Securities Industry Association

120 Broadway, New York, NY 10271-0080, (212) 608-1500, Fax (212) 608-1604
1401 Eye Street, NW, Washington, DC 20005-2225, (202) 296-9410, Fax (202) 296-9775
info@sia.com, http://www.sia.com

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Senator Christopher J. Dodd
SR-534 Dirksen Senate Office Building
Washington, D.C. 20510-6075

Dear Senator Dodd:

The Securities Industry Association's OTC Derivative Products Committee would like to commend you and your staff on the recently released Securities Subcommittee report on Proposals by the Securities and Exchange Commission and the Financial Accounting Standards Board for the Accounting Treatment of Financial Derivatives. The report, based on the Subcommittee's oversight hearing, reflects a reasoned consideration of the complex accounting and reporting issues involved in the SEC and FASB proposals. We strongly concur with the Report's findings and recommendations. In particular, the Subcommittee's recommendation that FASB re-expose its proposals for the Accounting Treatment of Financial Derivatives is timely and provides a compelling argument for FASB reconsideration.

As discussed at the Subcommittee hearing, the Financial Accounting Standards Board (FASB) is in the process of finalizing an accounting pronouncement that will radically change the way businesses report the results of risk management activities. The statement will, in many cases, force companies that have prudently minimized a host of real economic risks to report greater volatility on their financial statements than their competitors who choose to accept such risks.

Accounting experts at the Subcommittee hearing concluded that the proposed rules discriminate against the risk management tools that are the most efficient. These are tools which allow American companies to avoid risks, save money, and become more competitive. Good accounting practices should reflect the economic reality of business activity. This rule does not. Transactions that reduce economic volatility should reduce -- rather than increase -- financial statement volatility.

The FASB exposure draft is, and continues to be, a source of contention rather than consensus among each of the affected constituencies -- accountants, representatives from the investor community, and corporations. The exposure draft that FASB issued on this rule attracted more than 250 comment letters from industrial corporations, financial institutions, professional accounting firms and government regulators. That is an unusually high number of comments on a proposed accounting rule -- and the views expressed were almost universally negative.

We are not alone in expressing these concerns. The Chairmen of the Federal Reserve Board, the Federal Deposit Insurance Corporation, and the Comptroller of the Currency expressed concern to FASB that the rule ". . . may discourage prudent risk management activities and in some cases could present misleading financial information. Therefore, the proposal should not be adopted in its current form."

We believe that FASB should provide adequate due process in order to come up with the best rule possible. SIA's OTC Derivative Products Committee strongly endorses the Subcommittee's recommendation that FASB should re-expose its draft to test its implications thoroughly prior to imposing it as a final pronouncement. FASB should engage its critics in a genuine dialogue over the basic principles that are at stake here. If the Board does so, we believe it will ultimately write a rule materially different than the current version.

Once again, the SIA's OTC Derivative Products Committee would like to compliment the Securities Subcommittee and its staff on dealing with the complex issues presented by the SEC and FASB proposals. The Subcommittee' Findings and Recommendations provide a valuable basis for the continuing debate on these proposals. We look forward to working with the Subcommittee as the debate moves forward to ensure that accounting and disclosure standards are designed to represent economic realities to the benefit of the investing public.

Sincerely,

Zachary Snow
Chairman