FIRCA Financial Instruments Reporting and Convergence Alliance

October 15, 2014

The Honorable Hans Hoogervorst
Chairman
International Accounting Standards Board
30 Cannon Street
London, EC4M 6XH
United Kingdom

Re: *Discussion Paper on Accounting for Dynamic Risk Management: A Portfolio Revaluation Approach to Macro Hedging* (DP/2014/1)

Dear Chairman Hoogervorst:

The Financial Instruments Reporting and Convergence Alliance ("FIRCA") is a coalition of business, financial, insurance, and real estate trade organizations representing all sectors of the economy and areas of the financial services arena. FIRCA recognizes that accurate and transparent financial reporting is a cornerstone of our capital markets in the United States and globally.

An important priority of FIRCA is the convergence of accounting standards to create a universal financial reporting language that can be used by investors and issuers domestically and globally. FIRCA appreciates the work of the Financial Accounting Standards Board ("FASB") and the International Accounting Standards Board ("IASB") (also collectively as the "Boards") in attempting to create converged accounting standards on financial instruments and we have filed numerous comment letters with both Boards on the Financial Instruments projects.

While FIRCA is dismayed that it appears that many of the convergence efforts appear to be stalled or falling apart, we continue to believe that a single set of global accounting standards is an important goal that should be achieved to reflect the true global nature of business and investing in the 21st century. Accordingly, FIRCA appreciates the opportunity to comment on the IASB Discussion Paper on *Accounting* *for Dynamic Risk Management: A Portfolio Revaluation Approach to Macro Hedging* (the "Discussion Paper").

FIRCA Mission and Principles

The mission of FIRCA is:

- To support the use of high quality, robust international accounting standards developed and adopted jointly by the IASB and the FASB. These standards should be decision-useful, reliable, and relevant. Additionally, these standards should present financial information in a manner that reflects the business operations of the reporting entity. Appropriately crafted standards should transparently provide information and not drive economic activity.

- To assist standard setters in providing a wide range of input to ensure the proper consideration of business operations and potential unintended consequences in the development and implementation of accounting standards.

- Recognizing the ongoing impacts of the 2008 financial crisis and continued currency pressures in the Euro Zone are global in scope and magnitude, we will continue to work with standard setters and decision makers to ensure that these projects are conducted jointly to provide a comprehensive response to financial reporting policies.

FIRCA supports the premise that accounting and reporting for financial instruments should reflect both a reporting entity's business strategy and the characteristics of the financial instruments:

- Financial statements should help explain the business and its operations; and

- In order to do so, the classification, measurement, and disclosures for financial instruments need to reflect the entity's purpose for holding these assets and liabilities and its strategy for managing them.

Regarding derivatives and hedging, FIRCA supports the following principles:[1]

● Derivatives may be used to hedge:

- Exposures to changes in the fair value of a recorded asset or liability or an unrecognized firm commitment (fair value hedges);
- Exposures to variability in the cash flows of a recognized asset or liability (cash flow hedges);
- Forecasted transactions (forecasted transaction cash flow hedges);
- Net investment in a foreign operation;
- Foreign currency exposure present in other hedging relationships;
- An entire asset or liability, a portion of an asset or liability, a portfolio of homogenous assets, a portfolio of homogeneous liabilities, or a specifically-identified risk inherent in an asset or liability.

● At inception and throughout a hedging relationship, the reporting entity should assess the hedge relationship's effectiveness to ensure the expected economic relationship continues between the hedging instrument and the hedged risk and that changes in fair value of the hedging instrument continue to be reasonably effective (as defined) in offsetting changes in the hedged risk, the variability in hedged cash flows, or foreign currency risk.

● We also support the use of qualitative not quantitative hedge effectiveness testing.

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[1] FIRCA also supports replacing "highly complex, quantitative-based" hedging requirements with more qualitative-based assessments.

   - The ineffective portion of a hedge should be recorded in earnings immediately.

   - If requirements of hedge accounting are no longer met (e.g., the hedge is no longer effective), hedge accounting must be discontinued.

- Hedging instruments may be de-designated and re-designated.

- Derivative assets and liabilities should be carried at fair value on the balance sheet.

- Embedded derivatives should be bifurcated from the host contract and accounted for separately if the economic characteristics and risks of the embedded derivative are not clearly and closely related to the host contract and the embedded derivative has the characteristics of a derivative.

Comments on the Discussion Paper

FIRCA appreciates that IASB recognizes the importance of hedge accounting for both closed portfolios, with the recent publication of International Financial Reporting Standard ("IFRS") 9, *Financial Instruments,* the dynamic risk management of open portfolios and, accordingly dynamic hedging activities especially the need for a specific accounting approach to represent dynamic risk management in entities' financial statements as reflected in the Discussion Paper. FIRCA also understands that various principles underlying the Discussion Paper are consistent with FIRCA's principles, such as allowing for bifurcation by risk.

FIRCA recognizes that the Discussion Paper represents early thinking on the issues, which will evolve. However, FIRCA would like to note that the Discussion Paper in Section 5.4 on page 64 broaches the topic of possible eligibility criteria including hedge effectiveness criteria but does not elaborate on the anticipated testing form and substance. FIRCA recommends that the next exposure document be more specific on whether the tests will be qualitative or quantitative and whether the measurement will be highly effective, reasonably effective, or some other measure. In this regard, the IASB's guidance in Section 6.4.1 of IFRS 9 may provide a useful roadmap. FIRCA encourages IASB to continue to work to resolve these issues in accordance FIRCA's principles. Further, FIRCA urges IASB to continue to recognize that an entity's business model should be a consideration in any final standard.

Conclusion

FIRCA looks forward to continuing our efforts to work with the IASB to achieve our goals of robust accounting standards that reflect the economic activity of business operations in the furtherance of efficient and fair global capital markets. While convergence is a goal that should be attained, it must be done through the crucible of due process that will ensure high quality accounting standards. A failure to achieve high quality accounting standards will guarantee that converged standards will not meet the needs of investors and issuers and will make the global capital markets less efficient.

It is the hope of FIRCA that FASB and IASB can achieve this goal and we stand ready to assist you in doing so.

Sincerely,

American Council of Life Insurers
Barnert Global, Inc.
Mortgage Bankers Association
National Association of Real Estate Investment Trusts
U.S. Chamber of Commerce