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**Re: File Reference No. 2013-220 – Response to FASB Proposed Accounting Standards Update: *Financial Instruments – Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities***

Dear Ms. Cospers:

Deutsche Bank ("the Bank") appreciates the opportunity to provide feedback on the Proposed Accounting Standards Update: *Financial Instruments – Overall (Subtopic 825-10) - Recognition and Measurement of Financial Assets and Financial Liabilities* ("the Update"). We commented on the IASB *Exposure Draft 2012/4: Financial Instruments: Classification and Measurement; Limited Amendments to IFRS 9* on March 28, 2013, and the IASB is being sent a copy of this letter. We request that the FASB and the IASB target convergence as a priority.

The Bank appreciates the continued efforts to converge US GAAP and IFRS with the aim of creating a single set of high quality global accounting standards. Given the importance and high profile of accounting for financial instruments, a converged standard would illustrate significant progress towards achieving that goal. We therefore support the FASB's efforts to converge the recognition and measurement of financial assets and financial liabilities with IFRS 9. To ensure convergence, we urge the Boards to eliminate, whenever possible, differences in language that do not reflect differences in accounting principles. For example, the two Boards' have proposed different wording regarding the application of the business model test, specifically, when sales of assets are, or are not consistent with the objective to hold financial assets to collect contractual cash flows. Identical language will help avoid different interpretations and additional complexity for users and preparers alike. Where full convergence is not possible, we urge the FASB to work jointly with the IASB to clearly identify and explain any intended differences.

Deutsche Bank is overall supportive of the Update, however, before finalising the project, we suggest that the FASB considers the specific concern highlighted below.

### Contractual Cash Flow Characteristics

We are supportive of a principles based contractual cash flow test but we believe that certain concepts included in the Update are too restrictive and may result in vanilla instruments that fail the test and are classified into Fair Value through Net Income (FV-NI).

We are supportive of the exclusion of insignificant leverage or insignificant interest rate reset mismatch from the contractual cash flow test. However, we believe these exclusions are too narrowly defined, and the tests required to demonstrate the insignificance to be burdensome, complex and often resulting in inappropriate conclusions. Many instruments will, in principle, have cash flows that are solely payments of principal and interest (SPPI), as defined in paragraphs 825-10-25-17 to 825-10-25-20, but will nonetheless fail the contractual cash flow test due to the mechanics of the detailed tests required by paragraphs 825-10-55-14 to 825-10-55-27. The failed test results in an instrument that is measured at FV-NI when, in principle, the most appropriate and relevant measurement should be amortized cost.

For example, adjustable rate mortgages that reset annually to a rate based on Prime, which does not have a term structure, could fail the SPPI test and therefore be required to be classified as FV-NI. We are also aware of products in certain jurisdictions where interest rates are set by governmental authorities in those countries rather than the jurisdictions' benchmark rate.

We believe that the Update should provide further clarity on the SPPI test, by means of an illustrative example, for entities to assess whether there is a modified economic relationship and whether the instrument's cash flows are "more than insignificantly different" from benchmark cash flows. This will help illustrate the principle of SPPI without setting specific rules or exceptions, and will also promote consistency in application amongst preparers. For example, the application guidance for assessing a modified economic relationship is unclear and would benefit from an illustrative example. Our understanding of paragraph 825-10-55-20 requires the analysis of the cash flows of the existing instrument against a benchmark instrument for a range of reasonably possible future scenarios. We believe the selection of possible cash flow scenarios will be subjective and require significant management judgement. We would also welcome guidance on whether discounting is required.

Additionally we think the guidance on prepayment options could benefit from amendment. We think a prepayment option at par plus accrued should meet the SPPI test regardless of the trigger for prepayment (i.e. even if the prepayment is triggered by a contingent event which is not detailed in 825-10-55-21). The prepayment option speeds up the payments but with a strike price of par plus accrued interest, that cash flow should still meet the SPPI principle; however, the specific guidance in 825-10-55-21 could require instruments with these features to be classified as FV-NI.

We further believe that the wording of paragraph 825-10-55-16 needs to be clarified to avoid unintended consequences. An interest rate on an originated loan, for example, is calculated to include, among other things, funding costs, a return on the bank's equity, administrative costs and a profit margin. From the wording of the paragraph, it is unclear whether such components can be considered "consideration for the time value of money and the credit risk". We do not think that "market compliance testing" should have to be carried out on standard loan transactions (i.e. is the interest rate agreed with the client consistent with the time value of the money and the credit risk?). We assume that the FASB merely wishes this paragraph to cover a limited number of specific transactions (e.g. interest rate mismatch features in the

context of modified economic relationships), but we would prefer the FASB to clarify this point and/or delete paragraph 825-10-55-16.

While we are largely supportive of the principle of the contractual cash flow test, we would urge the FASB and IASB to engage with stakeholders to ensure that the Update does not unintentionally require classification in FV-NI for instruments when the most appropriate and relevant measurement should be amortized cost.

When addressing the concerns above, we prefer clarification on the principles of the contractual cash flow test rather than a list of products or features which may or may not meet the contractual cash flow characteristics test.

#### Definition of the Business Model:

We are supportive of the principle that the accounting classification for a financial instrument should be consistent with the business model in which it is held. However, we are concerned that the application guidance is overly restrictive in the activities permitted within a business model that manages financial assets for collection of contractual cash flows. Our concerns are highlighted in further detail below:

#### A. *The Sales criteria is too restrictive in regard to sales due to credit deterioration and for sales executed for regulatory reasons*

We agree with the guidance in paragraph 825-10-55-31 that sales due to credit deterioration should be exempted from the notion of 'sales' in regard to paragraph 825-10-55-28c. However, we believe that the current drafting implies that the credit deterioration would have already occurred to qualify for the exemption. We understand this was not the intent; rather, an entity would be allowed to sell and qualify for this exemption in cases where there was a future expectation of credit deterioration, so long as the deterioration was anchored in the entity's documented investment policy.

As such we propose adding the words 'actual or expected' when referring to credit quality deterioration.

On a separate but related note, the Update as drafted is also unclear as to how sales would be regarded if they arose from concentrations of risk, that is, where an entity effectively de-risked certain exposures due to the fact that its concentration to a particular risk exceeded its pre-defined limits as documented in investment policy. We believe that such instances should also make clear that this would fall into the notion of sales which were exempt. We recommend that the FASB and IASB work together to provide converged guidance that clarifies that such sales are not inconsistent with the objective of amortized cost classification.

Finally we do not believe the Board has adequately considered sales which are executed only or primarily for regulatory reasons; for example, sales executed to demonstrate liquidity of instruments to a regulator. Such sales are not executed for business reasons, other than to satisfy regulatory rules. As such we do not believe they should be regarded as sales which must be considered under paragraph 825-10-55-28c.

**Therefore we recommend that the Board consider permitting sales executed to manage credit concentration risk as well as sales executed to comply with regulatory requirements from the assessment in 825-10-55-28c.**

**B. Drafting suggestions relating to the examples starting in paragraph 825-10-55-70 - Financial versus Non Financial Entity Distinction**

In the examples illustrating the application of the guidance on identifying the business model within which financial assets are managed we note that there is often a prefix of whether the entity is a financial or nonfinancial entity. The financial versus nonfinancial status of an entity is not a factor in the business model test in the guidance on business model classification. The repeated inclusion of the financial versus non financial status of an entity in the examples might lead a user to conclude that this status is a factor in the business model classification. Whilst we acknowledge that this provides context to the discussion, we believe that the business model should be independent of the type of industry that the entity is operating in.

**We would therefore recommend removing the description of entity types in the examples.**

**C. More portfolios classified in FV-OCI or FV-NI**

The examples starting in paragraph 825-10-55-70 make clear that many liquidity portfolios will not meet the amortized cost business model, especially where there are frequent sales, regardless of the reason for the sale. This will mean that many of these portfolios will either be Fair Value through Other Comprehensive Income (FV-OCI) or FV-NI. Under both of these categories the fair value movement will impact regulatory capital under the revised Basel 3 rules. This could impact business decisions as to what the portfolios invest in which could have macro-economic effects and potentially impact financial stability if banks cannot absorb the additional regulatory capital volatility. We are concerned about the impact of this accounting classification on the banking industry and financial stability. Ideally we would have preferred these portfolios to be classified as amortized cost with associated additional disclosures if necessary to separately disclose the fair value for these portfolios (absent any changes in the regulatory rules for the new classification).

We encourage the FASB and IASB to maintain a dialogue with global regulators and the banking industry regarding the reintroduction of the OCI filter for regulatory capital purposes to alleviate concerns regarding the financial stability of liquidity portfolios (amongst others) held at Fair Value through Other Comprehensive Income (FV-OCI).

**We would encourage continued dialogue between the FASB, IASB, Banking Industry and Regulators on this issue.**

**Bifurcation of Financial Assets**

We strongly support the removal of bifurcation for financial assets to promote convergence and reduce complexity. These rules were a burden on preparers and the source of much complexity under Topic 815 and IAS 39.

### Fair Value Option

We are supportive of a fair value option that allows instruments classified at FV-OCI to be elected as FV-NI. Additionally, we do not think there should be a restriction on classifying a financial instrument at fair value through P&L on initial recognition. We are unaware of any abuse of this option. Elections are generally made amongst industry peers for the same reasons, typically to reduce complexity or accounting asymmetry.

The limited fair value option provided in the proposed Update cannot capture all potential examples of where a fair value option would otherwise be elected. The limited fair value option would not be provided for financial assets that meet the criteria for amortized cost classification, for example, instruments hedged using derivatives that cannot qualify for hedge accounting under existing GAAP. Additionally, the fair value option is commonly used to avoid accounting mismatch for financial liabilities with non-bifurcatible risks that are hedged using derivatives and hedge accounting is not otherwise available. We are concerned that the proposed conditional fair value option in paragraph 825-30-15-2 of the proposed Update will not always be available as a remedy for the examples above because of the limiting nature of the option.

If the Board disagrees and continues to support a limited fair value option, we ask the Board to converge with the IASB on this issue by permitting an issuer to elect the fair value option where doing so eliminates or significantly reduces a measurement or recognition inconsistency (sometimes referred to as an 'accounting mismatch').

### Own Credit

We support the recognition in other comprehensive income of the portion of the total change in the fair value of a financial liability designated under the fair value option that results from a change in the instrument-specific credit risk. We are supportive of the Board making the own credit rules available to preparers prior to the full implementation of the Update, in a manner that aligns the early adoption guidance in the IASB's limited amendments to IFRS 9.

Additionally, we agree with paragraph 825-10-45-18 that any OCI recognized above be recycled through net income upon derecognition of the financial liability.

### Equity Instruments

We support fair value accounting for equity securities as proposed in the Update.

### Non-recourse liabilities alignment with related assets

While this represents a divergence from IFRS 9, we support the concepts introduced in paragraph 825-10-35-11, and we would encourage the IASB to consider alignment to the FASB on this issue.

## Reclassification

We support reclassification where the business model has changed, but are concerned that the use of “very infrequent” would lead to an interpretation of “never.”

Given basic loan feature characteristics, if an entity’s business model determines the classification of an instrument, then reclassifications are necessary when a business model changes. To be consistent with the business model principle, reclassification should be required both into and out of fair value through net income when the business model changes. We would expect changes in business model to be infrequent, determined by an entity’s key management personnel and as a result of fundamental significant external or internal changes.

We would support total convergence with the IFRS 9 reclassification requirements, except that we would prefer that reclassifications be characterized as “infrequent” rather than “very infrequent.” Other than removing “very”, we urge the FASB to use the same language included in IFRS9, paragraphs 4.4.1 – 4.4.3, 5.6.1 – 5.6.3, and B4.4.1 – B4.4.3, to avoid any potential interpretational differences between USGAAP and IFRS.

## Disclosures

The incremental disclosures proposed in the Update would create an unnecessary divergence from IFRS. We believe the existing disclosure requirements for financial instruments and fair value are voluminous, complex and that the cost of disclosing this information outweighs the benefits. The additional disclosures proposed by the Update will make financial statements more complex and less understandable at a higher cost to preparers.

Specifically, parenthetical presentation on the face of the financial statements of fair value for items measured at amortized cost should not be required. This information is already disclosed in the footnotes, and would only serve to clutter the financial statements and further confuse users of those financial statements. Additionally, we do not agree with the proposed Level 3 quantitative disclosures of significant unobservable inputs for financial instruments that are measured at amortized cost. We do not believe providing highly unobservable management assumptions related to Level 3 data provides useful information for instruments held at fair value, and believe that information is even less useful for instruments held at amortized cost. We note that entities are currently required to disclose the level in the fair value hierarchy for financial instruments that are not measured at fair value. We believe this current level of information is sufficient for financial statement readers to assess the potential level of unobservability inherent in valuing financial instruments that are not currently carried at fair value.

We also strongly oppose the requirement to disclose our core deposit liability balance, the implied weighted-average maturity period and estimated all-in-cost-to-service rate on the basis that these terms are not adequately defined and therefore will not result in comparable or meaningful disclosures. Additionally, such information on core deposits represents proprietary information that we believe is inappropriate for use in financial statements.

In summary, the incremental disclosures proposed in the Update are not relevant to investors in understanding an entity’s financial statements and will needlessly increase the size and

complexity of the financial statements. We believe providing this information is operationally burdensome to preparers and provides very little benefit to investors.

Effective Dates

We encourage the FASB and IASB to clarify the plan for a converged effective date as soon as possible. An effective date of 1.1.2015 is now not achievable and clarity on a revised date would assist in our planning for adoption.

We hope you find these comments helpful. Should you have any questions or wish to discuss these matters further, please contact Karin Dohm on +49(69)910-31183 or via email to [karin.dohm@db.com](mailto:karin.dohm@db.com) or Michael Fehrman on +1(212)250-2660 or via email to [michael.fehrman@db.com](mailto:michael.fehrman@db.com).

Yours sincerely,



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