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The Accounting Principles & Auditing Standards Committee of the California Society of CPAs is pleased to respond to the July 1, 2013 Proposed Accounting Standards Update Derivatives and Hedging (Topic 815) Accounting for Certain Receive-Variable, Pay-Fixed Interest Rate Swaps on behalf of the Society.

**Question 1:** Please describe the entity or individual responding to this proposed Update. For example:

a. Please indicate whether you primarily are a preparer, user, public accountant, or other (if other, please specify).

b. If you are a preparer of financial statements, please indicate whether your entity is privately held or publicly held and describe your primary business and its size (in terms of annual revenue, the number of employees, or other relevant metric).

c. If you are a public accountant, please describe the size of your firm (in terms of number of partners or other relevant metric) and indicate whether your practice focuses primarily on public entities, private entities, or both.

d. If you are a user of financial statements, please indicate in what capacity (for example, lender, investor, analyst, or rating agency) and whether you primarily use financial statements of private entities or those of both private entities and public entities.

The Accounting Principles and Auditing Standards Committee ("Committee") of the California Society of Certified Public Accountants ("CalCPA") is the senior technical committee of CalCPA. CalCPA has approximately 40,000 members. The Committee includes 53 members, of whom 47 percent are from local or regional firms, 27 percent are from large multi-office firms, 12 percent are sole practitioners in public practice, 10 percent are in academia and 4 percent are in international firms.

**Question 2:** Do you agree that the scopes of both the combined instruments approach and the simplified hedge accounting approach should exclude financial institutions described in paragraph 942-320-50-1, such as banks, savings and loan associations, savings banks, credit unions, finance companies, and insurance entities? If not, please explain why. Are there any other entities that should be excluded? (See also Question 3 below.)

We agree with the exclusion of financial institutions.

**Question 3:** Should the Board consider expanding the scope of either the combined instruments approach or the simplified hedge accounting approach (or both) to other entities, such as publicly traded companies or not-for-profit entities? If the scope is expanded to other entities, what changes, if any, should the Board consider for these approaches? Please explain why.

In view of the recent publication of the Proposed Accounting Standards Update Definition of a Public Business Entity, the Committee will defer response to this question until it comments on that proposal.
Question 4: Do you agree with the required criteria for applying the combined instruments approach and the simplified hedge accounting approach, respectively? If not, please explain why.

Yes.

Question 5: Do you agree with the differences in criteria for applying the combined instruments approach versus the simplified hedge accounting approach? If not, please explain why.

Yes.

Question 6: For applying the combined instruments approach, should additional criteria about management's intent to hold the swap to maturity (unless the borrowing is prepaid) be included? Please explain why.

No, additional criteria about management's intent to hold the swap to maturity should not be added. This is inconsistent with the simplification that the PCC is trying to achieve. In addition to the factors cited in paragraph BC14, we note that, notwithstanding any expressed intent at inception of a swap, intent can readily change with changed circumstances, so expression of intent at inception of a swap is not important.

Question 7: Under the combined instruments approach, should there be a requirement that there have been no adverse developments regarding the risk of counterparty default such that the swap is not expected to be effective in economically converting variable-rate borrowing to fixed-rate borrowing? Please explain why or why not.

Yes, there should be a need to consider the effect of any adverse developments regarding the risk of counterparty default. The criteria for use of the combined instruments approach are sufficiently narrow that the only significant risk that correlation will not be achieved is risk of counterparty default. This risk should be considered when relevant, because correlation is important to the validity of accounting for the swap as a hedge.

Question 8: Do you agree that the primary difference between settlement value (that is, the amount to be paid to or received from the swap counterparty to terminate the swap) and fair value is that generally the nonperformance risk of the swap counterparties is not considered in the settlement value? If not, please explain why.

Yes.

Question 9: Would disclosure of the swap's settlement value (instead of its fair value) adequately provide users of financial statements with an indication of potential future cash flows if the swap were to be terminated at the reporting date? If not, please explain why.

Yes.

Question 10: Are the costs of obtaining and auditing settlement value significantly less than fair value? Please explain why.

Costs of obtaining settlement value would normally be less than fair value if the information is available from the counterparty. Auditing costs may be more variable.

Question 11: Do you agree that the following should be disclosed if the combined instruments approach is applied and that no additional disclosures should be required? If not, please explain why.

a. The settlement value of the swap (along with the valuation method and assumptions)
b. The principal amount of the borrowing for which the forecasted interest payments have been swapped to a fixed rate and the remaining principal amount of the borrowing that has not been swapped to a fixed rate
c. The location and amount of the gains and losses reported in the statement of financial performance arising from early termination, if any, of the swap

d. The nature and existence of credit-risk-related contingent features and the circumstances in which the features could be triggered in a swap that is in a loss position at the end of the reporting period.

Yes.

**Question 12**: Do you agree that the current U.S. GAAP disclosures, including those under Topics 815 and 820 should apply for a swap accounted for under the simplified hedge accounting approach and that the settlement value may be substituted for fair value, wherever applicable? If not, please explain why.

Yes.

**Question 13**: Do you agree with providing an entity-wide accounting policy election for applying the combined instruments approach? If that policy election is availed, should this approach be applicable for all qualifying swaps, whether entered into on or after the date of adoption or existing at that date? If not, please explain why.

Yes.

**Question 14**: Do you agree that the entity-wide accounting policy election to apply the combined instruments approach must be made upon adoption of the amendments in this proposed Update or, for entities that do not have existing eligible swaps, within a few weeks after the entity enters into its first transaction that is eligible for the accounting policy election? If not, please explain why.

Yes.

**Question 15**: Do you agree that the simplified hedge accounting approach could be elected for any qualifying swaps, whether existing at the date of adoption or entered into on or after the adoption date? If not, please explain why.

Yes.

**Question 16**: Do you agree that the election to apply the simplified hedge accounting approach to an existing qualifying swap must be made upon adoption of the amendments in this proposed Update? If not, please explain why.

Yes.

**Question 17**: Do you agree that the formal documentation required by paragraph 815-20-25-3 to qualify for hedge accounting must be completed within a few weeks of hedge designation under the simplified hedge accounting approach? If not, please explain why.

Yes.

**Question 18**: Do you agree that entities within the scope of this proposed Update should be provided with an option to apply the amendments in this proposed Update using either (a) a modified retrospective approach in which the opening balances of the current period presented would be adjusted to reflect application of the proposed amendments or (b) a full retrospective approach in which financial statements for each individual prior period presented and the opening balances of the earliest period presented would be adjusted to reflect the period-specific effects of applying the proposed amendments? If not, please explain why.

Yes.
Question 19: Do you agree that an entity within the scope of this proposed Update should be permitted to early adopt the proposed amendments? If not, please explain why.

Yes.

Question 20: How much time is needed to implement the proposed amendments? Please explain.

While the Committee did not attempt to quantify the actual time savings, we believe that the effort to implement and audit the proposed amendments would be significantly less than the efforts under the current standards.

Question 21: The scope of this proposed Update uses the term publicly traded company from an existing definition in the Master Glossary. In a separate project about the definition of a nonpublic entity, the Board is deliberating which types of business entities would be considered public and would not be included within the scope of the Private Company Decision-Making Framework. The Board and PCC expect that the final definition of a public business entity resulting from that project would be added to the Master Glossary and would amend the scope of this proposed Update. The Board has tentatively decided that a public business entity would be defined as a business entity meeting any one of the following criteria:

a. It is required to file or furnish financial statements with the Securities and Exchange Commission.

b. It is required to file or furnish financial statements with a regulatory agency in preparation for the sale of securities or for purposes of issuing securities.

c. It has issued (or is a conduit bond obligor) for unrestricted securities that can be traded on an exchange or an over-the-counter market.

d. Its securities are unrestricted, and it is required to provide U.S. GAAP financial statements to be made publicly available on a periodic basis pursuant to a legal or regulatory requirement.

Do you agree with the Board’s tentative decisions reached about the definition of a public business entity? If not, please explain why.

In view of the recent publication of the Proposed Accounting Standards Update Definition of a Public Business Entity, the Committee will defer response to this question until it comments on that proposal.

We thank you for the opportunity to comment on this matter. We would be glad to discuss our opinions with you further should you have any questions or require additional information.

Very truly yours,

Michael D. Feinstein

Michael D. Feinstein, Chair
Accounting Principles and Auditing Standards Committee
California Society of Certified Public Accountants