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c/o International Accounting Standards Board
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Our ref MT/288
Contact Mary Tokar

2 April 2009



LETTER OF COMMENT NO. 23

Dear Mr Goldschmid and Mr Hoogervorst

Financial Crisis Advisory Group Request for Written Input

We appreciate the opportunity to respond to the Financial Crisis Advisory Group's (FCAG) request for input in support of the FCAG's discussion of accounting and reporting matters related to the financial crisis and the development of recommendations thereon to the International Accounting Standards Board (IASB) and the U.S. Financial Accounting Standards Board (FASB) (the Boards). This letter represents the views of KPMG International and its member firms, including KPMG LLP (U.S.) and is being submitted to both the FASB and the IASB.

We continue to support the efforts of FCAG in identifying potential standard-setting priorities for the Boards in addressing accounting and reporting issues raised by the financial crisis. Appendix A to this letter provides our responses to the specific questions raised in the request for input.

If you have any questions about our comments or wish to discuss any of these matters further, please contact Mary Tokar with the KPMG International Financial Reporting Group in London at +44 (0)20 7694 8871 or Mark Bielstein with KPMG LLP in New York at +1 (212) 909-5419.

Yours sincerely

KPMG IFRG Limited

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cc: Mr Robert Herz, Financial Accounting Standards Board
Sir David Tweedie, International Accounting Standards Board

Appendix A: Responses to the questions set out in the request for input

1. From your perspective, where has general purpose financial reporting helped identify issues of concern during the financial crisis? Where has it not helped, or even possibly created unnecessary concerns? Please be as specific as possible in your answers.

We believe that the requirement to account for and disclose certain financial instruments at fair value has been a useful indicator that has helped to identify issues on a timely basis and inform market participants about the economic risks inherent in certain types of instruments and transactions. In our view, the requirement to account for certain financial instruments at fair value has not caused the financial crisis. However, we recognize that additional authoritative guidance on fair value measurements for assets that are not traded in active markets and the application of other-than-temporary impairment guidance in U.S. GAAP would be useful.

We note that the FCAG has previously discussed the issue of whose information needs should be the focus of general purpose financial statements (i.e., investors versus regulators). We believe this discussion has been very useful in bringing the issue to light and we agree with the preliminary conclusion that it should be investor-centered. We believe that accounting and reporting that is focused on the needs of investors has provided useful, timely and decision-useful information.

2. If prudential regulators were to require 'through-the-cycle' or 'dynamic' loan provisions that differ from the current IFRS or US GAAP requirements, how should general purpose financial statements best reflect the difference: (1) recognition in profit or loss (earnings); (2) recognition in other comprehensive income; (3) appropriation of equity outside of comprehensive income; (4) footnote disclosure only; (5) some other means; or (6) not at all? Please explain how your answer would promote transparency for investors and other resource providers.

We support the efforts of prudential regulators to re-examine capital adequacy requirements and help bring about greater stability within the financial sector. We believe also that prudential initiatives and requirements should not be constrained by current financial reporting requirements. To the extent that prudential regulatory changes create differences from financial reporting requirements, we believe that the differences should not be reflected in profit or loss or comprehensive income. Therefore, we would support reflecting any such difference in relation to loan provisions by appropriation of equity outside of comprehensive income or by footnote disclosure, assuming that the basis of calculation is transparent.

We believe that the Boards should, as a priority, reconsider the current financial asset impairment model, including an examination of the incurred and expected loss approaches for loan loss accounting. Prudential regulatory conclusions should be considered as part of the Boards' reconsideration. In our view, the footnotes to the financial statements should incorporate discussion of regulatory capital requirements set by prudential regulators. There may be other significant differences between regulatory capital and analogous financial statement measures aside from any new requirements for 'through-the-cycle' or 'dynamic' loan

loss provisions. Furthermore, regulatory capital requirements may involve complex and subjective calculations and voluminous data processing. Any new requirements to disclose information in relation to other capital measurements should consider whether such information is capable of evaluation according to specified criteria and the costs of compliance, including the costs of additional audit procedures.

3. Some FCAG members have indicated that they believe issues surrounding accounting for off-balance sheet items such as securitisations and other structured entities have been far more contributory to the financial crisis than issues surrounding fair value (including mark-to-market) accounting. Do you agree, and how can we best improve IFRS and US GAAP in that area?

The lack of transparency about the risks attached to securitised products has contributed to current conditions. These include the rapid growth of complex, opaque and risky instruments, their global distribution across unregulated markets, and reliance on external credit-ratings. Illiquidity, price declines and defaults have severely tested risk management and valuation processes. Regulatory treatments of securitisation structures may also have encouraged their use.

The existing US GAAP derecognition standards in FASB Statement No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishment of Liabilities* (SFAS 140), including its requirements for qualifying special purpose entities (QSPEs) may have influenced the structure of certain securitisation transactions. KPMG LLP (US) previously commented in a letter related to the proposed amendments to SFAS 140 to the FASB as of October 30, 2008 that it supports removal of the QSPE concept as an immediate priority.

We recently responded to the IASB's consolidation proposals, ED 10 *Consolidated financial statements*. We stated that the IASB should cease pursuing immediate fundamental changes to the IFRS consolidation model which we believe has performed reasonably well; instead it should focus in the short term on enhancing the disclosures relating to consolidation and off-balance sheet exposures, in particular risks arising from involvement with and support extended to non-consolidated structured entities.

Convergence of the derecognition, consolidation, and disclosure requirements for securitisations and structured entities is already part of the joint IASB/FASB MoU and we agree that the Boards should work together to achieve unified standards in the medium term.

4. Most constituents agree that the current mixed attributes model for accounting and reporting of financial instruments under IFRS and US GAAP is overly complex and otherwise suboptimal. Some constituents (mainly investors) support reporting all financial instruments at fair value. Others support a refined mixed attributes model. Which approach do you support and why? If you support a refined mixed attributes model, what should that look like, and why, and do you view that as an interim step toward full fair value or as an end goal? Whichever approach you support, what improvements, if any, to fair value accounting do you believe are essential prerequisites to your end goal?

Generally, we believe that financial statements will be more understandable if the number of measurement bases for financial instruments is reduced. We have previously commented that we believe that the long-term objective should be that all financial instruments should be measured at fair value. However, before that objective could be accomplished, there are significant concerns that would need to be addressed and other changes would be needed regarding fair value measurement guidance and the presentation and display of financial performance. These issues include: significant concerns around the definition and measurement of fair values under IFRS and the sometimes subjective nature of fair value estimates, including the valuation of instruments not traded in active markets; recognition of all fair value changes in profit or loss without differential display may result in an entity's reported performance not appropriately reflecting its business model; and the usefulness of recognising in profit or loss unrealised gains and losses on an entity's debt arising from changes in its own credit risk.

The current crisis has shown that preparers would benefit from additional authoritative guidance on fair value measurements when observable market prices are not available. In particular, additional guidance on the effect of illiquidity and risk premia could result in greater *comparability of information across industry sectors and geographic boundaries*. We believe that the guidance issued in October 2008 by the IASB's Expert Advisory Panel, *Measuring and disclosing the fair value of financial instruments in markets that are no longer active*, has been a useful source of information for measuring the fair value under IFRS of financial instruments that are not traded in active markets.

With respect to performance reporting, we believe that completion of the Boards' project on financial statement presentation could be an important step in clarifying the presentation of financial instruments. An appropriate financial statement presentation model is needed so that preparers can communicate clearly the results of their ongoing operations versus other fair value changes included in earnings in a manner that is informative to financial statement users. We believe that presentation rather than measurement is the most appropriate way to provide flexibility for preparers to reflect differences in their business models.

We acknowledge that an intermediate step could be to continue with mixed measurement models as long as it reduces existing complexity. For example, currently there are differences regarding impairment triggers, measurement of impairment losses, and reversals of impairment losses between IFRS and US GAAP and the models also differ within the respective frameworks. In our view, the Boards could work to converge their impairment models as a near-term improvement in the mixed measurement models currently in use. In particular, we support the approach to recognition of impairment losses on available-for-sale debt securities proposed by the FASB in Proposed FASB Staff Position FAS 115-a, FAS 124-a, and EITF 99-20-b, "Recognition and Presentation of Other-Than-Temporary Impairments" which could be a platform for achieving greater convergence between the impairment models under IFRS and U.S. GAAP.

5. What criteria should accounting standard-setters consider in balancing the need for resolving an 'emergency issue' on a timely basis and the need for active engagement from constituents through due process to help ensure high quality standards that are broadly accepted?

In our view, the due processes that have been established by the Boards provide constituents with the ability to meaningfully participate in the standard-setting process and support the development of high-quality standards. However, we recognise that there may be situations that *will require a Board to expedite, but not abandon, its due process. These situations might include extraordinary events whose effects reveal significant problems with the application of existing standards that were not previously understood or foreseen.* Therefore, we believe it would be useful for each Board to formalise an expedited due process and the general circumstances when its use would be warranted to ensure that even in these situations there is sufficient due process to allow the Board's constituents to provide meaningful input to its deliberations in support of high-quality, generally accepted standards.

6. Are there financial crisis-related issues that the IASB or the FASB have indicated they will be addressing that you believe are better addressed in combination with, or alternatively by, other organizations? If so, which issues and why, and which organizations?

In our view, the primary objective of accounting standard-setters and prudential regulators differ. Accounting standard-setters focus on developing accounting standards that help provide transparent information in general-purpose financial statements that are used by capital providers in making capital resource allocation decisions. Conversely, the objective of prudential regulators is to ensure financial stability.

However, we acknowledge that there may be circumstances in which standard-setters and prudential regulators (for example the Basel Committee on Banking Supervision) may find it useful to work together when the subject matter has an impact on both financial reporting and prudential regulation. In these situations, however, we would expect the Boards' perspective to continue to be the development of accounting and reporting requirements that best serve the information needs of capital providers.

7. Is there any other input that you'd like to convey to the FCAG?

Pending further progress on an overall model on accounting for all financial instruments, we support the development of a single impairment model for financial assets. There currently exist different models between different classes of financial assets both within and between the FASB and IASB standards that we believe should be a convergence priority.

In our view, one objective of the Boards should be to simplify hedge accounting. However, until completion of the financial statement presentation project, we believe that it is important to continue to allow existing hedge accounting models to remain in place to avoid the possibility of replacing one set of complexities with another (see our response to Question 4).