October 4, 2019

Mr. Shayne Kuhaneck
Acting Technical Director
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116


Dear Mr. Kuhaneck:

The 11 Federal Home Loan Banks (the “FHLBanks”) appreciate the opportunity to comment on the Financial Accounting Standards Board’s (the “FASB” or “Board”) Exposure Draft of a Proposed Accounting Standards Update (“ASU”), Reference Rate Reform (Topic 848): Facilitation of the Effects of Reference Rate Reform on Financial Reporting (hereinafter referred to as the “proposed update”). The FHLBanks are supportive of the provisions contained in the proposed update to ease the potential burden in accounting for reference rate reform on financial reporting. Also, outlined below is one additional issue related to reference rate reform that we believe the Board should consider.

Question 2—Additional Issues: Are there additional accounting issues or optional expedients related to reference rate reform that the Board should consider? Please be as specific as possible and explain why those issues require consideration.

Yes. The FHLBanks believe that the Board should explore temporary transition guidance that would allow for the sale or reclassification of London Inter-Bank Offered Rate (“LIBOR”) -indexed securities (including asset-backed securities supported by LIBOR-indexed loans) that were classified as held-to-maturity (“HTM”) prior to the announcement of the end of LIBOR. The subsequent announcement that panel banks will likely not support LIBOR after 2021 has a significant impact on the financial markets, impacting countless contracts and financial instruments, including investment securities that we have classified as HTM. As a result of these circumstances, there are significant interest rate related risks and concerns related to holding certain HTM securities during the intervening period between the July 2017 announcement of the end of LIBOR and the actual end of LIBOR (the “LIBOR transition period”).
The first potential issue that is a cause for concern is the interest rate fallback language in each investment security contract for those securities that are indexed to LIBOR. This fallback language will likely fundamentally change the nature of these investment securities. For example, there are concerns about fallback language for those contracts which 1) state that if no LIBOR rate is published, the security would use the last published rate of LIBOR (essentially turning the floating rate security into a fixed rate security), 2) are silent on what would happen if no LIBOR rate is published, or 3) state that a replacement index will be used. All of these scenarios will lead to additional interest-rate risk given the evolving interpretations and uncertainty surrounding the replacement of LIBOR.

The language, or absence of language, in these contracts could unintentionally fundamentally change the securities’ expected behavior or could result in protracted litigation or adverse outcomes as these uncertainties are eventually concluded.

A second issue of concern during this transitional period is the possibility that LIBOR may become an unreliable market indicator as market participants migrate away from LIBOR-indexed transactions to alternative indices (for example, the Secured Overnight Financing Rate) during the LIBOR transition period, even if LIBOR continues to be published during this time period. In this scenario, should it occur, LIBOR-indexed securities will continue to adjust to a rate of return that is not indicative of true market rates. Continuing to hold these securities during the LIBOR transition period under the noted environment presents interest-rate risk that did not exist prior to the announced discontinuance of LIBOR.

The outcomes based on the interest rate fallback language (or absence thereof) in each investment security contract may impact risk management strategies in ways which were previously unforeseeable. This may necessitate that entities re-evaluate their intent or strategies to mitigate the additional interest-rate risk generated by the announced and/or actual end of LIBOR. For example, an entity may want to either sell the securities or utilize derivatives to manage or mitigate the additional interest rate risk (for example, if a floating rate security becomes fixed), to continue to meet its risk management strategies. If derivatives are used to hedge investment securities, hedge accounting may be applied only if the securities are classified as available-for-sale (“AFS”).

The FHLBanks are aware of the guidance in ASC 320-10-25-6 through ASC 320-10-25-9 that outlines the criteria and conditions in which certain events may cause an entity to sell or transfer a HTM security without necessarily calling into question (tainting) its intent to hold other debt securities to maturity. ASC 320-10-25-9 further states:

"In addition to the changes in circumstances listed in paragraph 320-10-25-6(a) through (f), certain other events may cause the entity to sell or transfer a held-to-maturity security without necessarily calling into question (tainting) its intent to hold other debt securities to maturity. Such events must meet all of the following four conditions to avoid tainting its intent to hold other debt securities to maturity in the future:"
a. The event is isolated.
b. The event is nonrecurring.
c. The event is unusual for the reporting entity.
d. The event could not have been reasonably anticipated."

Furthermore, the FHLBanks are aware of the background information and basis for conclusions in Statement of Financial Accounting Standards No. 115, *Accounting for Certain Investments in Debt and Equity Securities*, (paragraph 62) which notes that the Board believes that an enterprise’s decision to classify a security as HTM implies that during the term of the security the enterprise’s decisions about continuing to hold that security will not be affected by changes in market interest rates, and that the decision is consistent with the view that a change in fair value is not relevant for a security that will be held to maturity. However, we do not believe that the announced end of LIBOR and its ensuing effects on market rates and contract terms is analogous to a “normal” change in market interest rates.

Based on the conditions outlined in the guidance above, we believe the announced end of LIBOR could qualify as a justifiable reason to sell or transfer HTM securities that are indexed to LIBOR without tainting our intent to hold other debt securities to maturity because the event is isolated, nonrecurring, unusual, and could not have been reasonably anticipated when the securities were purchased. However, the FHLBanks believe that the Board should directly address this issue within the final ASU on *Reference Rate Reform* to alleviate any potential inconsistency in interpretation and application of accounting principles and to provide clear guidance to both auditors and financial statement preparers.

Due to the factors outlined above, the FHLBanks believe that there should be transition guidance that provides flexibility to allow for the sale or reclassification of HTM LIBOR-indexed securities that were designated as HTM prior to the announcement of the end of LIBOR. As the proposed ASU guidance is temporary, the FHLBanks believe that entities should have the ability to sell or reclassify such securities at any time between the effective date of the final ASU and the earlier of the actual discontinuation of the applicable LIBOR index or the end date of the temporary ASU guidance.

We thank the Board for its consideration of our views and welcome the opportunity to discuss this matter with the Board and its staff. Please do not hesitate to contact me at (317) 465-0350.

Sincerely,

K. Lowell Short
Chair of the Federal Home Loan Banks Controllers’ Committee
Senior Vice President - Chief Accounting Officer
Federal Home Loan Bank of Indianapolis