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International Accounting Standards Board
30 Cannon Street
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15 January 2009

Dear Sir/Madam

Invitation to comment – Exposure Draft on Investments in Debt Instruments (Proposed amendments to IFRS 7)

Ernst & Young is pleased on the Exposure Draft (ED). In summary, we do not support the proposed amendments.

At the roundtables, certain preparers and auditors requested that the impairment measurement requirements for available-for-sale (AFS) debt instruments be amended, to align them with the requirements for financial assets held on an amortised cost basis. We appreciate that users were not enthusiastic about this proposal and so understand why the Board has only proposed changes in the disclosure requirements, but the proposed disclosure of the profit or loss that would have been reported, had AFS debt instruments been recorded at amortised cost, would not show the effect of the requested changes in the impairment requirements. Also, as far as we are aware, it is not information that is sought by users.

Similarly, the proposed disclosure of the effect of valuing all investments in debt instruments at fair value was not requested at the roundtables. We are concerned that this would provide a misleading number, since it would fail to include offsetting gains and losses that would arise if related liabilities were also recorded at fair value and the effects of any changes in hedging strategies that might be adopted if investments in debt instruments were recorded on this basis. It could also give an undue level of prominence to this information and so detract from the performance shown in the primary financial statements.

Finally, IAS 39 is based on a mixed measurement model, not a full fair value model, providing entities the opportunity to select the measurement basis that fits best with the nature and purpose of the financial instruments held. A requirement to disclose profit or loss as if that choice had been made differently for a subset of financial instruments does not provide meaningful additional information.

Accordingly, in principle, we are not supportive of the proposed changes and we do not believe that the cost of preparing the information would be commensurate with the benefits to users. Furthermore it would be impractical to expect all IFRS reporters to derive this information for 2008 calendar reporting periods.

We support the Board's tentative decision to consider urgently the accounting for impairment of AFS debt instruments, as requested at the roundtables. In the meantime, some preparers may find it useful to communicate the impairment loss which would have been reported had AFS debt instruments been recorded on an amortised cost basis. We would support the ability for such entities to make this disclosure but we are not clear that, apart perhaps for SEC registrants, such voluntary additional disclosure would require an amendment to IFRS 7. If the Board decides to change its amendment to require this more specific information, we believe that the amendment should not be required for 2008 year ends, although early adoption could be encouraged.

The Appendix sets out our responses to the specific questions asked in the Invitation to Comment, together with our comments on the draft wording.

Should you wish to discuss the contents of this letter with us, please contact Tony Clifford at the above address or on +44 (0)20 7951 2250.

Yours faithfully

Ernst & Young

Appendix – Responses to specific questions raised in the Exposure Draft

Question 1

The exposure draft proposes in paragraph 30A(a) to require entities to disclose the pre-tax profit or loss as though all investments in debt instruments (other than those classified as at fair value through profit or loss) had been (i) classified as at fair value through profit or loss and (ii) accounted for at amortised cost.

Do you agree with that proposal? If not, why? What would you propose instead, and why?

We do not agree with the proposal.

1. The disclosure of the pre-tax profit or loss as if investments had been classified at amortised cost does not provide the information necessary to show the effect of applying an amortised cost impairment approach, as requested at the roundtables. The disclosed number may be similar, but it would also include the effect of adjusting for other differences, such as any change in the effective interest rate on available for sale debt instruments, once impaired. Also, this is not information which we are aware has been requested by users or many preparers.

   We recommend that the proposal be amended to refer only to disclosure of the effect of the different impairment approaches, for the year and cumulatively, and that this disclosure should be voluntary rather than mandatory.

   Also, as we comment under question 5, it would be impractical to require all entities to derive this information in time for 2008 year ends, since (i) it may entail the construction of complex systems and processes to calculate impairment on both an individual and a collective basis, (ii) would require calculation of the amortised cost balances as at both the beginning and end of the year, and (iii) most entities with December year ends are already far advanced in their year end accounting procedures. Therefore we believe, if application is required, that the date of mandatory application should be 1 January 2009.

2. Disclosure of the pre-tax profit or loss had all investments in debt instruments been recorded at fair value through profit or loss was not requested at the roundtables. IAS 39 is based on a mixed measurement model, not a full fair value model, providing entities the opportunity to select the measurement basis that fits best with the nature and purpose of the financial instruments held. A requirement to disclose profit or loss as if that choice had been made differently for a subset of financial instruments does not provide meaningful additional information. We also believe that it would provide undue prominence to this information and so detract from the performance shown in the primary financial statements. More importantly, the proposed disclosure could be misleading. It would adjust the recorded value of fixed rate debt assets but not fixed rate liabilities, and so report distorted profits or losses which do not reflect the way that interest rate risk is managed economically or in a mixed attribute accounting model. Also, if entities were required to

record such assets at fair value they would often amend their hedging strategies, since it would no longer be necessary to meet the requirements of hedge accounting.

We also have concerns with the drafting of the proposed amendments:

1. The term "investments in debt instruments" is not defined. We understand debt instruments to include any financial instrument with fixed and determinable payments. This may include for example, certain available for sale instruments, held to maturity investments and loans and receivables (including trade accounts receivable). However, we are not sure if the term 'investments in debt instruments' is intended to be a subset of all debt instruments held, being only those held for an investment purpose. Accordingly, it would, perhaps, exclude trade accounts receivable. Therefore, in order to avoid diversity of application we believe that the terms 'debt instrument' and 'investment in debt instrument' should be formally defined (the first of which would also be helpful in applying the definition of a financial guarantee contract). Further, it is not clear whether "investments in debt instruments" would be limited to those within the scope of IAS 39. Would it include, for instance, finance lease receivables?

   We also note that the equivalent FASB proposal (FSP FAS 107-a) would not include trade receivables (with terms of less than one year) within its scope, thereby potentially creating a US GAAP/IFRS difference, which would be undesirable.

2. The wording of paragraph 30A(a), proposes disclosure for the "following for all investments in debt instruments" which implies that the number to be disclosed is just the profit or loss for those debt instruments on each of the two alternative accounting bases, whereas the example in IG 14A appears to show the total pre-tax profit or loss for the entire entity on those two bases. If the latter approach was intended, then we believe that the wording should be amended to make the requirement clear:

   "An entity shall disclose the pre-tax profit or loss as though all investments in debt instruments (other than those classified as at fair value though profit or loss) had been:

   i) classified at fair value through profit or loss; and

   ii) accounted for at amortised cost."

Question 2

The exposure draft proposes to require disclosing the pre-tax profit or loss amount that would have resulted under two alternative classification assumptions.

Should reconciliations be required between profit or loss and the profit or loss that would have resulted under the two scenarios? If so, why and what level of detail should be required for such reconciliations?

As we responded to question 1, we do not support the ED's proposals. We do not believe that the above-described reconciliations should be required. Although a reconciliation would show the effect of measuring impairment of AFS debt instruments on the two different bases, a reconciliation is not needed in order to disclose this information.

Question 3

The exposure draft proposes in paragraph 30A(b) to require entities to disclose for all investments in debt instruments (other than those classified as at fair value through profit or loss) a summary of the different measurement bases of these instruments that sets out (i) the measurement as in the statement of financial position, (ii) fair value and (iii) amortised cost.

Do you agree with that proposal? If not, why? What would you propose instead, and why?

No, we do not agree with the proposed disclosure. Fair values are already disclosed for all debt instruments and the only new information would be the amortised cost for AFS debt instruments. A comparison of the fair value and the amortised cost of such AFS assets would not provide the information to show the effect of the amendment requested at the roundtables, i.e. the effect of calculating impairment on the two different approaches, since it would aggregate situations where the fair value is greater than amortised cost, cases where the fair value is less than amortised cost but the asset is not impaired and instances where the fair value is less than the amortised cost and the asset is impaired.

Should the Board decide to continue with this amendment, we have the following more detailed comments on the proposals made. Paragraph 30A (b) does not specify whether the information should be on an aggregate level (i.e., including all debt instruments other than those classified as at fair value through profit or loss in one bucket) or at the individual asset category level (e.g. available for sale, held to maturity, loans and receivables). The example in the appendix to the ED shows disaggregated information by category of debt instrument, which would provide better disclosure and we suggest that paragraph 30A (b) should be amended to make it clear that the tabulation should be by category.

Question 4

The exposure draft proposes a scope that excludes investments in debt instruments classified as at fair value through profit or loss.

Do you agree with that proposal? If not, would you propose including investments in debt instruments designated as at fair value through profit or loss or those classified as held for trading or both, and if so, why?

Yes, we agree with the proposal to exclude debt instruments classified as at fair value though profit or loss. Calculation of interest and impairment on an amortised cost basis for debt instruments recorded at fair value through profit or loss would require significant systems modification and the information would not be useful in determining future cash flows since it would not normally be the entity's intention to hold the assets to maturity. Also, it would need to be clarified that "investments in debt instruments" would not include investments in derivative debt instruments, as it would not be meaningful to disclose derivatives on an amortised cost basis.

Further, disclosing the effect of recording investments in debt instruments classified at fair value through profit or loss on an amortised cost basis would be misleading, since it would take no account of economic hedging relationships involving liabilities or derivatives. Liabilities which are currently recorded at fair value through profit or loss (including those designated at a fair value to avoid a measurement mismatch) would continue to be recorded at fair value, as would hedging derivatives (unless they are deemed to be investments in debt instruments), creating distorted profits or losses.

Question 5

Do you agree with the proposed effective date? If not, why? What would you propose instead, and why?

No, we do not agree with the ED's effective date. Although we agree that disclosure of the effects of an amortised cost impairment method on available for sale assets may provide useful information, we do not believe that the disclosures should required for all entities for 2008, given that this amendment will be issued only after the year end, the substantial work and systems build that may be needed in order to comply and the advanced stage of reporting already reached by most entities with December year ends. If the Board decides to make the amendments, in our view they should be introduced for 2009 with early adoption encouraged for 2008.

Question 6

Are the transition requirements appropriate? If not, why? What would you propose instead, and why?

Yes, we agree with the proposed transition requirement not to require comparative information if the proposed disclosure requirements are required for 2008. If the proposed disclosures requirements are delayed until 2009 then we would recommend that comparative information be provided.