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Our Ref: ER02-0014

21 July 2004

Sandra Thompson
Senior Project Manager
International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
UNITED KINGDOM

Dear Sandra

EXPOSURE DRAFT OF PROPOSED AMENDMENTS TO IAS 39
FINANCIAL INSTRUMENTS: RECOGNITION AND MEASUREMENT
THE FAIR VALUE OPTION

This response to ED Proposed Amendments to IAS 39 is written on behalf of the following members of the Australasian Council of Auditors-General:

- Auditor-General of New South Wales
- Auditor-General for Tasmania
- Auditor-General for Western Australia
- Auditor-General of New Zealand

The non-inclusion of an ACAG member in the submission does not necessarily mean they disagree with the submission.

We do not support the amendments to IAS 39 proposed by this ED. Our comments on the specific questions asked are contained in the attachment to this letter.

The opportunity to provide comment is appreciated and we trust you will find the attached comments useful.

Yours sincerely

Kevin Brady

ATTACHMENT

RESPONSE TO EXPOSURE DRAFT OF PROPOSED AMENDMENTS TO IAS 39 FINANCIAL INSTRUMENTS: RECOGNITION AND MEASUREMENT THE FAIR VALUE OPTION

Question 1

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

We do not agree with the proposals in this Exposure Draft. We believe in principles-based standards and, in our view, the proposed changes to IAS 39 introduce a series of complex rules (as referred to in the Alternative Views section of the Exposure Draft). These complex rules may create an environment of confusion and uncertainty, which could potentially lead to misapplication of the Standard. We would prefer that none of the proposed changes are made to IAS 39.

Question 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?

We are not aware 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 the Exposure Draft.

Question 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?

In our view, use of the fair value option should not be limited. Nevertheless, we believe that the proposals contained in the Exposure Draft adequately address the concerns set out in paragraph BC9.

Question 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 recognises that a substantial number of financial assets and financial liabilities contain embedded derivatives and, accordingly, 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?

In our view, there should be an option for all financial instruments to be measured at fair value. The proposal in paragraph 9(b)(i) is consistent with that view, albeit that proposal does not go far enough. Given our view, we would not support any limiting of this category to financial assets or financial liabilities containing one or more embedded derivatives that paragraph 11 of IAS 39 requires to be separated.

Question 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 recognised 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 recognised.***

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.

We have no particular view on the appropriateness of the proposed transitional requirements.

Question 6

Do you have any other comments on the proposals?

We have no other comments.