

September 7, 2010

Mr. Russell Golden Technical Director Financial Accounting Standards Board 301 Merritt 7 P.O. Box 5116 Norwalk, CT 068956-5116

Via email: director @fasb.org

File Reference: No. 1830-100 — Amendments for Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs

Dear Mr. Golden:

Thank you for the opportunity to comment on the Proposed Accounting Standards Update, Amendments for Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs (the "Proposed ASU"). We support the FASB's efforts to improve the usefulness of financial statements for users by making refinements to the fair value disclosure requirements. However, we have some comments on the Proposed ASU that we believe are necessary to achieve the proper balance between providing increased transparency and the usefulness and operationality of the proposed disclosure enhancements.

With \$19.03 trillion of assets under custody and administration and \$1.78 trillion of assets under management as of June 30, 2010, State Street is the world's leading provider of financial services to institutional investors. This comment letter is written from State Street's perspective as the preparer of its own consolidated financial statements, as well as from its perspective as an asset manager and asset custodian.

#### **Overall Statement**

State Street continues to support the FASB's efforts to move toward IFRS convergence and to make enhancements to disclosure requirements to increase transparency surrounding fair value measurements. However, State Street continues to believe that enhanced qualitative disclosures would better achieve the objective of increased transparency, rather than additional quantitative information that may not be useful to financial statement users. The Proposed ASU, in its current form, would not improve understandability with respect to the proposed measurement uncertainty analysis for asset and liabilities categorized in Level 3 of the fair value hierarchy. Moreover, and in particular, with respect to the proposed requirement to disclose all transfers between

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levels, additional quantitative information may prove to be confusing for financial statement users.

State Street notes that several of the items within the Proposed ASU, such as the measurement uncertainty analysis and disclosure of Level 1-to-Level 2 transfers, were previously included in the proposal that became ASU 2010-6, *Improving Disclosures about Fair Value Measurements* (File Reference No. 1710-100). State Street reiterates its comments on that proposal, and has included those comments as Appendix A to this comment letter.

# Level Transfers – Proposed Update to paragraph 820-10-50-2(bb)

The Proposed ASU will be particularly burdensome for financial institutions as well as registered mutual funds, bank collective funds or other entities accounted for under Topic 946 ("investment companies"). The requirement to track <u>all</u> transfers between levels of the fair value hierarchy, as opposed to only significant transfers, will require significant modifications to controls, processes and systems. As we discuss in greater detail below, many transfers between fair value hierarchy levels are due to the structure of the financial instrument as opposed to the diminished observability of market inputs. Also, for many investment companies, the disclosure of transfers between fair value hierarchy levels provides little additional benefit to financial statement users, as the transfers generally do not highlight material risks to the financial statement users as described further below.

Certain financial instruments will be transferred between fair value hierarchy levels solely based on timing differences between trading and measurement periods. For instance, a right to purchase common stock will transfer between levels of the fair value hierarchy as a result of the trading period concluding prior to the payable date of the rights offering. During the trading period, these financial instruments are often categorized in Level 1, as they are valued using observable quoted market prices. The categorization of these financial instruments generally changes to Level 2 once the trading period has ended and the financial instrument is valued intrinsically using other observable market inputs, such as the strike price of the right and the current common stock price of the issuer. Tracking and reporting these level transfers, as well as transfers of a similar nature, will not provide significant benefit to the end user of the financial statements and may result in a greater lack of clarity by disclosing items that are not material to the overall financial condition of the entity.

Additionally, as a significant number of investment companies have an open-ended capital structure, certain quantitative comparisons can be skewed due to their relatively fluid capital base. For example, investment companies investing in emerging markets generally experience significant capital flows due to their historically volatile returns. Despite these large capital flows, the composition and concentrations of investments will remain relatively stable barring a change in investment strategy. Investments in a certain country or market may warrant transfers between fair value hierarchy levels due to the

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relative lack of trading in a specific financial instrument. However, when presented on a quantitative basis, the effect of equity inflows and outflows could result in significant movements between fair value hierarchy levels, whereas the specific investments warranting transfers between fair value hierarchy levels would likely be relatively constant as a percentage of total assets period-over-period.

Moreover, investment companies often utilize third-party valuation services for fair value measurements of international equity assets due to significant market movements, which occur after the close of the international markets. The use of these sources is generally driven by the broader market movements and they are not necessarily utilized as of each valuation date. Financial instruments valued utilizing these third-party valuation services are often categorized in Level 2 of the fair value hierarchy for any valuation date for which the service was employed. Accordingly, the categorization of these assets often changes between Level 1 and Level 2 on given valuation dates due to the use of these third-party valuation services, which are employed as a result of broader market movements during periods of volatility. Disclosure of the amount of these transfers would not be meaningful, whereas additional disclosure surrounding the nature of these transfers may provide additional insight into the fair value measurement process.

## Measurement Uncertainty Analysis – Proposed Update to paragraph 820-10-50-2(f)

While we support the FASB's efforts to increase transparency into fair value measurements categorized in Level 3 within the fair value hierarchy, we believe that the proposed requirement to present a measurement uncertainty analysis and the correlation between unobservable inputs would not be operational and would result in a significant increase in costs. We believe that the proposed Level 3 measurement analysis will result in the monitoring and maintenance of multiple sets of books and records for Level 3-categorized assets and liabilities.

Of particular concern to us is how the Proposed ASU interacts with the proposed changes contemplated in the Accounting for Financial Instruments and Revisions to the Accounting for Derivatives and Hedging Exposure Draft currently being considered by the FASB, which would require full mark-to-market accounting for all loans (among other financial instruments). Given the unique nature of a loan portfolio, which represents assets that banks intend to hold to maturity, there does not exist an active secondary market. As such, the "exit price" for these loans will contemplate significant management judgment around credit, interest rates and liquidity, which will vary widely among financial institutions. This will result in limited comparability among banks as to what inputs have been used in the valuation process, and, more importantly, the disclosed information will be of minimal value to financial statement users.

A Level 3 categorization already implies an inherent degree of uncertainty as to the precision of the valuation due to the significant reliance upon unobservable inputs. The disclosure of additional quantitative information for Level 3-categorized assets and

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liabilities will not increase the transparency surrounding valuation, whereas the inclusion of alternative valuations may create more uncertainty. Instead, the FASB should encourage disclosure of more qualitative information with respect to Level 3-categorized assets and liabilities, to enable the financial statement user to better understand how the fair value measurements have been derived.

If the FASB determines that additional quantitative information would be useful, we suggest the inclusion of additional information within the roll-forward of Level 3 activity, to disclose sale activity in comparison to the most recently reported valuation and the length of time between those measurements, as a better indicator of the precision of the Level 3-categorized valuation. The granularity of this information should be consistent with either the schedule of investments for investment companies or the tabular reconciliation of the fair value hierarchy as applicable.

#### Conclusion

We believe that increased transparency into fair value measurements is important, particularly for assets and liabilities valued using inputs other than observable market inputs. In summary, we believe that the objective of the Proposed ASU could be achieved with increased qualitative disclosures.

Also, we support the FASB's goal of seeking a single set of high-quality, international accounting standards that companies worldwide would use for both domestic and cross-border financial reporting, and its collaborative efforts with the International Accounting Standards Board. We urge the FASB to continue these efforts toward convergence.

We appreciate your consideration of these matters and welcome the opportunity to discuss them with you.

Sincerely,

James J. Malerba

Executive Vice President and Corporate Controller

## APPENDIX A



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October 8, 2009

Mr. Russell G. Golden Technical Director Financial Accounting Standards Board 401 Merritt 7 PO Box 5116 Norwalk, CT 06856

File Reference: No. 1710-100

# Re: Proposed Accounting Standards Update, Fair Value Measurements and Disclosures (Topic 820) – Improving Disclosures about Fair Value Measurements

State Street Corporation ("State Street") appreciates the opportunity to comment on the Proposed FASB Accounting Standards Update, *Improving Disclosures about Fair Value Measurements* ("Proposed ASU"). We support the efforts made by the FASB to enhance disclosures and transparency surrounding fair value measurements. Although we support the issuance of the Proposed ASU, we have some comments on the Proposed ASU that we believe are necessary to achieve the proper balance between providing increased transparency and the usefulness and operationality of the proposed enhancements to disclosures about fair value measurements.

With \$16 trillion in assets under custody and administration and \$1.6 trillion under management, State Street is the world's leading provider of financial services to institutional investors. This comment letter is written from the perspective of State Street as preparer of its own corporate financial statements as well as from our perspective of an asset manager and custodian of assets.

#### <u>Valuation Technique Disclosure – Proposed Update to paragraph 820-10-50-1(a)</u>

We support the FASB's proposal for enhanced disclosure surrounding valuation techniques, as it would be beneficial to investors to be provided additional qualitative information, particularly with respect to fixed-income securities.

<u>Sensitivity Analysis Disclosure – Proposed Updates to paragraph 820-10-50-1(b) and paragraph 820-10-50-2(f)</u>

While we support the FASB's efforts for increased transparency into fair value measurements classified as level 3 within the fair value hierarchy, we believe the proposed requirement to disclose the total effects on earnings (or changes in net assets) of reasonably possible alternative inputs for level 3-classified assets and liabilities would not be operational and would result in a significant increase in costs.

We believe that increased transparency into fair value measurements is important, particularly for assets and liabilities valued using inputs other than observable market inputs. Accordingly, we believe the objective of this Proposed ASU could be achieved with increased qualitative

disclosures. We believe the example disclosure in the first paragraph on page 17 of the Proposed ASU would be sufficient to achieve the objective of increased transparency.

Additionally, we recommend that the FASB provide additional guidance to suggest the amount and nature of qualitative disclosures, which require judgment and should be evaluated as to the proportion of the level 3-classified assets and liabilities to total assets, total liabilities, total equity or other relevant financial statement amounts.

# <u>Level 1 to Level 2 transfers - Proposed Update to paragraph 820-10-50-2(bb)</u>

We support the objective of increased transparency with respect to transfers between levels within the fair value hierarchy. However, we believe that qualitative disclosure of transfers from level 1 to level 2 would better achieve the objective of increased transparency.

The disclosure of quantitative amounts of transfers may in fact be misleading to a user of financial statements. For example, registered mutual funds, bank collective funds or other entities accounted for under Topic 946 ("Investment Companies") often utilize third-party pricing sources for fair value measurements of international equity assets due to significant market movements, which occur after the close of the international markets. The use of these sources is generally driven by the broader market movements and they are not necessarily utilized each valuation date. As a result, the hierarchy classification of these assets often changes between level 1 and level 2 on a given valuation date. Disclosure of the amount of these transfers would not be meaningful, whereas additional disclosure surrounding the nature of these transfers may provide additional insight into the fair value measurement process.

## Level 3 rollforward - Proposed Update to paragraph 820-10-50-2(c)(3)

We believe that the proposed separate disclosure of purchases, sales, issuances and settlements during the reporting period would provide financial statement users with meaningful information as to the gross activity of assets and liabilities classified in level 3 of the fair value hierarchy. We believe that the proposed disclosure requirements would be operational, as the current requirement to show transfers in and/or out of level 3 generally results in obtaining the information necessary for the proposed separate disclosure requirement.

## <u>Disaggregation - Proposed Update to paragraph 820-10-50-2A</u>

We support the FASB's proposal to require entities to utilize judgment in evaluating the proper level of disaggregation to provide meaningful disclosures with respect to disaggregation of classes of assets and liabilities for fair value hierarchy disclosures.

For most investment companies, complementary disclosures to the fair value hierarchy classifications exist in the financial statements and/or footnotes, particularly through detailed disclosures within the schedule of investments, which generally discloses security-level detail.

Moreover, the level of disaggregation required should be commensurate with the structure and design of the entity. For example, investors in a passively-managed equity mutual fund that tracks a broad market index may not be necessarily concerned with a level of disaggregation greater than investment type. A further level of detail would not necessarily be meaningful to investors in a fund that seeks to match the return of the fund's benchmark. However, investors in an actively-managed fund may find disaggregation by sector meaningful in reviewing fair value measurement disclosures.

In order to provide clarity regarding the use of judgment in determining the proper level of disaggregation of classes of assets and liabilities, the FASB should provide illustrative examples in a fashion similar to the items listed above.

## <u>Valuation Techniques and Inputs Disclosures – Proposed Update to paragraph 820-10-55-224</u>

As noted above, we do not believe that disclosure of quantitative information about key inputs, such as specific or weighted-average prepayment rates or collateral, would provide significant meaningful information. Additionally, entities, including most investment companies, utilize third-party pricing sources to assist in measuring the fair values of assets and liabilities. These assets and liabilities represent the majority of assets and liabilities classified in level 2 within the fair value hierarchy. These pricing sources generally do not have the ability to furnish quantitative input information, and the furnishing of such information on a broad scale to enable entities to comply with the proposed disclosure requirements may impact the pricing sources' proprietary business models. Moreover, this proposed quantitative disclosure requirement would result in a significant increase in costs for most entities.

However, we believe the proposed disclosure requirement under 820-10-55-22A(d) would be meaningful, as it would provide additional information surrounding the measurement of fair value.

## Effective Date

This Proposed ASU, as currently drafted, will require fairly significant cost and effort to implement. We believe that additional time would be required to effectively implement these changes as proposed. Accordingly, we recommend that the FASB modify the effective date of all provisions of the Proposed ASU to periods ending after June 15, 2010, with early adoption encouraged for those entities that may be able to implement within the currently proposed timeframe.

We appreciate your consideration of these comments and welcome the opportunity to discuss them with you.

Sincerely,

James J. Malerba

Executive Vice President and Corporate Controller