



Securities Industry Association

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David Kane
Office of the Chief Accountant
Securities and Exchange Commission
450 Fifth Street, NW
Washington, DC 20549

Re: Phone Call regarding Market Risk Disclosures

Dear David:

I thought that I would send you a brief follow-up to the recent phone call with representatives of SIA's Risk Management and Dealer Accounting Committees and two members of the staff of the International Swaps and Derivatives Association regarding industry experience with the market risk disclosure rule (Item 305 of Regulation S-K). I think we made the following points on the call:

- A. Impact of the Rule on firms' Risk Management Practices -- Generally speaking, the Rule had not significantly impacted firms' use of VaR, since they view their pre-existing practices as fairly robust. One firm reported that the Rule encouraged them to move towards making their VaR calculations somewhat more comprehensive, and to adopt VaR limits at the product level. All the firms stated that VaR is only one risk management tool, and has a number of limits, such as a failure to provide insight into liquidity differences in assets, and a reliance on co-variance, which tends to breakdown in times of market stress.
- B. Competitive Impact of the Rule -- Firms did not experience any competitive impact by reason of the rule's adoption. Concern was expressed, however, that a requirement for a detailed breakdown of VaR by subunits could potentially reveal proprietary information and begin to have a competitive impact. In addition, since firms generally view VaR on a global basis, reporting VaR numbers on the basis of subunits could be potentially misleading as well as possibly risking the disclosure of proprietary information.
- C. Practical Problems with the Rule -- Firms reported no significant practical difficulties in complying with the rule, which they attributed in large part to the flexibility it provides. Since the numbers are not computed on a uniform basis

some readers of financial statements may have some difficulty in using the numbers. However, firms believe that investors do find the numbers useful if they look at the trend of the numbers over time. Firms strongly warned against attempting to enforce comparability by imposing a uniform methodology. Apart from imposing significant compliance costs (since firms would have to change current practices) the result might not be meaningful. For example, it would fail to provide an insight into differences in liquidity of the assets, thus not providing an indication of possible losses in stress conditions. This would provide a very misleading notion of “comparability” among firms.

- D. Do you look at the numbers of your Competitors? – Firms do look at their competitors’ disclosures, but as there is a great deal of “noise” in the numbers, they must be read with an acknowledgement of the limitations listed above.
- E. Have your customers asked for assistance in complying with the Rule? The only requests that firms reported receiving from clients related to assistance in preparing sensitivity analyses.
- F. Have Customers Changed the products they use as a result of the Rule? – The Rule has not really impacted the mix of products sold to customers. Industry representatives confirmed that the market risk rules have not resulted in end-users seeking to use different products, nor have they noticed a shift to or from OTC products as distinct from exchange traded instruments.
- G. Has there been any change in Customer behavior as year-end approached? – Firms reported noticing no change either immediately before or after the beginning of the year that could be attributed to the Rule.

If you have any questions about our response or would like to follow up, please feel free to contact me.

Sincerely,

Gerard J. Quinn
Vice President and
Associate General Counsel