AUSTRALIAN BANKERS' ASSOCIATION INC.

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IASB
Comment letters
30 Cannon Street
London, EC4M 6XH
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Dear IASB,

Fair Value Option for Financial Liabilities

Thank you for the opportunity to comment on the Fair Value Option for Financial Liabilities Exposure Draft.

Please find attached comments from the Australian Bankers' Association (ABA).

Yours sincerely

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Tony Burke

APPENDIX – RESPONSE TO SPECIFIC QUESTIONS

Presenting the effects of changes in a liability's credit risk in profit or loss

Question 1

Do you agree that for all liabilities designated under the fair value option, changes in the credit risk of the liability should not affect profit or loss? If you disagree, why?

Question 2

Or alternatively, do you believe that changes in the credit risk of the liability should not affect profit or loss unless such treatment would create a mismatch in profit or loss (in which case, the entire fair value change would be required to be presented in profit or loss)? Why?

We agree that changes in the credit risk of financial liabilities designated under the fair value option should not affect profit or loss, except as contemplated in Question 7. The recognition in profit or loss of the effects of changes in own credit on financial liabilities does not provide useful information to users as it results in counterintuitive accounting.

Presenting the effects of changes in a liability's credit risk in other comprehensive income

Question 3

Do you agree that the portion of the fair value change that is attributable to changes in the credit risk of the liability should be presented in other comprehensive income? If not, why?

Question 4

Do you agree that the two-step approach provides useful information to users of financial statements? If not, what would you propose instead and why?

We agree that the portion of the fair value change that is attributable to changes in an entity's own credit risk on its liabilities (i.e. not general/industry credit risk which would continue to be recognised through profit or loss) should be presented in other comprehensive income, unless the entity repays an amount other than the contractual amount (refer Question 7).

We do not however, support the two-step approach as we believe that the one-step approach contemplated in the Exposure Draft better reflects the proposed accounting for financial liabilities designated under the fair value option – i.e. that own credit risk should not affect profit or loss.

We believe that the two-step approach adds additional complexity to the presentation of the financial statements while achieving the same net effect on profit or loss and other comprehensive income.

Presenting the effects of changes in a liability's credit risk in other comprehensive income

Question 5

Do you believe that the one-step approach is preferable to the two-step approach? If so, why?

We believe that the one-step approach is preferable - as explained in the response to Question 4 above.

Presenting the effects of changes in a liability's credit risk in other comprehensive income

Question 6

Do you believe that the effects of changes in the credit risk of the liability should be presented in equity (rather than in other comprehensive income)? If so, why?

We do not believe that the effects of changes in the credit risk of the liability should be presented directly in equity. We believe that such changes should be initially presented through other comprehensive income. As discussed in paragraph BC34(b) in the Basis for Conclusions to the Exposure Draft, we agree that re-measurements are not transactions with equity holders and hence presentation of changes in credit risk directly in equity would not be appropriate.

Reclassifying amounts to profit or loss

Question 7

Do you agree that gains or losses resulting from changes in a liability's credit risk included in other comprehensive income (or included in equity if you responded 'yes' to Question 6) should not be reclassified to profit or loss? If not, why and in what circumstances should they be reclassified?

We believe that gains or losses resulting from changes in a liability's credit risk should be reclassified to profit or loss if an entity repays an amount other than the contractual amount. This would ensure consistency with both the extinguished liabilities recognised at amortised cost, where the difference between the carrying amount and the consideration paid is recognised in profit or loss (IAS 39.41) and the treatment of debt for equity exchanges where differences in value of the fair value equity instruments and the carrying amount of debt extinguished is recognised in profit or loss (IFRIC 19).

Determining the effects of changes in a liability's credit risk

Question 8

For the purposes of the proposals in this exposure draft, do you agree that the guidance in IFRS 7 should be used for determining the amount of the change in fair value that is attributable to changes in a liability's credit risk? If not, what would you propose instead and why?

We agree that the guidance in IFRS 7 should be used for determining the amount of the change in fair value that is attributable to changes in a liability's credit risk as paragraph 10(a)(ii) of IFRS 7 provides the option to use a method that faithfully represents this change. However we request that additional guidance is included that clarifies that an entity should split out fair value changes with respect to its own credit risk rather than industry/general credit risk for recognition in OCI.

Effective date and transition

Question 9

Do you agree with the proposals related to early adoption? If not, what would you propose instead and why? How would those proposals address concerns about comparability?

We do not support the requirement that entities wishing to early adopt this limited amendment to IAS 39 be required to early adopt IFRS 9.

The proposed amendment is equally applicable to entities that continue to apply IAS 39 as to those entities that have early adopted IFRS 9. As the impact of adopting IFRS 9 has a significant impact on an entity's financial position and financial performance, the decision to early adopt is not straight forward.

Given the discrete impact that this proposed amendment has on the financial statements, a user could compare the results of an entity that has adopted the proposed amendment to an entity that is yet to adopt the proposed amendment. In our view, the level of comparability between preparers would not be noticeably impacted whether or not the adoption is dependent on the early adoption of IFRS 9.

Effective date and transition

Question 10

Do you agree with the proposed transition requirements? If not, what transition approach would you propose instead and why?

We support the proposed transition requirements of retrospective application. We recommend that the IASB require an entity to reassess the liabilities designated under the fair value option upon adoption to enable the full consideration of the impacts of the revised financial asset requirements under IFRS 9.