May 2, 2011

Ms. Leslie F. Seidman  
Chairman  
Financial Accounting Standards Board  
401 Merritt 7  
P.O.Box 5116  
Norwalk, Connecticut 06856-5116

Sir David Tweedie  
Chairman  
International Accounting Standards Board  
30 Cannon Street  
London, EC4M 6XH  
United Kingdom

Re:  Proposed Accounting Standards Update, Balance Sheet (Topic 210): Offsetting (File Reference No. 2011-100) and Exposure Draft, Offsetting (File Reference ED/2011/1)

Dear Ms. Seidman and Sir David:

We appreciate the opportunity to comment on the Proposed Accounting Standards Update, Balance Sheet (Topic 210): Offsetting and the Exposure Draft, Offsetting (together the Proposed Update). Bank of America Corporation (BAC) provides a diverse range of banking and non-banking financial services and products domestically and internationally. We are the largest bank in the U.S. in terms of total assets, and we routinely enter into derivatives and repurchase agreements to meet client needs and for internal risk management and financing purposes. The Proposed Update, if finalized in its current form, will result in a near doubling of the assets and liabilities reported in our statement of financial position. Accordingly, we are very focused on the efforts of the Financial Accounting Standards Board (the FASB) along with the International Accounting Standards Board (the IASB or together with the FASB, the Boards) to amend the guidance on offsetting.

We acknowledge the Boards’ efforts to develop a joint proposal to converge the requirements for offsetting, and we share the Boards’ goal of providing users of financial statements with meaningful financial information and disclosure. However, we strongly disagree with key aspects of the Proposed Update because we believe that the requirements will result in the presentation of financial information that does not provide users of financial statements with relevant information about the liquidity and solvency risk or credit exposure of the reporting entity. We believe that a net by counterparty derivative presentation generally provides more relevant information about credit exposure and solvency because the positions would be netted in the event of a counterparty default. In addition, we believe that the net position provides more relevant information about cash flows and liquidity because the current cash flows generally relate to collateral requirements, which are calculated based on the net exposure to counterparties.

We acknowledge that existing differences in the offsetting requirements in International Financial Reporting Standards (IFRS) and U.S. generally accepted accounting principles (U.S. GAAP) result in
significant quantitative differences in the statement of financial position of the preparers under their respective frameworks. Accordingly, convergence of offsetting standards would improve the comparability of such financial statements. However, we believe that the general principles set forth by the Boards to achieve such convergence sacrifice relevance for a theoretically pure argument that as a rule assets and liabilities should be reported gross. For example, an entity does not have credit exposure equal to the amount of its gross derivative assets, nor does an entity have liquidity risk equal to the amount of its gross derivative liabilities. These gross balances do not reflect the impact of widely used credit and liquidity risk management tools such as collateral requirements and master netting arrangements (MNAs). In addition, we are concerned that the resulting reporting of extremely large derivative balances will reduce the visibility of more critical assets and liabilities, which could appear insignificant by comparison.

We are concerned that the Boards have not demonstrated the appropriate level of consideration as to the cost/benefit of the Proposed Update, particularly with regard to the expanded disclosures. Further, we believe that the Proposed Update is at odds with the Boards’ shared goal of better aligning the accounting treatment and presentation with the risk management strategies of the reporting entity.

We are most concerned with the treatment of derivative instruments and secured financing arrangements. Specifically:

Derivative instruments – In the Basis for Conclusion in paragraph 10, the Boards conclude that a primary reason for the offsetting criteria to require the unconditional intent to net settle, which is unlikely to be met for most derivatives, is that the resulting gross information provides decision-useful information about the entity’s ability to generate cash and about an entity’s liquidity and solvency. We do not agree with these conclusions. It is clear that netting by counterparty provides more relevant information about exposure to counterparty credit. However, we also believe that the net position provides better information about cash flows and liquidity. Derivative instruments are carried at fair value on the balance sheet and that fair value is largely a measure of the markets at a point in time. In addition, many derivatives (e.g., interest rate and currency swaps) require two-directional cash flows throughout the life of the instrument; therefore the gross value of a single instrument does not necessarily provide information about that instrument’s cash flow requirements. As such, the gross carrying value does not bear a direct relationship to the actual cash flows of the entity. Instead, the net position, which is the basis for the required collateral cash flows, provides more information about the actual cash flows of the entity. Further, we do not agree that the gross positions provide insight into the liquidity or solvency of the entity. Instead, we would argue that the net positions, which reflect the application of the MNA netting requirements and the seniority in bankruptcy afforded these positions, provide better insight into both the liquidity and solvency of the entity. We believe that when taking into consideration the combination of the counterparty MNAs under which derivatives are transacted, collateral requirements, and the ranking in bankruptcy of these instruments, the net position more clearly represents the counterparty credit exposure, the future cash flow requirements, and the liquidity and solvency of the reporting entity (additional detail is provided in Appendix A).

Secured financing arrangements- We believe that the proposed simultaneous settlement requirement for offsetting secured financing arrangements (e.g., repurchase agreements) is too restrictive and is substantially less flexible than the existing requirements established in both U.S. GAAP and, in practice, in IFRS. We support the current view in U.S. GAAP\(^1\) whereby settlement of positions on the same day is considered the “functional equivalent of net settlement” as long as stringent conditions have been met.

\(^1\) FASB Interpretations No.41: Basis for Conclusions, paragraph 9
It is our view that the criteria established in the Proposed Update are too strict and would result in economically identical positions being accounted for differently simply because of the settlement mechanism.

We believe that the existing requirements for offsetting in U.S. GAAP provide a superior framework for reporting. These requirements provide meaningful, well understood and comprehensive information in the statement of financial position, and, supported by the required disclosures, meet the primary requirements of users of financial statements. In addition, the current presentation reflects the way that preparers manage risk exposure, particularly for derivative instruments. We believe that this framework, with additional disclosures as required (e.g., currently entities are not required to disclose the amount of counterparty netting for repurchase agreements, which we believe may be warranted) will meet the needs of users, preparers and the market, and provide an opportunity for IFRS reporters to converge with existing U.S. GAAP.

Although we urge the Boards to support the current U.S. GAAP because we believe that this would provide the most relevant information to users, if the Boards cannot support the current U.S. GAAP offsetting requirements we recommend that the Boards consider a more practical and relevant approach than the Proposed Update by introducing a practical expedient for derivatives and secured financing transactions that are cleared through established clearing houses. As explained in more detail in Appendix A, clearing house requirements and procedures are specifically designed to mitigate credit risk, and we believe that their collateral posting requirements are economically akin to the daily settlement of outstanding positions, thereby mitigating the liquidity concerns cited by the Boards.

Alternatively, if the Boards believe that gross balances must be presented on the statement of financial position, we request that the Boards consider a linked presentation whereby gross assets and liabilities, less a deduction for amounts currently offset in accordance with existing U.S. GAAP, and the resulting net balances would be reported on the statement of financial position within total assets and total liabilities, respectively. We believe that this treatment would provide users with more relevant information and is supportable, especially for derivatives, given the special treatment that is afforded these instruments in bankruptcy. We believe that this would represent a compromise that would meet the needs of all financial statement users.

In summary, we urge both the FASB and the IASB to reconsider the Proposed Update. We believe that the Proposed Update sacrifices relevance in favor of the theoretical principle that assets and liabilities should not be netted. We recommend that the Boards issue guidance that converges to current U.S. GAAP and, if this is not possible, encourage the Boards to consider one of the alternatives described above, which we believe will better meet the needs of both users and preparers of financial statements.

See Appendix A for our responses to certain questions presented by the Boards.

*   *   *
We appreciate the opportunity to express our views in this letter. Should you have any questions, please feel free to contact Randall Shearer (980.388.8433) or me (980.387.4997).

Sincerely,

John M. James  
Senior Vice President and  
Corporate Controller

cc: Charles H. Noski, Chief Financial Officer  
Neil A. Cotty, Chief Accounting Officer  
Randall J. Shearer, Accounting Policy Executive
Appendix A

The following are our responses to certain of the questions presented by the Boards:

<table>
<thead>
<tr>
<th>Question 1: Offsetting criteria: unconditional right and intention to settle net or simultaneously</th>
</tr>
</thead>
<tbody>
<tr>
<td>The proposals would require an entity to offset a recognised financial asset and a recognised financial liability when the entity has an unconditional and legally enforceable right to set off the financial asset and financial liability and intends either:</td>
</tr>
<tr>
<td>(a) to settle the financial asset and financial liability on a net basis or</td>
</tr>
<tr>
<td>(b) to realise the financial asset and settle the financial liability simultaneously.</td>
</tr>
</tbody>
</table>

Do you agree with this proposed requirement? If not, why? What criteria would you propose instead, and why?

<table>
<thead>
<tr>
<th>Question 2: Unconditional right of set-off must be enforceable in all circumstances</th>
</tr>
</thead>
<tbody>
<tr>
<td>It is proposed that financial assets and financial liabilities must be offset if, and only if, they are subject to an unconditional and legally enforceable right of set-off. The proposals specify that an unconditional and legally enforceable right of set-off is enforceable in all circumstances (i.e., it is enforceable in the normal course of business and on the default, insolvency or bankruptcy of a counterparty) and its exercisability is not contingent on a future event. Do you agree with this proposed requirement? If not, why? What would you propose instead, and why?</td>
</tr>
</tbody>
</table>

No. We do not agree that the proposed principle for offsetting financial assets and financial liabilities is the appropriate basis for reporting in the statement of financial position.

As preparers and users of financial statements, we believe that the presentation of assets and liabilities should correspond with the risk management profile of the reporting entity. We also believe that the current provisions for offsetting under U.S. GAAP\(^2\) appropriately reflect the credit risk and liquidity exposure of the reporting entity. In most instances, the Proposed Update as currently drafted is expected to result in the reporting of gross balances. We believe that this will reduce transparency and may even be misleading. We therefore recommend that the current guidance under U.S. GAAP, whereby derivatives are generally reported net by counterparty on the statement of financial position and gross in granular detail in the notes to the financial statements, be adopted for the converged standard. Below we have outlined concerns for specific areas affected by the Proposed Update.

**Derivative instruments**

We do not believe that the proposed guidance, which requires the unconditional right in order to offset, adequately addresses the unique features of derivative instruments. In particular, collateral requirements and master netting agreements are routinely used to mitigate risks arising from derivatives.

---

\(^2\) ASC 210-20-45
Appendix A

- Collateral requirements significantly mitigate credit risk and liquidity risk associated with derivative assets. Most derivatives require some level of cash collateral (or other liquid instruments), and many derivatives, including those cleared through clearing houses, are required to be fully collateralized through daily margining on a net basis by counterparty. We believe that these collateral arrangements mitigate both credit risk, protecting the net fair value exposure against counterparty default and liquidity risk, by requiring cash flows for the net fair value exposure on a daily basis.

Although we believe that this holds true for both over-the-counter derivatives and derivatives cleared through clearing houses, transactions with clearing houses have very specific and routine collateral requirements that are designed to mitigate credit and liquidity risk. These collateral arrangements are becoming more standardized as governments, in response to the credit crisis, encourage derivatives dealers to use clearing houses for common derivatives. Clearing houses require their participants to post variation margin, which is the single net collateral amount that is payable to/from each member bank. This amount is calculated daily based on the mark-to-market of all the positions that the member has with the clearing house. If the member is in a net liability position, the member posts collateral, which in most cases, is ultimately used to settle the net position. If the member is in a net receivable position, the member will receive a net cash payment from the clearing house, taken from variation margin posted by other members. Therefore, we believe that in substance the payment/receipt of the variation margin is used to settle, in cash, the net open position that a member has with the clearing house.

- MNAs that are effective upon the default, insolvency or bankruptcy of the counterparty also provide significant credit risk mitigation. Industry has found, through actual recent examples, that in jurisdictions where these arrangements are considered legally enforceable, they have been applied in bankruptcy. MNAs effectively consolidate individual contracts into a single agreement at that point in time when the counterparty’s ability to settle its obligations is most in doubt. The availability of such arrangements is an essential component of the risk management process of derivative dealers. We believe that the failure to reflect this factor in the statement of financial position, given the potential magnitude of the numbers involved, will result in an overstatement of an entity’s credit risk exposure. In addition, gross presentation will exaggerate the true liquidity needs and therefore the perceived riskiness of the reporting entity.

In our opinion, failure to reflect these powerful risk mitigants in the primary financial statements would represent a fundamental flaw in the standard.

---

3 Participants are also required to post “initial margin” to ensure that intraday movements on a member’s positions between the last payment of variation margin and the next payment are secured. Initial margin is returned to the participant when and if a clearing arrangement is terminated.
Appendix A

Paragraph 5 indicates that a primary reason that the Boards determined that netting should only be permitted when the entity has the intent to net is a belief that the resulting gross presentation, which would be applicable to most derivative instruments, would provide useful information for assessing “the entity’s ability to generate cash in the future” and “the entity’s liquidity and solvency”. We disagree with this conclusion. Specifically:

- **Ability to generate cash** – We do not agree with the assertion that the proposed presentation will provide better information about an entity’s ability to generate cash. Derivative instruments are reported at fair value, which is a representation of the current market view of future events that will impact future cash flows. In addition, many derivatives (e.g., interest rate and currency swaps) require two-directional cash flows throughout the life of the instrument; therefore the gross value of a single instrument does not necessarily provide information about that instrument’s cash flow requirements. Therefore, given the nature of derivative instruments, the gross fair value does not typically bear a direct relationship to the eventual cash flows realized. In contrast, collateral arrangements (including the variation margin practices described above), which are based on the positions netted in accordance with counterparty MNAs, result in actual outlays of cash or other liquid instruments (which can be readily converted to cash). Therefore, the immediate cash flow requirements for derivatives are more closely aligned with the net position than the gross position. As a result, in our view, net balances actually provide better insight into an entity’s ability to generate cash flows from derivative assets.

- **Liquidity and solvency** – We do not believe that the proposed presentation will provide better insight into a reporting entity’s liquidity and solvency. On the contrary, we believe that the gross presentation would misrepresent the reporting entity’s actual financial position at the reporting date because total assets and liabilities on the statement of financial position would fail to reflect the impact of collateral agreements and MNAs. The proposed presentation also ignores market practices whereby dealers in derivative instruments regularly close out derivative transactions by entering into an offsetting transaction rather than by terminating the original contract. Under the Proposed Update these instruments would likely be reported on a gross basis, thereby giving the erroneous impression that market and liquidity risks of the original contract have not been eliminated. In addition, from a legal perspective, derivative contracts transacted under MNAs are considered part of a single agreement. Typically, MNAs are enforceable in bankruptcy with individual transactions settled as one position that ranks senior to the general creditors of the bankrupt entity. As such, gross presentation of these transactions overstates the true liquidity exposure of the reporting entity.

Under the Proposed Update there is a significant risk that analysts, regulators and other users of financial statements may be led to believe that the reporting entity carries more risk and is more leveraged than is actually the case. However, if the Boards disagree with our position and adopt the criteria for offsetting as set forth in the Proposed Update, we urge the Boards to develop a practical expedient that permits offsetting when derivative dealers transact through clearing houses, as these institutions are designed to mitigate credit and liquidity risk for derivative dealers. In our view, this type of practical expedient would result in more meaningful reporting and would have the added benefit of encouraging entities to maximize the volume and type of transactions being cleared through such organizations in accordance with the aims of both governments and regulators.
Secured borrowings

For secured borrowing arrangements like repurchase agreements, we specifically object to the simultaneous settlement guidance where simultaneous is defined to be “at the same moment”. We believe that this is too strict, especially because it does not consider the practical operation of the various clearing houses. We believe that the U.S. GAAP approach whereby stringent criteria have been established that, if met, are considered to be the functional equivalent of net settlement results in a better understanding of the cash flow position as well as the credit risk position of the reporting entity because the requirements permit offsetting where transactions settle on the same day, that is, the net position would reflect the daily cash flow requirement. Similarly, we believe that a more substance based approach would be achieved by adopting the existing interpretation of the in IAS 32, paragraph 48 where it is noted that “simultaneous settlement of two financial instruments may occur through, for example, the operation of a clearing house in an organized financial market or face-to-face exchange. In these circumstances the cash flows are, in effect, equivalent to a single net amount and there is no exposure to credit or liquidity risk.”

It is our understanding that, for centrally cleared, bilateral repurchase agreements clearing houses cannot perform instantaneous settlement given the volume of daily activity. Instead, clearing houses typically settle transactions through a combination of batch settlements and real time cash flows. It is impossible for a reporting entity to know which individual transactions will be settled when because this is at the sole discretion of the clearing house. This is an issue under the Proposed Update since netting is required where settlement is simultaneous. Thus, a reporting entity would not be able to comply with the requirement to net as it would not be able to identify how individual transactions are settled. More importantly, from an economic perspective this settlement process, while not at the same moment, is substantively the same as simultaneous settlement by virtue of the credit and liquidity arrangements in effect at the clearing houses. Given the above, we believe that it is inappropriate to differentiate and apply offsetting only where there are actual net cash flows. In light of this, we request that the Boards reconsider the prohibitively narrow interpretation of “simultaneous settlement” to accommodate these types of processes.

We also believe that the simultaneous settlement requirement is too strict when considering bilateral securities financing arrangements between counterparties. We believe that the current requirements of ASC 210-20-45 provide reasonable guidelines for netting when, in substance, the arrangements result in the functional equivalent of net settlement. Specifically, netting is currently permissible in instances where cash flows would occur on the same day, providing that there are associated banking arrangements that provide sufficient daylight overdraft or other intraday credit facilities to enable net settlement by either party. We consider that permitting netting in the above circumstances is appropriate and consistent with the commercial and economic effect of such arrangements.

Given the above facts and circumstances, we urge the Boards to reconsider the Proposed Update to ensure that the information included within the statement of financial position is consistent with existing U.S. GAAP requirements, supported by additional disclosure as necessary.
Question 4: Disclosures
Do you agree with the proposed disclosure requirements in paragraphs 11–15? If not, why? How would you propose to amend those requirements, and why?

As currently drafted the disclosures required in the Proposed Update are anticipated to be operationally intensive. They will require systems that can identify, collate, report and control information about netting arrangements for all financial assets and liabilities. It is important to note that this data is not housed in a single system and therefore this process is likely to be manually intensive. Further, significant disclosure requirements are already in place in both U.S. GAAP and IFRS, particularly with respect to derivative instruments; their nature, cash flows and related risk exposures. Therefore, we urge the Boards to consider the necessity of the additional disclosure requirements, in light of the existing extensive disclosures that are currently provided, to evaluate whether the existing disclosures requirements could be enhanced rather than requiring extensive additional disclosures and tables.

In relation to the specific disclosure requirements we have the following comments:

- The Proposed Update, specifically paragraph 12(d), requires the disclosure of the amount of financial assets and financial liabilities that the reporting entity has a conditional right to set off. Under this guidance, the reporting entity will be required to disclose all arrangements that allow for contingent offsetting, such as default, for all financial assets and liabilities. Assuming that the Proposed Update is finalized in its current form, the disclosure of this information would be essential for derivatives because the master netting arrangements and collateral arrangements are fundamental to the risk management of these instruments. However, it is not clear that detailed netting information will be relevant for other assets and liabilities, (e.g., for cash instruments including loans). Under current disclosure requirements, extensive collateral information is required for loans and secured borrowing arrangements and qualitative disclosure about the availability of offsetting in default is typically provided. We believe that the additional quantitative requirements will be burdensome and add little value for most assets and liabilities. Further, we believe that there are already sufficient credit disclosures for cash instruments. Therefore, we urge the Boards to reconsider the necessity of this disclosure for all instruments and instead require quantitative the disclosures only for derivatives.

- Paragraph 12(b)(ii) of the Proposed Update would require that any portfolio-level credit adjustments to assets and liabilities measured at fair value be separately disclosed in the table to reflect the effect of the entity’s net exposure to the credit risk of the counterparties or the counterparties’ net exposure to the credit risk of the entity. We do not consider it appropriate to separately disclose this information in this table given that these adjustments are part of the measurement of the assets and liabilities and therefore, should instead be provided with other fair value measurement related disclosures. Additionally, because this information is calculated on a net by counterparty basis, it would be difficult to allocate the value by class of financial instrument on anything other than an arbitrary basis and would therefore result in largely meaningless information.

- Paragraph 12(c) requires disclosure of those financial assets and financial liabilities that the reporting entity has the unconditional and legally enforceable right, but not the intent to net
settle/settle simultaneously. Identifying these transactions will be particularly challenging and may be construed as a requirement to identify an inadvertent right of offset, which is inconsistent with the guidance in paragraph C10 of the Proposed Update. If, as is indicated in paragraph C9 of the Proposed Update, individual payments for financial assets and financial liabilities meet the requirements for this disclosure (e.g., due to the fact that they meet the unconditional and legally enforceable requirements but there is no intent to net settle/settle simultaneously), the identification and reporting of such information would require extensive system and operational changes. Further, it is not clear that this disclosure would be of any value to the users of financial statements.

We urge the Boards to reconsider the disclosure requirements to avoid excessive non-essential disclosure.

**Question 5: Effective date and transition**

a) Do you agree with the proposed transition requirements in Appendix A? If not, why? How would you propose to amend those requirements, and why?
b) Please provide an estimate of how long an entity would reasonably require to implement the proposed requirements.

If the Boards vote to proceed with the Proposed Update as currently drafted, it is critically important that they recognize the magnitude of change that the proposal will have on U.S. GAAP reporters. These reporters, including BAC, will need time to educate users of financial statements, including regulators, analysts, lenders and taxing authorities (where taxes are calculated, in part, based on the U.S. GAAP financial statements), and to allow those parties to respond.

Specifically, the Proposed Update will have a considerable impact on the leverage ratio for U.S. banks. Under the U.S. bank regulatory framework, U.S. banks are required to maintain certain leverage ratios in order to be considered adequately capitalized. Under the current framework, this ratio is tier 1 equity divided by quarterly U.S. GAAP based average assets (adjusted for equity deductions listed in footnote 4). For banks that have significant derivative trading operations, the increase in the U.S. GAAP asset balances arising from these proposals could result in banks no longer being in compliance with regulatory guidelines. Further, because derivative balances are highly volatile, banks could swing in and out of compliance simply as a result of market movements that do not expose the firm to solvency or liquidity risk. If the proposal is finalized as currently drafted, it is imperative that regulated entities have sufficient time to engage and work with the regulatory authorities to address the resulting changes.

Furthermore, if the current operational framework of clearing houses is not considered sufficient to achieve balance sheet netting in light of the stringent requirements of the Proposed Update, it is important that the Boards allow adequate time for firms to work with the clearing houses to evaluate and develop compliant solutions.

---

4 Tier 1 capital includes qualifying common shareholders’ equity, qualifying nonecumulative perpetual preferred stock, qualifying Trust Securities, hybrid securities and qualifying non-controlling interests, less goodwill and other adjustments.
Appendix A

Finally, the expanded disclosure requirements will require significant changes to systems and processes in order to identify, collate and report such sizeable volumes of data.

Based on the above, we would reasonably estimate that in order to implement the Proposed Update no less than a two year transition period, with an additional year for each year that is required to be presented on a retrospective basis, would be warranted. We would also recommend that the Boards consider the effective date and transition for the Proposed Update to be part of the wider deliberations for the project on effective dates and transition methods.
Other Concerns
In addition to the comments in the covering letter and Appendix A, we have additional concerns about the proposed guidance. These concerns are reflected below:

Unsettled regular way trades

In accordance with existing U.S. GAAP industry guidance, specifically the broker/dealer guide (ASC 940-320-45-30), receivables and payables for unsettled regular way transactions are permitted to be presented net. The proposed guidance would preclude this netting. It should be noted that unwinding this netting to facilitate gross presentation presents significant operational challenges because often systems and processes are designed to record the position net or in the same account. If this change in the guidance is considered to be essential, an appropriate implementation timeframe must be provided so that the necessary systems changes can be made.

Settlement

As noted in Appendix A question 1, we disagree with the broad concept that variation margin is a form of collateral that is include in paragraph C14 of the Proposed Update because we believe that, in many cases, daily margining requirements for derivatives are substantially the same as settlement from both a liquidity and a credit perspective. That being said, we are also concerned with the unequivocal statement that margin accounts are a form of collateral. We do not believe that this is the case in, for example, the futures market where trades settle daily through the variation margin process. Thus, if the Boards decide to finalize the Proposed Update as currently drafted, we urge the Boards to remove the language that concludes that all variation margin is collateral so that reporting entities will be able to make distinctions between clearing houses and exchanges based on specific facts and circumstances.