May 31, 2013

Ms. Leslie Seidman, Chairman
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, Connecticut 06856-5116
VIA EMAIL: director@fasb.org

Project: Financial Instruments – Credit Losses (File Reference No. 2012-260)

Dear Ms. Seidman:

Cisco Systems, Inc. ("Cisco") appreciates the opportunity to comment on the Exposure Draft of the Proposed Accounting Standards Update, Accounting for Financial Instruments – Credit Losses (Subtopic 825-15) ("Proposal" or "Exposure Draft"). This Exposure Draft is another critical test to the overall convergence efforts of the Financial Accounting Standards Board ("FASB") and the International Accounting Standards Board ("IASB"). We believe this Proposal highlights the issues with developing principle-based standards and applying general concepts to disparate items. One of our primary concerns highlighted in our letter is that a "one size fits all" financial assets credit loss model does not acknowledge the fundamental differences that exist between the following items in scope of this Proposal – accounts receivable, leases, loans and investments in debt securities. Moreover, as significant differences exist between the FASB and the IASB proposals, we believe it is imperative that both Boards strive to minimize or eliminate differences in their proposals to avoid confusion among users, unnecessary costs to preparers, and to inspire confidence in a single set of high quality, unified standards.

Cisco’s primary business activities are to design, manufacture, and sell Internet Protocol ("IP")-based networking and other products related to the communications and information technology ("IT") industry and provide services associated with these products and their use. Most of our sales are on an open credit basis, with typical payment terms of 30 days in the United States and, because of local customs or conditions, longer in some markets internationally. Beyond our open credit arrangements, we also have demands for customer financing arrangements. Our financing arrangements include leases, loans and financed service contracts. We believe customer financing is a competitive factor in obtaining business, particularly in serving customers involved in significant infrastructure projects.

We maintain an investment portfolio of various holdings, types, and maturities. These securities are classified as available-for-sale and, consequently, are reported at fair value with unrealized gains or losses reported as a component of
accumulated other comprehensive income, net of tax. We believe the overall credit quality of our portfolio is strong, with our fixed income investment portfolio consisting primarily of high quality, investment-grade securities. Our philosophy for investing in fixed income securities is based on three primary objectives: 1) preserve capital; 2) provide an optimized rate of return consistent with the first objective; and 3) keep the portfolio invested in liquid securities to meet the eventual cash demands of the business. Cisco's investment strategy is not designed to generate short-term returns and does not strive to monetize temporary changes in the fair value of its securities. In short, we manage our investments for fundamental business use, as opposed to speculative investment purposes.

**Overview and Summary**

Cisco supports the Board’s efforts to address the issues raised by various constituents with respect to the measurement of credit losses for financial assets that are not accounted for at fair value through net income. We understand the Board’s objective to provide users with more timely and decision-useful information while also reducing complexity and achieving increased consistency in U.S. GAAP.

However, we believe there are more reasonable alternatives than the proposed model and that such alternatives should be focused on improving the existing model as opposed to the introduction of an entirely new model. Fundamentally, we do not believe there is a conceptual basis for recognizing expected credit losses (ECL) at the date of recognition of financial instruments (i.e., upon inception) in the income statement. Specifically, our concerns are as follows:

- Accounts receivable, lease receivables, loan receivables and investments in debt securities are inherently different in terms of the underlying business model and the associated credit risk management practices. Therefore, we do not believe that a holistic approach represented by the proposed ECL model that would apply to each of these financial instruments is either practical or results in a more appropriate recognition of credit losses.

- Initial ECL are non-economic losses, as the transaction price should already reflect all ECL at the time a financial asset is purchased or originated. To assume otherwise would imply that these transactions are not arms-length or are executed in a market with valuations that do not capture the underlying risks and terms associated with that particular instrument.

- The determination of ECL introduces an incremental element of subjectivity and therefore, decreases consistency and transparency in the financial statements, and allows for potential manipulation. Further, the proposal incorrectly assumes that there are reliable forward-looking indicators available to predict credit losses, and that by relying on those indicators investors will receive better information from preparers in advance of events like a financial crisis.
• There is no correlation between the proposed recognition timing for ECL (at inception) and historical loss experience, which will result in the overstatement of credit losses if ECL are recognized up-front. The Board acknowledges this issue in the Basis for Conclusions, but does not provide a compelling argument to support that up-front recognition is the best available "practical" approach.

• Recognition of ECL at inception would contribute to significant income statement volatility and provides an avenue for potential earnings management. For example, under the Proposal, we would record a credit loss at the time of purchase of a financial instrument that is not driven by an economic event. Subsequently, if we sold that same financial instrument in a different reporting period, we may record a gain even though there is not a change in credit risk.

• Finally, recognition of ECL at inception results in more aggressive credit loss recognition than for those financial assets held at fair value through net income.

We believe the limited informational benefits do not outweigh the additional operational and compliance costs associated with the proposed model, especially for financial assets that have not historically experienced significant credit losses and where existing models are effective, well understood and currently operational. For debt securities in particular, we understand the Board’s intention in introducing the practical expedient but do not believe there is any practical benefit for preparers in its current form. As currently proposed, changes in fair value unrelated to credit risk may drive the timing for recognition of credit losses, regardless of the significance of the related credit losses. Additionally, for trade accounts receivables, we find that applying an ECL model would provide limited user information given the short-term nature of these instruments.

We believe there are more reasonable alternatives than the proposed model and that such alternatives should be focused on improving the existing model as opposed to the introduction of an entirely new model. We recommend the Board focus on either modifications to the existing impairment recognition thresholds or incremental disclosures for financial assets with significant credit risk. As an example, the current probability threshold for recognizing a credit loss is at the "probable" level. If this level was lowered to a "more likely than not" threshold rather than the complete elimination of the probability threshold as is proposed in the Exposure Draft, we believe this would satisfy the Board's objective without misrepresenting the financial statements of preparers. We also believe that the Board can enhance the existing model by providing additional guidance and examples to encourage earlier recognition of credit losses within an event-driven credit loss model.
We have similar conceptual and practical concerns regarding the IASB proposal and are concerned that the Boards have been unable to agree on a converged model. Accordingly, we believe it is imperative that the FASB and IASB refocus on developing a single converged standard for measuring credit losses for financial assets. Anything short of that outcome creates additional burden for both preparers and users and promotes additional differences among global organizations. In addition, although not currently an element of the Proposal, we would not support a revised proposal requiring incremental disclosures that are solely intended to reconcile US GAAP to IFRS as it would burden preparers with the application of two separate accounting standards.

**Specific Comments**

Our specific comments related to the Exposure Draft are expressed below.

*Exposure Draft is not Consistent with the IASB Proposal*

Cisco fully supports the convergence efforts between the FASB and IASB. As a large multinational company, we are concerned by the disparate proposed standards from the two Boards related to this topic. We are required to file our consolidated results in accordance with U.S. GAAP and have hundreds of international entities that are or will be required to file statutory reports under IFRS. Thus by default we will be required to adopt both standards and therefore we will experience increasing costs and complexity of implementation. We expect this will be a significant cost to most multinational companies.

More extensive outreach activities with a variety of user, preparer and auditor audiences should be performed to better understand the practical impacts, costs, and potential alternatives. At the end of these efforts, we would expect to see a converged viewpoint that then can be re-exposed for final approval. This approach may delay the issuance of the final standard, but would be in the best interest of users, preparers, and auditors.

**Scope**

For trade receivables, the underlying business model and the nature of credit risk are fundamentally different than other business activities, such as investing and financing, and consequently the related credit risk management processes differ. As noted above, most of our accounts receivable balances are due within 30 days. Therefore, adapting the existing model to include forward-looking information would add little, if any, value. If there were a potential credit risk identified, our existing methods would contemplate the ECL. In other words, we do not believe that given the Proposal, we would see a significant change to our financial statements. The most significant change is that operationally, we would need to comply with incremental disclosure requirements for risks that are already appropriately captured and communicated in existing disclosures. As such, we do not believe the cost to change from the current method of determining the
allowance for doubtful accounts outweighs the benefit of applying a new model, nor do we believe that the results that are derived under the new model are fundamentally more useful to the user of a company's financial statements. Therefore, we recommend excluding short-term receivables from the scope of the Proposal.

Individual debt securities have unique attributes and characteristics requiring those securities to be evaluated individually by preparers, investment analysts and rating agencies. As a result, we do not expect the Proposal to change how most preparers evaluate debt securities for impairment (i.e., on an individual basis). For high-quality, investment grade securities, which by definition have an extremely low probability of credit loss, application of a new model should not trigger the recognition of up-front credit losses. As such, we specifically encourage the Board to further consider the relevance, operational impact and implementation effort that an ECL model will have for debt securities that are highly liquid, high credit-quality securities, including highly-rated government issued and government-guaranteed obligations and certain other high credit-quality securities. Even for investments with lower credit quality, the up-front recognition of ECL does not properly consider the decreased exposure that results from dynamic management of the investment portfolio.

Rather than offering the proposed practical expedient that does not actually minimize the operational burden for preparers, we strongly suggest maintaining the existing impairment model for debt securities, which already provides an appropriate treatment for these securities.

Recognition and Measurement
The Board refers to impairment, which is reflected as an allowance for ECL, as the current estimate of contractual cash flows not expected to be collected on financial assets held at the reporting date. As the Board is aware, although certain contractual cash flows may not be expected at inception, an economic loss does not arise unless credit risk changes after inception.

To reflect the expected shortfall in contractual cash flows from an accounting perspective, the Board decided the most appropriate methodology should be to record the present value of this amount up-front through recognition of a credit loss. Although we do support timely recognition of credit losses, we do not support immediate recognition of ECL. The proposed approach results in significant recognition of losses that are not economic losses, which requires increased estimation and subjectivity, and obscures the true operating results. The proposed approach may also provide an avenue for earnings management. For example, under the Proposal, we would record a credit loss at the time of purchase of a financial instrument that is not driven by an economic event. Subsequently, if we sold that same financial instrument in a different reporting period, we may record a gain even though the credit risk has not changed since the date of purchase. This
gain represents a recovery of the initial credit loss rather than an indication of credit risk movement. An appropriate model should only reflect changes in credit risk and should support a rational method of credit loss recognition. Therefore, we recommend retaining the existing models and request the Boards to explore a lower threshold with enhanced guidance within the framework of the incurred loss model.

Disclosures
We believe that clear, concise and transparent presentation and disclosures are vital in order to achieve high quality financial reporting. Additionally, we believe the purpose of the financial statements is to provide a "snap shot" view of a company's consolidated financial performance and financial position. As such, the proposed inclusion of non-economic losses will likely create more confusion rather than additional insight.

We also believe the purpose of disclosures should be to clarify and provide more details regarding the information on the face of the financial statements, especially those areas where there is heightened financial risk. On the other hand, we are concerned that certain information needed for the proposed incremental disclosures will not be readily available and will require significant cost and effort to build systems to provide data that has limited benefit to the users of the financial statements. For investment grade securities and trade receivables in particular, incremental disclosures requiring roll-forwards and disaggregation of data does not seem consistent with the Board's intention to improve the overall value of disclosures.

Transition and Effective Date
We believe that most of the proposed changes under the proposed guidance would be operationally feasible but would require significant transition time to update systems and processes. We urge the Boards to continue to focus on operational and implementation issues prior to the issuance of a final standard.

However, if the Boards continue to diverge in their opinions and issue final standards that are not converged, we will have additional difficulties applying these changes. As noted earlier in our letter, we are required to not only file our financial statements in accordance with U.S. GAAP on a consolidated basis, but also file local statutory financial statements in accordance with IFRS.

We ask that the Board consider the implementation timeline for this proposed guidance in connection with the Exposure Draft of the Proposed Accounting Standards Update, Financial Instruments - Overall Recognition and Measurement of Financial Assets and Financial Liabilities Credit Losses (Subtopic 825-10) and other significant convergence projects where Exposure Drafts have been issued or are forthcoming. The Exposure Drafts issued thus far will require significant updates to accounting systems, processes and related controls and it is questionable that these
changes will provide our financial statement users with a significant incremental benefit.

We thank the Board for the opportunity to provide our comments on this Exposure Draft. If you have any questions regarding our letter or would like to discuss our views in further detail, please feel free to contact me at (408) 526-7815 or Roger at (408) 525-2225.

Sincerely,

Prat Bhatt
SVP, Corporate Controller &
Chief Accounting Officer
Cisco Systems, Inc.

Roger Biscay
VP, Treasury and Risk Management
Cisco Systems, Inc.