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LETTER OF COMMENT NO. 15



September 14, 2007

Mr. Russell G. Golden
Director of Technical Application & Implementation Activities – FSP
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116

File Reference: Proposed FSP FAS 140-d, Accounting for Transfers of Financial Assets and Repurchase Financing Transactions (the “Proposed FSP”)

Dear Mr. Golden:

Goldman Sachs appreciates the opportunity to comment on Proposed FSP FAS 140-d, *Accounting for Transfers of Financial Assets and Repurchase Financing Transactions* (the “Proposed FSP”). We understand the catalyst for the Proposed FSP was an accounting – motivated transaction. While we support the original intent of the Proposed FSP, we believe it rests on a broad interpretation of paragraph 55 of SFAS 140, sacrificing many legitimate and economically sound transactions for theoretical purity. Moreover, the Proposed FSP raises serious operational issues that cannot be overcome without broad based assumptions. It also could lead to a significant reduction in reported leverage as more transactions are viewed as forwards, an outcome that may not have been intended by the Board. Finally, the effective date of the proposed FSP is less than three months from now. The effective date is unrealistic and needs to be delayed by one year. For these reasons we do not support the Proposed FSP in its current form.

Linkage Model

Some have questioned whether a Repurchase Financing (as defined in the Proposed FSP) should be considered a linked transaction under the premise that all ongoing involvement with a transferred asset should be considered, and have sought clarification from the

Board. We note, however, that there is currently little to no diversity in practice in accounting for these transactions. Practitioners, absent additional guidance, currently analyze Repurchase Financing using a substance over form argument, and account for a Repurchase Financing as two distinct transactions (sale and a financing), unless evidence exists to the contrary. In our view, a key component of the analysis is whether the transferor's risk profile with respect to the underlying asset has changed, such that it no longer has market risk but instead has credit risk to the transferee consistent with collateralized financing agreements. Credit risk is informed by, among other factors, the credit quality of the transferee/borrower, loan-to-value ratios, liquidity of the underlying collateral, maturity date, frequency of margining and market conditions. Consider the following:

Example 1:

Dealer A's sales desk sells an illiquid security to Company B. Company B indicates that they are looking to finance the purchase and requests a quote. Dealer A's sales desk contacts Dealer A's financing desk for assistance with providing a quote to Company B. After considering the credit risk, the financing desk of Dealer A recommends repurchase financing and quotes an interest rate of X%, contingent upon a 30% haircut (equity) on the loan with appropriate margining and other key terms. Company B may obtain quotes for the financing from other sources for comparative purposes. Dealer A, however, will likely be able to quote a slightly cheaper financing rate than other lenders that do not currently own the asset. This difference predominately is attributable to how familiar/comfortable the lender is with the asset.

Analysis under the Proposed FSP

The transferred asset is not actively traded, and as a result, the Repurchase Financing would be deemed linked and would require further analysis under paragraph 9(a). As observed in the Proposed FSP, if we require legal counsel to consider the initial transfer and the repurchase financing "linked," we likely would not be able to obtain a "would" level true sale opinion for this transaction.

Analysis under current practice

We would analyze the above transaction as follows:

- a) Was the Repurchase Financing entered into to obtain a preferential tax or accounting result?
- b) Is the Repurchase Financing contractually or implicitly linked, i.e., is the transferor required to provide financing as a condition of the sale?
- c) Did the transferee (borrower) retain the risks and rewards of the transferred asset through appropriate interest rates on the financing, margining, haircuts and other key terms?
- d) Was the transaction entered into at market, and can the transferee obtain third party quotes for financing the transferred asset?
- e) Does the Repurchase Financing allow the borrower to finance other assets purchased from third-party dealers?

Based on the factors above, we would conclude that the Repurchase Financing was entered into in the normal course of business and should be evaluated as two separate transactions.

We believe this approach correctly identifies those transactions that should be accounted for separately. The alternative approach, adopted by the Proposed FSP, is to interpret paragraph 55 of SFAS 140 broadly and require linkage in all cases unless the Repurchase Financing meets the very limited exception provided by paragraph 7 of the Proposed FSP. As the exception provided for in paragraph 7 lacks the breadth of a substance over form analysis, many Repurchase Financings will be deemed linked, even in cases where it is apparent to us that linkage is not appropriate. The Board has acknowledged that this Proposed FSP would be a short term solution, recognizing that SFAS 140 will be significantly amended in the near future. It is unclear to us why the Board supports, as a short term solution, a model that diverges from current practice and all other “linkage” models in GAAP² and IFRS, and above all, is operationally difficult if not impossible to put into practice.

Analysis of the Proposed FSP’s Linkage Model

As stated above, we believe the linkage model described by the Proposed FSP does not distinguish between transactions that should be linked from those that should not. In our view, this is a direct result of a) presuming linkage unless the Repurchase Financing meets all of the factors provided by paragraph 7 and b) incorporating factors related to “transfer of control.”

We recognize that SFAS 140 uses a “transfer of control” model to analyze whether a transfer should be accounted for as a sale. However, we do not believe the model for determining linkage should be based on control. Rather, we believe the linkage model should be based on economic substance. If the transaction lacks economic substance, then it should be analyzed as a single unit using the control based model within SFAS 140.

We support the requirement to analyze the business purpose of a Repurchase Financing and believe this is key to identifying those transactions that should be accounted for separately. Large financial institutions provide a full array of financial services including buying and selling financial assets and providing financing on market terms. We believe that collateralized financing represents a service offered, at market, by an arm of a full service organization – a service that if not offered, will be offered by a competitor. As such, we believe there should be a general presumption that market making and collateralized financing provided to the same counterparty are two distinct transactions that have a valid business purpose, that is, market risk has transferred, and the initial transferor retains credit risk set at an appropriate level for the counterparty. We believe FASB should focus on this criterion and expand on the factors a practitioner should use to conclude whether the financing has a valid and necessary business purpose, separate and distinct from the initial transfer of the financial asset.

We support inclusion of paragraph 7(a) of the Proposed FSP as this factor is generally consistent with other linkage models in GAAP. However, we disagree with the inclusion of paragraphs 7(b), 7(c) and 7(d) of the Proposed FSP. While we acknowledge that recourse and marketability of the transferred asset can be factors to consider in determining whether the Repurchase Financing has a separate valid business purpose, we

² We attach, as Exhibit I, an analysis of other linkage models used in GAAP that provide indicators for determining whether separate transactions should be viewed as a single arrangement or unit. As summarized in the exhibit, the models consistently use a “factors to consider approach” which differs from the model used in the Proposed FSP which requires “all” criteria to be met.

disagree with the premise that it *cannot* have a valid business purpose unless these factors exist. Moreover, we believe the first part of 7(d) is inconsistent with standard SIFMA/BMA or ISMA repurchase agreements. Although the standard agreement can provide the ability for the two parties to negotiate substitution of collateral in the future, this generally must be agreed upon by both parties at the time of substitution. As such, Repurchase Financings will generally be deemed linked (including those involving highly liquid assets) under the Proposed FSP. We believe 7(e) is an unnecessary criterion as it is already a part of SFAS 140.

Scope

We believe the scope of the Proposed FSP requires further clarification. Footnote 1 combined with Footnote 2 of the Proposed FSP can be viewed as applying to any financing arrangement where collateral is held in custody by the lender. For example, the Proposed FSP can apply to, among other things, stock borrow and stock lending transactions, margin lending, and prime brokerage accounts. If the Board did not intend to include these transactions in scope, we believe footnote 1² and footnote 2³ of FIN 41, *Offsetting of Amounts Related to Certain Repurchase and Reverse Repurchase Agreements*, more concisely defines a repurchase agreement.

However, from a theoretical standpoint, if the Board intends to pursue a broad interpretation of paragraph 55 of SFAS 140, it has a duty to develop a linkage model that can be applied to transactions that are economically similar. If the Board narrows the scope of the Proposed FSP to apply to repurchase agreements only, and retains the linkage model in its current form, that suggests the model is not robust and needs rethinking because it cannot be applied to economically similar transactions.

Operational Concerns

We do not believe the criteria in paragraph 7 of the Proposed FSP are operational when applied to a Repurchase Financing entered into after an initial transfer (“Subsequent Repurchase Financing”) of a financial asset. Paragraph 4 of the ED, as currently drafted, would require a company to consider whether collateral received in a repurchase financing is linked to a prior transfer of the same asset or (substantially the same asset), regardless of the amount of time that may have elapsed between the initial transfer and the subsequent Repurchase Financing. This would require a company to perform due diligence on all collateral accepted in a repurchase agreement to ensure that the collateral accepted was never previously transferred from the company’s balance sheet to the same

² Footnote 1 of FIN 41 states: “For purposes of this Interpretation, a repurchase agreement (repo) refers to a transaction that is accounted for as a collateralized borrowing in which a seller-borrower of securities sells those securities to a buyer-lender with an agreement to repurchase them at a stated price plus interest at a specified date or in specified circumstances. The “payable” under a repurchase agreement refers to the amount of the seller-borrower’s obligation recognized for the future repurchase of the securities from the buyer-lender. In certain industries, the terminology is reversed; that is, entities in those industries refer to this type of agreement as a ‘reverse repo’.”

³ Footnote 2 of FIN 41 states: “For purposes of this Interpretation, a reverse repurchase agreement (reverse repo) refers to a transaction that is accounted for as a collateralized lending in which a buyer-lender buys securities with an agreement to resell them to the seller-borrower at a stated price plus interest at a specified date or in specified circumstances. The “receivable” under a reverse repurchase agreement refers to the amount due from the seller-borrower for the repurchase of the securities from the buyer-lender. In certain industries, the terminology is reversed; that is, entities in those industries refer to this type of agreement as a ‘repo’.”

counterparty. As proposed, if the company historically transferred the asset or substantially the same asset to the repo counterparty, the company would be required to analyze the initial transfer and the repurchase financing, (regardless of the passage of time) under the criteria in paragraph 7 as a potential linked transaction. Even if the transaction meets the requirements of paragraph 7(a) and is not deemed contractually or implicitly linked, the repurchase agreement can fail to meet 7(b) through 7(e). This would require the initial transfer (which may have occurred years earlier) and subsequent repurchase, to be analyzed as a linked transaction for purposes of determining whether the initial transfer was a true sale. Consider the following:

Example 2:

Broker A transfers a newly issued 10 year treasury security to Broker B. Four years later Broker B approaches Broker A and requests repurchase financing for a treasury security.

Analysis

Paragraph 4 of the ED requires a transferor to consider all future involvements with the transferred asset even if those involvements occur at a later date than the initial transfer. Broker A would be required to perform an analysis of whether the treasury security (or substantially the same asset) was ever on its balance sheet and transferred to Broker B. If there was a previous transfer, then the transfer together with the repurchase financing would be analyzed under criterion 7(a). *If the initial transfer did not contemplate a repurchase financing and all the other criteria were met, then the repo financing would be accounted for as a separate transaction.*

Example 3:

Same as Example 2 except the transferred asset is an illiquid security.

Analysis

Paragraph 4 of the ED requires a transferor to consider all future involvements with the transferred asset even if those involvements occurred at a later date than the initial transfer. Broker A would be required to perform an analysis of whether the illiquid security (or substantially the same asset) was ever on its balance sheet and transferred to Broker B. If there was a previous transfer, then the transfer together with the repurchase financing would be analyzed under criterion 7(a). The initial transfer did not contemplate a repurchase financing and therefore would meet the requirements of paragraph 7(a); however, the illiquid security is not an actively traded asset as required by paragraph 7(c) and as a result, the repo financing would need to be accounted for as linked transaction with the initial transfer.

Other Operational Concerns

The timing issue also presents itself in stock borrow and stock loan transactions. In the normal course of business, we sell stock into the market and enter into stock borrow transactions to cover short positions. We believe the ED, without further clarification, would require us to consider whether we ever previously transferred the stock to the counterparty. We would most likely conclude that we had transferred the stock to the counterparty, as we trade most equity securities. We would then be required to analyze the repurchase financing under paragraph 7 of the ED. As stock borrow and loan transactions generally do not provide the transferee with the ability to substitute collateral, all such transactions would be deemed “linked” under part 1 of paragraph 7(d).

Additionally, the market for stock borrow and stock loan transactions encompasses potentially scarce or “hard to borrow” stock. Part 2 of paragraph 7(d) limits the ability of the initial transferor to rehypothecate the collateral received unless the collateral is “readily available.” As the business of stock borrow and stock loan transactions depends on the ability to rehypothecate collateral that may be hard to borrow (because of its potential scarcity), many stock borrow and stock loan transactions would be deemed linked transactions under part 2 of paragraph 7(d).

We both purchase and sell financial assets and enter into financing arrangements where we take possession of collateral thousands of times daily, and frequently with the same counterparties. Because of the sheer volume of transactions we enter into each day, we cannot keep a real time history for any significant length of time. Nor do we maintain a perpetual history of transactions. In theory, to comply with the Proposed FSP, we would need to retain this information in perpetuity and in a readily accessible format in order to match collateral transferred or received in a repo trade against a history of all inventory purchased or sold. As a practical matter, we do not believe such a system could be built nor would such a system be useful other than to comply with the Proposed FSP. We believe the Proposed FSP can never be operational if it retains its requirement to apply paragraph 7 to Subsequent Repurchase Financings. If the Board decides to proceed with the model used in the Proposed FSP, we believe this issue can be clarified, in part, by requiring that a company must fail paragraph 7(a) for repurchase financing not entered into simultaneously with the initial transfer before analyzing the repurchase agreement under paragraphs 7(b) through 7(e).

Decreased Transparency in Financial Reporting

We are concerned that the Proposed FSP would significantly reduce financial statement transparency and reported leverage. Under current practice, the transferor/lender reports securities purchased under agreements to resell as a separate asset. The effect of applying the Proposed FSP would be to reverse the transferred asset back into inventory and record a forward sale. The net effect is to report what is economically a collateralized lending transaction within inventory. Additionally, the transferee (borrower) will be required to net the repurchase obligation (on balance sheet debt) against the purchased asset and record a forward purchase contract. The net effect of the Proposed FSP is less debt recognized on balance sheet.

Moreover, regulated entities such as financial institutions must adhere to regulatory capital requirements determined in accordance with the rules of their relevant regulatory agency. These rules are generally aligned with the GAAP balance sheet. We note that inventory and a forward sales contract would attract a lower capital charge than reverse repurchase agreements for us. As we believe the proposed GAAP reporting will not present the underlying economics of these transactions, we encourage the Board to seek out the views of regulators and possible changes to regulatory capital calculations.

Interaction with Other Accounting Literature

We ask the Board whether there was full consideration of the effect of the Proposed FSP on reconsideration events required under FIN 46(R). We believe in certain instances, such as the current environment, where an entity’s actual losses exceed expected losses, recording collateral received in a repurchase financings as inventory at the onset, as a result of a deemed “linked transaction,” would not be a reconsideration event under FIN 46(R). Consider the following:

Example 4:

Same as Example 1 except the asset sold is 100% of the securities from a mezzanine tranche of a securitization vehicle. The tranche does not absorb a majority of the vehicle's expected losses at the time of initial sale. Subsequent to the sale, actual losses exceed expected losses, exposing the mezzanine tranche to significant losses.

Analysis under current practice

We would conclude as a result of the sale, that we do not have a variable interest in the securitization vehicle. If the buyer (borrower) defaults and we take title to the mezzanine collateral, we would conclude we now have a variable interest in the securitization vehicle and, would likely consolidate.

Analysis under the Proposed FSP

As the Repurchase Financing would be deemed a linked transaction, we would continue to hold the underlying securities in inventory. We would have performed a FIN 46(R) analysis on the mezzanine tranche when we first became involved and concluded that we are not the primary beneficiary. If the buyer (borrower) defaults on its forward contract, the default of the borrower would not be considered a reconsideration event. Equally so, we believe the buyer (borrower) would never perform a FIN 46(R) analysis.

Transition and Effective Date:

As discussed above, significant changes to systems, controls and processes will need to be made and implemented. This process cannot start until after a final FSP is issued. For entities with a November 30th year end, the proposed effective date would allow little time for implementation. We ask the Board to delay the effective date at least a year after issuance. Further, we do not agree that the proposed FSP should apply to outstanding Repurchase Financings. We acknowledge that the majority of Repurchase Financings are short-term in nature. However, we would not be able to apply the final FSP to those transactions that have maturity dates that extend beyond the implementation period granted in the final FSP, as we lack the necessary historical tracking information to apply the provisions of paragraph 7 to these transactions. We ask the Board to require prospective application for new transactions only.

If we can be of further assistance or if you have questions about our comments, please contact me.

Sincerely,



Matthew L. Schroeder

Exhibit I

Indicators for Determining Whether Separate Transactions Should be Viewed as a Single Arrangement or Unit ¹	ED FSP 140-d	EITF 04-13	DIG Issue K1	Noncontrolling Interest ED ²	EITF 00-21 ³
Contemporaneous / contemplation of one another (7a)	X	X	X	X	X
Same counterparty (7)	X	X	X		X
Legally contingent / dependent (7a)	X	X		X	
Legal right of offset		X			
Off-market terms/At market terms (7c)	X	X			
Relative certainty of occurrence of reciprocal transaction		X			
Same risk/Full recourse to Transferee/Transferee retains risk (7b)	X		X		
No economic / substantive purpose for structuring separately (7)	X		X	X	
Achieving a single overall commercial effect				X	
Transferee can substitute collateral/Transferor cannot repledge unless readily obtainable (7d)	X				
Financial asset and repo financing are not coterminous (7e)	X				
Indicators Needed					
Some		X	X		X
All	X				
Just one				X	

Notes

1. For the purpose of this analysis, we have attempted to combine similar concepts, although the precise wording is different across the documents. Paragraph references refer to the Proposed FSP.

2. Paragraph 29 of the Proposed Statement of Financial Accounting Standards: Consolidated Financial Statements Including Accounting and Reporting of Noncontrolling Interests in Subsidiaries (“Non-controlling interest ED”)

3. For the purpose of this analysis, we did not include paragraph 9 criteria because they are in the context of revenue recognition guidance.