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Mr. Russell Golden, Technical Director
File Reference No. 1810-100,
Financial Accounting Standards Board
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September 30, 2010

***Re: Proposed Accounting Standards Update: Accounting for Financial Instruments and Revisions to the Accounting for Derivative Instruments and Hedging Activities***

Dear Mr. Golden,

Deutsche Bank (DB) appreciates the opportunity to comment on the Proposed Accounting Standards Update: Accounting for Financial Instruments and Revisions to the Accounting for Derivative Instruments and Hedging Activities (the proposed ASU).

We believe that the objective of a comprehensive review of the accounting for financial instruments should be among others to increase transparency by reducing complexity and to ensure that information is relevant so that financial reporting is aligned with the management of the business. Moreover, DB firmly supports the G-20's statement that the accounting standards setters should work together to achieve one set of high quality global accounting standards.

Therefore, we are deeply concerned with the different positions the FASB has adopted in the proposed ASU in comparison to the models proposed by the IASB relating to classification and measurement, as well as credit impairment and hedge accounting. In this comment letter, we outline the key messages and our concerns. Our responses to the individual questions as a preparer are in the Appendix following the Key Messages section.

**Key Messages**:

**Classification and Measurement**:

- The proposed ASU would significantly modify the recognition and measurement criteria for financial instruments. While DB supports fair value as a relevant measure for certain financial instruments (trading and instruments managed on a fair value basis), we do not believe that it should be the default measurement attribute for all financial instruments. We support a mixed measurement model in both the profit and loss statement and the balance sheet in which the entity's business model together with the characteristics of the financial instrument drives their classification. We support the concept that financial instruments for which the business strategy is to collect or pay related contractual cash flows and for which contractual cash flows meet certain characteristics should be measured at amortized cost in order to reflect the underlying business model, i.e. collecting or paying contractual cash flows rather than holding for fair value movements. The proposed ASU looks to measure these types of instruments at fair value and introduces complexity. We do not support introducing measurement principles other than amortized cost and fair value through profit and loss. Therefore we strongly encourage the FASB to consider the classification and measurement model in IFRS 9 Financial Instruments, as it is a more relevant and decision-useful approach for users than that in the proposed ASU.

- We do not support the FASB's decision to limit investments accounted for under the equity method to those where the investor has significant influence over the investee and the operations of the investee are related to the investor's consolidated operations. This introduces significant judgment which will lead to diversity in practice as well as divergence from IFRS. Moreover, determining fair value can also be problematic for some private equity investments currently accounted for under the equity method, due to the subjectivity involved. We believe that where an entity has significant influence in an investee, equity method of accounting best reflects the underlying business model. However we acknowledge that where entities are held for short term gains, a FVO election should be allowed.

- We do not support a recognition model which generally requires debt issued by an entity to be measured at fair value. We believe that the proposed criteria for measuring such liabilities at amortized cost are too stringent and not in line with how these instruments are managed. As the standard is currently written there will be significant divergence from IFRS especially in the case of hybrid financial liabilities and convertible debt. We therefore recommend the final standard to permit a broader application of the amortized cost measurement approach for an entity's own issued debt by following the IASB approach which retains embedded derivative rules for financial liabilities. Consistent with our recommendations to the IASB, we urge the FASB to simplify the embedded derivatives rules by making them more principles based.

- For hybrid financial liabilities measured at fair value to net income, we recommend requiring the portion of the changes in fair value related to changes in the entity's own credit risk to be recognized in other comprehensive income (OCI).

As changes in own credit risk associated with financial liabilities issued for longer term funding purposes are generally not realizable as they are not traded instruments, presentation of changes in credit risk in OCI more faithfully represents the underlying economics of these liabilities.

- Moreover, we believe that amounts in OCI should be recycled to the profit and loss statement upon extinguishment or derecognition of the liability. These recommendations are consistent with our comment letter on the Fair Value Option for Financial Liabilities submitted to the IASB.

- We do not agree with the proposed measurement basis for core deposit liabilities. While we entirely agree with the Board that the expected and actual maturity of a portfolio of such deposits is longer than their contractual maturity; we believe that core deposits should be reported at amortized cost as it is unlikely that the entity will ever settle the liability at lower than the amount due on demand. Also see our comments under 'Hedge Accounting".

- We note that financial guarantees held not covered in the scope exclusions would be accounted for at fair value through profit and loss. While we are pleased that the FASB has moved closer to a more principle based standard (by eliminating the scope exception of financial guarantees), we believe that the FASB should specifically explore hedge accounting for credit risk. See further comments in our response to question 57 under "Hedge Accounting".

- The FASB and IASB both include a business model test to determine classification of financial assets and liabilities. The FASB's fair value through OCI election requires that the business strategy is to collect or pay the related cash flows on the instrument but that a large number of sales or settlements may indicate that an entity's business strategy has changed and that future instruments should be measured at fair value through profit and loss. In contrast, the IASB's requirements are less stringent and would allow for some sales without calling the business model into question. We believe that these differences may cause divergence in classification principles and therefore we recommend the Boards work together to align the wording of the two standards.

- There appear to be different approaches in analyzing interests in a securitization vehicle between the proposed ASU and IFRS 9. We believe that the inclusion of the embedded derivative rules in the FASB's approach would drive a difference in accounting between the standards but are still uncertain of the full effect of the difference. Therefore we recommend that the boards review and better align the approaches before finalizing the respective standards. The proposed ASU as drafted prohibits any reclassification. However, we believe that in specific instances where the business model changes, reclassification should be required. Therefore, we recommend that the FASB consider allowing reclassification in certain instances in line with the guidance in IFRS 9.

- Finally, we believe classification and measurement of financial instruments should be converged with IFRS 9 and other IFRS guidance as part of the FASB and IASB's joint project initiatives under the Boards' Memorandum of Understanding.

**Credit Impairment**:

- We agree with the need to improve the credit impairment model as we believe that the current incurred loss model does not allow for the timely recognition of credit losses and does not provide adequate information to the users of the financial statements about management's view of the expected losses. While we support the removal of the probability threshold and the use of loss rates that reflect losses expected to occur over the estimated life of a pool of loans as introduced in the proposed ASU, we believe a revised credit impairment model should:

  - Allow for earlier recognition of expected credit losses;
  - Ensure that the provisions for financial instruments that are carried at amortized cost and that reflect realized credit losses immediately and unrealized but expected losses appropriately;
  - Adopt an approach for assessing credit losses that is practical and consistent with internal risk management policies and practices;
  - Adopt a measurement basis for financial instruments at amortized cost which is consistent with the entity's underlying business model; and
  - Require disclosures that are relevant and useful for financial statement users.

- While we encourage the FASB to continue their work to develop a provisioning model which incorporates a broader range of credit information, we believe that the operational challenges presented by the particular expected cash flow approach outlined will ultimately have no practical, cost-beneficial solutions to deem the approach to be feasible for implementation for the overwhelming majority of firms affected. Based on the previous criteria we have a number of concerns in relation to the proposed ASU as published and urge the FASB to give the below items and those in the appendix due consideration before moving to a final standard.

- We have concern over the proposed assessment of credit impairment under which an entity shall assume at each reporting date unchanging economic conditions for the remaining life of the financial asset and shall not use relevant forward looking information. We do not believe this assumption is realistic and seek clarification that this accurately reflects the Board's intentions. We believe that the assessment of credit impairment should be forward looking and an entity should be able to consider in its analysis current market information which incorporates expectation of future events, or if not available, use management's best estimate of the expected loss based on current market conditions.

- In evaluating the credit impairment for financial assets, the proposed ASU states that "an entity shall consider both the timing and amount of the cash flows to be collected." This implies that financial institutions can accurately determine both the extent and the timing of individual cash flows, which are to be updated at each reporting period. This differs greatly with the procedures that DB and other financial institutions use to manage credit risk in relation to their amortized cost portfolios. In practice, financial institutions calculate estimates of expected loss (an estimate of loss frequency multiplied by an estimated loss severity) at a portfolio level using statistical models calibrated on historical averages whereby the model inputs are continuously adjusted for current circumstances impacting that portfolio and do not extrapolate cash flows for individual financial assets at the end of each reporting period.

- While the proposed update allows for impairment to be assessed and measured collectively for a pool of loans, we want to emphasize that any new impairment model must be applicable to open portfolios as this is consistent with how we risk manage our businesses. In principle, open portfolios for accounting purposes should be defined consistently with portfolios used for internal risk management purposes, which are based on the information, provided internally to the key management personnel responsible for management of credit risk exposures and should be disclosed externally.

- The calculation of interest income in the proposed ASU is determined by applying the effective interest rate (EIR) to the amortized cost balance net of any allowance for credit losses. The difference in the amount of interest contractually due that exceeds interest accrued on basis of EIR would be recognized as an increase to the allowance for credit losses. We do not agree with this treatment as it is our view that mixing interest income recognition with credit impairment loss recognition adds a significant amount of complexity and also reduces the information usefulness by mixing the highly predictable cash flows resulting from contractual terms with the expected losses of which the timing and amounts are uncertain. We believe that the different nature of the contractual cash flows and expected losses of credit impairment justifies a separation for the recognition and presentation of the interest income and credit losses. While there is a theoretical link between the yield for an amortized-cost financial instrument and a lender's perception of the credit risk at the date of issuance, there is not a link between interest revenue recognition of an individual financial instrument and allocation of a portfolio's expected losses. DB supports a mixed measurement attribute for financial assets and believes that amortized cost should be appropriate measurement model for those financial assets where the objective is to hold and collect contractual cash flows based on a business model. Therefore, decoupling the interest income recognition from credit losses is appropriate because it reflects how managements views and manages interest and credit risk. Furthermore, it reduces the operational complexity which would be consistent with the Board's objective to reduce such complexity.

- We believe that any impairment model should be based on a "performing and non-performing" approach with changes in expectations in the "performing" or "good" book recognized over the remaining life of the financial instrument, whereas changes in estimates for the "non-performing" or "bad" book are recognized immediately in profit or loss as outlined in the findings of the Expert Advisory Panel on Impairment ("EAP"). Furthermore, we recommend that the FASB and the IASB work together with regulators to develop a standardized definition for non-performing loans. This would help enhance the comparability of financial statements and regulatory disclosures.

- The issues we raise have been discussed in significant detail by the EAP Impairment. Specifically the EAP has discussed three different approaches addressing two points, a) the methodologies for the transfer of instruments from the good book to the bad book and b) the build-up of provisions for the good book.

We are also aware of the development of an alternative impairment approach by the European Banking Federation (“EBF”). The EBF and EAP approaches share a great deal of commonality, all of which we support, in particular:

- Preference for an expected loss impairment model over the expected cash flow model as outlined in the ED.
- The need for decoupling of credit losses from the EIR calculation and recognition.
- The requirement that a new impairment model must be applicable to open portfolios

- A new credit impairment model would distinguish between performing and non-performing amortized cost financial instruments which would result in charges for realized losses being taken to the P&L as they occur. The only difference that remains between the approaches discussed is the principles regarding the build up and usage of the provisions for the performing book. We have a preference for an approach which combines a balance sheet and P&L view regarding the build up and usage of the performing book provisions. This approach would take the entire provision required for the non-performing book instrument from the performing book provision (or the portfolio from which the instrument was removed). The performing book provision would be evaluated against a one year expected loss floor and any additional provisions for allowance are made as needed.

**Hedge Accounting**:

- DB welcomes the Board’s proposals to simplify hedge accounting; however, there are certain issues with the proposed guidance, including divergence from IASB’s well-received positions and lack of guidance on specific areas of significant concern e.g. hedges of portions, partial term hedges and portfolio hedges. We would urge the Board to consider a wider array of topics on hedge accounting in order to achieve a converged position with IASB before moving to a final standard. For clarity, we believe that carrying out a broader review of hedge accounting and issuing a comprehensive standard is preferable to a piecemeal approach of improving guidance in certain areas without addressing some fundamental issues in other areas. The latter approach risks convergence goals and would increase (not reduce) complexity for users. We also do not agree with the current transition guidance related to hedge accounting as the impact of new requirements on many hedges would be highly difficult if not impractical.

- We appreciate the significant improvements and simplifications in the proposed ASU and in general support the Board’s proposals on:

    - Abolishing the bright lines from effectiveness criteria and relaxing the effectiveness threshold from highly effective to reasonably effective;
    - Emphasizing qualitative assessments of effectiveness rather than quantitative assessment; and

    - Abolishing the requirement to assess effectiveness on a quarterly basis.

- We strongly urge the Board to seek further improvements in the current hedge accounting model. We see merit in the direction that the IASB is taking in improving various aspects of hedge accounting standards.

  We would therefore urge the Board to consider both the recent topics discussed at IASB and certain IASB positions (which are generally well received by the market) including:

    - Hedge accounting for portfolios of financial instruments;
    - Hedges of portions of an instruments cash flows and term;
    - Broader definition of "benchmark interest rate" which includes a broader set of well accepted and readily observable reference rates;
    - Hedges of specific risk in a non-financial instrument.

- The current hedge documentation requirements are very strict and create unnecessary accounting complexity. We would urge the Board to simplify the documentation requirements and provide guidance to allow broader interpretation of the documentation requirements especially in the following situations:

    - Documentation should be allowed to be completed within a reasonable period after the hedge transaction rather than "concurrently" as long as the intention to designate an accounting hedge is documented concurrently;
    - Changes in a hedged item's designated proportion should not be considered as a change in the documentation (consistent with the current FASB proposal to allow such a change in the hedging instrument without affecting the hedge documentation);
    - Change in the date of the forecast transaction should not affect the original designation as long as it occurs or is still expected to occur within a reasonable period of time;
    - Changes to the method of assessing hedge effectiveness or measuring ineffectiveness should not affect the original designation.

- Certain financial guarantees are scoped into the standard and will be required to be measured at fair value through profit and loss under the proposed ASU as financial guarantees will not meet the definition of a "debt instrument". To the extent these financial guarantees held are economic hedges of the credit risk of instruments which are accounted for at fair value through comprehensive income, a mismatch in the profit and loss will result unless hedge accounting is applied. Therefore in addition to the issues listed above, we also encourage the FASB to address hedges of credit risk and specifically examine the significant barriers to achieving credit risk hedging today, with the objective of allowing more entities to align their financial reporting with their internal risk management practices.

- We do not support the Board's decision to prohibit de-designation of existing hedges. As changes occur in the risk profile of the underlying hedged exposures, firms will commonly add new hedging relationships and remove or de-designate existing hedge relationships to bring accounting hedges in line with the entity's economic hedge position. Entering into an exactly offsetting derivative purely to achieve an accounting result i.e. de-designation, is a costly and unnecessary exercise and does not make economic sense. De-designation is generally a knock-on effect of the problem that portfolio hedging cannot be achieved in US GAAP.

This highlights the fundamental shortcomings of FASB's current hedge accounting model when it comes to portfolio hedging and Asset Liability Management practices. This is an area of concern for DB and as such, we would urge the Board to focus on making its hedge accounting model more relevant to the portfolio hedging rather than take away the tools currently employed to overcome the shortcomings of the current model e.g. voluntary de-designations. We appreciate that the IASB is addressing portfolio hedging in this respect and would request FASB to give due consideration to the progress made by IASB.

- We do not believe that the basis for the Board's decision to require recognition of any ineffectiveness on cash flow hedges arising from under-hedging in income statement is justified.

- We believe the current basis for conclusions in BC226-228 in the proposed ASU does not address why this fundamental change from FAS 133 (ASC Topic 815) represents an improvement to financial reporting and results in simplification. Furthermore it does not explain why the conclusion the Board reached when it issued FAS 133 (ASC Topic 815) in 1998 is no longer correct. We strongly oppose this approach and would urge the Board to reconsider. In respect of cash flow hedges, we also strongly oppose the withdrawal of "critical terms matching" method of testing effectiveness. These new proposals by FASB will create significant divergence from the current IASB standard and its anticipated positions. This divergence could put US entities, especially banks, at a significant disadvantage compared to their peers who reports under IFRS and can apply a simple and cost efficient macro cash flow hedge on their Asset Liability Management portfolios.

- While we believe that the core deposits should be carried at amortised cost (see our comments in the 'Classification and Measurement' section), we are pleased that the Board has recognised that a portfolio of core deposit liabilities could have a term which is longer than the contractual term of the individual liabilities and that reflection of the expected term in any valuation adjustment will present a better view of the underlying position. From a hedge accounting perspective, we would urge the Board to clarify that groups of such deposits can be designated in fair value hedges (with hedged item adjustment computed with reference to a benchmark interest rate rather than a rate net of any servicing costs) based on their expected term.

We hope you find our comments useful and relevant and we would be happy to work with you in the deliberation. We continue to urge the FASB and IASB to continue working together to resolve differences and achieve convergence in this important subject area. Should you wish to discuss any of the comments or responses in this letter, please do not hesitate to contact Cynthia Mustafa at Cynthia.mustafa@db.com or +44 (0) 20 754 50978.

Yours sincerely,

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Managing Director
Global Head, Accounting Policy and Advisory Group
Deutsche Bank AG

## Appendix – Responses to Questions

**Note**: Certain questions have not been responded to in this appendix as they either relate to users or are not significant to our business.

### Scope

### Questions for All Respondents

**Question 1**
**Do you agree with the scope of financial instruments included in this proposed Update? If not, which other financial instruments do you believe should be excluded or which financial instruments should be included that are proposed to be excluded? Why?**

Yes. We generally agree with the scope of financial instruments included in the proposed ASU except for the exclusion of certain loan commitments (please see our responses to **Question 2**) and the scope in for equity investments (please see our responses to **Question 4**) as these exclusions will cause divergence from IFRS and do not support a principles based approach.

As we noted in our cover letter, financial guarantees not covered in the scope exclusions would be required to be accounted for at fair value though profit and loss. While we are pleased that the FASB has moved closer to a more principle based standard (by eliminating the scope exception for financial guarantees), we believe the FASB should specifically explore hedge accounting for credit risk. See our further comments below under 'Hedge Accounting.'

**Question 2**
**The proposed guidance would require loan commitments, other than loan commitments related to a revolving line of credit issued under a credit card arrangement, to be measured at fair value. Do you agree that loan commitments related to a revolving line of credit issued under a credit card arrangement should be excluded from the scope of this proposed Update? If not, why?**

No. We believe that the exclusion of certain financial instruments from the scope of the proposed ASU should be principles-based. Excluding only revolving lines of credit under a credit card arrangement and not other types of loan commitments does not seem to support a principles-based approach. The Board should indicate the underlying principle for excluding certain loan commitments from the scope of the proposed Update.

We reiterate our support for a mixed measurement model including amortized cost and fair value through profit and loss categories only which will provide consistency between the profit and loss statement and the balance sheet. Once determined whether in scope or not, we agree that classification of loan commitments should then be based on the classification of the related loan to be issued. Not only will application of this principle provide more consistency, but will also increase convergence between US GAAP and IFRS.

**Question 3**
**The proposed guidance would require deposit-type and investment contracts of insurance and other entities to be measured at fair value. Do you agree that deposit-type and investment contracts should be included in the scope? If not, why?**

Yes. We agree that deposit-type and investment contracts of insurance and other entities contracts should be included in the scope and measured at fair value when they do not have significant insurance risk.

**Question 4**
**The proposed guidance would require an entity to not only determine if they have significant influence over the investee as described currently in Topic 323 on accounting for equity method investments and joint ventures but also to determine if the operations of the investee are related to the entity's consolidated business to qualify for the equity method of accounting. Do you agree with this proposed change to the criteria for equity method of accounting? If not, why?**

No. We do not believe the application of equity method accounting should be overlaid with a requirement that the operations of the investee are related to the entity's consolidated business. This would produce inconsistency with the consolidation criteria for subsidiaries and divergence with IFRS. We believe that determining whether the operations of an investee are related to the entity's consolidated business may provide some difficulty and significant need for interpretation and judgement. Moreover, measuring such instruments at fair value through profit and loss is not the most appropriate basis for certain associates which are strategic investments (for example, an investment entered into by the reporting entity to gain access to the local market). We believe that where an entity has significant influence in an investee, equity method of accounting best reflects the underlying business model. However we acknowledge that where entities are held for short term gains, a FVO election should be allowed.

**Note**: Questions 5-7 were deleted as they are questions for users.

**Initial Measurement**

**Questions for All Respondents**

**Question 8**
**Do you agree with the initial measurement principles for financial instruments? If not, why?**

We reiterate our support for a mixed measurement model including amortized cost and fair value through profit and loss categories only (please see our responses to **Question 13**). We believe treatment of the initial measurement of financial instruments should be consistent with this dual category model. We believe in the general principle that transaction fees and costs should be expensed immediately for financial instruments measured at fair value with subsequent changes in fair value to be recognized in net income.

Transaction fees and costs for other categories of financial instruments should be deferred and amortized as a yield adjustment.

Although we do not support the fair value through OCI income category, we agree that the initial measurement for those financial instruments that are not subsequently measured at fair value through profit and loss should be the transaction price, which normally represents fair value, apart from other elements that qualify as an asset or a liability under the existing US GAAP that will be separately accounted for.

We do not support a recognition model which generally requires debt issued by an entity to be measured at fair value. We believe that the proposed criteria for measuring such liabilities at amortized cost are too stringent and not in line with how these instruments are managed. As the standard is currently written there will be significant divergence from IFRS especially in the case of hybrid financial liabilities and convertible debt. We therefore recommend the final standard to permit a broader application of the amortized cost measurement approach for an entity's own issued debt by following the IASB approach which retains embedded derivative rules for financial liabilities. Consistent with our recommendation to the IASB, we urge the FASB to simplify the embedded derivative rules by making them more principles-based.

**Question 9**
**For financial instruments for which qualifying changes in fair value are recognized in other comprehensive income, do you agree that a significant difference between the transaction price and the fair value on the transaction date should be recognized in net income if the significant difference relates to something other than fees or costs or because the market in which the transaction occurs is different from the market in which the reporting entity would transact? If not, why?**

We believe that conceptually a day one profit should only be recognized for those financial instruments that are subsequently measured at fair value through profit or loss. For financial instruments not subsequently measured at fair value through profit or loss, we believe the subsequent measurement principles should drive the treatment of a significant difference between inception fair value and transaction price. For example, if a significant difference between fair value and transaction price exists for instruments subsequently to be measured at fair value through OCI and if market observable data exists to support such a difference, the difference should be reflected in OCI and there should be no day one recognition in the profit and loss. We believe that the wording as currently drafted in the proposed ASU ("reliable evidence") may potentially open the door for day one recognition and hence recommend the Board to clarify in the final statement.

As discussed in the key messages and above, we do not believe that fair value is a relevant measure for all financial instruments and support a mixed measurement model for financial instruments of either amortized cost or fair value through profit and loss. For a further discussion of the mixed measurement model, please see our responses to **Question 13**.

**Question 10**
**Do you believe that there should be a single initial measurement principle regardless of whether changes in fair value of a financial instrument are recognized in net income or other comprehensive income? If yes, should that principle require initial measurement at the transaction price or fair value? Why?**

Please see our responses to **Questions 8** and **9**

**Question 11**
**Do you agree that transaction fees and costs should be (1) expensed immediately for financial instruments measured at fair value with all changes in fair value recognized in net income and (2) deferred and amortized as an adjustment of the yield for financial instruments measured at fair value with qualifying changes in fair value recognized in other comprehensive income? If not, why?**

Yes. We believe in the general principle that transaction fees and costs should be expensed immediately for financial instruments measured at fair value with subsequent changes in fair value to be recognized in net income. Transaction fees and costs for other categories of financial instruments should be deferred and amortized as a yield adjustment. Please see our responses to **Question 8**.

**Questions for Preparers and Auditors**

**Question 12**
**For financial instruments initially measured at the transaction price, do you believe that the proposed guidance is operational to determine whether there is a significant difference between the transaction price and fair value? If not, why?**

Yes. The proposed guidance is sufficiently operational if market observable data exists to indicate that there is a significant difference between the transaction price and fair value.

**Subsequent Measurement**

**Questions for All Respondents**

**Question 13**
**The Board believes that both fair value information and amortized cost information should be provided for financial instruments an entity intends to hold for collection or payment(s) of contractual cash flows. Most Board members believe that this information should be provided in the totals on the face of the financial statements with changes in fair value recognized in reported stockholders' equity as a net increase (decrease) in net assets. Some Board members believe fair value should be presented parenthetically in the statement of financial position. The basis for conclusions and the alternative views describe the reasons for those views. Do you believe the default measurement attribute for financial instruments should be fair value? If not, why? Do you believe that certain financial instruments should be measured using a different measurement attribute? If so, why?**

No. We do not believe fair value should be the default measurement attribute for all financial instruments.

We reiterate the importance of the mixed measurement model. We believe the entity's business model together with the characteristics of the financial instrument should drive whether a financial instrument is classified as fair value through profit and loss or as amortized cost. We do not believe providing fair value information on the face of the balance sheet will aid the user in understanding the financial position of the entity for those entities whose business model is not such.

We support the concept that financial instruments for which the business strategy is to collect or pay related contractual cash flows and for which contractual cash flows meet certain characteristics should be measured at amortized cost. This is because amortized cost is consistent with the business model, i.e. collecting or paying contractual cash flows rather than holding for fair value movements. Therefore we strongly encourage the FASB to consider the classification and measurement model in IFRS 9 Financial Instruments, as it is a more relevant and decision-useful approach for users than that proposed in the ASU.

**Question 14**
**The proposed guidance would require that interest income or expense, credit impairments and reversals (for financial assets), and realized gains and losses be recognized in net income for financial instruments that meet the criteria for qualifying changes in fair value to be recognized in other comprehensive income. Do you believe that any other fair value changes should be recognized in net income for these financial instruments? If yes, which changes in fair value should be separately recognized in net income? Why?**

For financial instruments not measured at fair value with changes to profit and loss, we believe that effective interest, credit impairment & reversal and realized gains & losses should be recognized in net income.

In addition, we believe that all foreign exchange transaction gains and losses on monetary items should be recorded in net income. Unlike other interim changes in fair value that may not be realized in cash if held to maturity (absent credit impairment), foreign exchange gains and losses in a monetary item will be realized. Under the proposed ASU, an entity would be required to defer recognition of significant foreign exchange gains and losses in net income upon disposition of the monetary item, even though those gains and losses arose in the prior periods. As noted in the above discussions, DB supports a mixed measurement model including amortized cost. Recording all foreign exchange gains and losses on monetary items in net income will align the US GAAP guidance with the requirements of IFRS 9 “Financial Instruments”.

Furthermore, we believe that this treatment will also reduce the need of and complexity of current hedge accounting practises for entities that hedge the foreign exchange risk on financial instruments measured at fair value through OCI, whereas a natural offset in net income may exist between the foreign currency in the hedged item and hedging instrument.

**Question 15**
**Do you believe that the subsequent measurement principles should be the same for financial assets and financial liabilities? If not, why?**

We believe, in principle, the classification and measurement criteria should be consistent between financial assets and financial liabilities. We reiterate the importance of the mixed measurement model (fair value and amortized cost) and the reporting entity's business model (together with the instrument's characteristics) to drive financial instrument classification and measurement. However, we believe additional guidance is needed to address the accounting surrounding an entity's own credit risk. We do not believe an entity's own credit should affect the profit and loss of that entity.

For entities that hold the same type of financial instrument but under different business models, we believe note disclosures would be adequate for users to compare these instruments on the same basis. We believe that financial reporting should allow the user to assess financial results based on management's business model and the characteristics of the financial instrument.

**Question 16**
**The proposed guidance would require an entity to decide whether to measure a financial instrument at fair value with all changes in fair value recognized in net income, at fair value with qualifying changes in fair value recognized in other comprehensive income, or at amortized cost (for certain financial liabilities) at initial recognition. The proposed guidance would prohibit an entity from subsequently changing that decision. Do you agree that reclassifications should be prohibited? If not, in which circumstances do you believe that reclassifications should be permitted or required? Why?**

No. As previously stated, we believe that the reporting entity's business model (together with the instrument's characteristics) should drive classification and measurement. Therefore we believe an entity should be required to reclassify instruments to align with possible substantial changes in an entity's business model. We believe these reclassifications would be infrequent. Therefore we urge the FASB to reconsider the issue and align its guidance with IFRS 9 as it relates to reclassifications.

The FASB's fair value through OCI election requires that the business strategy is to collect or pay the related cash flows on the instrument and prohibits reclassification. However a large number of subsequent sales or settlements may indicate that an entity's business strategy has changed and therefore, reclassification should be permitted to reflect the change of business strategy and allow these instruments to be measured at fair value through profit and loss. The IASB's requirements are less stringent and would allow for some sales without calling the business model within question. We believe that these differences may cause divergence in classification principles and therefore recommend the Boards work together to align the wording in the standards.

**Question 17**
**The proposed guidance would require an entity to measure its core deposit liabilities at the present value of the average core deposit amount discounted at the difference between the alternative funds rate and the all-in cost-to-service rate over the implied maturity of the deposits. Do you believe that this remeasurement approach is appropriate? If not, why? Do you believe that the remeasurement amount should be disclosed in the notes to the financial statements rather than presented on the face of the financial statements? Why or why not?**

No. We do not believe that remeasurement of core deposit liabilities is appropriate. We believe remeasurement introduces a concept that is neither fair value nor amortized cost to the measurement of core deposit liabilities, adding complexity to overall financial instrument reporting. We do not believe remeasurement provides decision-useful information to the user of the financial statements as the value does not represent the cash flows that are likely to flow from the entity for the liability (as the counterparty will likely not accept an amount below par). For the above reasons we urge the Board to follow the IASB's approach.

Nevertheless, we are pleased that the Board has recognized that a portfolio of core deposit liabilities could have a term longer than the contractual term of the individual deposits and that reflection of the expected term in any valuation adjustment will present a better view of the underlying financial position. This is a generally accepted practice at banks to manage interest rate risk on such deposits on the basis of the expected term of the portfolio instead of its contractual term. From hedge accounting perspective, we would urge the Board to clarify that groups of such deposits can be designated in fair value hedges (with hedged item adjustment computed with reference to a benchmark interest rate rather than a rate net of any servicing costs) based on their expected term. This improvement will be a significant step towards aligning the hedge accounting model with prudent generally accepted risk management practices.

**Question 18**
**Do you agree that a financial liability should be permitted to be measured at amortized cost if it meets the criteria for recognizing qualifying changes in fair value in other comprehensive income and if measuring the liability at fair value would create or exacerbate a measurement attribute mismatch? If not, why?**

We believe in a principles based mixed measurement model, so if a reporting entity's intention in relation to a funding transaction is to pay all its contractual cash flows and the instrument has predictable cash flows, such instrument should be carried at amortized cost. We do not support a recognition model which generally requires an entity's own issued debt to be measured at fair value and believe that the proposed criteria for measuring such liabilities at amortized cost are lacking a principle that is in line with the economic objectives of how these instruments are managed. As the standard is currently written there will be significant divergence from IFRS especially in the case of hybrid financial liabilities and convertible debt. We therefore recommend the final standard to permit a broader application of the amortized cost measurement approach for an entity's own issued debt by following the IASB approach which retains embedded derivative rules for financial liabilities. Consistent with our recommendations to the IASB, we urge the FASB to simplify the embedded derivatives rules by making them more principles based.

Furthermore, we recommend requiring the portion of the changes in fair value of a hybrid financial liability (e.g., hybrid financial liabilities) measured at fair value with changes in net income related to changes in the entity's own credit risk to be recognized in OCI. As changes in own credit risk associated with financial liabilities issued for longer term funding purposes are generally not realizable, presentation of changes in credit risk in OCI more faithfully represents the underlying economics of these liabilities. Moreover any buybacks or extinguishments should be recycled to the profit and loss statement. We believe that the gain or loss resulting from changes in a liability's credit risk should be recycled from OCI to the profit and loss statement (P&L) upon extinguishment of that liability prior to maturity instead of retained earnings as that gain or loss has been realized.

For hybrid financial liabilities containing the entity's own credit, we support bifurcation of the embedded derivative (not symmetrical with financial assets) as we do not believe own credit should be recorded at fair value unless the instrument will be bought and sold for short-term profit considerations. We believe that the bifurcation rules should be simplified and principles-based.

**Note**: Question 19 was deleted as it is not significant to our business.

**Question 20**
**Do you agree that an entity should evaluate the need for a valuation allowance on a deferred tax asset related to a debt instrument measured at fair value with qualifying changes in fair value recognized in other comprehensive income in combination with other deferred tax assets of the entity (rather than segregated and analyzed separately)? If not, why?**

We believe that the evaluation to determine the need for a valuation allowance for deferred tax assets should not be done on an item by item basis. An entity needs to weigh all evidence under the "more likely than not" standard to ensure that there is sufficient taxable income of the appropriate character to support the future realization of all its deferred tax assets.

**Question 21**
**The Proposed Implementation Guidance section of this proposed Update provides an example to illustrate the application of the subsequent measurement guidance to convertible debt (Example 10). The Board currently has a project on its technical agenda on financial instruments with characteristics of equity. That project will determine the classification for convertible debt from the issuer's perspective and whether convertible debt should continue to be classified as a liability in its entirety or whether the Board should require bifurcation into a liability component and an equity component. However, based on existing U.S. GAAP, the Board believes that convertible debt would not meet the criterion for a debt instrument under paragraph 21(a)(1) to qualify for changes in fair value to be recognized in other comprehensive income because the principal will not be returned to the creditor (investor) at maturity or other settlement. Do you agree with the Board's application of the proposed subsequent measurement guidance to convertible debt? If not, why?**

The proposed ASU to account for convertible debt at fair value to profit and loss will create even further divergence between US GAAP and IFRS. We recommend that such convertible debt instruments should be scoped out of the proposed ASU and addressed as part of the financial instruments with characteristics of equity project.

**Note**: Questions 22-27 were deleted as they are questions for users.

**Questions for Preparers and Auditors**

**Question 28**
**Do you believe that the proposed criteria for recognizing qualifying changes in fair value in other comprehensive income are operational? If not, why?**

As previously noted, we do not support a model which recognizes qualifying changes in fair value in other comprehensive income. We believe that a mixed measurement model for amortized cost and fair value should be used in the statement of financial position. We believe the proposed ASU would add unnecessary complexity and obscure key messages to users. We do not support the fair value through OCI model.

**Question 29**
**Do you believe that measuring financial liabilities at fair value is operational? If not, why?**

As previously discussed, we believe that a debt instrument issued which will pay contractual cash flows will not generally be affected by market fluctuations and should therefore be measured at amortized cost. Hence, we do not support a recognition model which generally requires debt issued by an entity to be measured at fair value. Please see our responses to **Question 33**.

**Question 30**
**Do you believe that the proposed criteria are operational to qualify for measuring a financial liability at amortized cost? If not, why?**

We believe that the proposed criteria for measuring such liabilities at amortized cost are too stringent and not in line with how these instruments are managed. As the standard is currently written there will be significant divergence from IFRS especially in the case of hybrid financial liabilities and convertible debt. We therefore recommend the final standard to permit a broader application of the amortized cost measurement approach for an entity's own issued debt by following the IASB approach which retains embedded derivative rules for financial liabilities.

**Question 31**
**The proposed guidance would require an entity to measure its core deposit liabilities at the present value of the average core deposit amount discounted at the difference between the alternative funds rate and the all-in cost-to-service rate over the implied maturity of the deposits. Do you believe that this remeasurement approach is operational? Do you believe that the remeasurement approach is clearly defined? If not, what, if any, additional guidance is needed?**

By adding remeasurement of core deposit liabilities into the proposed ASU, we believe FASB has created a third measurement category that does not result in reduction of complexity. We do not support remeasurement of core deposit liabilities nor do we believe it provides decision-useful information. Please see our responses to **Question 17**.

**Presentation**

**Questions for All Respondents**

**Question 32**
**For financial liabilities measured at fair value with all changes in fair value recognized in net income, do you agree that separate presentation of changes in an entity's credit standing (excluding changes in the price of credit) is appropriate, or do you believe that it is more appropriate to recognize the changes in an entity's credit standing (with or without changes in the price of credit) in other comprehensive income, which would be consistent with the IASB's tentative decisions on financial liabilities measured at fair value under the fair value option? Why?**

We believe that changes in fair value attributable to own credit for non-trading liabilities held at fair value should be reported through OCI as, unlike trading liabilities, these changes are generally not realizable. Changes for trading liabilities should be reported through earnings.

Therefore we agree with the IASB's tentative decisions on this topic in this respect. Moreover, we believe that the amounts in OCI should be recycled to the profit and loss upon extinguishment of the liability. Therefore we're strongly opposed to a recognition model which generally requires debt issued by an entity to be measured at fair value.

**Question 33**
**Appendix B describes two possible methods for determining the change in fair value of a financial liability attributable to a change in the entity's credit standing (excluding the changes in the price of credit). What are the strengths and weaknesses of each method? Would it be appropriate to use either method as long as it was done consistently, or would it be better to use Method 2 for all entities given that some entities are not rated? Alternatively, are there better methods for determining the change in fair value attributable to a change in the entity's credit standing, excluding the price of credit? If so, please explain why those methods would better measure that change.**

We do not believe presenting changes in an entity's own credit standing separate from changes in the entity's overall credit standing, including market credit factors, provides the user with decision-useful information.

We do not believe **Method 1** is an appropriate measure for the fair value of an entity's credit risk as credit ratings are a blunt measure of credit risk (as seen during the recent credit crisis) and are not updated frequently enough to provide an accurate reflection of an entity's true credit risk. **Method 2** is more appropriate, but as noted above, attempting to separate the change in fair value due to changes in the entity's credit standing from the change in fair value due to other factors is highly subjective and does not provide the user with decision-useful information.

We prefer the existing requirements included in IFRS 7, which do not separate the change in an entity's credit standing from the overall change in the credit risk of the liability. Additionally, IFRS 7 permits any method the entity believes "faithfully represents the amount of change in its fair value that is attributable to changes in the credit risk of the liability." Moreover we support disclosure in the footnotes of how own credit changes have been measured so as to allow transparency to users in how own credit has been calculated.

**Question 34**
**The methods described in Appendix B for determining the change in fair value of a financial liability attributable to a change in an entity's credit standing (excluding the changes in the price of credit) assume that the entity would look to the cost of debt of other entities in its industry to estimate the change in credit standing, excluding the change in the price of credit. Is it appropriate to look to other entities within an entity's industry, or should some other index, such as all entities in the market of a similar size or all entities in the industry of a similar size, be used? If so, please explain why another index would better measure the change in the price of credit.**

Please see our responses to **Question 33**. We do not believe presenting changes in an entity's own credit standing separate from changes in the entity's overall credit standing, including market credit factors, provides the user with decision-useful information.

<u>**Note**</u>: Questions 35-36 were deleted as they are questions for users.

**Credit Impairment**

**Questions for All Respondents**

**Question 37**
**Do you believe that the objective of the credit impairment model in this proposed Update is clear? If not, what objective would you propose and why?**

As noted above, while we do not agree with the classification of fair value through other comprehensive income for items that are not managed on a fair value basis, we would agree that the following broad objective is clear: "to establish a model for recognition and measurement of credit impairment of financial assets measured at fair value with qualifying changes in fair value recognized in other comprehensive income on the basis of an entity's expectations about the collectability of cash flows, including the determination of cash flows not expected to be collected."

However, it is not clear what information would be permissible to use when an entity determines their expectations about collectability of cash flows, specifically, exactly when available information relating to existing conditions turns into information relating to potential future events beyond the reporting date. For example, an observable CDS spread would consider potential future events; would this information not be relevant in determining an entity's expectations about the collectability of cash flows?

We would propose including the following at the end of the last sentence in paragraph 36 "…that are not already incorporated into the currently available information." This would make it clear that current market information, which by definition incorporates expectations about future events, is appropriate information to use when determining an entity's expectations about the collectability of cash flows.

**Question 38**

**The proposed guidance would require an entity to recognize credit impairment immediately in net income when the entity does not expect to collect all contractual amounts due for originated financial asset(s) and all amounts originally expected to be collected for purchased financial asset(s). The IASB Exposure Draft, Financial Instruments Amortized Cost and Impairment (Exposure Draft on impairment), would require an entity to forecast credit losses upon acquisition and allocate a portion of the initially expected credit losses to each reporting period as a reduction in interest income by using the effective interest rate method. Thus, initially expected credit losses would be recorded over the life of the financial asset as a reduction in interest income. If an entity revises its estimate of cash flows, the entity would adjust the carrying amount (amortized cost) of the financial asset and immediately recognize the amount of the adjustment in net income as an impairment gain or loss. Do you believe that an entity should immediately recognize a credit impairment in net income when an entity does not expect to collect all contractual amounts due for originated financial asset(s) and all amounts originally expected to be collected for purchased financial asset(s) as proposed in this Update, or do you believe that an entity should recognize initially expected credit losses over the life of the financial instrument as a reduction in interest income, as proposed in the IASB Exposure Draft on impairment?**

We do not believe that changes in the estimates of credit losses should be taken in full to the income statement in the current period. Instead, we believe that a mechanism whereby changes to expected credit losses are amortized over the remaining life of the portfolio to which they relate would provide accounting which would be more consistent with amortized cost instruments and remove the potential for these instruments to be held at quasi-fair value. Estimates of expected losses encompass both current and future losses and therefore have consequences for future periods as well as for the current period.

While we welcome the opportunity for preparers to be able to build expected credit loss allowances over the life of their portfolios, we do not support the IASB's assertion that initial estimates of credit losses should form part of a loan's EIR. We believe that the IASB's ED does not clearly justify the rationale for the assertion that the "initial estimate of expected credit losses" should be included in the calculation of the effective return.

The inclusion of such an initial estimate will lead to significant future revisions which will closely track the fair value of the loan. As these loans are held, under the IASB's model at amortized cost with the business purpose to receive contractual cash flows, we believe that it is inappropriate to introduce revenue volatility that would track the loans' fair value.

As such the definition of EIR should remain consistent with that used under current IAS 39 and the estimates of expected credit losses should be calculated on a portfolio basis and presented independently of EIR.

This approach adopted by the IASB's Exposure Draft seems to be based on the idea that financial institutions include in their pricing an explicit or measurable margin for credit risk at the inception of the financial instrument. In practice however, the compensation for credit risk is embedded in the contractual rate, and is not necessarily explicit to the borrower.

We do not support the model proposed in the ASU which leads to immediate recognition of credit losses, resulting in artificial distribution of revenues (understating of revenues in early years and overstating of revenues in later years). We believe that expected losses should be amortized over the life of portfolio. As expected losses represent expectations of losses occurring in the future, these are distinguished from losses that have been incurred. Any changes in those expectations also relate to possible future events and should therefore also be recognized prospectively. We believe that such an approach would provide for a treatment in the income statement consistent with the principles of the revenue recognition over the life of the instruments and also with the risk management practices of financial institutions. It would also avoid introducing artificial P&L volatility resulting from the inaccuracy of expected loss estimations.

**Question 39**
**Do you agree that credit impairment should not result from a decline in cash flows expected to be collected due to changes in foreign exchange rates, changes in expected prepayments, or changes in a variable interest rate? If not, why?**

Yes, however we believe that a decline in cash flows expected to be collected due to non-contractual prepayments would result in credit impairment and we also believe that changes in expected prepayments would be an indicator of impairment. We recommend that the FASB clarify this in the final standard.

**Question 40**
**For a financial asset evaluated in a pool, the proposed guidance does not specify a particular methodology to be applied by individual entities for determining historical loss rates. Should a specific method be prescribed for determining historical loss rates? If yes, what specific method would you recommend and why?**

While we believe that guidance is required as to what constitutes an expected loss methodology, care must be taken to not make it overly specific. However, we have included some factors that we think the FASB should consider for the inclusion in application guidance to be issued as part of the final standard.

The guidance should be based on the premise that expected loss estimates determined over the life of an open portfolio are the best estimate of the most likely losses that will be incurred over the expected lives of the financial assets in the portfolio as at the reporting date. These estimates are developed using statistical analysis. Implementation guidance should address and highlight the following factors:

- Historical loss experience should provide the basis for estimating expected losses in a group of financial assets. Expected losses for a group of financial assets are estimated on the basis of historical loss experience for assets with credit risk characteristics similar to those in the group.
- Entities that have no loss experience of their own or insufficient experience should use peer group experience for comparable groups of financial assets. This data should be consistent with the characteristics of the group of financial assets to which it will be applied.
- Historical loss experience should be adjusted, on the basis of observable data, to reflect the effects of current conditions that did not affect the period on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not exist currently.

Estimates of changes in expected loss are directionally consistent with changes in related observable data from period to period (such as changes in unemployment rates, property prices, commodity prices, payment status or other factors that are indicative of incurred losses in the group and their magnitude).

**Question 41**
**Do you agree that if an entity subsequently expects to collect more cash flows than originally expected to be collected for a purchased financial asset, the entity should recognize no immediate gain in net income but should adjust the effective interest rate so that the additional cash flows are recognized as an increase in interest income over the remaining life of the financial asset? If not, why?**

We believe the accounting for purchased and originated loans should be consistent.

We believe that changes in expected cash flows should be accounted in line with how the financial instrument is risk managed. If the instrument is held in a performing “good” book portfolio any changes (both downward as well as upward) in credit risk factors, should not be recognized immediately in the income statement. However, if the instrument is held in the non-performing “bad” book any changes in cash flows should be reflected immediately in the income statement. This ensures a consistent approach to changes in estimates for both performing and non-performing loans.

**Question 42**
**If a financial asset that is evaluated for impairment on an individual basis has no indicators of being individually impaired, the proposed guidance would require an entity to determine whether assessing the financial asset together with other financial assets that have similar characteristics indicates that credit impairment exists. The amount of the credit impairment, if any, would be measured by applying the historical loss rate (adjusted for existing economic factors and conditions) applicable to the group of similar financial assets to the individual financial asset. Do you agree with this requirement? If not, why?**

Yes, we generally agree with the approach proposed. DB manages performing and non-performing instruments differently. We will build our expectations of expected losses on a total portfolio basis, but when instruments are specifically identified as non-performing, i.e., a bad loan, it is segregated from other instruments and some portion of the expected loss provision needs to be allocated to the specific instrument.

We believe that the proposed ASU should seek to ensure that changes in estimates of expected losses do not introduce an element of quasi-fair value, nor bring in undue income volatility. Such volatility would be inconsistent with the underlying business model and put undue reliance on future expectations in the context of amortized cost assets. Amortized cost instruments therefore should reflect, by implication, a long term hold view and, unlike traded instruments, are primarily held to achieve a yield (an interest return) over their contractual life, not for short term profit.

We believe it is also operationally easier to use a “performing and non-performing” approach with changes in expectations in the “performing” book recognized over the remaining life of the instrument, whereas changes in estimates for the “non performing” book are recognized immediately in profit or loss. This would also mean that a definition would be required for performing and non-performing instruments; this would also facilitate comparability between entities. We recommend that the FASB, IASB and regulators work together to develop a standardized definition for non-performing loans. This would help enhance comparability of financial statements and regulatory disclosures for users from both analyst and regulatory communities.

The issues we raise have been discussed in significant detail by the EAP. Specifically the EAP has discussed three different approaches addressing two points, a) the methodologies for the transfer of instruments from the good book to the bad book and b) the build up of provisions for the good book.

We are also aware of the development of an alternative impairment approach by the European Banking Federation (“EBF”). The EBF and EAP approaches share a great deal of commonality, all of which we support, in particular:

- Preference for an expected loss impairment model over the expected cash flow model as outlined in the ED.
- The need for decoupling of credit losses from the EIR calculation and recognition.
- The requirement of a new impairment model must be applicable to open portfolios as this is how we risk manage our business.
- A new impairment model would distinguish between performing and non-performing amortized cost financial instruments which would result in charges for realized losses being taken to the P&L as they occur.

The main differences between the approaches outlined above are the principles regarding the build up and usage of the provisions for the performing “good” book.

We have a preference for an approach which combines a balance sheet approach for the non-performing book and P&L view regarding the build up and usage of the performing book provisions. This approach would take the entire provision required for the non-performing book instrument from the performing book provision (of the portfolio from which the instrument was removed). The performing book provision would be evaluated against a one year expected loss floor and any additional provisions for allowance are made as needed. Such an approach would minimise operational complexity and ensure that the good book allowance is used and does not act as a buffer.

**Note**: Questions 43-45 were deleted as they are questions for users.

**Questions for Preparers and Auditors**

**Question 46**
**The proposed guidance would require that in determining whether credit impairment exists, an entity consider all available information relating to past events and existing conditions and their implications for the ~~25~~collectability of the cash flows attributable to the financial asset(s) at the date of the financial statements. An entity would assume that the economic conditions existing at the end of the reporting period would remain unchanged for the remaining life of the financial asset(s) and would not forecast future events or economic conditions that did not exist at the reporting date. In contrast, the IASB Exposure Draft on Impairment proposes an expected loss approach and would require an entity to estimate credit losses on basis of probability-weighted possible outcomes. Do you agree that an entity should assume that economic conditions existing at the reporting date would remain unchanged in determining whether a credit impairment exists, or do you believe that an expected loss approach that would include forecasting future events or economic conditions that did not exist at the end of the reporting period would be more appropriate? Are both methods operational? If not, why?**

We support an open portfolio based expected loss model, as it best aligns the financial reporting with internal risk management practices. When determining expected losses, we believe that an entity should use all relevant information available as of the reporting date and in a manner consistent with how the portfolios are risk managed.

This information will consist mainly of historical data and current market information (which includes the markets view of potential future events). Where current market information is not available the entity shall use management's best estimate of the expected loss based on current market conditions.

We do not support a proposal based on an expected cash flow model as it would introduce undue operational complexity with little/no benefit to users and has no connection to internal risk management practices.

**Question 47**
**The proposed guidance would require that an appropriate historical loss rate (adjusted for existing economic factors and conditions) be determined for each individual pool of similar financial assets. Historical loss rates would reflect cash flows that the entity does not expect to collect over the life of the financial assets in the pool. Would such an approach result in a significant change in practice (that is, do historical loss rates typically reflect cash flows that the entity does not expect to collect over the life of the financial assets in the pool or some shorter period)?**

Please see to our response to **Question 40**.

**Interest Income**

**Questions for All Respondents**

**Question 48**
**The proposed guidance would require interest income to be calculated for financial assets measured at fair value with qualifying changes in fair value recognized in other comprehensive income by applying the effective interest rate to the amortized cost balance net of any allowance for credit losses. Do you believe that the recognition of interest income should be affected by the recognition or reversal of credit impairments? If not, why?**

No. The proposed ASU would require the combining of the interest and provisioning components of amortized cost financial instruments in the EIR calculation. It is our view that this adds a significant amount of complexity to an already highly complex calculation. This also reduces information usefulness by mixing the highly predictable cash flows resulting from contractual terms with the uncertain and less objective expected losses of which the timing and amount are uncertain. We believe that the different nature of contractual cash flows and expected losses justifies separate methodologies for the recognition and presentation of interest income and expected losses.

While there is a theoretical link between the yield for an amortized cost instrument and the lenders perception of credit risk as of the date of issuance, these risks are managed separately and therefore we do not believe it would be appropriate to link interest revenue recognition with the allocation of expected losses. Decoupling is appropriate and required to reduce the operational complexity of the proposed ASU and also reflects how management assesses and manages interest rate and credit risks.

We support the presentation of provisioning in a separate line of the income statement. Retaining separate methodologies for the recognition and presentation of interest income and expected losses improves transparency and better aligns the accounting and risk management practices.

**Question 49**
**Do you agree that the difference in the amount of interest contractually due that exceeds interest accrued on the basis of an entity's current estimate of cash flows expected to be collected for financial assets should be recognized as an increase to the allowance for credit losses? If not, why?**

This issue would be largely mitigated by the decoupling of interest and loan loss provisioning suggested in **Question 48** above.

**Question 50**
**The proposed guidance would permit, but would not require, separate presentation of interest income on the statement of comprehensive income for financial assets measured at fair value with all changes in fair value recognized in net income. If an entity chooses to present separately interest income for those financial assets, the proposed guidance does not specify a particular method for determining the amount of interest income to be recognized on the face of the statement of comprehensive income. Do you believe that the interest income recognition guidance should be the same for all financial assets?**

Interest income may not always be the most relevant measure for instruments held for trading and therefore it should not be required to separate interest income from trading income. However, if an entity believes that interest income is a relevant measure for its assets held at FVTPL, it should be permitted to present it separate from trading revenue, and the interest income recognition guidance should be the same for all assets. Each entity should clearly disclose which approach is applied in its financial statements.

**Question 51**
**Do you believe that the implementation guidance and illustrative examples included in this proposed Update are sufficient to understand the proposed credit impairment and interest income models? If not, what additional guidance or examples are needed?**

The implementation guidance and illustrative examples are useful and will help readers understand the proposed models. To further this understanding, an example on how to evaluate financial assets for credit impairment on a pool basis should be added.

**Note:** Questions 52-55 were deleted as they are questions for users**.**

**Hedge Accounting – Questions for All Respondents**

**Question 56**
**Do you believe that modifying the effectiveness threshold from highly effective to reasonably effective is appropriate? Why or why not?**

Yes. We support the modification of the effectiveness threshold from “highly effective” to “reasonably effective” and a shift from a pure qualitative assessment towards more qualitative assessment of effectiveness. This modification is likely to provide much needed flexibility in accounting hedge designation. This would allow entities to take a longer term view on the hedge rather than bear the risk of a failed hedge due to the disproportionate consideration given under the current guidance to unusual or irregular behaviour of fair values during a short period.

We support the Board’s decision not to define “reasonably effective” and allow the market participants to use judgment in specific cases. However, we believe that the Board should provide more guidance on when a quantitative assessment will be necessary and what would be considered “reasonably effective” in the context of specific types of hedge relationships. We believe the Board should elaborate further on this subject e.g. factors that could be viewed as sources of variability/volatility, eligibility of economic or accounting volatility, lack of direct business link between the hedged volatility and the hedging instrument, consideration of different methods when they provide different results, effect of basis between the hedged item and the hedging instrument and consideration of option features in the hedged item when not mirrored in the hedging instrument i.e. hedged beyond first call date.

**Question 57**
**Should no effectiveness evaluation be required under any circumstances after inception of a hedging relationship if it was determined at inception that the hedging relationship was expected to be reasonably effective over the expected hedge term? Why or why not?**

No. We support the Board's decision to continue to require a reassessment of hedge effectiveness subsequent to inception if circumstances suggest that the hedging relationship may no longer be reasonably effective. We believe that hedge accounting should only be used where it can be justified based on the underlying facts. If those facts change, hedge accounting should be discontinued; however, we strongly recommend that the Board consider more narrowly defining the circumstances that would necessitate a reassessment of hedge effectiveness.

We recommend that a subsequent reassessment of hedge effectiveness should only be required if any of the following scenarios occurs:

- If there is a change in any of the critical terms of the hedging instrument or the hedged item;
- If there is a significant increase in the credit risk of any of the counter parties to the hedging instrument or the hedging instrument is transferred to a new counterparty that has a significantly higher credit risk;
- Due to changes in the market conditions, the hedge relationship may no longer be expected to be reasonably effective for the remainder of the designated period e.g., disappearance of a market, or significant market wide shift in valuation basis of a particular instrument.

Certain financial guarantees are scoped into the standard and will be required to be measured at fair value through profit and loss under the proposed ASU as financial guarantees will not meet the definition of 'debt instrument.' To the extent these financial guarantees held are economic hedges of the credit risk of instruments which are accounted for at fair value through comprehensive income, a mismatch in the profit and loss will result unless hedge accounting is applied. Therefore in addition to the issues listed above, we also encourage the FASB to address hedges of credit risk and specifically examine the significant barriers to achieving credit risk hedging today, with the objective of allowing more entities to align their financial reporting with their internal risk management practices.

**Question 58**
**Do you believe that requiring an effectiveness evaluation after inception only if circumstances suggest that the hedging relationship may no longer be reasonably effective would result in a reduction in the number of times hedging relationships would be discontinued? Why or why not?**

No. We do not believe that requiring an effectiveness evaluation after inception only if circumstances suggest that the hedging relationship may no longer be reasonably effective will necessarily reduce the number of times hedging relationships would be discontinued.

In general, due to the rigorous effectiveness evaluation at inception, the results of regular subsequent effectiveness evaluations rarely present a surprise i.e. resulting in a failed relationship, unless there is a change in circumstances. Furthermore, we expect that the practical application of the requirement to assess when “circumstances suggest that the hedging relationship may no longer be reasonably effective” will lead to regular informal assessment of effectiveness in any case; therefore, it is unlikely that any hedges which would have been discontinued for failing the existing testing requirements will be continued under the proposed guidance.

**Question 59**
**Do you believe that a hedge accounting model that recognizes in net income changes in the fair value and changes in the cash flows of the risk being hedged along with changes in fair value of the hedging instrument provides decision-useful information? If yes, how would that information be used? If not, why?**

No. The Board’s basis for conclusions does not address why this fundamental change from FAS 133 (ASC Topic 815) is an improvement to financial reporting, results in simplification, and further does not address the change in the conclusion the FASB reached when it issued Statement 133 (ASC Topic 815) previously. In paragraphs 379 and 380 of FAS 133 (ASC Topic 815), the FASB explained its decision to prohibit recognition in OCI of nonexistent gains or losses relating to the change in present value of the cash flows associated with non-contractual, forecasted transactions. This proposed ASU is likely to introduce complexity in financial statements and distort earnings and asset related ratios.

We support the rationale for the requirements of the current FAS 133 (ASC Topic 815) to limit recognition of ineffectiveness in earnings to amounts by which the actual derivative instrument exceeds, on an absolute basis, the projected present value of the hedged cash flows. Therefore we do not agree that such a significant change to FAS 133 (ASC Topic 815) should be made without a more robust justification that directly addresses how this proposed ASU provides more transparent financial statements, and achieves the appropriate cost-benefit conclusion.

Furthermore, this represents a clear divergence from IASB’s position in this respect and we would expect the two Boards to focus on convergence and avoid creating new differences.

**Questions for Preparers and Auditors**

**Question 61**
**Do you foresee any significant operational concerns or constraints in calculating ineffectiveness for cash flow hedging relationships? If yes, what constraints do you foresee and how would you alleviate them?**

Yes. We expect this requirement will lead to a disproportionate increase in the cost of cash flow hedge designations compared to any benefits that the Board may believe it to achieve. The proposed ASU requires measurement of ineffectiveness even if the hedging instrument is hedging only the bottom layer of cash flows (under hedging).

This will have a profound impact on a vast majority of existing cash flow hedges which are designed to be under hedges so that there is no need to separately measure ineffectiveness as long as the critical terms are matched in the designation.

Under this proposed ASU, each derivative designated in a cash flow hedge will be required to be compared to a "hypothetical derivative". This will result in an immediate requirement to model, book, determine the value and monitor a number of "hypothetical derivatives" which only exist for hedge accounting purposes. We expect this proposed ASU will result in significant increase in complexity and costs as designation, testing and monitoring of cash flow hedges will need additional staff and management time along with appropriate access to adequate derivative booking and valuation systems.

While most financial institutions like Deutsche Bank have the proper systems in place to model, book and value hypothetical derivatives, however, to carry out these tasks will require significant changes to access rights to such systems and allocation of additional time and suitably qualified resources to support the valuation process necessary for effectiveness measurement. During the current economic environment when cost rationalization is high on the agenda, it is likely that many finance functions within an entity's organization will not be able to cope with the expected implementation of the new proposed ASU, especially when these hypothetical derivative bookings will have no other use for management or external users.

We would like to mention that where an entity does not have adequate systems to value trades and in the past had relied on derivative valuations received from external parties to post entries for cash flow hedges, they are likely to struggle to measure the ineffectiveness by valuing a "hypothetical derivative".

**Question 62**
**Do you foresee any significant operational concerns or constraints in creating processes that will determine when changes in circumstances suggest that a hedging relationship may no longer be reasonably effective without requiring reassessment of the hedge effectiveness at each reporting period? If yes, what constraints do you foresee and how would you alleviate them?**

Yes. If the "circumstances" are not defined in a specific narrow manner, we expect that in order to avoid the risk of failures or restatements some entities may chose to continue with an extensive effectiveness testing approach not too different from the current practice.

Furthermore, entities which chose not to adopt a rigorous effectiveness testing approach may be forced to restate if their hedges are later discovered to be ineffective due to a different interpretation of "circumstances" by a later review whether internal or external e.g. audit or regulatory.

Therefore, we would urge the Board to consider defining the "circumstances" so as to limit the scope and nature of such monitoring processes. If the Board defines the circumstances in a narrow manner, we would expect that the reassessment methodology will be based on a review of the terms of the hedged item and the hedging instrument on a qualitative basis instead of relying on operationally intensive statistical based models. Such a review will include monitoring of any change in the structural basis between the hedged item and the hedging instrument including credit and other differences in valuation.

**Question 63**
**Do you foresee any significant operational concerns or constraints arising from the inability to discontinue fair value hedge accounting or cash flow hedge accounting by simply dedesignating the hedging relationship? If yes, what constraints do you foresee and how would you alleviate them?**

Yes. In our experience, this requirement will exacerbate the impact of misalignment of the hedge accounting framework with the risk management framework generally applied in many entities particularly banks. The shortcomings of the current accounting guidance in respect of the portfolio hedging practiced by banks as part of their Asset Liability Management are a well discussed subject. In order to overcome some of these shortcomings, banks would normally seek to regularly balance their accounting hedges and as part of this process may carefully select and de-designate some of the hedges to better reflect the underlying economic hedge position. These de-designations are not aimed at manipulating income but are a way to better reflect the actual hedged risk position and the impact of such hedges on financial statements.

We would support a requirement to justify the de-designations based on underlying circumstances. However, we are strongly against abolishing the voluntary de-designation in the proposed guidance.

We understand that one way to work around this proposed requirement, at least in respect of the fair value hedges, would be to designate and re-designate hedges on a monthly basis. In this case, management will be able to choose when not to designate those that it would have de-designated under the current guidance. This possibility is acknowledged by the Board in paragraph BC223 of the proposed ASU, and we would request the Board to drop this proposal as it unnecessarily increases the complexity and significantly hinders the hedge accounting without any real benefits.

Furthermore, the Board has allowed the addition of partially offsetting hedging instruments to an existing hedge if it improves effectiveness of the hedge and it is perplexing why it has not allowed a de-designation of a hedging instrument if it improves the hedge effectiveness.

**Question 64**
**Do you foresee any significant operational concerns or constraints arising from the required concurrent documentation of the effective termination of a hedging derivative attributable to the entity's entering into an offsetting derivative instrument? If yes, what constraints do you foresee and how would you alleviate them?**

Yes. In an Asset Liability Management perspective, the risks are monitored and hedged on a portfolio basis, therefore, it would be highly unlikely to transact a derivative that "fully offsets" the fair value or cash flow of an existing derivative – except by coincidence or at a significant cost. In this case the Board seems to encourage entities to undertake transactions purely to achieve an accounting outcome and with no underlying economic reason. It is highly unlikely that an entity will do so in their normal course of business.

Transacting an offsetting derivative as a means to terminate the existing hedge accounting relationship is a costly and unnecessary expense when the existing hedging derivative may be re-used and possibly re-designated for other purposes including risk management in another qualifying hedge accounting relationship. Furthermore, the Board has allowed addition of an offsetting hedging instrument to an existing hedge if it improves effectiveness of the hedge so it is perplexing why it has not allowed a de-designation of a hedging instrument if it improves the hedge effectiveness.

Furthermore, the proposed guidance requires the ability to track both the original and offsetting derivatives in the system for their life and does not allow their use in any future hedges. This again highlights the lack of attention given by the Board to the portfolio nature of risk management activities. By implication, entities would be unable to terminate any hedges even if the underlying risk exposure has been cancelled out as part of the portfolio management activities and no longer exists. Considering the impracticality of the proposed ASU we would urge the Board to continue to allow the entities to de-designate hedges at their discretion as discussed in **Question 63** above.

**Disclosures – Question for All Respondents**

**Question 65**
**Do you agree with the proposed disclosure requirements? If not, which disclosure requirement do you believe should not be required and why?**

Overall as expressed in the key messages and answers to the individual questions, DB supports a mixed measurement model for financial assets and financial liabilities that is driven by an entity's business model. In general, we believe that the disclosure requirements should be linked to the above measurement objective and provides users with useful and relevant information, rather than burdening them with redundant information. Therefore, it is important that the Board carefully weighs the costs and benefits of the user community with that of the preparers. For disclosure requirements related to hedge accounting, we support the proposed additional disclosures for fair value hedges and interest hedges linked to own debt or other liabilities as long as the proposed ASU is fully supported by the user community.

We have listed our concerns about the following disclosure requirements:

- Requirement for qualitative information about the reasons for changes in fair value attributable to changes in the entity's credit standing and how the gains and losses attributable to changes in the entity's credit standing were determined (paragraph 98 of the proposed ASU) – We believe the OCI is the best classification of own credit. We want to see a clearer definition of the own credit in order to provide relevant information.
- Requirement for disclosing detailed information about sales before maturity for financial assets classified at fair value through OCI (paragraph 100 of the proposed ASU) – We support the amortized cost measurement for financial assets that are held for purposes of collecting contractual cash flows based on a business model and believe that collection for contractual cash flows does not mean "held-to-maturity". We also support the elimination of the concept of "tainting" and an entity should be permitted to sell financial assets before maturity in this classification for purposes of strategic need and management of asset and liabilities. Disclosure of detailed information about the sale proceeds, gross realized gains / losses, and the reasons of the sale would not be consistent with this measurement principle and would only create undue cost without providing additional useful information to the users of financial statements.
- For disclosure requirement related to credit impairment – We believe that the objective of disclosure for credit impairment should be to provide information to enable the users of the financial statements to understand the key processes, assumptions and techniques used to manage credit risk. We broadly support the disclosure requirements as proposed in paragraph 104 of the proposed ASU in relation to a description of the accounting policies and methodology used to estimate the allowance for credit losses and analysis of the activities / changes in the allowance account. Furthermore, for credit impairment assessed on a portfolio basis, an entity should disclose explanation of how these pools are defined, how this is aligned with the management of credit risk, management's assumptions and methodology for determining the credit impairment for these portfolios and description of events which led to a material change in the allowance for credit loss during the period and amount of the change by reporting portfolio.
- Disclosure requirements for hedge accounting activities again focus on one-on-one hedges and do not address the portfolio nature of the risk management at banks. Banks have had to artificially designate hedges of net positions as hedges of individual assets or liabilities and by having to disclose this artificial designation to the users will lead to additional complexity in the financial statements and distortion of income and other ratios. We suggest that the Board resolves the portfolio hedging issues before proposing any further quantitative disclosures for hedging activities.

**Disclosures**

**Note**: Questions 66-67 were deleted as they are questions for users.

**Effective Date and Transaction**

**Questions for All Respondents**

**Note**: We have provided a combined response to Questions 68-71.

**Question 68**
**Do you agree with the transition provision in this proposed update? If not, why?**

**Question 70**
**How much time do you believe is needed to implement the proposed guidance?**

**Question 71**
**Do you believe the proposed transition provision is operational? If not, why?**

We generally agree that a cumulative effective adjustment is the appropriate method of transition for this proposed ASU (except for hedge accounting as discussed below).

Given the magnitude of the proposed changes, we believe that it would take at least 3-4 years for financial institutions to evaluate the impact and implement the proposed provisions. Furthermore, as discussed in our key messages, we are deeply concerned with the different positions the FASB has adopted in the Proposed ASU in comparison to the models proposed by the IASB and urge the two Boards to continue to work together to resolve differences, We do welcome the joint statement by the IASB and the FASB on June 24th, 2010 regarding their convergence work that a consultation document will be issued seeking stakeholders input about effective dates and transaction methods. We urge the two Boards to work together to develop transaction rules that are operational. As some other IFRS reporters, certain DB US entities prepare financial statement under US GAAP, to implement two accounting standards on financial instruments at different effective dates would create undue operational costs and would not be an effective allocation of resources.

In respect of hedge accounting, the cumulative adjustment may not be possible as the relevant hedges were not in place or could not be put in place in the comparative period. The Board should only require prospective implementation of the hedge accounting guidance and should not require a restatement of comparatives in this respect.