting estimates under current US GAAP, and we believe they currently are in practice. A good example of this is the impact of wildfires and hurricanes on estimates of the allowance for credit losses. Additionally, the SEC's guidance on risk factors and the reasons for changes in the results of operations should capture the impacts of ESG matters if they are material drivers. Beyond this, we believe that ESG disclosures are important and increasingly relevant and, to that end, certain of our member firms currently provide separate sustainability reports to capture this information. Given the evolution in this space and because ESG is often much broader than the impacts it may have on financial reporting and accounting matters, we believe these and similar forms of disclosure are currently the best tools as they provide management with reasonable flexibility to meet the needs of users. That said, we are closely monitoring efforts of the SEC and its Climate and ESG Task Force to refine and enhance these types of disclosures, and believe they are best positioned in the U.S. to make such determinations (e.g., by identifying existing frameworks and/or standard-setting bodies focused on ESG and leveraging accordingly). Therefore, we do not suggest the Board explores a project on ESG disclosures at this time.*

*Generally, our member firms believe that targeted review of disclosure effectiveness can be more appropriately addressed on a topic-by-topic basis, like the Board's observation related to its* *project on tax disclosure information. As such, we would recommend that any changes to disclosures for taxes and business combinations be addressed in the context of specific projects. Both topics are complex and already subject to significant disclosure requirements. Additionally, the SEC's guidance on business combinations provides incremental disclosure information and requirements that should be considered in any changes to disclosures for business combinations.*

*Our member firms also believe that disclosure effectiveness, including considerations for disaggregation, should be driven by principles rather than required minimum information that does not allow for judgment and materiality in determining what information is relevant and useful. This is especially true for our industry where many of the topics listed in Chapter 1 of the ITC are not as meaningful to the financial statements and could result in significantly more disclosures and cost to produce such information without a corresponding benefit to users.*

*#3C – Financial KPIs and Non-GAAP metrics*

*We believe the Board should not explore a project to standardize non-GAAP metrics or other key performance indicators. As alluded to in the preparer feedback included in the ITC, we believe these types of measures are important tools that allow management to articulate their specific view of the business and its performance; therefore, by design these are and should be entity-specific. Forcing consistency would diminish their usefulness and/or would lead management to simply adjust them in a non-GAAP manner. Further, while we appreciate how this diversity may create complexities for users of the financial statements, entities are generally required to reconcile all such measures to the corresponding reported US GAAP balances/activities and, therefore, their calculations are fully transparent. Additionally, the SEC already has regulations[7] and related interpretations on the use of non-GAAP measures in place which provide a necessary framework for these measures. Finally, as it relates specifically to EBITDA and free cash flow, we observe that these metrics are generally not used by our member firms; instead, efficiency ratios and/or measures of return on equity are typically more relevant. As a result, if the Board does in fact elect to proceed with a project focusing on those measures, we strongly encourage them to consider excluding certain industries from the scope thereof.*

*#3D – Recognition and measurement of government grants for business entities*

*Accounting for government grants is not a key area of concern for our member firms and, therefore, we would not suggest the Board explores a project at this time. However, if the Board does decide to proceed, we agree with the comments in the ITC that the scope should be very narrow and targeted to a well-defined subset of this activity, to avoid any unintended consequences from a broader more ambiguous scope.*

[7] For example, Regulation G and Regulation S-K, including Item 10(e), with related Compliance and Disclosure Interpretations.

**Question 4:** Are there any financial reporting topics beyond those in this ITC that should be a top priority for the Board to address? Please describe:

a. The nature of the topic
b. The reason for the change
c. Whether the topic is specific to a subset of companies, such as public companies, private companies, or NFPs, or specific to a certain industry
d. How the Board should address this topic (that is, the potential project scope, objective, potential solutions, and the expected costs and benefits of those solutions)
e. What the urgency is of the Board completing a project on this topic (that is, how quickly the issues need to be addressed).

*>Response: We believe that Board should focus on the following topics which are not captured in the ITC or on the current technical agenda:*

*#4A – Expanding the fair value option to certain nonfinancial assets*

*We believe the Board should consider expanding the scope of the fair value option that is provided under Topic 825 "Financial Instruments" to include physical commodity inventories as well as executory contracts related to physical commodities (e.g., storage, transportation, non-derivative purchase or sale contracts) that are managed on a trading basis. This would reduce the administrative burden of applying hedge accounting in certain of these cases or, where hedge accounting is not practical, result in a better reflection of the entity's risk management activities in the financial statements. As it relates to hedge accounting, given the rules do not have a "benchmark" concept for nonfinancial assets in a fair value hedging context, in practice some form of basis typically will exist in the relationship, for example, due to differences in location and/or the physical characteristics of the commodity itself versus what may underlie common, liquid hedging instruments. Therefore, the cost of administering such relationships is often onerous given the quantitative requirements, although such hedges may in fact be highly effective. Separately, where hedge accounting is applied, it can be burdensome to track costs and hedge accounting basis adjustments at the individual hedged item level, among other complexities. Therefore, we believe entities should be permitted to measure both a physical commodity position and its economic hedge at fair value, so that the net risk is clearer to users of the financial statements. We believe a project of this nature would align with the Board's objective of reducing unnecessary complexity given the cost and administrative burden associated with hedge accounting can be significant, and such an option may in fact increase transparency for users of the financial statements by way of having more information about risk management activities included directly in the financial statements.*

*#4B – Alternative recognition of the effect of changes in foreign currency on available-for-sale securities denominated in other than the entity's functional currency*

*It is not uncommon that an entity will use cash instruments to economically hedge various liability-related exposures. One approach is to purchase available-for-sale debt securities denominated in nonfunctional currency to hedge the foreign currency risk associated with nonfunctional currency-denominated liabilities. While this generally serves as a legitimate and effective economic hedge, an accounting mismatch exists as the nonfunctional currency-related remeasurement of the available-for-sale debt securities is recognized in other comprehensive income, while the remeasurement of the nonfunctional currency-denominated liability is recognized in earnings. One alternative would be to provide entities an accounting policy election to instead recognize the nonfunctional currency-related remeasurement of available-for-sale debt securities directly in earnings, which would allow an entity to choose to be consistent with the guidance under IFRS. This would be a simple and practical solution to this issue, reducing the cost and administrative burden associated with certain derivative-based hedging strategies that may be employed to address the issue. Alternatively, see #5A below regarding "Expanding the use of non-derivatives as hedging instruments" for hedge accounting-specific alternatives to the aforementioned accounting mismatch.*

**Question 5:** The objective of this ITC and the related 2021 Agenda Consultation process is to ensure that the FASB continues to allocate its finite resources to standard-setting activities that fulfill its primary mission of improving financial accounting and reporting standards and that are of the highest priority to its stakeholders. Therefore, feedback on the prioritization of projects on the FASB's technical agenda (see Appendix A) would be helpful. Do you have any feedback on the FASB's technical agenda, including the following:

a. Which projects on the FASB's agenda should the Board prioritize completing? Please explain.
b. Which projects, if any, should the Board deprioritize or consider removing from the agenda? Please explain.
c. Which projects, if any, need to be redefined to improve the objective and/or scope? Please explain.

*>Response: We believe the Board should prioritize or deprioritize (as indicated) completing the following projects on its current agenda:*

*#5A – Hedge Accounting – Phase 2 (Prioritize)*

*We applaud the Board's past efforts to amend the hedge accounting rules such that they are easier for preparers to apply and users to understand, while also expanding the scope of risk* *management activities that can qualify. For example, ASU 2017-12 resulted in significant improvements across the entire model and, more recently, the proposed amendments to hedging of closed portfolios of prepayable financial assets (i.e., portfolio-layer hedging) appear to be heading in a positive direction. However, we believe there remain a number of additional targeted improvement and simplifications that would further enhance the overall framework, including some that have been highlighted and discussed in the past though continue to be areas of focus for our member firms and/or clients. The following outlines some of the key targeted improvements, noting the first is generally the most pressing:*

- *<u>Clarifying hedged risk concepts for cash flow hedges</u>. We believe that a key element of this project should address issues in practice related to the distinction between "hedged risk" and "hedged item". An example of this is where an entity is hedging forecasted interest receipts on a portfolio of loans that are currently expected to pay 1-month U.S. Dollar LIBOR, and the question is whether the hedged item is cash flows related to: (1) interest, generically; (2) LIBOR-based interest; or (3) 1-month U.S. Dollar LIBOR-based interest. Ultimately, this can drive the level of quantitative analysis necessary to support hedge accounting (e.g., via homogeneity and/or effectiveness testing), as well as when de-designation of an existing relationship is required and/or amounts need to be reclassified from other comprehensive income to earnings. Historically, there has been diversity in practice regarding the interpretation of this concept, and the hope was that the amendments made by ASU 2017-12 to the hedged risk guidance for cash flow hedges in paragraph 815-30-35-37A would align views. However, issues persist while the Board has looked to further clarify its intent through its current project on "Codification Improvements – Hedge Accounting". We believe that left unresolved, this issue becomes even more complex as loan books transition away from LIBOR over time, as we expect there will be a number of forms of certain replacement references rates (e.g., compounded in advance or arrears; term versus overnight) that may permeate a given portfolio, and at such time there may not be sufficient clarity regarding how this mix evolves over the forecasted period of the relationship. Therefore, we believe if not captured as part of the aforementioned on-going project, the Board should aim to resolve this matter as part of "Hedge Accounting – Phase 2."*

- *<u>Expanding the scope of permissible hedges of foreign currency risk to include foreign-denominated business combinations and issuances of debt</u>. These are common exposures that many entities face, and we believe there should be a mechanism in place to align the accounting treatment with overall economics of these reasonable risk management strategies, rather than acting to impede them. As a technical matter, we believe the foreign currency risk related to the former does ultimately have the potential to impact earnings, for example, by way of impacting the carrying value of goodwill recognized at close, which is subject to impairment post-acquisition (with the additional observation* *that the Board is currently exploring a project that may in fact require amortization). As it relates to the latter, although the foreign currency risk prior to issuance does not impact earnings, we question the relevance of such concept in this particular context as the entity is clearly exposed from an economics perspective and, therefore, allowing hedge accounting does not appear to be unreasonable or to run the risk of abuse.*

- <u>*Expanding the use of non-derivatives as hedging instruments*</u>*. For example, we believe it would be helpful to permit the following to be used as hedging instruments: (1) fixed-rate U.S. Treasury securities in a fair value hedge of the benchmark interest rate risk inherent in a U.S. Dollar-denominated fixed-rate debt obligation; or (2) U.K. Gilt securities to hedge the foreign currency risk associated with Sterling-denominated depository obligations of a U.S. Dollar-functional entity. We believe these are common risk management strategies that should be permissible within the rules, and would provide some level of convergence with hedge accounting under IFRS.*

- <u>*Simplify fair value hedges of nonfinancial assets*</u>*. To the extent the suggestion above to expand the fair value option to physical commodities and commodity-related contracts is not explored by the Board, we believe the Board should consider refinements to the hedge accounting model. One alternative would be to eliminate the effectiveness assessment concept in its entirety for fair value hedges of nonfinancial assets (i.e., no need to meet a quantitative effectiveness threshold). On the surface, it may seem that this would open the rules up to potential abuse, such as using hedging instruments that are entirely unrelated to the hedge items speculative activities (e.g., use an equity-linked total return swap to hedge an exposure to precious metals). However, we believe this risk is actually quite low primarily given that in a fair value hedging context, all mark-to-market on the hedged item and hedging instrument are recognized in earnings, and are classified within the same line item on the income statement. Therefore, the effect of these activities would be transparent – and the lack of a natural offset would be unlikely to "hide" any nefarious activities. Also, we would expect that detailed qualitative and quantitative disclosures would be required to articulate managements objectives, how it assesses its performance against these objectives and the results thereof. Another alternative would be to develop a "benchmark" concept for fair value hedges of nonfinancial assets to support effectiveness assessment. In other words, an entity would still generally be required to quantitatively support that the relationship is highly effective – but such analysis would focus on only a portion of the change in fair value of the position. And assuming the relationship is highly effective, it could also be the case that the commodity is still marked-to-market entirely through earnings (i.e., total changes in fair value), which would retain full transparency on the overall economic effect of the entity's risk management activities.*

- *<u>Expanding the portfolio-layer hedging concept to prepayable financial liabilities</u>. A common product offering for bank holding companies is term deposits that become prepayable at par upon death or adjudicated incompetency of the holder. Across a large portfolio of such deposits, redemption rates as a function of these provisions tend to be very low (e.g., less than a one percent of notional, including in periods of rising interest rates). However, it can be challenging to hedge the underlying benchmark interest rate risk because in practice it is impossible to know: (1) the demographics of any particular holder (e.g., mortality rates); and (2) when the redemption features become exercisable (e.g., the holder has passed away). Therefore, it is difficult at inception to support the likelihood of any individual deposit become redeemable and the corresponding homogeneity of a portfolio of such deposits. Further, to the extent one can overcome those challenges, prospectively one cannot identify, for example, when specific deposits should be removed from the portfolio or, if left in the portfolio, the extent of the optionality that should be factored into the measurement of changes in fair value of the hedged item. Expanding the portfolio-layer hedging concept to these and similar fact patterns is another example of how the rules could be better aligned with reasonable risk management activities.*

- *<u>Expanding cash flow hedging to equity-classified preferred shares with floating-rate dividends</u>. We observe this is another relatively common risk management strategy, and while the dividends do not impact earnings, they do in fact impact earnings per share which is arguably equally if not more prominent a measure.*

*#5B – Effect of Sale Restrictions on Fair Value Measurements (Prioritize)*

*Although we expect the Board will ultimately finalize amendments that when measuring an equity security at fair value, the exit price should not include contractual restrictions that are not a characteristic of the security (e.g., an IPO lock up agreement), we continue to believe that the economic effect of such arrangements is meaningful to users of the financial statements. Therefore, absent a change in view we encourage the Board to incorporate this research project into its existing "Fair Value Measurement of Equity Securities Subject to Contractual Sale Restrictions" project such that the final standard also includes a model that contemplates recognition and measurement of such arrangements at fair value, for example, by expanding the availability of the fair value option. Alternatively, the Board should elevate the separate research project and actively pursue this concept separately.*

*#5C – Business combinations and asset acquisitions (Prioritize)*

*We support the Board's project to improve the accounting for asset acquisitions and business combinations by narrowing the differences between those two acquisition models including the* *accounting for contingent consideration, transaction costs, certain recognition and measurement exceptions. Specifically, in practice the accounting for transaction costs in accordance with Topic 805-50 can lead to inconsistent accounting for similar transactions. For example, following the adoption of ASU 2017-01 "Business Combinations (Topic 805): Clarifying the Definition of a Business", if a company acquires an entity where substantially all of the fair value of its gross assets is concentrated in a group of similar financial instruments, the guidance in Topic 805-50 indicates that the transaction costs should be capitalized, which is different than the guidance to expense transaction costs as incurred for business combinations and is also inconsistent with Topic 820 "Fair Value Measurement", which states that the fair value of an asset is not adjusted for transactions costs. A solution to this inconsistency would be to consider the type of asset that makes up substantially all of the fair value of the gross assets and follow the underlying guidance (i.e., if the substantially all of the assets acquired were property, plant and equipment the acquirer would capitalize the transaction costs, and if the substantially all of the assets acquired is a group of similar financial instruments, the acquirer would expense the transaction costs).*

*#5D – Financial Instruments – Credit Losses (Vintage Disclosures: Gross Write-offs and Gross Recoveries) (Deprioritize)*

*We acknowledge the Board voted to leave this project on the agenda at the July 14, 2021 meeting. As the Board continues deliberations, we encourage them to consider the additional cost and the corresponding benefit of requiring gross write-off and gross recoveries in the CECL vintage tables. If the Board ultimately decides to require additional disclosures, we request that it considers prospective adoption given the anticipated cost and effort that may be required by many institutions to obtain retrospective data that meets the completeness and accuracy standards of the financial statements.*

***Chapter 1—Disaggregation of Financial Reporting Information***

**Question 6:** Greater disaggregation and granularity of the types of financial reporting information described in Chapter 1 have been identified as decision useful to investors. The following insights would be helpful to the FASB when considering this area:

a. Investors and other financial statement users—Which, if any, of the areas described in Chapter 1 should be a top priority for the FASB to consider requiring greater disaggregation—on the income statement, the statement of cash flows, or the notes to financial statements? Would this information be most useful in the financial statements or in the notes to financial statements? How would this information be used to analyze a company and make capital allocation decisions?

b. Preparers—What requests or questions does your company receive from analysts on the areas described within Chapter 1? Please explain any requests or questions your company has received.

>*Response: See Question 3.*

Presentation of the Statement of Cash Flows

**Question 7:** Investors and other financial statement users—What cash flow information, if any, required for your analysis is missing in a statement of cash flows prepared using the indirect method? How would this information influence your decisions and behavior? Please explain.

**Question 8:** Preparers—What requests or questions, if any, does your company receive from analysts on cash flow information? Please explain.

>*Response: As an extension of the comments in #3B above, it is very rare for our member firms to receive questions on the statement of cash flows. Given the nature of our businesses, this is generally not an area of focus by our respective investor bases.*

***Chapter 2—Emerging Areas in Financial Reporting***

Definition of a Derivative

**Question 9:** What challenges, if any, are there in applying the guidance on the definition of a derivative and the related derivative scope exceptions in Subtopic 815-10? Please explain the challenges and whether and how they could be addressed through standard setting.

>*Response: See Question 2.*

Digital Assets

**Question 10:** Investors—How significant are holdings in digital assets, such as crypto assets, in the companies you analyze? What type of financial reporting information about holdings in digital assets do you use in your analysis of a company? How does that information influence your decisions and behaviors? If there is other financial reporting information about digital assets that would be decision useful, what is that information and why is it decision useful?

>*Response: See Question 2.*

**Question 11:** Preparers and practitioners—Does your company (or companies that you are involved with) hold significant digital assets, such as crypto assets? What is the purpose of those holdings?

*>Response: Our member firms do not currently hold digital assets such as Bitcoin. However, our clients are much more active in this area, and we are seeing elevated interest from them with regard to custody, investment and hedging strategies; therefore, we believe this is a key accounting matter that should be addressed for their benefit as well as the likely future benefit of our member firms, as we continue to explore principal holdings in such assets to facilitate market making activities. Further, it is worth noting that the Basel Committee on Banking Supervision recently issued a public consultation[8] on preliminary proposals for the prudential treatment of banks' crypto asset exposures noting that while banks' exposures thereto are currently limited, continued growth and innovation in crypto assets and related services suggests it is relevant to explore. See comments in #2A above for more information.*

**Question 12:** If the Board were to pursue a project on digital assets, which improvements are most important, what types of digital assets should be included within the scope, and should this guidance apply to other nonfinancial assets?

*>Response: See Question 2.*

<u>ESG-Related Transactions</u>

**Question 13:** Are there common ESG-related transactions in which there is a lack of clarity or a need to improve the associated accounting requirements? Please describe the specific transactions and why standard setting is needed.

*>Response: See Question 2.*

<u>Financial KPIs or Non-GAAP Metrics</u>

**Question 14:** Are there common financial KPIs or metrics—either widely applicable to all companies or industry specific—that would provide decision-useful information if they were defined by the FASB? Please explain.

*>Response: See Question 3.*

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[8] https://www.bis.org/bcbs/publ/d519.pdf

**Question 15:** If the FASB were to define certain financial KPIs or metrics, should all companies be required to provide those metrics or should providing those metrics be optional?

>*Response: See Question 3.*

Recognition and Measurement of Government Grants for Business Entities

**Question 16:** If the Board were to pursue a project on the recognition and measurement of government grants, should the FASB leverage an existing grant or contribution model (such as the models in IAS 20 or Subtopic 958-605) or develop a new model? If you prefer leveraging an existing model, which would be most appropriate and why? If the FASB were to develop a new model, what should the model be?

>*Response: See Question 3.*

**Question 17:** The FASB has encountered challenges in identifying a project scope that can be sufficiently described for government grants. If the Board were to pursue a project on the recognition and measurement of government grants, what types of government grants should be included within the scope and why (for example, narrow or broad scope)?

>*Response: See Question 3.*

Intangible Assets, Including Software

**Question 18:** The FASB has encountered challenges in identifying a project scope that can be sufficiently described for intangible assets. If the Board were to pursue a project on intangible assets, what types of intangible assets should be included within the scope and why? Within that scope, should a project on intangible assets be primarily focused on improvements to recognition and measurement or to disclosure?

>*Response: See Question 2.*

**Question 19:** What challenges, if any, exist in applying the capitalization thresholds in Subtopics 350-40 and 985-20? What improvements, if any, could be made to the software capitalization guidance to overcome those challenges? Should there continue to be a capitalization threshold when accounting for software depending on whether it is for internal use or whether it is to be sold, leased, or otherwise marketed? Please explain.

>*Response: See Question 2.*

***Chapter 3—Reduction of Unnecessary Complexity in Current GAAP***

Balance Sheet Classification

**Question 20:** Should the Board prioritize a potential project on current and noncurrent classification of assets and/or liabilities in a classified balance sheet? If yes, what should be the scope? Please explain.

*>Response: Balance sheet classification as a broad concept is not an area of significant concern for our member firms. However, one targeted area that can create some complexity is the classification of instruments that are contingently redeemable on a short-term basis as a function of factors outside the control of either party (e.g., a structured note with a stated 5-year maturity that is automatically accelerated if an observable index, such as the S&P 500, reaches a certain level). As a result, to the extent the Board considers another project on balance sheet classification, it should consider addressing this concept; however, absent feedback on other issues – whether broadly or narrowly focused – we do not believe the Board should prioritize a project solely to address this specific matter.*

Consolidation

**Question 21:** Should the Board prioritize a potential project to simplify the consolidation guidance in Topic 810? Please explain why or why not. If yes, should the approach focus on targeted improvements or a holistic review of Topic 810?

*>Response: See Question 3.*

Debt Modifications

**Question 22:** What challenges, if any, exist in accounting for debt modifications in accordance with the guidance in Subtopic 470-50, Debt—Modifications and Extinguishments? Please explain the challenges and how they could be overcome through standard setting.

*>Response: We agree with the stakeholder feedback in the ITC that the accounting for debt modifications can be complex in practice. For example, where refinancing activities involve debt arrangements that are widely held (e.g., syndicated loans, publicly-issued or privately-placed debt securities, including those that may be held by affiliated entities, such as the separate lending and asset management of a particular financial institution), determining whether and to what extent there is continuing involvement of a particular creditor can be burdensome. Additionally, determining what amounts are paid to the lenders as part of a refinancing can also*

*present challenges where, for example, a creditor also serves in an administrative agent role for a syndicate. Further, the guidance does not consider situations where, for example, a broker/dealer subsidiary purchases debt issued by its bank holding company parent/affiliate as part of its normal market making activities, which is common for many of our member firms. As a result, we do believe some targeted improvements may be helpful.*

*Regarding the complexities identified with certain refinancing activities, a practical solution may be to incorporate a qualitative assessment to the test as well, similar to what exists for loan modifications in Subtopic 310-40. In certain cases, this may alleviate some of the burden related to the quantitative analysis that currently exists. Alternatively, simply providing preparers an option to treat such transactions as an "extinguishment" without any analysis may be most optimal, as it would reduce the risk that a qualitative analysis is challenged. Separately, as it relates to market making activities in one's own debt in the context of bank holding companies, we strongly believe that acknowledging such activities do not result in the extinguishment of the debt held would help address diversity in practice and reduce the complexities that can arise where, for example, such debt treated is in fact treated as being "extinguished" and is held in a fair value hedge accounting relationship (i.e., need to de/re-designation, which can have knock-on consequences to, for example, the level at which benchmark interest rate cash flows are set for purposes of computing changes in fair value of the debt due thereto).*

<u>Distinguishing Liabilities from Equity</u>

**Question 23:** Stakeholders noted many challenges in applying the liabilities and equity guidance, but they had mixed views on how the Board should improve the accounting for financial instruments with characteristics of equity. The Distinguishing Liabilities from Equity Phase 2 project is intended to align the two existing indexation models in Topic 480 and Subtopic 815-40. Should the Board continue pursuing this project in its current scope and objective, or does the Board need to reevaluate this project? Please explain why or why not and if the project scope and objective need to be reevaluated, what should the approach be?

*>Response: Distinguishing liabilities from equity continues to be an area of significant complexity in U.S. GAAP, particularly as it relates to the "indexation" concepts in Subtopic 815-40-15. Despite this guidance having been in place for many years, there continue to be misinterpretations with significant implications. That said, despite the Board's best efforts and multiple attempts at fixing these rules, a reasonable solution has not yet been identified that does not introduce more complexity, either by introducing complex judgments (e.g., likelihood that certain unobservable events occur) or increasing the need to fair value instruments (including those unobservable events), which introduces additional costs to preparers. As a result, we believe it may be more appropriate for the Board to consider targeted improvements (e.g., similar to the recent amendments to Subtopic 815-10-15 related to "down-round" provisions)*

*and/or provide some level of good faith protection in the guidance to the extent the preparer's assessment proves to be incorrect, such as accounting for changes in classification prospectively (i.e., similar in spirit to the amendments made in ASU 2017-12, which permitted use of the long-haul method as/if/when it is determined that the short-cut method was not or no longer appropriate). That said, even on a more targeted basis we believe this should not be a top priority of the Board – for example, it would be our strong preference that focus is first placed on the items outlined above in response to Question 2 as well as our comments regarding "Hedging – Phase 2." Either way, as this accounting area is very relevant and important to our clients, we would be happy to connect with the FASB Staff directly to share our perspectives and discuss the issues we see in practice.*

<u>Materiality Considerations for Disclosures</u>

**Question 24:** How helpful would it be in evaluating disclosure materiality if the materiality guidance in paragraph 105-10-05-06 that "the provisions of the Codification need not be applied to immaterial items" was repeated in the Disclosure Section of each Codification Subtopic? Please explain.

*>Response: Although we would not expect such an amendment to change practice, this may add some value from a logistical standpoint. We suggest considering this as part of Board's recurring codification improvement process as opposed to creating a separate project/effort.*

## ***<u>Chapter 4—Improvements to FASB Standard-Setting Processes</u>***

**Question 25:** Which, if any, of the FASB processes described in Chapter 4 of this ITC could be improved? Please explain your rationale for each, including the following:

a. Why that process needs improvement
b. How the FASB should improve that process
c. What the urgency is of that process improvement.

*>Response: See Question 2.*