

October 7th, 2019

Mr. Shayne Kuhaneck
Technical Director
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116

By email: director@fasb.org

Re: File Reference Number 2019-770, Exposure Draft, Reference Rate Reform (Topic 848)

Dear Mr. Kuhaneck,

The International Swaps and Derivatives Association's (ISDA)¹ Accounting Policy Committee appreciates the opportunity to comment on the Financial Accounting Standards Board's (FASB) Exposure Draft, *Reference Rate Reform* (Topic 848) (the Exposure Draft). Collectively, the Committee members have substantial professional and practical expertise addressing accounting policy issues related to financial instruments. This letter provides our organization's overall views on the Exposure Draft and our responses to the questions for respondents included within the Exposure Draft.

Overview

ISDA supports the FASB's proposals in the Exposure Draft to provide optional expedients and exceptions to applying certain generally accepted accounting principles (GAAP) to contracts, hedging relationships, and other transactions that will be affected by reference rate reform. We believe the Exposure Draft achieves the FASB's objective to ease the burden in accounting for (or recognizing the effects of) reference rate reform on financial reporting in response to concerns about structural risks of interbank offered rates (IBORs).

¹ Since 1985, the International Swaps and Derivatives Association has worked to make the global derivatives markets safer and more efficient. ISDA's pioneering work in developing the ISDA Master Agreement and a wide range of related documentation materials, and in ensuring the enforceability of their netting and collateral provisions, has helped to significantly reduce credit and legal risk. The Association has been a leader in promoting sound risk management practices and processes, and engages constructively with policymakers and legislators around the world to advance the understanding and treatment of derivatives as a risk management tool. Today, ISDA has over 850 member institutions from 67 countries. These members comprise of a broad range of derivatives market participants, including corporations, investment managers, government and supranational entities, insurance companies, energy and commodities firms, and international and regional banks. In addition to market participants, members also include key components of the derivatives market infrastructure, such as exchanges, intermediaries, clearing houses and repositories, as well as law firms, accounting firms and other service providers. ISDA's work in three key areas – reducing counterparty credit risk, increasing transparency, and improving the industry's operational infrastructure – show the strong commitment of the Association toward its primary goals; to build robust, stable financial markets and a strong financial regulatory framework. Information about ISDA and its activities is available on the Association's web site: www.isda.org.

International Swaps and Derivatives Association, Inc.

10 East 53rd Street, 9th Floor
New York, NY 10022

P 212 901 6000 F 212 901 6001

www.isda.org

NEW YORK	WASHINGTON
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HONG KONG	SINGAPORE
TOKYO	

In particular, ISDA is supportive of the proposed targeted improvements, including:

- Allowing entities to account for changes as a result of reference rate reform on a prospective basis;
- Not requiring a re-assessment of embedded derivatives for bifurcation for contracts affected by reference rate reform under Topic 815, *Derivatives and Hedging*;
- Allowing entities to modify the critical terms affected by reference rate reform of items within a designated hedging relationship under Topic 815 without requiring de-designation of the hedge;
- Providing optional expedients for existing fair value hedging relationships under Topic 815 for which the derivative designated as the hedging instrument is affected by reference rate reform; and
- Providing optional expedients for existing cash flow hedging relationships under Topic 815 for which either or both the forecasted hedged transaction and the derivative designated as the hedging instrument are affected by reference rate reform.

In the remainder of this letter, we provide specific comments on the Exposure Draft. We believe there are aspects of the Exposure Draft that would benefit from additional clarification in order to avoid unintended consequences. We have also responded to the Questions for Respondents in the Appendix of this letter.

Substantive Comments for Clarification

Reference Rate Reform - Overall Scope

The scope in ASC 848-10-15-3 states that this Topic “shall apply to contracts or other transactions that reference the London Interbank Offered Rate (LIBOR) or a reference rate that is expected to be discontinued as a result of reference rate reform.” We believe the proposed guidance already includes sufficient scoping criteria for when the guidance can be applied (ASC 848-10-15-3 to 15-4) and therefore believe a principles-based sunset provision would be more appropriate. As currently drafted, the FASB has acknowledged that the selected sunset date of December 31, 2022 is based on the expected timing of LIBOR discontinuance. This US-centric approach is not consistent with providing global relief from reference rate reform, as different jurisdictions are in different lifecycle stages of identifying, approving and implementing replacement reference rates. For example, certain interest rates such as EURIBOR or TIBOR may eventually be discontinued but potentially not before the sunset date proposed in the Exposure Draft (or the certain date may not be known). It is also possible that certain IBORs may continue to exist in parallel with their replacement rates for a period of time.

Our members believe timely issuance of this relief guidance is important; therefore, we recommend the FASB issue this guidance without a specific sunset date. This will allow the Board to monitor and deliberate whether to set a more appropriate sunset date, or alternatively, to provide more principles-based guidance whereby an instrument is no longer within the scope of the guidance once it references a replacement rate, which will be a market-driven change for each instrument, and not a unilateral decision.

Instead of a sunset date, the FASB could use an approach similar to that used in Statement of Financial

Accounting Standard No. 150, *Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity*, where the provisions of the standard would apply indefinitely, pending further Board action. This would allow the Board to monitor reference rate reform and determine when and if the guidance should be removed. We also recommend that the Board provide a minimum period of time that the guidance will continue to apply (such as two years) once the Board decides to remove the guidance so that entities can plan ahead for its transition efforts.

Reference Rate Reform - Contract Modifications

Changes to Terms Related and Unrelated to the Replacement of Reference Rate

The Exposure Draft proposes to provide relief for the modification of terms due to reference rate reform and includes examples of terms in ASC 848-20-15-5 and 15-6 that are deemed to be related and unrelated, respectively, to reference rate reform. We believe it is important to explicitly state that immaterial changes will not preclude an entity from applying this guidance. We also believe it is important to state that the intention of the relief is to lessen the accounting impact of market-wide IBOR transitions. As such, we recommend the following clarifications or confirmations to make the relief operable and in line with the project's intent and objectives.

We believe there should be a presumption that any change to the critical terms outlined within ASC 848-20-15-5 is related to reference rate reform, unless there is evidence to the contrary. This would make the guidance more operable and auditable, as it would set the burden of evidence that must be provided by preparers at a more appropriate level. For example, we believe it would be more appropriate to have a presumption that spread adjustments are related to reference rate reform unless there is substantial evidence to the contrary as opposed to a presumption that they represent a new credit or underwriting decision.

The FASB should also clarify in ASC 848-20-15-5(a) that changes to a fixed rate are permitted and that changes to a new index interest rate as a result of reference rate reform are presumed to not include leverage. Market-based fallback language, as established by the Alternative Reference Rates Committee² (ARRC), permits entities to move to a borrower or lender-specified rate, which could include a fixed rate. We believe such contracts should not be precluded from applying the relief when they are in compliance with voluntary market-based fallback language.

ASC 848-20-15-6(h) should also include a presumption that the examples listed therein are changes unrelated to reference rate reform, but that presumption may be overcome based on specific facts and circumstances. For example, a debt instrument may be modified to include the addition or removal of a prepayment option if certain characteristics of the market (i.e. term rates) do not develop before the application of the fall back language. In addition, market fallback language, as established by the ARRC, suggests entities may incorporate a prepayment option in the event an alternative term rate is not established.

In addition, related to the spread adjustment discussed above, we recommend that the FASB clarify in the Basis for Conclusions that any market-supported approach for determining a spread adjustment is permitted, such as using a forward-looking approach for cash products and a historical mean/median

² ARRC is a group of private-market participants convened by the Federal Reserve Board and the New York Fed to help ensure a successful transition from U.S. dollar (USD) LIBOR to a more robust reference rate, its recommended alternative, the Secured Overnight Financing Rate (SOFR). The ARRC is comprised of a diverse set of private-sector entities that have an important presence in markets affected by USD LIBOR and a wide array of official-sector entities, including banking and financial sector regulators, as ex-officio members.

approach for derivatives. We also suggest that the FASB clarify that changes to a counterparty credit spread are presumed to be unrelated to reference rate reform, which would align with BC28.

As it relates to modifications of terms unrelated to reference rate reform, the Committee believes it was not the Board's intent to exclude existing novation guidance, and therefore, recommends that the Board clarify that an entity may change counterparties as permitted in current US GAAP and not be precluded from applying the optional expedients. If the change in counterparty is made contemporaneously with other changes related to reference rate reform that would qualify under ASC 815-20-55-56A, we believe that if the timing and amount of cash flows does not change, the change in counterparty should be permissible.

Based on our comments above, please see our proposed edits to the Exposure Draft.

ASC 848-20-15-5 Changes to terms that are related to the replacement of the reference rate are those that are made to effect the transition for reference rate reform. Changes to terms on the list below are presumed to be related to reference rate reform unless there is substantial evidence to the contrary. Examples of changes to terms that are related to the replacement of a reference rate in accordance with the guidance in paragraph 848-20-15-2 include the following:

ASC 848-20-15-5(a) ...from London Interbank Offered Rate [LIBOR] to another interest rate index or a fixed rate. A change from one interest rate index to another is presumed to not introduce leverage to the underlying instrument.

ASC 848-20-15-5(b) Changes to a spread adjustment for the ~~difference between the existing reference rate and the~~ replacement reference rate

ASC 848-20-15-6 ... Examples of changes to terms that are presumed to be unrelated to the replacement of a reference rate in accordance with paragraph 848-20-15-3 include the following... This presumption may be overcome with specific facts and circumstances.

ASC 848-20-15-6(d) Changes to the counterparty credit risk or risk premium spread (other than an adjustment of the overall spread to include the spread adjustment described in paragraph 848-20-15-5(b))

ASC 848-20-15-6(i) The addition or removal of a feature that is intended to provide leverage feature."

ASC 848-20-15-6(l) Changes to the counterparty to the agreement except where contemplated by other guidance (for example, ASU 2016-05, 815-20-55-56A and 815-30-40-1A).

Scope of Modifications

It is our understanding that the relief provided in ASC 848-20-15-2 should be applied at the Topic level. Our interpretation is that amendments that are not in scope of ASC 848-20-15-2 would not preclude entities from applying this relief to other amendments covered by that Topic. For example, if a modification is made that does not qualify for relief under ASC 848-20-15-2, this out-of-scope modification would not preclude entities from applying the relief to any other instrument covered by that Topic that would otherwise qualify for the relief. We suggest the following edits to clarify the Board's intent:

ASC 848-20-35-1 An entity may elect to apply the guidance in this Subtopic to account for contract modifications that meet the scope of paragraphs 848-20-15-2 through 15-3. If an entity

elects to apply the guidance in this Subtopic, the entity shall apply it for all contract modifications that meet the scope of paragraphs 848-20-15-2 through 15-3 that otherwise would be accounted for in accordance with the same Topic or Subtopic (including the intersecting Subtopics within the Industry Topics). That is, if some contracts within a specific Subtopic do not meet the scope requirements, those contracts governed by the same Subtopic that do meet the scope requirements are not precluded from applying the optional relief.

Debt Exchanges or Modifications within a Year

We believe the intent of this relief is to permit entities to only consider modifications subsequent to the application of the optional relief to be contemplated under current US GAAP guidance and therefore suggest the following edit in line with the relief's intent.

ASC 848-20-35-9 If the optional expedient in paragraph 848-20-35-7 is elected, an entity that applies the 10 percent cash flow test described in paragraph 470-50-40-10 for any subsequent contract modifications shall consider only the contract modifications made subsequent to the application of the optional relief.

Reference Rate Reform - Hedging

Scope of ASC 848 on Net Investment Hedging Relationships

We note that net investment hedges are referenced in the Summary of the Exposure Draft but are not discussed in the Codification amendments. As such, we suggest the following edit.

ASC 848-10-05-1 The Reference Rate Reform Topic includes the following Subtopics:

f. Net Investment Hedges

Cross-currency Basis Spread for Cross-currency Swaps

We believe that the optional relief should also be available for cross-currency swaps. When a cross-currency swap is executed, the initial cross-currency basis is observable and reflected in the contractual terms of the swap. Thereafter, if the instrument was designated in a fair value hedge where cross-currency basis was an excluded component, an entity may elect to record the changes in the value of the derivative associated with cross-currency basis in other comprehensive income (OCI), while the originally observed basis is recognized in earnings on a systematic and rational basis. As noted in the Basis for Conclusions of ASU 2017-12, no explicit amortization is necessary for at-market cross-currency swaps because the initial value of the cross-currency basis spread is systematically and rationally amortized to earnings through the interest accrual process.

When the floating leg(s) of a cross-currency swap changes from referencing existing IBOR rates to referencing replacement reference rates, the resulting cross-currency basis spread could differ, and it is possible that this could occur more than once (e.g., if the interest rate indices for each leg of a float-to-float cross-currency swap differ with regard to transition timing). Because cross-currency swaps referencing replacement rates are not yet trading, it is not yet possible to determine the cross-currency basis spread with a reasonable degree of certainty, and therefore, it is not possible to quantify any potential differences. To avoid having any aforementioned cross-currency basis spread amounts stranded in OCI at the end of the hedging relationship, we request a solution that gives entities flexibility with the changes in the cross-currency basis spread. Specifically, we recommend that the FASB allow an election for entities to amend the accounting policy application around the systematic and rational method used

for amortizing the excluded cross-currency basis spread to ensure amounts are not stranded in OCI at the end of the hedging relationship, including an election to record the change in value of the derivative due to a change in the cross-currency basis spread under IBOR and the alternative reference rate immediately to earnings.

Cash Flow Hedges

The proposed guidance in ASC 848-50-35-2 states that an entity shall assess the hedging relationship using the optional expedient method prospectively beginning on the date the expedient method is first applied.

For existing IBOR-based cash flow hedges that include forecasted variable payments that extend past the expected reference rate transition date for the hedged item, we believe that the future expected payments of the hedged item that will be based on a new contractually-specified rate may be referenced to support the entity's assertion that the hedged forecasted payments remain probable of occurring. We suggest the following edits to ASC 848-50-35-18:

ASC 848-50-35-18 If an entity applies an optional expedient method for assessing hedge effectiveness in accordance with paragraphs 848-50-35-1 through 35-16, and the hedging relationship is expected to continue after the entity ceases applying the optional expedient method, the entity shall revert to applying the qualifying criteria and hedge assessment methods in Subtopics 815-20 and 815-30. For a hedging relationship that continues after ceasing application of an optional expedient method, an entity shall apply a hedge assessment method in accordance with Subtopics 815-20 and 815-30, both prospectively and retrospectively, from the date on which that assessment method is first applied. The forecast future payments that are expected to be based on a new contractually-specified rate or rates may support the entity's assertion that the hedged forecasted payments remain probable of occurring. For example, an entity that has elected to apply the shortcut method optional expedient for a new cash flow hedging relationship in accordance with paragraph 848-50-25-6, or for an existing cash flow hedging relationship in accordance with paragraph 848-50-35-5, shall revert to a hedge assessment method in accordance with Subtopics 815-20 and 815-30 in assessing whether the hedging relationship continues to qualify for hedge accounting from the date that the new assessment method is first applied.

We believe the FASB's intent in ASC 848-50-35-15 is to allow entities to assume that the hypothetically perfect derivative references a new contractually-specified rate on the same date the hedged forecasted transactions will reference a new contractually-specified rate. As such, we request the following edits.

ASC 848-50-35-15 If either the hedged forecasted transaction or the hedging instrument references a rate that meets the scope of paragraph 848-10-15-3, the terms of the hedged forecasted transaction may be altered to match the hedging instrument for the following (that is the hypothetically perfect derivative is permitted to be altered to reflect a change to a successor rate at the same time that the forecasted hedged transactions will reference the successor rate.)

Shortcut Method

We note that under ASC 848-40-25-8, if an entity elects the practical expedient for an existing fair value hedge for which the shortcut method is applied, the entity will not be required to periodically evaluate the conditions in ASC 815-20-25-104 for the remaining life of the hedging relationship. There does not

appear to be a similar “grandfathering” with respect to the conditions in ASC 815-20-25-105 for fair value hedges, and there does not appear to be any grandfathering for cash flow hedges that apply the shortcut method in accordance with ASC 815-20-25-104 and 106.

As a result, it is not clear if it is the FASB’s intention for certain fair value and cash flow hedging relationships that apply the shortcut method to cease to qualify for the shortcut upon any expiry of the practical expedients (see comments elsewhere in this letter related to the sunset provision). Given the generally uncomplicated nature of hedge relationships that qualify for the shortcut method and the fact that entities applying the shortcut method commonly may only have one or a few hedging relationships and a limited ability to apply “long-haul” effectiveness assessment techniques, we believe the grandfathering of the shortcut method fair value hedges to not require a periodic evaluation of the conditions under ASC 815-20-25-104 should be expanded to include cash flow hedges under the shortcut method and also should include the conditions in ASC 815-20-25-105 and 106 for fair value and cash flow hedges, respectively. Absent such grandfathering, the practical expedients will ultimately provide no relief from reference rate reform for hedges that apply the shortcut method, as entities will ultimately not qualify to apply the shortcut method without the targeted relief on a delayed basis. If it is the intent of the FASB to only provide temporary relief for these shortcut method hedges, transition and subsequent measurement guidance should be provided for these hedging relationships.

Reference Rate Reform - Disclosures

Currently, public entities disclose information about IBOR transition in the MD&A section of their SEC filings. This information includes background on why IBORs are being replaced, a description of products that reference IBORs, the risks an entity may face in transition, and high-level plans for the entity to adapt to the replacement of an IBOR. Given the uncertainty regarding this transition, entities provide information that is known or expected at the time of reporting, as well as considerations of current factors that are expected to be updated to provide additional relevant information in a timely fashion.

There are currently no disclosure requirements in US GAAP regarding an entity’s exposure to specific variable interest rates, such as IBORs. We believe any quantitative disclosures related to our exposure or risk to IBORs would contain a level of uncertainty given the current and future uncertainty around reference rate reform and adoption, which most public companies currently disclose as risk factors and within MD&A. Additionally, quantitative disclosures of information related to contract modifications executed in connection with IBOR reform would be a requirement that is above and beyond what is required in US GAAP today and would negate the value of the relief the FASB has provided. There is no required disclosure associated with minor contract modifications or interest rate resets today, and quantitative disclosures related to this information would be operationally burdensome given the processes and robust controls that would need to be developed and implemented in order to compile this information in a timely and accurate manner. Of additional concern, the costs associated with generating these disclosures would far outweigh the benefits, as there will be no need for these disclosures after the relatively short period remaining before the completion of reference rate reform.

Quantitative disclosures as proposed in paragraph BC91 would require implementation of proper SOX controls in order to ensure that disclosures are accurate. The time required to implement such controls could extend beyond the end of the relief for certain jurisdictions and would use resources that otherwise could be used to focus on effecting a smooth transition.

As a result, we believe entities will be able to provide relevant and informative qualitative disclosures on a timely basis, which would be more cost effective for preparers and more decision-useful than quantitative disclosures for investors. We are not aware of quantitative information we could provide about our IBOR exposures that would be useful to investors above and beyond what is included in our footnotes today. For example, derivative notional for interest rate contracts and hedge basis adjustments are already disclosed today, and specifically disclosing the amount of these exposures that will be impacted by IBOR reform would be hard to disclose accurately and would not be decision-useful.

In addition, the SEC has already released public statements providing specific disclosure guidance from the SEC's division of Corporate Finance, Investment Management, and Trading and Markets and its Office of Chief Accountant noting that they are reviewing disclosures of preparers. As such, we believe the guidance from the SEC will be sufficient for disclosures regarding IBOR reform.

Our members also would suggest clarifying the disclosures that will be required for private companies under Topic 848. Per paragraph 89 of the Basis for Conclusions, the effective date of this guidance will be the same for public and private companies. We suggest involving the Private Company Council when considering which disclosures should be required.

Other/Editorial Comments

1. The amendments in this proposed update would be effective upon issuance of the final update, which is expected to be Q1 2020. Our members believe an effective date at the beginning of the period would be more efficient. Changing the effective date to the beginning of the reporting period does not appear to have an impact to hedge accounting but may affect the election of the contract modification relief. Entities may be more inclined to insert fallback language right after year end if they know that the relief can be applied to the beginning of the period.
2. The guidance in ASC 848-20-15-5(c) includes the following example of a change that is related to the replacement of a reference rate, stating, "a change from a forward-looking term rate to an overnight rate or a compound overnight rate in arrears with the same payment frequency." Our members believe this requirement may have unintended consequences. For example, if entities move from 3M LIBOR to overnight SOFR, the payment frequency may not be the same due to different conventions between the rates. Please see our proposed edit to this paragraph below.

ASC 848-20-15-5(c) Changes to reset period, reset dates, day-count, business-day conventions, payment dates, and repricing calculation (for example, a change from a forward-looking term rate to an overnight rate or a compounded overnight rate in arrears ~~with the same payment frequency~~).

3. BC 26 states, "In proposing that entities would be required to consider whether modifications of terms that affect or have the potential to affect the amount or timing of future cash flows are related to reference rate reform, the Board was intentionally broad such that this criterion would capture any changes in terms that could have a potential effect on future cash flows in certain circumstances, such as changes to collateral arrangements, changes in the priority of an obligation, and changes to debt covenants." We observe that if an entity is modifying terms such as collateral or priority, there would likely be changes to cash flows upon such an event (e.g. a reduction in priority would likely lead to an increased coupon or other consideration), which would already be captured by the scoping guidance as drafted. That said, it is not clear whether the expanded articulation of the Board's intent in this manner is necessary and in fact could make the relief less operable. For

example, the guidance in ASC 815-40-15 and 40-25 related to equity indexation and classification is difficult to apply in practice given the breadth of scenarios that must be considered (e.g., anything that *could* occur, no matter how remote). Therefore, while we appreciate the Board's intent, we ask that it consider refining this discussion to avoid unintended consequences. We also recommend that the FASB remove the reference to collateral arrangements because under current GAAP and market practice, aspects of collateral that secure derivatives (e.g., currencies, eligible assets, etc.) are not considered to be critical terms of the derivative itself.

4. We recommend adding the following provision to ASC 848-20-15-3 to allow for additional flexibility.

ASC 848-20-15-3 The guidance in this Subtopic shall not apply if a contract modification is made to a term that changes, or has the potential to change, the amount or timing of contractual cash flows and is unrelated to the replacement of a reference rate. That is, this Subtopic shall not apply if contract modifications are made contemporaneously to terms that are unrelated to the replacement of a reference rate. However, reasonable judgment should be applied to assess whether contract modifications are minor or minimal (for example, the maturity date of a loan changed by a few days)

Additionally, if immaterial changes to the contract are permissible, we note that the scope of the proposed guidance does not scope in the modification tests for revolving line of credit agreements. Our members believe immaterial changes should not preclude application of this guidance, and as a result, there should also be a reference to the "line of credit test" for revolvers (ASC 470-50-40-21) in this proposed guidance.

5. The guidance in ASC 848-20-35-2 discusses optional expedients for Topic 310, Topic 470 and Topic 842; however, it does not mention anything regarding Topic 320 or Topic 321 (debt and equity securities). Considering that this population of affected contracts is relevant for a significant number of our members and their clients, we suggest stating explicitly that these Topics are also within the scope of the relief despite the "catch-all" guidance provided in ASC 848-20-35-3. In addition, given the lack of existing guidance in US GAAP regarding the modification of equity classified preferred stock instruments, we suggest similar explicit guidance for equity-classified preferred stock. We suggest the FASB address these instruments explicitly or add them to the examples in the table in ASC 848-20-55-2.
6. BC52 states, "Because a change in the designated benchmark interest rate is not allowed in current GAAP." Our members recommend removing this statement from the Basis for Conclusions because there are cases in current GAAP (i.e. in accordance with ASU 2017-12) where a change in the designated benchmark interest rate is permitted.
7. The proposed guidance in ASC 848-30-25-6 states, "A change to the interest rate used for margining, discounting, and contract price alignment for a centrally cleared derivative that is an existing hedging instrument shall not be considered a change to the critical terms of the hedging relationship that requires dedesignating the hedging relationship due to that change." As written, our members are concerned that this guidance could be interpreted to exclude OTC derivatives, and price alignment is only meant to apply to centrally cleared derivatives. We do not believe this was the FASB's intent and, therefore, request clarification as follows:

ASC 848-30-25-6 A change to the interest rate used for margining, discounting, or contract price alignment for a ~~centrally cleared derivative that is~~ an existing hedging instrument shall

...

8. The proposed guidance in ASC 848-30-25-3 would require an entity to add an addendum to its hedge documentation noting the changes made to the hedging relationship by the time it performs its first assessment of effectiveness after the change is executed. The FASB did not require such documentation for transition elections when entities adopted ASU 2017-12, which instead allowed entities flexibility in how they documented the changes. We believe a requirement for entities to add an addendum to each relationship is too specific, and the FASB should provide entities flexibility with respect to documentation so they can follow any standard practices for how they prepare and document hedge programs and hedge relationship documentation (i.e. at the transaction level or policy level). Our members believe that an overlying adoption of the optional expedients will cover this documentation requirement and that specific hedge level documentation is not required.
9. ASC 848-40-25-2 states, “In an existing hedge of the changes in fair value attributable to the benchmark interest rate, if the referenced interest rate index of the hedging instrument changes or an entity changes the designated hedging instrument to combine two or more derivative instruments to be jointly designated as the hedging instrument in accordance with paragraph...” We request that the FASB clarify that the ability to layer on new basis swaps is explicitly permissible under this guidance.

ASC 848-40-25-2 ...to combine two or more derivative instruments (e.g., a new basis swap and an existing interest rate swap) to be jointly designated.

Closing

We hope you find ISDA’s comments and responses informative and useful. Should you have any questions or desire further clarification on any of the matters discussed in this letter please do not hesitate to contact the undersigned.

Jeannine Hyman
Citigroup Inc.
Chair, North America Accounting Committee

Antonio Corbi
ISDA, Inc.
Director, Risk and Capital

*Appendix**Responses to FASB's Questions for Respondents**General*

Question 1—Costs and Complexities: Are the amendments in this proposed Update operable and auditable? If not, which proposed amendment(s) pose operability or auditability issues and why?

Yes, the amendments are operable and auditable when our proposed edits are considered. Specifically, as it relates to determining the adjustments to the spreads, we believe there may be audit challenges when applying the guidance as written. Under the proposed guidance, it may be difficult to audit and verify that a spread adjustment is related entirely to reference rate reform and not to the counterparty's credit. We believe the guidance in ASC 848-20-15-5 should include a statement indicating there is a presumption that any change is related to reference rate reform unless there is evidence to the contrary. Without such a presumption, there could be minor differences by basis points that could result in extensive additional audit work and costs.

Question 2—Additional Issues: Are there additional accounting issues or optional expedients related to reference rate reform that the Board should consider? Please be as specific as possible and explain why those issues require consideration.

Please see substantive comments above as it relates to cross-currency basis excluded from fair value hedges and recorded to OCI.

As an additional matter, the Committee believes that as part of the transition of price alignment, discounting, and margining of derivatives, central clearing houses are expected to compensate parties for the difference in discount rates for impacted derivatives such that the process is neutral from a net economic effect perspective (i.e., based on the net derivative exposure under one master netting agreement). An ability to allocate this compensation to each individual derivative and/or hedge relationship may be operationally burdensome and, therefore, we ask for an ability to make an election to ignore the effect of the change in discount rates (and make whole) as it relates to derivatives in hedging relationships, and instead, to present all fair value changes and compensating amounts directly where trading derivatives are presented. Any future changes will be presented in the line item where the hedging presentation is required.

Finally, under reference rate reform, in certain circumstances, a floating-rate debt security that references a to-be-discontinued IBOR will contractually convert to a fixed-rate coupon. If an entity has classified any such debt security as Held-to-Maturity ("HTM"), the entity will be precluded from selling the security or designating the security in a fair value hedge of its benchmark interest rate risk. As a result, for these securities, entities will have no ability to respond to the impact of reference rate reform. To address this unanticipated concern, we recommend that the FASB provide specific targeted relief to allow entities a one-time election to transfer any such securities out of the HTM classification, as holding such fixed-rate securities to maturity may be inconsistent with the entity's risk management strategies and objectives. We do not believe this targeted relief will have a significant impact on entities with HTM portfolios.

Contract Modifications

Question 3—Expedients: Do you agree with the proposed expedients for the accounting for contract modifications? If not, please explain which proposed amendment(s) you disagree with and why.

Yes, we generally agree with the proposed expedients for contract modifications. Please see comments above for clarification regarding the spread adjustments.

Question 4—Election Level: Do you agree that the optional expedients for contract modifications should be applied at the relevant Topic, Subtopic, or Industry Subtopic level? If not, what alternative do you suggest and why?

Yes, we agree the optional expedients for contract modifications should be applied at the Subtopic level. See comments for clarification above related to certain Topics and Subtopics unaddressed in the proposed guidance.

Hedge Accounting

Question 5—Change in Critical Terms: Do you agree with the proposed exceptions to the requirement in Topic 815 to dedesignate a hedging relationship for a change in critical terms of the hedging relationship? If not, please explain which proposed amendment(s) you disagree with and why.

Yes, we generally agree with the proposed exceptions to the requirement in Topic 815 to dedesignate a hedging relationship for a change in critical terms of the hedging relationship. Please see comments above for clarification.

Question 6—Fair Value Hedges: Do you agree with the proposed optional expedients for fair value hedge accounting? If not, please explain which proposed amendment(s) you disagree with and why.

Yes, we generally agree with the proposed optional expedients for fair value hedge accounting. Please see comments above for clarification.

Question 7—Cash Flow Hedges: Do you agree with the proposed optional expedients for cash flow hedge accounting? If not, please explain which proposed amendment(s) you disagree with and why.

Yes, we generally agree with the proposed optional expedients for cash flow hedge accounting. Please see comments above for clarification.

Question 8—Election Level: Do you agree that the proposed exceptions and optional expedients related to hedge accounting should be applied on an individual hedging relationship basis? If not, please explain why.

Yes, we agree the proposed exceptions and optional expedients related to hedge accounting should be applied at the individual hedge relationship level.

Disclosures

Question 9—Contracts or Holdings: What quantitative and qualitative disclosures should be provided to help users understand a reporting entity’s current contracts or holdings (as of the reporting date) that are affected by reference rate reform? For financial statement preparers, what costs would be incurred in providing these disclosures? For financial statement users, what alternative sources of information would be used if a reporting entity does not provide any quantitative and qualitative disclosures? What costs would be incurred to obtain quantitative and qualitative information to better understand a reporting entity’s exposure to reference rate reform? Should the quantitative and qualitative disclosures, if any, have a termination date after December 31, 2022? If not, when should such disclosures expire and why?

Please see comments above for clarification.

Question 10—Hedge Accounting: What quantitative and qualitative disclosures should be provided to help users understand the financial reporting effects of expedients elected by a reporting entity? For financial statement preparers, what costs would be incurred in providing these disclosures? For financial statement users, what costs would be incurred if a reporting entity does not provide any quantitative and qualitative disclosures to help financial statement users understand the financial reporting effects of any hedge accounting expedients elected?

Please see comments above for clarification.

Question 11—Transition: Do the proposed transition disclosure requirements provide decision-useful information? If not, what would you recommend and why?

We do not believe the transition disclosure requirements provide decision-useful information. The nature of and reason for electing to apply the reference rate reform guidance should be self-explanatory, and there is no need to require additional disclosure beyond what is included in MD&A. We do not believe transition disclosure requirements are necessary beyond the usual MD&A disclosure requirements as part of SAB 74 already covered by SEC guidance. Please also see comments above for clarification.

Transition and Termination Date

Question 12—Transition: Do you agree that the proposed optional expedients should be applied on a prospective basis upon election? If not, what alternative do you suggest and why?

Yes, we agree that the proposed optional expedients should be applied on a prospective basis upon election. See comments for clarification above related to assessments of hedge effectiveness if a quantitative method is utilized.

Question 13—Termination Date: Do you agree that the proposed amendments should not apply to contract modifications made and hedging relationships entered into or evaluated after December 31, 2022? If not, when should the proposed amendments expire and why?

Please see comments above.