October 7, 2019

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

RE: Proposed Accounting Standards Update, Reference Rate Reform (Topic 848), Facilitation of the Effects of Reference Rate Reform on Financial Reporting (File Reference No. 2019-770)

Dear Mr. Kuhaneck:

We appreciate the opportunity to comment on the proposed ASU, Reference Rate Reform (Topic 848) – Facilitation of the Effects of Reference Rate Reform on Financial Reporting.

We support the Board’s efforts to respond to stakeholder concerns about accounting for contract modifications and changes in hedge accounting due to reference rate reform. We believe the proposals would address those concerns and assist in easing the burden in accounting for reference rate reform.

The Appendix provides our responses to the questions in the proposed ASU. As part of those responses, we included some specific recommendations for the Board to consider.

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If you have questions about our comments or wish to discuss the matters addressed in this comment letter, please contact Kimber Bascom at (212) 909-5664 or kbascom@kpmg.com or Mark Northan at (212) 954-6927 or mnorthan@kpmg.com.

Sincerely,

KPMG LLP

KPMG LLP
Appendix – Responses to Questions for Respondents

General Questions

Question 1: Costs and Complexities: Are the amendments in this proposed Update operable and auditable? If not, which proposed amendment(s) pose operability or auditability issues and why?

Yes, we believe the proposed guidance generally is operable and auditable. The proposed guidance in paragraph 848-20-15-6 suggests an entity is required to assess whether a contract modification is due to a new underwriting or business decision in order to determine whether the modification is within the scope of the guidance. Conversely, the proposed guidance in paragraphs 848-20-15-2 and 15-3 suggests that an entity is only required to assess whether a change to contractual terms is related or unrelated to the replacement of a reference rate. Determining whether a contract modification is made as a result of a new underwriting or business decision would require insight into the lender’s reasons for making specific modifications, which the borrower may not be in the position to evaluate. To improve the operability and auditability of the guidance, we recommend that the Board clarify that the assessment relates solely to whether a change to contractual terms is related or unrelated to the replacement of a reference rate.

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.

We believe the Board should clarify that a modification to a fallback provision that changes a preexisting fixed fallback rate to a variable replacement rate (such as SOFR) would be considered to be related to reference rate reform, and therefore within the scope of proposed Topic 848. It is our understanding that some entities have existing fixed rate fallback provisions that would take effect if LIBOR was not published. We also understand that those provisions may have been designed with temporary disruptions of LIBOR in mind, as opposed to a permanent replacement of LIBOR with an alternative rate. It is possible that some entities with contracts for which LIBOR is the operative rate may prefer that the contract continue being based on LIBOR unless LIBOR ceases to be published. As a result, rather than replacing LIBOR as the operative rate, they may wish to modify the contract to introduce a replacement reference rate in the fallback provisions (effectively replacing a preexisting fixed fallback interest rate with a variable rate such as SOFR). The objective of this change would be to maintain a variable rate in the event that LIBOR ceases to be published.

The Board indicates in paragraph BC23 that an entity would be permitted to apply the guidance in the proposed Update when fallback provisions are modified, however it does not specifically address whether a change in fallback provisions from a fixed rate to a variable replacement rate (such as SOFR) would be permitted.

The Board indicates in paragraph BC24 that a change from a variable rate to a fixed rate would not be eligible to apply the guidance in the proposed Update because that would reflect a credit decision that is separate from reference rate reform. We believe that the intent of paragraph BC24 was to address changes in the active rate, as opposed to changes to a fallback rate. We also
believe that a change from a fixed fallback rate to a variable fallback rate is different from the scenario envisioned in paragraph BC24, because it would have the objective of keeping the active rate as a variable rate in the event that LIBOR is discontinued. For that reason, it would be reasonable to expect that no addition credit decision would need to be made when the modification takes place.

We are not aware of other accounting issues related to reference rate reform that the Board should consider, other than as addressed in this letter.

Contract Modifications

Question 3: Expedients: Do you agree with the proposed expedients for the accounting for contract modifications? If not, please explain which proposed amendment(s) you disagree with and why.

Yes. We agree with the proposed expedients for the accounting for contract modifications; however, we believe that certain aspects of the guidance should be clarified.

First, proposed paragraph 848-30-25-5 states that an entity may change the contractual terms of an existing instrument and not be required to redesignate the hedging relationship if the changes are within the scope of paragraph 848-20-15-2. The proposed ASU indicates that changes to the counterparty to the agreement are outside the scope of paragraph 848-20-15-2. However, we observe that Topic 815 indicates that a change in the counterparty to a derivative hedging instrument, in and of itself, is not a change in a critical term, and does not result in termination, of a hedging relationship.1 We recommend the Board clarify that a change in the counterparty to a derivative hedging instrument would not, in and of itself, result in the entity being ineligible to apply the optional expedient in paragraph 848-30-25-5.

Second, paragraph BC24 of the Basis for Conclusions indicates that a change from a variable to a fixed rate would not be eligible for the contract modification optional expedients. Although the proposed guidance in paragraphs 848-20-15-2 and 15-5(a) indicates that replacement with another interest rate index is related, none of the proposed Codification paragraphs specify whether a fixed rate is an eligible replacement rate. Therefore, we recommend the Board clarify within Topic 848 that replacement of the reference rate with a fixed rate is unrelated to replacement of the reference rate.

Question 4: Election Level: Do you agree that the optional expedients for contract modifications should be applied at the relevant Topic, Subtopic, or Industry Subtopic level? If not, what alternative do you suggest and why?

Yes, we agree that the optional expedients for contract modifications should be applied at the relevant Topic or the intersecting Subtopic level within the Industry Topics.

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1 See 815-20-55-56A, 815-25-40-1A, 815-30-40-1A.
Hedge Accounting

Question 5: Change in Critical Terms: Do you agree with the proposed exceptions to the requirement in Topic 815 to redesignate a hedging relationship for a change in critical terms of the hedging relationship? If not, please explain which proposed amendment(s) you disagree with and why.

Yes, we agree with the proposed exceptions.

Question 6: Fair Value Hedges: Do you agree with the proposed optional expedients for fair value hedge accounting? If not, please explain which proposed amendment(s) you disagree with and why.

Yes, we agree with the proposed optional expedients for fair value hedge accounting. However, we recommend some clarifications to the proposed option to adjust the existing basis adjustment to reflect the cumulative fair value hedge basis adjustment attributable to changing to the replacement designated benchmark interest rate.

When an entity elects to adjust the basis adjustment, the proposed guidance permits the entity to either:

— recognize the adjustment currently in earnings; or
— adjust the basis adjustment and record an offsetting entry to the carrying amount of the hedged asset or liability, and subsequently recognize the adjustment resulting from the offsetting entry in earnings in the same manner as other components of the carrying amount in accordance with the guidance in paragraphs 815-25-35-9 or 35-9A.

The objective of the second alternative is not clear because it creates offsetting entries to the same item. It is also not clear how this alternative is different from simply maintaining the hedged item’s basis adjustment immediately before the change (which is already an option permitted by the Board).

We recommend the Board not permit an entity to record an offsetting entry to the carrying amount of the same item and then choose different amortization approaches for the offsetting amounts. Doing so would permit an entity to elect to recognize gains (i.e. through amortization) while deferring losses (i.e. by not amortizing them during the hedging relationship).

Question 7: Cash Flow Hedges: Do you agree with the proposed optional expedients for cash flow hedge accounting? If not, please explain which proposed amendment(s) you disagree with and why.

Yes, we agree with the proposed optional expedients for cash flow hedging.

Question 8: Election Level: Do you agree that the proposed exceptions and optional expedients related to hedge accounting should be applied on an individual hedging relationship basis? If not, please explain why.

Yes. We believe that there may be cases where it will be most efficient to continue using existing systems and processes for some existing relationships while applying the proposed exceptions and expedients to other relationships.
**Disclosures**

**Question 9:** Contracts or Holdings: What quantitative and qualitative disclosures should be provided to help users understand a reporting entity’s current contracts or holdings (as of the reporting date) that are affected by reference rate reform? For financial statement preparers, what costs would be incurred in providing these disclosures? For financial statement users, what alternative sources of information would be used if a reporting entity does not provide any quantitative and qualitative disclosures? What costs would be incurred to obtain quantitative and qualitative information to better understand a reporting entity’s exposure to reference rate reform? Should the quantitative and qualitative disclosures, if any, have a termination date after December 31, 2022? If not, when should such disclosures expire and why?

**Question 10:** Hedge Accounting: What quantitative and qualitative disclosures should be provided to help users understand the financial reporting effects of expedients elected by a reporting entity? For financial statement preparers, what costs would be incurred in providing these disclosures? For financial statement users, what costs would be incurred if a reporting entity does not provide any quantitative and qualitative disclosures to help financial statement users understand the financial reporting effects of any hedge accounting expedients elected?

**Question 11:** Transition: Do the proposed transition disclosure requirements provide decision-useful information? If not, what would you recommend and why?

We believe financial statement users and preparers are best positioned to comment on the proposed disclosure requirement.

**Transition and Termination Date**

**Question 12:** Transition: Do you agree that the proposed optional expedients should be applied on a prospective basis upon election? If not, what alternative do you suggest and why?

Yes, we believe the proposed optional expedients should be applied on a prospective basis. We believe requiring adoption on another basis would counteract the benefits of providing optional expedients because an entity would be required to expend efforts to determine the effects of a retrospective (or modified retrospective) method.

**Question 13:** Termination Date: Do you agree that the proposed amendments should not apply to contract modifications made and hedging relationships entered into or evaluated after December 31, 2022? If not, when should the proposed amendments expire and why?

Yes. We agree that the proposed amendments should not have an indefinite life. We believe the proposed expiration date of the guidance is appropriate in view of the expectation that LIBOR will be discontinued by December 31, 2021. Further, we agree with the Board’s decision expressed in paragraphs BC9 and BC85 of the Basis for Conclusions to continue to monitor developments in the marketplace and consider whether those developments warrant changes to any final guidance, including changes to the proposed amendments’ end date.
The proposed amendments in paragraph 848-40-25-8 permit an entity that uses the shortcut method to assess effectiveness of a fair value hedging relationship to disregard certain criteria for the remaining life of the hedging relationship (rather than only through December 31, 2022). We recommend that the Board consider how to make that guidance available once Topic 848 is no longer effective.

Further, once Topic 848 is no longer effective, the proposed optional expedients that permit an entity to disregard certain mismatches between the terms of a derivative hedging instrument and a hedged forecasted transaction(s) when assessing effectiveness will no longer be available. As a result, when an entity performs its first effectiveness assessment after December 31, 2022, the entity may conclude that the relationship was not highly effective in the absence of those expedients. We recommend the Board clarify that termination of a hedging relationship in this circumstance is prospective and therefore does not affect the accounting in previous periods.