October 7, 2019

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

RE: File Reference No. 2019-770

Dear Mr. Kuhaneck:

PricewaterhouseCoopers LLP appreciates the opportunity to comment on the Proposed Accounting Standards Update, Reference Rate Reform (Topic 848), Facilitation of the Effects of Reference Rate Reform on Financial Reporting. We commend the FASB for its efforts to ease the potential burden in accounting for the effects of reference rate reform.

We generally agree with the proposed amendments. Appendix A contains our responses to the Questions for Respondents, including certain instances when we recommend additional amendments.

We recommend the Board consider establishing a resource group comprised of users, preparers, auditors, and regulators, including members of the Alternative Reference Rates Committee, to continue to potentially assist the Board in reacting to market developments related to reference rate reform.

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If you have any questions regarding our comments, please contact David Schmid at (973) 997-0768.

Sincerely,

PricewaterhouseCoopers LLP
Appendix

General Questions

Question 1—Cost 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 amendments are operable and auditable.

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, we believe the Board should consider adding explicit guidance on whether the optional expedients provided in this proposed Update could be applied to the accounting for net investment hedges under Subtopic 815-35. Reference rate reform has the potential to impact both derivatives and non-derivative instruments designated in a net investment hedge. While the Board made reference to net investment hedges in BC46, we believe more comprehensive guidance on net investment hedging should be included within Topic 848.

Additionally, reference rate reform has the potential to impact amounts excluded from a hedging relationship in accordance with paragraph 815-20-25-28. We believe the proposed Update should address how an entity should apply the guidance in paragraphs 815-20-25-83A and 815-35-35-5A when the hedging instrument is impacted by a modification related to reference rate reform. We believe this could be accomplished by establishing principles similar to the guidance related to the change in fair value of the hedged item due to a change in the designated benchmark interest rate.

We also believe the amendments in the proposed Update may not allow entities that are not public business entities (PBE) from applying the proposed Update. The proposed guidance in paragraph 848-10-65-1(b) states (emphasis added):

An entity may elect the optional expedients in Subtopics 848-30, 848-40, and 848-50 only if it has adopted the amendments in Accounting Standards Update No. 2017-12, Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities.

Currently, a non-PBE is required to adopt Update 2017-12 in fiscal years beginning after December 15, 2019. However, the Board has proposed\(^1\) to defer the effective date for non-PBEs for an additional year. Consequently, the requirement in 848-10-65-1(b) may effectively override any accommodation the Board is intending to provide non-PBEs in its project to defer the effective date of Update 2017-12. That is, a non-PBE will not be able to apply the deferral if it wants to apply the hedging guidance in the proposed Update.

As noted in paragraph BC65, we understand that the added presentation guidance in Update 2017-12 was an important consideration in developing the proposed optional expedients. We believe the Board should consider whether it would be acceptable for a non-PBE that has not yet adopted Update 2017-12 to be permitted to apply the guidance in this proposed Update if it applies (potentially as an accounting policy election) the presentation guidance in Update 2017-12.

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\(^1\) See Proposed Accounting Standards Update, Financial Instruments—Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842).
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.

We support the proposed expedients for the accounting for contract modifications. We also agree with the Board’s decision to include indicators within the proposed Update that will assist in determining whether a modification is related to, or unrelated to, the replacement of the reference rate.

We suggest clarifying the concept in BC30, which notes: “if a maturity date of a loan changed by a few days potentially because of structural changes as a result of reference rate reform, the Board would not intend for the contract to be excluded from the scope of the amendments in this proposed Update.” Specifically, this may be interpreted to conflict with the proposed guidance in paragraph 848-20-15-6(b), which states that a change to the maturity date is unrelated to the replacement of the reference rate. We believe the Board should amend paragraph 848-20-15-6(b) to refer to only significant changes to the maturity date. We also believe the examples in paragraph 848-20-55-2 are helpful, but suggest expanding the first example (modification of a derivative instrument) to clarify that pursuant to paragraph 848-20-35-3, an entity would not need to reassess whether the instrument is a hybrid instrument consisting of a host instrument and an embedded derivative upon a modification.

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?

We agree that the optional expedients for contract modifications should be applied at the relevant Topic, Subtopic, or Industry Subtopic level.

We believe paragraph 848-20-35-3 should be clarified to reflect the fact that the guidance in the proposed Update is optional and not required. We suggest the following edit:

If an entity has modified a contract that meets the scope of paragraphs 848-20-15-2 through 15-3 but that contract is not within the scope of the Topics referenced in paragraph 848-20-35-2, the entity shall have the option to account for and present the modified contract as a continuation of the contract existing before the modification for reference rate reform—that is, an entity shall have the option to follow the guidance that applies to a modification that does not result in the derecognition (or extinguishment) of a contract and the initial recognition of a new contract. In addition, if an entity elects to account for and present a modification that meets the scope of paragraphs 848-20-15-2 through 15-3 as a continuation of the contract, it shall not be considered an event that requires reassessment of a previous determination required under the relevant Topic or Subtopic. Paragraph 848-20-55-2 includes examples that illustrate the application of that guidance.

Hedge Accounting

Question 5—Change in Critical Terms: Do you agree with the proposed exceptions to the requirement in Topic 815 to desiginate 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.

We generally agree with the proposed exceptions upon a change in critical terms. However, we propose the Board provide a few clarifications.
Paragraph 848-20-15-6(l) indicates that a change in the counterparty to a contract would be considered a change that is unrelated to the replacement of a reference rate. As it relates to derivative instruments, the proposed guidance in paragraph 848-20-15-6(l) appears to be inconsistent with the guidance that permits a change to the derivative counterparty without it being considered a termination of the derivative instrument, as discussed in paragraphs 815-30-40-1A and paragraph 815-25-40-1A. We suggest clarifying that the proposed guidance in paragraph 848-20-15-6(l) does not apply to derivatives designated in a hedging relationship, as it was previously determined that a change solely related to a derivative counterparty does not trigger a dedesignation under Topic 815.

We also suggest providing further clarity as it relates to hedge documentation and the options available for assessing effectiveness when transitioning into and out of the guidance in the proposed Update. As currently written, we are unclear on a number of points, including:

- Is an entity required to document the method that will be used to assess effectiveness when it no longer applies the temporary guidance in the proposed Update? If an entity is designating a new hedge under the proposed Update, does it need to include anything within its documentation that would be applicable upon ceasing to apply the temporary guidance in the proposed Update?
- Can the effectiveness assessment be a new method? For example, if an entity assessing effectiveness on a quantitative basis for a cash flow hedge applies the guidance in the proposed Update, can it elect to apply a qualitative method of assessing effectiveness (assuming it qualifies) after ceasing to apply the guidance in this proposed Update?
- Is an entity restricted to applying the same methodology that was applied to a hedging relationship prior to the adoption of the proposed Update?
- Upon transitioning from the guidance in the proposed Update, can an entity elect to exclude a component from the hedging relationship if that component was not previously excluded?

We suggest making further clarifications to the guidance to clarify matters relevant to “transitioning onto” as well as “transitioning from” the proposed Update.

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.

We agree with the proposed optional expedients for fair value hedge accounting; however, we suggest making the following clarifications.

- Paragraph 848-30-25-9 addresses changes to the designated hedging instrument in a fair value hedge, and states that “the entity shall assess the hedge effectiveness of the amended hedging relationship using a method under Subtopics 815-20 and 815-25.” As noted in our response to question 5, we believe the Board should clarify whether an entity can choose a new method for assessing effectiveness or if the method used prior to the application of this proposed Update must be used to assess effectiveness.

- Paragraph 848-40-25-2(c) notes that an entity must ensure that the hedging instrument is expected to be prospectively highly effective. We believe it would be helpful to consider clarifying how this prospective assessment would be performed when the terms of the hedging instrument change, the designated benchmark interest rate changes and no dedesignation is required. Specifically, it would be helpful to clarify that the prospective assessment would be performed based upon the amended terms of the hedging relationship. As a result, if a hedge
assessment is performed using historical data points (e.g., regression analysis) the hedge should be assessed using new data points (for historical periods).

- Paragraph 848-40-25-4(a) allows for the remaining designated cash flows to be adjusted under the optional expedient, but we are unclear as to the Board’s intent. For example, this could be read as guidance on adjusting the cash flows used when calculating changes in fair value of the hedged item to avoid having to change the basis adjustment. It could also be read to permit an entity to elect to apply partial term hedging pursuant to this proposed amendment.

- Paragraph 848-40-25-5(a) provides an approach to adjust the hedged item’s cumulative basis adjustment due to a change in the initially designated benchmark interest rate. However, paragraph 848-40-25-7(b) appears to provide guidance for the offsetting entry when applying paragraph 848-40-25-5(a), which also calls for an adjustment to the carrying value of the hedged item. If the result of this guidance is offsetting adjustments such that there is no change to the cumulative basis adjustment, it is unclear how this is different than applying paragraph 848-40-25-5(b).

The guidance in the proposed Update is temporary and will no longer be applicable after December 31, 2022. However, it is unclear whether this applies to all elements of the proposed Update. For example, within paragraph 848-40-25-8 it states (emphasis added): “If an entity elects the practical expedient in this paragraph for an existing fair value hedge for which the shortcut method is applied, the entity is not required to periodically evaluate the conditions in paragraph 815-20-25-104 for the remaining life of the hedging relationship.” There will be instances when the remaining life of the hedging relationship spans beyond the sunset date of December 31, 2022. In addition, if adjustments are made based on the guidance in paragraph 848-40-25-4, it would be helpful to clarify that these adjustments should be continued when an entity is no longer applying Topic 848.

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.

We agree with the proposed optional expedients for cash flow hedges; however, we suggest making the following clarifications.

- Within paragraphs 848-50-25-9 and 848-50-35-8, we suggest expanding the proposed guidance beyond paragraphs 815-30-35-22(a) and 815-30-35-22(b) when outlining the critical terms an entity may disregard when assessing whether the change-in-variable-cash-flows method will result in a perfectly effective hedge. There may be situations when a cap or floor is modified in the hedged item (or hedging instrument) due to reference rate reform, but the corresponding cap or floor in the hedging instrument (or hedged item) has not yet been modified (creating a mismatch). For example, the strike price of a cap in a hedged item may be modified in connection with the modification of a debt instrument before the hedging instrument is modified. Without also including elements of paragraph 815-30-35-22(c) in paragraphs 848-50-25-9 or 848-50-35-8, the proposed Update would not accommodate such mismatches under the change-in-variable-cash-flows method.

- In the cash flow hedging guidance, we note there are multiple instances when the proposed guidance seems to only refer to modifications of the hedging instruments, as opposed to modifications of the hedging instruments or hedged items. For example, paragraph 848-50-35-5 appears to be limited to the hedging instrument whereas, 848-50-25-6 does not. We believe the guidance should accommodate changes in the hedging instrument or hedged item.
• We believe paragraph 848-50-35-12 should be amended to include the following edit, as it could be interpreted as eliminating the need to do other assessments the guidance may require; for example, to ensure the hedged items is probable of occurring.

An entity shall verify and document whenever financial statements or earnings are reported and at least every three months that only the facts and circumstances related to the hedging relationship in accordance with paragraph 848-50-35-11 have not changed such that the entity can assert qualitatively that the hedging relationship was and continues to qualify for this optional expedient method. No other facts and circumstances related to paragraph 815-20-35-2A through 815-20-35-2F need to be assessed as part of this evaluation.

• Paragraph 848-50-35-17(b) includes a reference to paragraph 848-10-65-1(d), which does not appear to exist.

• We believe it is sufficient for paragraph 848-50-35-18 to refer to Subtopics 815-20 and 815-30 without the need to reference prospective and retrospective assessments. We believe the following edit should be made.

If an entity applies an optional expedient method for assessing hedge effectiveness in accordance with paragraphs 848-50-35-1 through 35-16 and the hedging relationship continues after the entity ceases applying the optional expedient method, the entity shall revert to applying the qualifying criteria and hedge assessment methods in Subtopics 815-20 and 815-30. For a hedging relationship that continues after ceasing application of an optional expedient method, an entity shall apply a hedge assessment method in accordance with Subtopics 815-20 and 815-30. both prospectively and retrospectively from the date on which that assessment method is first applied. For example, an entity that is using the shortcut method optional expedient for a new cash flow hedging relationship in accordance with paragraph 848-50-25-6 or for an existing cash flow hedging relationship in accordance with paragraph 848-50-35-5 shall revert to a hedge assessment method in accordance with Subtopics 815-20 and 815-30 in assessing whether the hedging relationship continues to qualify for hedge accounting from the date that the new assessment method is first applied.

In addition, the flowchart in paragraph 848-50-55-1 does not illustrate that the elections provided are optional. It also seems to contemplate a situation in which the hedging relationship fails to pass an assessment of effectiveness using an optional expedient in accordance with this proposed Update, but qualifies for hedge accounting under ASC 815, which seems unlikely.

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 agree that the proposed exceptions and optional expedients related to hedge accounting should be applied on an individual hedging relationship basis.
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?

We believe this question is best addressed by financial statement preparers and users.

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?

We believe this question is best addressed by financial statement preparers and users.

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

We support the proposed transition disclosure requirements.

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?

We support applying the proposed optional expedients on a prospective basis.

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?

We agree that the proposed amendments should not apply to contract modifications made and hedging relations entered into or evaluated after December 31, 2022 provided the Board remains committed to monitoring market developments to determine if an extension of this date is required.