CL 7

6 July 2004

Ms Sandra Thompson
Senior Project Manager
IASB
30 Cannon Street
London EC4M 6XH
UNITED KINGDOM

Dear Ms Thompson

IAS 39 Fair Value Option

The Group of 100 (G100) is pleased to comment on the Exposure Draft. Our comments on the specific questions are attached. However, our more general concerns about the process relating to the proposed amendments are outlined below.

The G100 is concerned that the proposed amendments are clearly in response to issues raised by a regulator. We consider that the purpose of the process should be to address financial reporting issues and develop accounting standards that meet the information needs of a broad range of users. If regulators need different information for regulatory purposes it is within their powers to set their own requirements.

The G100 is also concerned about the impact of the proposed amendments on the use of fair values. Fair value measurement is required by a number of IASB Standards and, reliability, which is well established in the IASB Framework, is a criterion that must be satisfied for recognition to occur. The proposals to introduce a further test of 'verifiability' for the use of fair values in respect of financial instruments are unwarranted. In a principle-based system (where fair value is defined and substantial guidance is provided on the determination of fair values in different circumstances) the introduction of a verifiability test has all the hallmarks of resorting to a rule to address a limited situation.

In our view the notion of verifiability as explained is already subsumed in applying the qualitative characteristic of reliability as part of the recognition criteria. If the proposed additional 'test' of fair value is required in this context it would be consistent for the IASB to apply it in all applications of fair value.

Yours sincerely

John V Stanhope
National President

c.c. Mr D. Boymal, Chairman AASB

EXPOSURE DRAFT IAS 39 : FINANCIAL INSTRUMENTS - FAIR VALUE OPTION

1. *Do you agree with the proposals in this Exposure Draft? If not, why not? What changes do you propose and why?*

   No. The proposals reflect an undesirable tampering with the application of fair values as presently applied in IASB Standards. The verifiability test does not add anything to the reliability test and would appear to be the use of different terminology for cosmetic purposes as verifiability would be a factor considered in determining whether a measure is reliable. If adopted the change in fair values of some items would be required to be recognized in the profit and loss whereas for others it would not be permitted. In addition we do not believe accounting standards should be designed to satisfy the needs of regulators who are likely to have different information needs than users of general purpose financial reports.

2. *Are you aware of any financial instruments to which entities are applying, or are intending to apply, the fair value option that would not be eligible for the option if it were revised as set out in this Exposure Draft? If so:*
   - *(a) please give details of the instrument(s) and why it (they) would not be eligible.*
   - *(b) is the fair value of the instrument(s) verifiable (see paragraph 48B) and if not, why not?*
   - *(c) How would applying the fair value option to the instrument(s) simplify the practical application of IAS 39?*

   In view of the genesis of the proposals we presume that the verifiability test is more stringent than the reliability criterion. Under the proposals the ability to manage positions (asset and liability holdings) to reduce volatility in results would be restricted where some items are measured at verifiable fair value and others measured on a different basis.

3. *Do the proposals contained in this Exposure Draft appropriately limit the use of the fair value option so as to address adequately the concerns set out in paragraph BC9? If not, how would you further limit the use of the option and why?*

   The fair value requirements in IAS 39 are operational. The G100 believes that the concerns identified in BC9 could be addressed more directly by the relevant regulator issuing separate rules for prudential purposes and by the IASB dealing directly with the 'own credit worthiness' issue.

4. *Paragraph 9(b)(i) proposes that the fair value option could be used for a financial asset or financial liability that contains one or more embedded derivatives, whether or not paragraph 11 of IAS 39 requires the embedded derivative to be separated. The Board proposes this category for the reasons set out in paragraphs BC6(a) and BC16-BC18 of the Basis for Conclusions on this Exposure Draft. However, the Board recognizes that a substantial number of financial assets and financial liabilities would qualify for the fair value option under this proposal.*

   Is the proposal in paragraph 9(b)(i) appropriate? If not, should this category be limited to a financial asset or financial liability containing one or more embedded derivatives that paragraph 11 of IAS 39 requires to be separated?

   The operation of current requirements of IAS 39 in respect of fair values should not be changed at this stage. From an Australian point of view retention of the current requirements are of particular importance in respect of accounting for insurance contracts because net market values are used in current practice. The overlay of the verifiability test is likely to impede the ongoing use of fair values in this industry and the way in which entities undertake hedging arrangements.

5. *Paragraph 103A proposes that an entity that adopts early the December 2003 version of IAS 39 may change the financial assets and financial liabilities designated as at fair value through profit or loss from the beginning of the first period for which it adopts the amendments in this Exposure Draft. It also proposes that in the case of a financial asset or financial liability that was previously designated as at fair value through profit or loss but is no longer so designated:*

   (a) if the financial asset or financial liability is subsequently measured at cost or amortised cost, its fair value at the beginning of the period for which it ceases to be designated as at fair value through profit or loss is deemed to be its cost or amortised cost.

   (b) if the financial asset is subsequently classified as available for sale, any amounts previously recognized in profit or loss shall not be reclassified into the separate component of equity in which gains and losses on available-for-sale assets are recognized.

   However, in the case of a financial asset or financial liability that was not previously designated as at fair value through profit or loss, the entity shall restate the financial asset or financial liability using the new designation in the comparative financial statements.

   Finally, this paragraph proposes that the entity shall disclose:

   (a) for financial assets and financial liabilities newly designated as at fair value through profit or loss, their fair value and the classification and carrying amount in the previous financial statements.

   (b) for financial assets and financial liabilities no longer designated as at fair value through profit or loss, their fair value and the classification and carrying amount in the current financial statements.

Are those proposed transitional requirements appropriate? If not, what changes do you propose and why? Specifically, should all changes to the measurement basis of a financial asset or financial liability that result from adopting the amendments proposed in this Exposure Draft be applied retrospectively by restating the comparative financial statements?

The transitional requirements should be flexible to facilitate implementation by entities and retrospective application avoided particularly because of difficulties in respect of comparatives.

6. *Do you have any other comments on the proposals?*

The G100 believes that the stable platform as at 31 March should be the basis for 2005 reporting. Accordingly, we believe that the operative date for any amendments to the stable platform should be 2006 with entities being able to early adopt the proposals.

July 2004

6 July 2004

Mr David Boymal
Chairman
AASB
PO Box 204
Collins Street West Vic 8007

Dear David

IAS 39 Fair Value Option

The Group of 100 (G100) submission to the IASB on this exposure draft is attached. As indicated, the G100's views in respect of the IASB proposals are similar to the AASB's preliminary views.

An objective of the convergence process is that companies are able to make an unreserved statement of compliance with IASB Standards. The G100 believes that the proposed changes, if introduced, should apply for 2006 with companies being permitted to early-adopt the amendments in their 2005 financial reports.

Yours sincerely

John V Stanhope
National President