September 25, 2012

Ms. Susan M. Cosper
Technical Director
Financial Accounting Standards Board
401 Merritt 7, P.O. Box 5116
Norwalk, CT 06856-5116
File Reference No. 2012-200

Dear Ms. Cosper:

The Federal Housing Finance Agency (FHFA or Agency) welcomes the opportunity to comment on the Financial Accounting Standards Board’s (FASB or Board) proposed Accounting Standards Update on Financial Instruments (Topic 825) - Disclosures about Liquidity Risk and Interest Rate Risk (the proposed ASU).

As the regulator and conservator of Fannie Mae and Freddie Mac and the regulator of the Federal Home Loan Bank System, FHFA considers audited financial reports an important resource for the Agency’s supervision process. Therefore, FHFA supports high-quality accounting and auditing standards that promote the reporting of unbiased, transparent, and relevant information about the performance and condition of FHFA’s regulated entities.

FHFA appreciates the Board’s efforts to provide financial statement users with more transparent information about an entity’s liquidity risk and interest rate risk related to financial instruments. At present, disclosures about these critical risks for public financial institutions are included in the Management’s Discussion and Analysis (MD&A) section of periodic filings with the Securities and Exchange Commission (SEC). SEC rules permit reporting entities to select the manner in which they present the required information, and the SEC does not require an external auditor to audit the disclosures.

FHFA believes the proposed ASU would provide the following benefits to financial statement users:

- The disclosures would provide information to identify the potential vulnerabilities associated with an entity’s liquidity and interest rate risks and facilitate further discussions between management and financial statement users regarding the entity’s plans to address the potential exposures.
The inclusion of the proposed disclosures in the notes to the financial statements would strengthen the reliability of the disclosed information by: (i) subjecting the preparation of the disclosures to the internal control requirements of the Sarbanes-Oxley Act of 2002, Pub.L. 107-204 (2002), (SOX); and (ii) requiring that independent auditors audit the disclosures.

The standardization of disclosures would provide consistent and comparable information for financial statement users to perform trend and peer analyses.

Below are the Agency’s answers to the questions that are relevant to FHFA. FHFA also provides the Board with suggestions for the content and format of the disclosures referred to in the respective questions. FHFA’s goal in providing these suggestions is to enhance the usefulness of the proposed disclosures.

I. Questions for Users – Liquidity Risk

Question 7: Does the liquidity gap table described in paragraphs 825-10-50-23E through 50-23K provide decision-useful information about the liquidity risk of a financial institution? If yes, how would you use that information in analyzing a financial institution? If not, what information would be more useful?

The proposed liquidity gap table has the potential to provide financial statement users with decision-useful information if the Board should consider making the following modifications or clarifications on the format and content of the table.

- As proposed in ASC 825-10-50-23E through 50-23K, the data in the liquidity gap table includes “the carrying amount of classes of financial assets and financial liabilities segregated into time intervals by their expected maturities” [emphasis added]. To properly reflect liquidity risk information, FHFA suggests the Board consider clarifying that the data reporting entities present in this table should be primarily based on the undiscounted cash flows that the reporting entity expects to occur per the contractual terms of the related financial instruments. FHFA also recommends that the Board refer to this table as the “Schedule of 12-month’s expected cash flows from recognized financial instruments and off-balance-sheet commitments.” FHFA believes that:
  - This new title more faithfully represents the nature of the disclosed information.
  - The term “liquidity gap” does not fully convey the “liquidity position” of the entity at the end of the reporting period because of the limit in the scope (information pertaining only to financial instruments) and the constraint imposed in the preparation of the disclosed information (expected sales or transfers of the instruments are precluded).

- The Board also should consider providing guidance for presenting the undiscounted cash flows for financial instruments with a floating interest rate or other non-bifurcated embedded derivatives.
• Because reporting entities may use many forecast scenarios to estimate the contractual cash flows they expect to collect or pay, the Board may wish to clarify whether the term “expected maturity” means the “most likely maturity” or “the probability-weighted maturity” to ensure consistency in practice.

• To provide a complete picture of an entity’s liquidity risk, the Board should consider requiring reporting entities to present undiscounted cash flow data by applicable time intervals for all debt instruments subsequently measured at fair value through net income (FVNI). Also, in requiring the disclosure of undiscounted cash flows for FVNI debt instruments, the Board could consider exempting the requirement for those FVNI debt instruments that the entity frequently trade (held-for-trading debt instruments). For these held-for-trading debt instruments, the Board should only require the reporting entity to present the instruments’ carrying amount in a separate line item, in the total amount column.

• For swap derivative instruments with no payment options, the Board should consider requiring reporting entities to present data on undiscounted cash flows in the applicable time interval in which the reporting entity expects the (net) cash flows to occur based on the contractual terms of the swap derivative instruments.

• For derivative instruments with payment options, the Board should consider whether the information presented for these instruments should be presented in accordance with the instruments’ expected maturity to correspond with the expected maturity of the related items that the reporting entity hedges with these derivative instruments.

• For financial assets and liabilities (e.g. derivatives, repurchase agreements) that qualify for netting and are presented as a net amount on the statement of financial position, additional guidance on the manner in which reporting entities should present cash flow information in the table may need to be provided.

• Additionally, guidance on how to present the information for items such as allowance for loan losses that are measured on a collective basis would be helpful to reporting entities and may prevent diversity in practice.

Question 9: Paragraphs 825-10-50-23S through 50-23V would require an entity to disclose its available liquid funds. Would this table provide decision-useful information in your analysis? If not, what information would be more useful?

The available liquid fund table would provide decision-useful information to financial statement users. However, to improve the relevance and comparability of the disclosed information, FASB should consider providing the following clarifications and modifications:
The Board should consider clarifying that reporting entities may consider only unencumbered cash and unencumbered high-quality liquid assets as available liquid funds.

To prevent diversity in practice, the Board should consider providing more descriptive guidance to narrowly define the term “high quality.” The current version of ASC 825-10-50-23V would provide entities with wide discretion to define “high quality” assets and would likely result in significant differences between entities in their implementation of the proposed disclosure. The Board also should consider aligning its definition of “high quality” with the Basel III definition.

The Board should consider adding a new section to the proposed “available liquid funds” table to provide data for financial liabilities and off-balance-sheet commitments that are contractually due in the next quarter. This addition would enable financial statement users to assess an entity’s ability to meet its contractual obligations in the next quarter based solely on available liquid funds.

Question 10: Are the proposed time intervals in the tables appropriate to provide decision-useful information about an entity’s liquidity risk? If not, what time intervals would you suggest? Do you believe that there are any reasons that these required time intervals should be different for financial institutions and entities that are not financial institutions?

The proposed time intervals in the tables would not provide decision-useful information about an entity’s liquidity risk. With regard to a reporting entity’s liquidity exposures, capital providers tend to focus their liquidity concerns on a short-term basis. Therefore, to enhance the relevance of the disclosed information, the Board should consider requiring the disclosure of undiscounted cash flows in the liquidity gap table, on a monthly basis, for the next twelve months after the reporting date. Disclosures of information beyond the next twelve months should not be required. FHFA also notes that the twelve-month period is consistent with the time period commonly used to assess the reporting entity ability to continue as a going concern.

Question 11: With respect to the time intervals, should further disaggregation beyond what is proposed in this Update be required to provide more decision-useful information to the extent that significant amounts are concentrated within a specific period (for example, if a significant amount of liabilities are due in Year 10 of the —past 5 years time interval)? Please explain.

Yes. The Board should consider requiring additional narrative disclosures to complement the quantitative data for scenarios in which “significant” amounts of liabilities are expected to be paid within a specific period just beyond the twelve months after the reporting date.
II. Questions for Users – Interest Rate Risk

Question 16: Would the repricing gap analysis in paragraphs 825-10-50-23Y through 50-23AC provide decision-useful information in your analysis of financial institutions? If yes, how would this disclosure be helpful in your analysis? If not, what information would be more useful?

The proposed repricing gap analysis would provide decision-useful information about an entity’s exposure to changes in interest rates. However, to enhance the relevance of the disclosure, the Board should consider requiring reporting entities to base the disclosed information on the expected, not the contractual maturity of the financial assets and financial liabilities. This modification would better reflect the repricing information for financial assets and financial liabilities whose contracts include prepayment options.

Question 17: Are the proposed time intervals in the repricing gap table in paragraphs 825-10-50-23AB through 50-23AC appropriate to provide decision-useful information about the interest rate risk to which a financial institution is exposed? If not, which time intervals would you suggest?

Yes. The proposed time intervals in the repricing gap table in paragraphs 825-10-50-23AB through 50-23AC would provide decision-useful information about the interest rate risk to which a financial institution is exposed.

Question 18: The interest rate risk disclosures in this proposed Update would include a sensitivity analysis portraying the effects that specified changes in interest rates would have on net income and shareholders’ equity. Currently, many banks and insurance companies provide a sensitivity analysis of the economic value of equity instead of shareholders’ equity. A sensitivity analysis of economic value would include the changes in economic value of financial instruments measured at amortized cost, such as loans and deposits. A sensitivity analysis of shareholders’ equity would only include those changes that affect shareholders’ equity. Therefore, the changes in the economic value of financial instruments measured at amortized cost would not be reflected in the sensitivity analysis although changes in interest income would be reflected. Do you think that a sensitivity analysis of shareholders’ equity would provide more decision-useful information than would a sensitivity analysis of economic value? Please discuss the reasons why or why not.

While the proposed interest rate sensitivity analysis disclosure could provide financial statement users with relevant information, the Board should consider providing the following clarifications and modification to improve the usefulness of the disclosed information:

- As currently drafted, the effect of ASC 825-10-50-23AD through 50-23AF on net income and shareholders’ equity resulting from the different interest rate change scenarios for financial (debt) instruments that are measured at amortized cost or at fair value through other comprehensive income (FVOCI) is unclear. For example, for these debt instruments, the effect on net income is primarily the result of recognizing credit
impairment for financial assets and interest income or expense. If the Board intends for entities to consider the impact of the interest rate changes on the prepayment and default rates that, in turn, would result in changes in the amounts reporting entities recognize for interest income or expense and/or credit impairment for these debt instruments, then some clarification would be helpful.

- The Board should consider providing additional guidance for the selection of a more appropriate level of interest rate changes (beyond the proposed 100 and 200 basis point of interest rate change) to facilitate a better assessment of interest rate risk in a low interest rate environment (like the current environment).

- The Board should consider replacing the proposed magnitude of 100 basis point shift in the shape of the yield curve with smaller shifts to ensure the disclosed effects on the financial statements provide useful information to financial statement users.

- The Board should consider modifying the interest rate sensitivity analysis table to present information on the sensitivity of the fair value for all financial assets and financial liabilities of the reporting entity regardless of how these assets and liabilities are recognized and measured of the statement of financial position.

- The Board should consider requiring the measurement of the effects of interest rate changes on a pre-tax basis, instead of post-tax basis as proposed. Since the proposed ASU focuses on providing information regarding interest rate risks, presenting the information on a post-tax basis would result in more complexity in the preparation of the disclosed information and introduces the effects of tax planning activities into an interest rate risk disclosure.

III. Questions for All Respondents

Question 21: Although the proposed amendments do not have an effective date, the Board intends to address the needs of users of financial statements for more information about liquidity risk and interest rate risk. Therefore, the Board will strive to make these proposed amendments effective on a timely basis. How much time do you think stakeholders would require to prepare for and implement the amendments in this proposed Update? Should nonpublic entities be provided with a delayed effective date? If so, how long of a delay should be permitted and why? Are there specific amendments that would require more time to implement than others? If so, please identify which ones and explain why.

If the Board issues the final ASU at the end of 2012, an effective date for fiscal years and interim periods beginning on or after January 1, 2014 is appropriate for public entities.

Question 22: Do you believe that any of the amendments in this proposed Update provide information that overlaps with the SEC’s current disclosure requirements for public companies without providing incremental information? If yes, please identify which proposed amendments
you believe overlap and discuss whether you believe that the costs in implementing the potentially overlapping amendments outweigh their benefits? Please explain why.

FHFA believes that, with the clarifications and amendments suggested above, the proposed ASU would improve the reliability of disclosed information by a reporting entity and would provide helpful information to financial statement users to identify and analyze the potential liquidity and interest rate exposures of a reporting entity.

To avoid duplication in the disclosures, perhaps the Board should work with the SEC to delineate the disclosures of information to identify liquidity and interest rate risks in the notes to the financial statements and the disclosures of information about risk management policies and practices in the MD&A of the periodic SEC filings.

Thank you for the opportunity to comment. FHFA hopes the Board and staff find these comments and suggestions helpful. If the Board and staff have any questions regarding this letter, please feel free to contact me at 202-649-3450.

Sincerely,

[N. Satriano]

Nicholas J. Satriano
Chief Accountant
Federal Housing Finance Agency