

May 15, 2013

Susan M. Cosper
Technical Director
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116

Via email: director@fasb.org

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

Dear Ms. Cosper:

This letter represents the comments of certain members (see list on page 5) of the Asset Management Industry Accounting Policy Group (“AMIAPG”), comprising a forum of companies primarily engaged in the asset management business. The AMIAPG companies represented by this letter include both publicly-traded and privately-held asset managers who collectively manage more than 5,150 investment funds, both domestically and internationally, including registered investment companies, hedge funds, private equity funds, exchange-traded funds and collective investment trusts, in addition to separate accounts and other sponsored investment products. The companies represented by this letter collectively have subsidiaries registered as investment advisors, broker/dealers, trust banks and insurance companies, and oversee approximately \$7.5 trillion of assets under management.

We appreciate the opportunity to provide comments to the Financial Accounting Standards Board (the “FASB” or the “Board”) on the Proposed Accounting Standards Update (“ASU”), *Financial Instruments – Overall (Subtopic 825-10) Recognition and Measurement of Financial Assets and Financial Liabilities* (the “Proposal” or the “Proposed ASU”). We support the Board’s intention to reduce the complexity present in the current framework for accounting for financial instruments. We also support the Board’s progress towards achieving convergence with the International Accounting Standards Board (“IASB”) in the area of financial instruments.

We believe an accounting model that retains amortized cost (“AC”), fair value through other comprehensive income (“FV-OCI”) and fair value through net income (“FV-NI”) accounting for financial instruments is appropriate and serves the needs of financial statement users. However, we believe there are a number of areas that would benefit from revisions or further consideration in order to better balance the usefulness of the financial statements with the costs to comply with the Proposed ASU. Areas for revision or further consideration include the complexity of the model, the accounting for equity investments, the application of specialized accounting for investment companies, consistent accounting treatment for consolidated collateralized financing entities and disclosures. These areas are further discussed below.

I. Complexity of the Model

The Proposed ASU creates an accounting definition for financial instrument classification that is overly complex, operationally difficult and expensive to implement consistently and apply across industries. We are most concerned with the requirement to evaluate the cash flow characteristics of individual financial instruments purchased by an entity, particularly structured investments. To comply with the Proposed ASU, significant technology solutions would be necessary to facilitate systematic cash flow characteristic analyses on an individual financial instrument basis. Additionally, significant human capital costs would be incurred to conduct the analysis and document the conclusions in a manner that could be audited. Internal controls over financial reporting must also be designed, implemented and tested by management, as well as internal and external auditors, contributing significantly to the ultimate cost of compliance. We request the Board seek additional input from constituents via working groups and field-testing with the objective of developing a more cost-effective model. For example, one alternative would be to modify the *solely payments of principal and interest* concept to be a *substantially payments of principal and interest* concept. Determining whether a financial instrument is *substantially payments of principal and interest* would most likely require less modeling which would allow an entity to consider the primary components of an investment rather than searching for any type of payment that might be something other than principal and interest.

II. Accounting for Equity Investments

With regard to the proposed mandatory FV-NI classification and measurement of equity investments that do not qualify for equity method accounting, we oppose a model that does not consider a company's long-term business strategy for holding an equity investment. The Proposed ASU states that the intention of the new model is to link "the measurement of financial assets to the way in which an entity expects to benefit from the cash flows embedded in those assets." Reflecting on this overall objective, the Proposed ASU's separate model for debt and equity securities overemphasizes an instrument's legal form.

We believe companies should classify equity instruments based on their business models for holding the equity instruments and that consideration should be given to the company's ability and intent to hold or trade the investment. We often hold investments in our sponsored funds for long-term corporate investment purposes, including the implementation of multi-year tax strategies or the seeding of a fund, or for other reasons. Additionally, some equity instruments pay significant dividend yields while others are supported by fixed-income securities (e.g., mutual funds invested in fixed-income securities). Our business strategy for holding these equity instruments may not be for short-term trading gains and losses. In such cases, FV-OCI should be permitted.

Under the proposed framework, the income statement will be affected by the volatility of market appreciation and depreciation for investments the entity intends to hold for more than a short period of time. This volatility in earnings may not reflect the likely realization of actual market gains or losses upon ultimate sale of the investment. We note that financial statement users have expressed concerns over the income statement recognition of unrealized gains and losses on equity instruments that are not held for trading purposes. They believe that recognition of those unrealized gains and losses may reduce the usefulness of the financial statements as this accounting does not reflect actual operating results or economic reality. Such financial statement users have indicated they may require non-GAAP disclosures to exclude these amounts from net income.

The principle underlying the current U.S. GAAP model regarding consideration of a company's ability and intent to hold or trade marketable equity securities, as supplemented by diligent impairment monitoring, is well understood by preparers and users alike and should be retained for equity investments. With the recent enhancements to the presentation and disclosure requirements for other comprehensive income and fair value measurements, we believe information regarding the fair value of these equity investments and the unrealized gain or loss positions as of a balance sheet date are highly transparent to users of our financial statements and, therefore, eliminating the concept of a company's ability and intent to hold or trade marketable investment securities is unnecessary.

The Board and the IASB provided additional guidance, as noted in BC112-114 (the Board) and BC 47-48 (the IASB), that permits the application of the cash flow characteristics for beneficial interests in securitized financial assets. The Board and the IASB both observed that the contractual features of a beneficial interest "would not capture the economic characteristics of the instrument due to credit risk arising from subordination of one tranche to another." As a result, the cash flow characteristics of a pool of financial instruments may enable a tranche to qualify for a measurement attribute other than FV-NI (a look-through concept). Most investment companies issue equity shares or units of beneficial interest, yet may invest in fixed-income securities whose contractual cash flows are solely payments of principal and interest. Some investment companies, such as unit investment trusts and certain defined-maturity trusts, may have a life that coincides with the maturity of underlying fixed-income investments. Proposed ASU 825-10-35-13 requires that equity investments shall measure all changes at FV-NI. This requirement seems inconsistent with the look-through concept and should be reconsidered. While investment companies carry their assets at fair value, certain institutional investors may purchase those shares or units because they expect to hold the shares or units to maturity and because they seek the underlying contractual cash flows.

Finally, we note that the Proposed ASU is a significant divergence from IFRS 9, *Financial Instruments*, which provides the ability to elect FV-OCI accounting for equity investments that are not held for trading. We strongly urge the Board to reconsider permitting FV-OCI for equity investments in circumstances when an entity's business strategy is not to hold for trading purposes. If the Board decides not to allow FV-OCI for equity investments that are not held for trading, we strongly encourage the Board to allow a look-through approach which would result in FV-OCI accounting for certain equity instruments when the underlying investments generate cash flows that are consistent with payments of substantially principal and interest (as described above) and the FV-OCI requirements within the Proposed ASU.

III. Scope of the Proposed ASU – Application of Specialized Accounting for Investment Companies

We support the FASB's retention of specialized industry guidance for investment companies set forth in ASC 825-10-15-9(b) and the exclusion of an investment company's investments in debt and equity securities from the scope of the Proposed ASU. We believe, however, that the Proposed ASU unintentionally excluded an investment company's purchased loans and other financial assets and liabilities from the scope exception and ask the Board to include an explicit scope exception for these instruments as well as the proposed disclosures.

IV. Consistent Accounting Treatment for Consolidated Collateralized Financing Entities

We urge the Board to reconsider its fair value option decisions. We believe that IFRS 9's fair value option criteria, which allow an entity to opt to measure financial assets at fair value rather than amortized cost in an effort to eliminate accounting mismatches between assets and liabilities, is appropriate and should be included in the Proposed ASU.

Many asset managers consolidate collateralized financing entities ("CFEs"). Consolidated CFEs have various models by which the collateral pools can be managed, yet these CFEs have a similar overarching business model of returning cash flows generated by the underlying collateral pool to the beneficial interest investors regardless of how the cash flows are achieved. The collateral management models are typically dictated by the governing documents of the CFE. For example, a CFE may manage its collateral pool on a fair value basis ("market value CFE"). Other CFEs may be managed considering the expected cash flows of the collateral pool at deal origination ("cash flow CFEs"). Cash flow CFEs may have either static collateral pools or discretionary collateral pools. Collateral within a static pool is typically not sold prior to maturity unless credit deteriorates, whereas discretionary collateral pools allow a collateral manager to sell collateral for reasons other than credit deterioration.

Applying the principles set forth in the Proposed ASU to consolidated CFEs may result in a mixed classification measurement model for consolidated CFEs. We believe the Proposed ASU would require FV-NI classification for market value CFEs, AC classification for cash flow CFEs with static collateral pools and FV-OCI for cash flow CFEs with discretionary collateral pools. For CFEs qualifying for FV-OCI accounting, an entity may elect the fair value option. In addition, the Proposed ASU section 825-10-35-11 allows nonrecourse financial liabilities to be measured on the same basis as the related financial assets.

We believe that most asset managers that currently consolidate CFEs are carrying the assets at FV-NI as a result of the reporting entity's fair value option election irrespective of the type of CFE. Additionally, given the fair value model, impairment analysis and amortization/accretion processes are not necessary. Disallowing the election of the fair value option for cash flow CFEs would introduce unnecessary additional complexity and require credit impairment analyses for static pools of cash flow CFEs as well as separate calculations of accretion and amortization. Currently, accretion and amortization are not calculated for assets of these CFEs as the assets' fair value changes are reflected in net income. The Proposed ASU would require reporting entities to expend significant effort to rebuild the CFE's amortized cost and credit allowance to arrive at the cumulative adjustment necessary at transition and subsequent thereto. Therefore, we ask the Board to retain the fair value option for cash flow CFEs.

To the extent the FASB does not allow the fair value option for cash flow CFEs, recent decisions reached under Emerging Issues Task Force Issue No. 12-G "*Accounting for the Difference between the Fair Value of the Assets and the Fair Value of the Liabilities of a Consolidated Collateralized Financing Entity*" may need to be revisited as they only apply in situations where the reporting entity measures the consolidated financial assets and financial liabilities of a CFE at FV-NI.

V. Disclosures

We agree with the FASB's proposal to group financial assets and liabilities separately on the face of the statement of financial position by measurement category. However, we believe that the proposed parenthetical disclosures of fair value and amortized cost and disclosures associated with components of investment income would be better suited in the footnotes to the financial statements. When coupled with the other pending changes discussed in the projects for revenue recognition, insurance contracts and leases, we believe this parenthetical presentation would result in lengthy, cluttered and confusing financial statements. Under U.S. GAAP disclosure requirements, users of the financial statements currently obtain detailed information regarding fair value, amortized cost and income statement impact within the footnotes to the financial statements. Accordingly, we suggest the FASB allow entities the option to include these disclosures either parenthetically on the face of the statement of financial position and income statement or in the notes to the financial statements.

VI. Transition and Effective Date

We concur with the Board's proposal requiring a prospective transition. We also agree that early adoption should not be permitted as differences in adoption dates would decrease comparability. We believe that the effective date of the amendments should be the same for both public and non-public reporting entities to avoid comparability issues as well as differences between a parent's consolidated and subsidiary's standalone financial results.

Due to the interrelated nature of the Proposed ASU and the concepts covered in the Proposed ASU, *Financial Instruments – Credit Losses (Subtopic 825-15)*, we suggest the Board include concurrent effective dates for both proposals no earlier than January 1, 2017.

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We appreciate the opportunity to provide comments on the Proposed ASU. Should you have any questions, please feel free to contact any of the representatives below.

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