



October 12, 2009

BY EMAIL TO: director@fasb.org

Mr. Russell G. Golden
Technical Director
Financial Accounting Standards Board
401 Merritt 7
PO Box 5116
Norwalk, CT 06856-5116

Re: Proposed Accounting Standards Update to Topic 820, *Improving Disclosures about Fair Value Measurements* (File Ref No. 1710-100)

Dear Mr. Golden:

The Dealer Accounting Committee of the Securities Industry and Financial Markets Association¹ is pleased to offer you our comments on the above-captioned proposed Accounting Standards Update (the “proposed ASU”). The Committee consists of large, internationally active dealers that operate across the full spectrum of the global capital markets. Committee members have extensive practical experience in the application of fair value measurements.

The Committee commends the Board’s efforts to improve disclosures regarding fair value measurements. However, in our view, the bulk of the Board’s proposals do not improve disclosures; they merely increase disclosures without increasing the usefulness of the information being provided. We believe that disclosures about fair value measurements should enable financial statements users to understand the methods, assumptions and inputs involved in developing fair value measurements. Much of the proposals do not achieve this objective, yet the proposed disclosures will be operationally burdensome to produce. Before proceeding with the proposed ASU, we recommend that the Board reassess whether increased quantitative

¹ SIFMA brings together the shared interests of more than 600 securities firms, banks and asset managers locally and globally through offices in New York, Washington, D.C., and London. Its associated firm, the Asia Securities Industry and Financial Markets Association, is based in Hong Kong. SIFMA’s mission is to champion policies and practices that benefit investors and issuers, expand and perfect global capital markets, and foster the development of new products and services. Fundamental to achieving this mission is earning, inspiring and upholding the public’s trust in the industry and the markets. More information about SIFMA is available at <http://www.sifma.org>

disclosures, particularly around Level 3 activity and potential estimation error, will be meaningful, particularly given the significant cost and effort to produce the requested information.

We provide our detailed comments to the proposed ASU in an Attachment to this letter but wish to highlight a few of the more significant points regarding the disclosure of the effect of reasonably possible alternative inputs (“Sensitivity Analysis”), the gross presentation of Level 3 activity, and the proposed effective date.

Effect of Reasonably Possible Alternative Inputs (“Sensitivity Analysis”)

While a Sensitivity Analysis may be relevant for reporting entities with relatively few unobservable inputs, it raises legitimate cost-benefit concerns when applied to large, complex financial institutions operating across the full spectrum of the global capital markets. Its usefulness as a means to measure or present estimation error is also lost when applied to multiple financial instruments or when aggregated with the results from other financial instruments. Level 3 fair value estimates are complex and are based on multiple interrelated assumptions. The Sensitivity Analysis could give financial statement users a false sense of precision in areas that are inherently subjective, as well as a false sense of the comparability of disclosures of different companies, whose application of the sensitivity analysis will necessarily be idiosyncratic. By focusing users on what will be an arbitrary quantitative analysis, the Board’s proposed approach will distract from what in our view is the most important disclosure – that is, a qualitative discussion of the scope, nature and integrity of the procedures the companies use to assure that their estimates and assumptions are reasonable as well as a clear, concise, qualitative discussion of the inputs and valuation techniques used in the fair value measurements.

Gross Disclosure of Level 3 Activity

As global dealers, our members execute thousands of purchases, sales, issuances, and settlements on a daily basis. Isolating those transactions related to instruments classified as Level 3 within the fair value hierarchy would add substantial complexity to the current Level 3 reconciliation process for disclosure of information that, in our view, is not meaningful or otherwise used to manage the business. The cash movements of a particular instrument do not affect profit or loss under mark-to-market accounting. We do not believe that this information will be useful to our financial statement users as management does not use the information.

Effective Date

If the proposed ASU is finalized as currently drafted, we believe the proposed effective date is unreasonable. We would recommend the proposed ASU be effective for interim or annual periods beginning after December 15, 2010. It is unrealistic to expect that all financial institutions will be in a position to implement a standard that will be, in all likelihood, issued just prior to the end of the reporting period in which it is to be applied.

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If you have any questions about the comments above, please feel free to contact the undersigned (212-357-8437; matthew.schroeder@gs.com) or Jerry Quinn (212-313-1207; jqinn@sifma.org) or Kyle Brandon (212-313-1280; kbrandon@sifma.org), the staff advisors to the Committee.

Sincerely,

A handwritten signature in black ink that reads "Matthew Schroeder". The signature is written in a cursive style with a large initial "M".

Matthew L. Schroeder
Chair
SIFMA Dealer Accounting Committee

Attachment

Attachment
SIFMA Comments on Specific Provisions of the Proposed Accounting Standards Update

Effect of Reasonably Possible Alternative Inputs (820-10-50-2(f)) (“Sensitivity Analysis”)

For financial institutions operating in a mark-to-market environment, the proposed Sensitivity Analysis presents issues of both interpretation and complexity due to the number of factors involved in estimating fair value and the interaction of those factors, including but not limited to the following:

Diversity of inputs. As global dealers, our members are counterparties to millions of derivative contracts of which approximately 5-10% are classified as Level 3. We each have thousands of cash positions classified as Level 3. These positions reflect a broad set of product categories with valuations dependent on many diverse inputs and methodologies. These inputs and methods, and therefore the valuations, are not necessarily correlated with each other, expressed in similar units of measure, or additive. Additionally, transactions reported in Level 3 of the fair value hierarchy are generally sensitive to both Level 2 and Level 3 inputs. Often, transactions are classified within Level 3 because they have sensitivity to multiple inputs.

Model structure. For most financial instruments, subjective estimates and assumptions relating to the estimate of fair value fall into three principal categories: (i) model structure, (ii) market data that is not directly observable or derived from reliable third-party quotation sources due to market illiquidity (Level 3 inputs), and (iii) assumptions regarding the correlations of these inputs. It is unclear how to apply the Sensitivity Analysis to assumptions in the form of model structure. This element of uncertainty is not, of course, susceptible to variances that could be reflected in a meaningful quantitative way. One could simply vary the numeric result of the operation of a model (i.e., the “estimate” resulting from the assumption). However, nothing in the model provides a basis on which to inform the range within which it would be appropriate to vary the result of the computation for the purpose of generating an alternative range of outcomes. Disclosure in this area would be further complicated by the fact that valuation models, the assumptions underlying those models and the composition of a company’s portfolio all often involve highly sensitive and proprietary information.

Correlation. As noted above, any fair value estimate includes assumptions regarding the correlation of individual inputs within the model. The proposed ASU would require consideration of the expected effects of correlation among changes in significant inputs if estimating the effect of more than one reasonably possible alternative input. This superficially treats a key problem with the proposed Sensitivity Analysis. It is reasonable to consider correlation of inputs when changing one or several inputs within one fair value estimate. However, the Sensitivity Analysis will be aggregated and thus correlation within the asset class and between asset classes should also be considered. We see no practical way to incorporate correlation within and between asset classes. We believe the only practical way to deal with correlation is to explicitly exclude it from the Sensitivity

Analysis, as the IASB has proposed in its May 2009 Exposure Draft, *Fair Value Measurement*, and disclose that interdependency of the inputs have not been considered.

Lack of alignment with risk management practices. Our risk management generally is based on net risk exposure to a particular sensitivity. For example, our members actively hedge single name credit derivatives with indices. Risk management and risk limits tend to be based on sensitivity to changes in the same inputs across different types of derivative contracts and cash instruments which span various levels within the fair value hierarchy. Building the infrastructure needed to comply with the Sensitivity Analysis disclosure would be done solely for this disclosure rather than to support risk management or to satisfy other management reporting objectives.

The potential for data that can easily be misinterpreted by financial statement users or that overstates the true risks involved would be significant in our view. For these reasons, we question the usefulness of this disclosure for large, complex financial institutions with numerous financial instruments across the full spectrum of capital markets, especially given the cost to comply with the proposed disclosure and the lack of comparability of the disclosure among similar financial institutions.

We question the utility of the information if it is aggregated across the reporting entity, which users will invariably do. While a sensitivity analysis does provide some benefit at a position level, it quickly loses its relevance when aggregated, because aggregation assumes all positions have the same degree of potential estimation error at the same time. In short, aggregation assumes valuation uncertainty is perfectly correlated across all positions and ignores the benefits of portfolio diversification. The aggregate impact is not the algebraic sum of the underlying variances. Most users grasp that concept, and would then ask us, or attempt, to quantify the diversification benefit. Inherently, portfolio estimates of valuation uncertainty are complex qualitative judgments by seasoned professionals with extensive experience in the relevant markets. By their nature, these judgments do not translate well to aggregated disclosure, given their subjective nature and uniqueness.

Our members do not currently perform a sensitivity analysis or otherwise attempt to measure estimation error in this way, so any system build-out to disclose the proposed Sensitivity Analysis will be done purely to comply with the disclosure requirement. Instead, management mitigates estimation error through the strength of the company's internal controls around the valuation process. In order for a financial statement user to understand potential estimation error, they should understand the scope, nature and integrity of the procedures a company uses to assure that its estimates and assumptions are reasonable. This cannot be conveyed via the proposed Sensitivity Analysis, but rather through a clear, concise qualitative discussion of the company's valuation processes and controls, including the subsequent validation of its estimates through actual sales activity.

Moreover, the sensitivity analysis has limited value in predicting changes in market liquidity, a perceived underlying concern of financial statement users. We note that most AAA-rated structured credit tranches, as well as auction rate securities, were classified in Level 2 of the fair value hierarchy prior to the onset of the credit crisis.

Further, we understand that the Board believes that users would benefit from information about a range of fair value for Level 3 measurements because of the greater degree of uncertainty and subjectivity of Level 3 measurements. We note that the subjectivity of Level 3 measurements is the chief reason why disclosure of fair value measurements by their classification within the fair value hierarchy is required by FAS 157. The fact that a measurement is classified as Level 3 is indicative of the measurement's level of subjectivity. A Level 3 classification, along with qualitative disclosure of the inputs and valuation techniques, seems sufficient to convey the level of subjectivity of the fair value measurement.

In summary, while Sensitivity Analysis may be relevant for reporting entities with relatively few unobservable inputs, it raises legitimate cost-benefit concerns when applied to large, complex financial institutions operating across the full spectrum of the global capital markets. Level 3 fair value estimates are complex and are based on multiple interrelated assumptions. In most cases, the potential impacts of using reasonably possible alternative inputs in Level 3 measurements are not additive. An investor may well be better informed by a clear, concise qualitative discussion of the inputs, valuation techniques, and uncertainty of the measurements than by a lengthy, complex sensitivity analysis. For these reasons, we recommend that the Board remove the proposal to disclose a Sensitivity Analysis for Level 3 fair value measurements.

Instead of a Sensitivity Analysis, the Committee would propose disclosures that would seem more useful for investors and other interested parties. Examples of such disclosures might include estimated value at risk, stress tests, scenario analysis or other measures of the potential change in fair value resulting from market movements. Any proposed disclosure should be integrated with management's existing risk management and control processes.

Gross Disclosure of Level 3 Activity (820-10-50-2(c)-2)

We do not believe disclosure of Level 3 gross purchases, sales, issuances and settlements is operational for the reasons preparers provided the FASB when the Statement 157 disclosures were being finalized (hence why Topic 820 currently provides for net presentation). As stated then, in a fair value model, changes in fair value are recorded in income regardless of whether gains or losses are realized or unrealized, that is, the receipt or payment of cash flows does not affect income. For this reason, our members do not track and store purchases, sales, issuances or settlements on a gross basis. As global dealers, our members have thousands of purchases, sales, issuances, and settlements occurring on a daily basis. Isolating those transactions related to instruments classified as Level 3 within the fair value hierarchy would add substantial complexity to the current Level 3 reconciliation process. The level of complexity required is highlighted particularly by the need to perform this analysis retroactively for instruments transferred into Level 3 during the reporting period. Accordingly, we consider the cost of tagging large volumes of cash flows as either a purchase/sale/issuance/settlement prohibitive in comparison to the potential benefits. Furthermore, it is unlikely that we will have significant cash flows which are classified as "sales," because such sales generally provide price transparency, requiring the instrument to be transferred to Level 2. Building the infrastructure needed to comply with this proposed requirement would be done solely for this disclosure rather than to support risk management or to satisfy other management reporting objectives.

In addition to the significant cost and effort to provide Level 3 gross purchases, sales, issuances and settlements, we question the usefulness of presenting this information on a gross basis. As noted above, cash movements in a fair value book are not particularly relevant. Separate disclosure of purchases, sales, issuances and settlements will not provide insight into the risk of the measurement or the market risk exposure of a given class of financial instruments. As such, member firms have not developed systems and processes to gather this information as the information is not used to manage the business or report performance.

We recommend that the Board remove the proposal to present Level 3 purchases, sales, issuances and settlements on a gross basis.

Effective Date and Transition (820-10-65-XX)

The proposed ASU would require companies to make the proposed disclosures in reporting periods ending after December 15, 2009, except for the sensitivity analysis, which would be effective one quarter later in reporting periods ending after March 15, 2010. At best, this might give financial statement preparers one month from the date of the final Update's issuance to the end of the reporting period in which the disclosures are to be applied. The Board has expressed their belief that such an abbreviated adoption period is warranted because the "information necessary to comply with the new disclosure requirements and clarification of existing disclosure requirements would be available without significant changes to entities' information systems..."

While much of the raw data may exist, the majority of our members have not developed the systems to gather, collate, and analyze this data. For example, 820-10-50-2(c)-2 of the proposed ASU would require that we disclose the Level 3 gross purchases, sales, issuances and settlements. For financial institutions operating in a mark-to-market environment, changes in fair value are recorded in income regardless of whether gains or losses are realized or unrealized; that is, regardless of the receipt or payment of cash. Thus, companies have not developed the systems to link the cash movements of financial instruments with the fair value measurement process, as there is no need other than to comply with this proposed disclosure.

Development of the needed systems and application to all transactions for the reporting period will require more than one month. In addition, the companies most affected by this proposed ASU will also be heavily impacted by the adoption of Financial Accounting Standards No. 166, *Accounting for Transfers of Financial Assets, an amendment of FASB Statement No. 140*, and Financial Accounting Standards No. 167, *Amendments to FASB Interpretation No. 46(R)*. Adoption of FAS 166 and FAS 167 is ongoing for our members and may significantly increase the amount of assets and liabilities recognized at fair value, compounding the complexity and burden of implementing the proposed ASU.

For these reasons, we recommend that, if the proposed ASU is finalized as currently drafted, it be effective for interim or annual periods beginning after December 15, 2010.