
**AICPA Stockbrokerage and Investment Banking Expert Panel**
**January 2021 meeting highlights**

1. The Expert Panel (EP) members compiled the following draft considerations when SEC-registered broker-dealers develop an accounting policy footnote related to FASB ASC Topic 326:

**The AICPA Stockbrokerage and Investment Banking Expert Panel compiled the following draft potential considerations for SEC-registered broker-dealers as they develop an accounting policy footnote related to FASB ASC Topic 326 – "Financial Instruments – Credit Losses". These are not authoritative positions or interpretations. They have not yet been considered or acted upon by the AICPA FinREC. Individual facts and circumstances could differ based on activities of an SEC-registered broker-dealer. This working draft contemplates a hypothetical broker-dealer's facts and circumstances and does not reflect all disclosures required in FASB ASC 326 under accounting principles generally accepted in the United States of America. This example only illustrates some considerations. This example does not illustrate other disclosures which are required by ASC 326 and other areas of US GAAP.**
**When finalized, information from this working draft will be incorporated into the 2021 edition of the AICPA Accounting Guide *Brokers and Dealers in Securities*.**

The Company accounts for estimated credit losses[1] on financial assets measured at an amortized cost basis and certain off-balance sheet credit exposures in accordance with FASB ASC 326-20, *Financial Instruments – Credit Losses*. FASB ASC 326-20 requires the Company to estimate expected credit losses over the life of its financial assets and certain off-balance sheet exposures as of the reporting date based on relevant information about past events, current conditions, and reasonable and supportable forecasts.

The Company records the estimate of expected credit losses as an allowance for credit losses. For financial assets measured at an amortized cost basis the allowance for credit losses is reported as a valuation account on the balance sheet that is deducted from the asset's amortized cost basis. Changes in the allowance for credit losses are reported in Credit Loss expense.[2]

[1] Individual facts and circumstances could differ based on activities of a SEC registered broker-dealer. This example contemplates this hypothetical broker dealer's facts and circumstances and does not reflect all disclosures required in FASB ASC 326 under accounting principles generally accepted in the United States of America. This example only illustrates some considerations in developing the ASC 326 related content of an accounting policy footnote. This example does not illustrate other disclosures which are required by ASC 326 and other areas of US GAAP.
[2] FASB ASC 326-20-30-1 and 326-20-35-1 require that the establishment of, or subsequent adjustment to, the allowance for credit loss be reported as a credit loss expense or reversal of credit loss expense, therefore the Company should consider the materiality of the exposure when determining the financial statement line item for any amounts to be reported in.

*Financial assets measured at amortized cost basis that are eligible for the collateral maintenance practical expedient*. Many of the Company's financial assets measured at amortized cost basis are eligible for the collateral maintenance practical expedient as described in FASB ASC 326-20-35-6. The practical expedient may be elected for contracts when the counterparty is contractually obligated to continue to fully replenish the collateral to meet the requirements of the contract and the Company reasonably expects the counterparty to continue to replenish the collateral. The Company elects to use the practical expedient when eligible. The Company determines if it is eligible for the collateral maintenance provision practical expedient, considers the credit quality of these assets, and the related need for an allowance for credit losses, based on several factors, including: 1) the daily revaluation of the underlying collateral used to secure the customer's borrowings and collateral, 2) the customer's continuing ability to meet additional collateral requests based on decreases in the market value of the collateral, and 3) its right to sell the securities collateralizing the borrowings, if additional collateral requests are not met by the customer or the amounts borrowed are not returned on demand. Under the collateral maintenance provision practical expedient, the Company compares the amortized cost basis with the fair value of collateral at the reporting date. When the fair value of the collateral is equal to or exceeds the amortized cost basis of the financial asset and the Company reasonably expects the counterparty to continue to replenish the collateral as necessary to meet the requirements of the contract, the practical expedient permits the Company to consider that the expectation of nonpayment of the amortized cost basis is zero. When the fair value of the collateral is less than the amortized cost basis of the financial assets, and the Company reasonably expects the counterparty to continue to replenish the collateral as necessary to meet the requirements of the contract ,the Company establishes an allowance for credit losses for the unsecured amount of the amortized cost basis. The allowance for credit losses on the financial asset is limited to the difference between the fair value of the collateral at the reporting date and the amortized cost basis of the financial assets.

*Financial assets measured at amortized cost basis that are not eligible for the collateral maintenance practical expedient*. For financial assets measured at amortized cost basis that are not eligible for the collateral maintenance practical expedient (and any unsecured amounts for instruments applying the practical expedient), the Company estimates expected credit losses over the life of the financial assets as of the reporting date based on relevant information about past events, current conditions, and reasonable and supportable forecasts.

*Certain off-balance sheet credit exposures*. The Company estimates credit losses on certain off-balance sheet credit exposures over the contractual period of a present obligation to extend credit, unless that obligation is unconditionally cancellable by the Company. The Company provides letters of credit and other guarantees primarily to enable clients to enhance their credit standing and complete transactions. Other than the estimation of the probability of funding on such arrangements, the allowance for credit losses is estimated in a manner similar to the methodology used for funded credit exposures and as such, the Company estimates expected credit losses over the life of the instruments as of the reporting date based on relevant information about past events, current conditions, and reasonable and supportable forecasts.
For off-balance sheet credit exposures, the allowance for credit losses is reported as a liability. Changes in the allowance for credit losses are reported in Credit Loss expense.

*Receivables from Customers.* The Company's receivables from its brokerage customers include margin loans and accrued interest on these loans. Margin loans represent credit extended to customers to finance their purchases of securities by borrowing against securities they own and are fully collateralized by these securities in customer accounts. Collateral is maintained at required levels at all times. The borrowers of a margin loan are contractually required to continually adjust the amount of the collateral as its fair value changes. The Company subjects the borrowers to an internal qualification process and an interview to align investing objectives, and monitors customer activity. The Company applies the practical expedient based on collateral maintenance provisions in estimating an allowance for credit losses for margin loans. [3]

*Securities borrowed*. Securities borrowed transactions require the Company to deliver cash to the lender in exchange for securities. Interest on such transactions is accrued and is included in the consolidated statement of financial condition in receivables from and payables to broker dealers and clearing organizations. The market value of securities borrowed is monitored, with additional collateral obtained to ensure full collateralization. The Company applies the practical expedient based on collateral maintenance provisions in estimating an allowance for credit losses for securities borrowed receivables. The Company has established policies and procedures for mitigating credit risk on securities borrowed transactions, including reviewing and establishing limits for credit exposure, maintaining collateral, and continually assessing the creditworthiness of counterparties. The Company minimizes credit risk associated with these activities by daily monitoring collateral values and requiring additional collateral to be deposited with the Company as permitted under contractual provisions. [4]

*Receivables from broker-dealers and Clearing Organizations.* The Company's receivables from broker-dealers and clearing organizations include amounts receivable from unsettled trades, including amounts related to futures and options on futures contracts executed on behalf of customers, amounts receivable for securities failed to deliver, accrued interest receivables and cash deposits. A portion of the Company's trades and contracts are cleared through a clearing organization and settled daily between the clearing organization and the Company. Because of this daily settlement, the amount of unsettled credit exposures is limited to the amount owed the Company for a very short period of time. The Company continually reviews the credit quality of its counterparties.[5]
[*Securities Purchased Under Agreements to Resell* ("*Reverse Repo"*)[6]]. The Company enters into short-term reverse repo agreements. Interest on such contract amounts is accrued and is included in the consolidated statement of financial condition in receivables from and payables to broker-dealers and clearing organizations. Reverse repos are collateralized by securities with a market value in excess of the obligation under the contract which may result in unsecured credit exposure in the event the

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[3] The Company should consider all the disclosure requirements in FASB ASC 326-20-50, including credit quality information, details and rollforwards of the allowance for credit losses by portfolio segment and major security type, past due and non-accrual status receivables, etc. The Company should also consider accrued interest receivables in its computation of credit losses under ASC 326-20.

[4] The Company should consider all the disclosure requirements in FASB ASC 326-20-50, credit quality information, details and rollforwards of the allowance for credit losses by portfolio segment and major security type, past due and non-accrual status receivables, etc. The Company should also consider accrued interest receivables in its computation of credit losses under ASC 326-20.

[5] The Company should consider all the disclosure requirements in FASB ASC 326-20-50, credit quality information, details and rollforwards of the allowance for credit losses by portfolio segment and major security type, past due and non-accrual status receivables, etc. The Company should also consider accrued interest receivables in its computation of credit losses under ASC 326-20.

[6] For those scenarios when the Company has not elected a fair value option for the reverse repos.

counterparty to a transaction is unable to fulfill its contractual obligations timely. The Company applies the practical expedient based on collateral maintenance provisions in estimating an allowance for credit losses for reverse repurchase agreements. The Company has established policies and procedures for mitigating credit risk on reverse repo transactions including reviewing and establishing limits for credit exposure, maintaining collateral, and continually assessing the creditworthiness of counterparties. The Company minimizes credit risk associated with reverse repo activities by daily monitoring type and grade of securities posted as collateral and requiring additional collateral to be deposited with the Company. [7]

*[Loans to employees].* The Company grants loans to employees in conjunction with a program established primarily to recruit and retain certain employees. These loans are contingent on the employees' continued employment with the Company and generally require repayment if employees leave during a contractual service period. These loans generally amortize over a contractual service period of 3 to 10 years from the initial date of the loan and amounts related to accrued interest are reported in the same balance sheet line item as the other elements of the loan's amortized cost. The outstanding loan becomes due on demand in the event the employee departs during the service period. The Company estimates the allowance for credit losses by considering credit quality indicators and the recoverability of an outstanding loan balance from employees that left the Company. A loan is placed on non-accrual status when, based on current information, it is probable that the Company will be unable to collect scheduled payments of principal and interest when due according to the contractual terms of the underlying loan agreement. Generally, loans with principal or interest payments that are more than 30 days past due are placed on non-accrual status. The amortized cost basis of these loans is written-off against the allowance for credit losses when management deems the amount to be uncollectible. [8]

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[7] The Company should consider all the disclosure requirements in FASB ASC 326-20-50, credit quality information, details and rollforwards of the allowance for credit losses by portfolio segment and major security type, past due and non-accrual status receivables, etc.

[8] In addition to the additional disclosure considerations in footnote 2, disclosures around modifications, renewals, or extensions, as well as the year of origination, related to any loans should be disclosed. Additionally, if an entity discloses internal risk ratings, they should provide qualitative information on how those internal risk ratings relate to the likelihood of loss.

2. The Expert Panel (EP) members discussed with regulators the impact of Accounting Standards Update ("ASU") 2019-12, *Simplifying the Accounting for Income Taxes*, on 17 C.F.R. §240.15c3-1 ("Net Capital"). The discussion specifically focused on the amendment in the ASU which specifies that "an entity is not required to allocate the consolidated amount of the current and deferred tax expense to a legal entity that is not subject to tax in its separate financial statements."

   Assuming a broker-dealer adopts the guidance as described above, the EP members expressed the following views:

   - the above would not have an impact on the periodic computations of Net Capital if a liability has not been recorded on the separately issued financial statements/monthly or quarterly Form X-17A-5 Part II/IIa (FOCUS Reports).
   - the amounts to be withdrawn from the broker-dealer for tax payments to be made by the parent or ultimate taxpayer, six months subsequent to the date of the FOCUS Report, should be included in the FOCUS Report schedule – "Ownership Equity and Subordinated Liabilities maturing or proposed to the withdrawn within the next six months and accruals, which have not been deducted in the computation of Net Capital".

   In response to the EP members inquiry, the SEC Staff for the SEC Division of Trading and Markets stated that they do not object to the above views.

3. The Expert Panel (EP) members discussed with regulators the impact of the October 22, 2020 no-action letter "*Broker-Dealers Borrowing Fully Paid and Excess Margin Securities from Customers*" (NAL) and related reporting requirements. The discussion specifically focused on evaluating compliance with the customer protection rule and internal controls over compliance, where certain broker-dealers operate programs in which they borrow fully paid and excess margin securities from their customers (FPL Programs). The NAL provided six months for broker-dealers to "come into compliance with Rule 15c3-3" either through modification to the terms of the plan or winding down the FPL Programs in an orderly manner, during which time the SEC Trading and Markets Division staff would not recommend enforcement action.

   The EP members expressed the following views:

   - Broker-dealers that have engaged in an FPL program during the year ended December 31, 2020 will need to evaluate their programs for compliance with 15c3-3(b)(3) and the severity of any non-compliance arising from the practices employed.
   - Broker-dealers that have determined their FPL Programs are not in compliance with 15c3-3(b)(3) will need to evaluate the impact of noncompliance on the broker-dealers' Internal Control Over Compliance.
   - As long as the broker-dealer is complying with the terms of the NAL and undertaking steps to remediate the root cause of noncompliance, the broker–dealer can rely on the NAL in its conclusion that there is not an instance of noncompliance for the period from October 23, 2020 to December 31, 2020 and as of December 31, 2020.
   - If the broker-dealers FPL program has not been remediated as of December 31, 2020 and the broker dealer is relying on the NAL, as specified above, the broker-dealer can continue reporting possession or control requirements in the **INFORMATION RELATING TO THE POSSESSION OR CONTROL REQUIREMENTS** supplemental schedule without accounting for the FPL Program impact. However, the broker-dealer may include a disclosure in the supplemental schedule as follows:

     Note: *"The Company is following the guidance provided in the October 22, 2020 no-action letter titled "Broker-Dealers Borrowing Fully Paid and Excess Margin Securities from Customers" issued by the Securities and Exchange Commission Division of Trading and Markets. At December 31, 2020, the Company has not included in the amounts above a total of $xxxx of customer fully paid and excess margin securities borrowed from XX customers in connection with the Company's fully paid and excess margin securities lending program. This no-action relief is for a period of six months from the date of the no-action letter."*

   In response to the EP members inquiry, the SEC Staff for the SEC Division of Trading and Markets stated that they do not object to the above views.

**INFORMATION RELATING TO THE POSSESSION OR CONTROL REQUIREMENTS UNDER RULE 15c3-3**
**December 31, 2020**
**(In dollars)**

Customers' fully paid securities and excess margin securities not in The Company's possession or control as of December 31, 2020 (for which instructions to reduce to possession or control had been issued as of December 31, 2020) but for which the required action was not taken by the Company within the time frames specified under Rule 15c3-3.

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| Market Value | $ 0 |
| Number of Items | 0 |

Customers' fully paid securities and excess margin securities for which instructions to reduce to possession or control had not been issued as of December 31, 2020, excluding items arising from "temporary lags which result from normal business operations" as permitted under Rule 15c3-3. $ -

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| Market Value | $ 0 |
| Number of Items | 0 |

Note: The Company is following the guidance provided in the October 22, 2020 no-action letter titled "Broker-Dealers Borrowing Fully Paid and Excess Margin Securities from Customers" issued by the Securities and Exchange Commission Division of Trading and Markets. At December 31, 2020, the Company has not included in the amounts above a total of $xxxx of customer fully paid and excess margin securities borrowed from XX customers in connection with the Company's fully paid and excess margin securities lending program. This no-action relief is for a period of six months from the date of the no-action letter.

There were no material differences between the above computation and the Company's corresponding unaudited FOCUS Report.