

September 25, 2012

Ms. Leslie Seidman Chairman Financial Accounting Standards Board 401 Merritt 7 P.O. Box 5116 Norwalk, CT 06856-5116

Re: Financial Instruments (Topic 825): Disclosures about Liquidity Risk and Interest Rate Risk

Dear Ms. Seidman:

The Global Financial Institutions Accounting Committee of the Securities Industry and Financial Markets Association (SIFMA)¹ appreciates the opportunity to provide comments on the FASB's Proposed Accounting Standards Update, *Financial Instruments* (Topic 825) Disclosures about Liquidity Risk and Interest Rate Risk (the "Proposed Update").

We do not support the Proposed Update, as it does not improve current US financial reporting and will require disclosure of information that is less useful than existing disclosures in the Management's Discussion & Analysis (MD&A) section of the Form 10-K and Form 10-Q filings with the SEC. Respectfully, we strongly recommend that the FASB withdraw the Proposed Update and work with the prudential regulators to develop a consistent measurement and disclosure framework for these risks, then partner with the SEC to enhance or clarify existing MD&A disclosure requirements.

Specific concerns we would like to bring to the Board's attention which we believe to be critical to the Board's decision regarding the Proposed Update include:

• Liquidity Risk: The Proposed Update does not distinguish between information that would be useful to an investor, proprietary information and information that could generate confusion and lead to an unjustified loss of confidence in a financial institution. The Liquidity Gap table in the Proposed Update, by

New York | Washington

¹SIFMA brings together the shared interests of hundreds of securities firms, banks and asset managers. SIFMA's mission is to support a strong financial industry, investor opportunity, capital formation, job creation and economic growth, while building trust and confidence in the financial markets. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association. For more information, visit www.sifma.org.

excluding asset sales, securitizations, debt issuances and other common liquidity management practices, assumes that the only source of funding for maturing liabilities is from maturing assets. The table therefore presents an incomplete view of the sources of liquidity available to a financial institution. To the extent that users of financial statements do not understand the limitations of the disclosures in the Proposed Update and draw erroneous conclusions about the liquidity position of a financial institution, it is easily possible that the disclosures themselves could lead to a reduction in the financing available to that financial institution. We strongly but respectfully request that the FASB reconsider its current approach in the Proposed Updates regarding liquidity disclosures.

- **Disclosure framework:** The objectives of this Proposed Update are not consistent with how the objectives of financial reporting in the FASB's Concepts Statement 8, *Conceptual Framework for Financial Reporting* are typically met, which is by providing information about an entity's financial position as of specific points in time, as well as its results of operations for historical periods. This proposal represents a significant departure from the content of general purpose financial statements, and such departure requires further conceptual consideration of the proper content of notes to the financial statements.
- **Duplicative information**: Disclosures regarding financial institutions' management of interest rate and liquidity risk already exist in the MD&A section of the Form 10-K and Form 10-Q filings with the SEC. Even though it is the Board's intent to supplement rather than duplicate the information disclosed in the MD&A, the tables will be duplicative, and will be populated with inconsistently generated information resulting from a lack of nonconforming definitions, creating duplicative, confusing and/or misleading information for financial statement users. Moreover, we believe the cost of generating this information outweighs the perceived benefits of this information.
- **Perceived comparability**: The disclosures required by the Exposure Draft create an illusion of comparability by requiring financial institutions to run prescribed scenarios that may not take into consideration company-specific factors. The static testing requirements do not provide information that is relevant or reliable.
- Forward-looking nature of the Proposed Update: The overarching objective of the MD&A section is to provide investors with both a short- and long-term analysis of the business of the company. This objective of the MD&A, in contrast with the objective of financial reporting as noted in the second bullet above, is more in line with the predictive purpose of the proposed disclosures; thus, any

additional disclosures aligned with the Board's objectives in the Proposed Update are better-suited for the MD&A.

• Auditability: We anticipate that it will be extremely difficult (if not impossible) to audit (i) effects of specified hypothetical, instantaneous interest rate changes as of the measurement date on net income and on shareholders' equity (825-10-50-23AD), (ii) the calculation of "expected maturity" for instruments that are long-dated and/or involve significant unobservable inputs, and (iii) the qualitative disclosures that are required to provide users with an understanding of a financial institution's liquidity and interest rate risk.

Appendix A includes a detailed discussion of the above points as well as comments on scope and operational implementation regarding Examples 4, 7, 8, 9 and 11 in the Proposed Update.

If the FASB decides to proceed with disclosures similar in scope and magnitude to the Proposed Update, we request that the Board consider an effective date no earlier than 2015 in order to provide financial institutions with sufficient time to develop these new processes, implement the appropriate controls, and test these new controls. A 2015 effective date would also align this Proposed Update with the beginning of the Basel III implementation timeline for the Liquidity Coverage Ratio (LCR).

We thank you for the opportunity to provide our industry view. The Global Financial Institutions Accounting Committee would be pleased to discuss our response with the FASB staff. Please contact me at 212-357-8437 if you have questions or comments concerning our letter.

Regards,

Matthew L. Schroeder

Matt Schooler

Chairman, SIFMA Global Financial Institutions Accounting Committee

Copy to:

Paul Beswick, Acting Chief Accountant, Office of the Chief Accountant, SEC Susan Cosper, Technical Director, FASB Jill Switter, Project Manager Mary Kay Scucci, PhD, CPA, Managing Director, SIFMA

APPENDIX A

Critical Implementation Concerns

Disclosure Framework

While we support the FASB's intentions of improving the decision-usefulness of financial statements, the objectives of this Proposed Update are not consistent with how the foundational objectives of financial reporting have historically been met. Specifically, as outlined in FASB Concepts Statement 8, *Conceptual Framework for Financial Reporting*, financial reporting should provide information about the economic resources of an enterprise; the claims to those resources (obligations); and the effects of transactions, events, and circumstances that cause changes in resources and claims to those resources. Said differently, financial reporting is meant to provide information about an entity's financial position as of specific points in time, as well as its results of operations for historical periods. The forward-looking requirements in this proposal do not align with the current information required to be included in the footnotes to the financial statements.

Duplicative Information

Information about how financial institutions manage interest rate and liquidity risk is currently presented in the MD&A section of the Form 10-K and Form 10-Q filings with the SEC. Such information includes qualitative and quantitative information intended to provide information that would be relevant and useful to enable investors to understand how liquidity and interest rate risks are managed, including what modeling is performed and what scenarios are contemplated. The flexibility management has with presenting this information allows the information to be tailored to the specific risk management activities of an organization, which results in the information being more meaningful to a financial statement user. Although the Board's intention is for the tables in the footnotes to supplement rather than duplicate the information disclosed in the MD&A, the standardized tables will not align with the presentation and discussion within the MD&A and thus would result in conflicting information within the financial statements. This may confuse or mislead financial statement users.

Perceived Comparability

The disclosures required by the Proposed Update create an illusion of comparability by requiring financial institutions to run prescribed scenarios that may not take into consideration company-specific factors. In practice, many financial institutions run dynamic scenarios using various assumptions to capture the institution's risk profile. In contrast, the static testing requirements in the Proposed Update are more simplified; such static analyses do not provide information that is relevant or reliable because they prevent reflection of common risk management practices that would likely be undertaken in the scenarios that the disclosures attempt to depict.

Forward-looking Nature of the Proposed Update

Certain disclosures in the Proposed Update are more appropriate for the MD&A due to their forward-looking nature. Specifically, SEC Regulation S-K Item 303 identifies a basic and overriding requirement of MD&A, which is to "provide such other information that the registrant believes to be necessary to an understanding of its financial condition, changes in financial condition and results of operations." ² The SEC recognizes that a narrative explanation of the financial statements is useful in providing an investor with information to judge the quality of earnings. This objective of the MD&A contrasts with the point in time and past performance content of general purpose financial statements noted above and thus makes the disclosures proposed in the Proposed Update better-suited for MD&A.

Auditability

We question the auditability of some of the required information. Specific items that may not be auditable include:

- The effects of specified hypothetical, instantaneous interest rate changes as of the measurement date on net income and on shareholders' equity (825-10-50-23AD).
- The calculation of "expected maturity" for instruments that are long-dated and/or involve significant unobservable inputs subject to significant judgment regarding management and/or investor behavior within a contractual funding period.
 - While we do not expect significant audit issues with plain vanilla instruments (e.g., 5-year callable debt), management judgment becomes more significant and the determination of expected maturity becomes less auditable as inputs become less observable for instruments such as demand deposits.
- The qualitative disclosures intended to enhance users understanding of a financial institution's liquidity and interest rate risk.
 - O An entity generally will utilize the MD&A to explain these risks and how they are managed. Included in the MD&A is information, (i.e., forecasts, potential economic conditions, etc.) that is considered in an entity's management of its liquidity and interest rate risks, which is not information that can be audited.

It is also unclear whether such predictive information would expose companies (and their auditors) to litigation risk if future actual performance does not align with the projected performance in the footnotes to the financial statements. Rather than requiring forward looking information in the footnotes, we would encourage the FASB to collaborate with the SEC in clarifying the MD&A disclosure requirements and, if necessary, the SEC

_

² Regulation S-K: Management's Discussion and Analysis of Financial Condition and Results of Operations (MD&A), Item 303 Paragraph (a).

could consider providing further guidance. We also encourage collaboration with the federal banking regulators in order to achieve alignment of objectives and consistency in the information reported by financial institutions, resulting in a more harmonious regulatory and financial reporting framework.

Scope

We recommend the Board clarify the scope of the disclosures that apply to financial institutions. Specifically, we believe it is unclear whether an entity that meets the definition of a financial institution should provide the financial institution disclosures for the entity as a whole or solely for its reporting segments that meet the definition of a financial institution.

The Background Information and Basis for Conclusions in the Proposed Update describes how the Board intended the interest rate and liquidity risk disclosures to apply to reporting segments of entities that do not meet the definition of a financial institution but have reportable segments that do meet the definition of a financial institution. However, there is not a discussion relating to entities that meet the definition of a financial institution but have reporting segments that do not meet the definition of a financial institution. Reporting segments that do not meet the definition of a financial institution may not be managed in an asset-liability manner for net interest income and therefore would have to create the required disclosure information in the Proposed Update.

Additionally, applying the financial institution liquidity and interest rate risk disclosures to segments that are not financial institutions could lead users to misconstrue the disclosures at the aggregate firm level. Furthermore, because these segments would not meet the definition of a financial institution on a stand-alone basis, they would be required to maintain two sets of parallel data for financial reporting purposes (data to satisfy the consolidated reporting requirements and data to satisfy stand-alone reporting requirements). However, an entity that meets the definition of a financial institution may manage the liquidity and interest rate risks of its non-financial institution segments centrally with reporting segments that do meet the definition of a financial institution.

We recommend that the interest rate and liquidity risk disclosures applicable to a financial institution be required solely for reporting segments that meet the definition of a financial institution but provide entities the option to present the interest rate and liquidity risk disclosures applicable to a financial institution to the entity as a whole.

Liquidity

Liquidity Gap Maturity for a Bank (Example 4)

Proprietary Information and Liquidity Risk

The Proposed Update does not distinguish between information that would be useful to an investor, proprietary information and information that could generate confusion and lead to an unjustified loss of confidence in a financial institution. The Proposed Update liquidity tables and disclosures could easily lead to misunderstandings, confusion, and result in inappropriate conclusions creating an adverse liquidity event. Prudential regulators understand the unique risks inherent in liquidity and have incorporated that understanding in the development of the Basel standards. We strongly but respectfully request that the FASB reconsider its current approach in the Proposed Updates regarding liquidity disclosures.

While strongly recommending withdrawing the Proposed Update, we have identified information that is either proprietary or unreflective of a financial institution's ability to sell, pledge or originate new business as sources of liquidity:

- Expected maturity assumptions A singular focus on the financial assets and liabilities maturing in a single time period are not reflective of the access firms have to a variety of cash generation options in addition to cash generated from maturing financial instruments. An expected maturity table is not a reliable tool for conveying an understanding of financial institutions' liquidity risk profiles, or comparing risk profiles across financial institutions.
- Disclosures requiring the use of static portfolio assumptions will lead to disclosure results that are not representative of a financial institution's true liquidity position. If users of financial statements do not understand the limitations of the proposed disclosures, it is likely that conclusions could be drawn about a financial institution's liquidity risk position that are inaccurate, potentially causing harm to an individual financial institution and/or to the broader market. Additionally, disclosure of deposit runoff assumptions could lead to competitive harm by signaling the pricing actions a bank would take in certain scenarios.
- Off-balance sheet commitment assumptions Loan commitment draw assumptions are based on proprietary predictions of counterparty/borrower behavior regarding when and how much will be drawn under various market and idiosyncratic scenarios and should not be disclosed.

Specific Issues on Comparability and Assumptions

 Our understanding of the intended goal of the table is to provide users with standardized, comparable and auditable liquidity risk information across financial institutions. The only way to achieve this goal is to prescribe not only the contents of the table, but also the underlying assumptions used, which would be a difficult undertaking, considering the number and significance of assumptions inherent in preparing the table. If the liquidity gap maturity table is included as proposed in a final standard, specific disclosure information in the table will not be standardized or comparable due to the varied assumptions used in practice based on risk management and portfolio differences, including:

- "Expected maturity" assumptions The expected maturity assumptions for loans and deposits will vary by bank.
- Off-balance sheet commitment assumptions The commitments will have draw assumptions that vary by financial institution due to borrower behavior and specific market scenarios.

<u>Lack of Usefulness – Basel III and Internal risk management measures</u>

Liquidity risk is complex due to the behavioral assumptions utilized to quantify the unexpected cash outflows in a stress scenario. The Basel III proposed liquidity rules have two ratios regarding liquidity. The first is the Liquidity Coverage Ratio (LCR), under which banks are required to maintain a stock of high quality liquid assets sufficient to cover net cash outflows for a 30-day period under a stress scenario. The second is the Net Stable Funding Ratio (NSFR) which calculates the proportion of long-term assets which are funded by long-term, stable funding sources. The NSFR is structured to ensure that long-term assets are funded with at least a minimum amount of stable liabilities in relation to their liquidity risk profiles.

The development of "accounting-based" liquidity measures will generate a third and confusing liquidity measurement construct which differs from both internal liquidity measurements used today for risk management and liquidity measurements required by banking institutions' prudential regulators, specifically the Basel III construct. The "accounting-based" liquidity disclosures are not risk-based and create confusion when discussing the liquidity position of a firm. The FASB should not develop "accounting-based" liquidity measures but instead should defer to the work of the prudential regulators (i.e., the Federal Reserve) and the Basel Committee on Banking Supervision (BCBS) for all liquidity risk disclosures.

We propose disclosure of Basel III liquidity ratios in the MD&A section of the financial statements in the timeframes prescribed by jurisdictional prudential regulators, similar to the disclosure approach for capital ratios and results of the Comprehensive Capital Analysis and Review (CCAR). The liquidity ratios, specifically the LCR, have standardized stress test scenarios and assumptions that all the banks have to apply, thus it is more comparable than the proposed liquidity gap maturity table.

Specific Concerns - "Accounting-Based" Liquidity Measures

We are concerned about the operational cost to report the liquidity gap maturity tables. A significant amount of time, resources and money have been and are being spent on preparing for the implementation of the Basel III liquidity ratios, the first of which is

effective January 1, 2015. We will have to further build our systems to be able to produce the proposed information in the liquidity gap maturity table.

Our investors consistently ask questions about Basel III. By adding accounting-based liquidity measures, we will have to explain why these measures differ from the Basel III ratios. By definition, the banks will have to manage to the Basel III ratios; accounting-based liquidity measures would lead to confusion and non-comparability as noted in the above examples.

Available Liquid Funds (Example 7)

Clarification of Disclosure Requirements

We suggest the definition of high quality liquid assets be consistent with one determined by the financial institution's prudential regulator or the ones determined by the Basel standards to ensure comparability. Paragraph 825-10-50-23U states that an entity shall include a narrative discussion about the effect of regulatory, tax, legal, repatriation and other conditions that could limit transferability of funds among entities, and that this disclosure shall include quantitative amounts related to funds subject to those conditions, if applicable. For complex global institutions, entity-level, quantitative disclosures will add a significant volume of disclosures without providing a coherent understanding of the liquidity impact from transferability restrictions. A narrative of the effect of the regulatory, tax, legal, repatriation and other conditions that may limit transferability of funds may be a better approach. We ask the FASB for clarification of the disclosure requirements for transferability of funds among legal entities, specifically, the scope of this disclosure and an example of the quantitative disclosure for a complex global financial institution.

Time Deposit Issuance (Example 8)

Lack of Usefulness

This information is not used for liquidity risk management or to determine the "cost of funding" and thus is not useful to the users of financial statements. Further, this information could cause competitive harm since it will provide competitive pricing information that could lead peers to adjust their own deposit pricing. If the FASB proceeds with a similar disclosure requirement, we request clarification regarding how to treat rollovers of deposits (which are frequent, even daily in some cases).

Interest Rate Risk

Repricing Gap for Bank (Example 9)

Lack of Usefulness and Comparability

The repricing gap is not useful information as the industry no longer uses interest rate repricing analyses in the form proposed in the Proposed Update. The approach is no longer used due to the inherent optionality in cash flows, which under the proposed approach would cause flawed, unreliable conclusions (i.e., for residential MBS given the borrower prepayment options inherent in the underlying mortgages).

Alternatively, we would support providing firms' assumptions together with the earningsat-risk analysis currently included by most large financial institutions in the MD&A section of the financial statements.

Proprietary Information

The Proposed Update does not address the distinction between information that would be useful to the user and information that is proprietary in nature and could damage a firm's positions. Specifically, disclosures of securities positions along the yield curve by nature or class of risk are proprietary and such disclosure could cause competitive harm and impair a firm's ability to hedge interest rate risk on a cost-efficient basis. Additionally, deposit repricing forecasts are also highly proprietary competitive information.

Hypothetical Yield Curves and Interest Rate Sensitivity (Example 11)

Lack of Usefulness

Interest rate sensitivity analysis is not useful for fair value financial assets and liabilities. Interest rate risk is already reflected in fair value and financial institutions use risk management tools such as VaR, stress or limit testing to provide analytics on their fair value instruments. As mentioned previously, financial institutions use analyses such as the earnings-at-risk analyses for their accrual financial instruments. The earnings-at-risk analysis measures the impact to net interest income, which we believe is a better sensitivity measure than the impact to net income. Estimating the effects of specified hypothetical, instantaneous interest rate changes as of the measurement date on net income and on shareholders' equity would be highly subjective and not comparable across financial institutions given the number and significance of assumptions regarding the secondary impacts that a change in interest rates would have on comprehensive income. Please refer to Example 9 above for our recommendation for interest rate sensitivity analysis for accrual instruments.