Korea Accounting Institute KAI

Korea Accounting Standards Board KASB

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8 October 2004

CL 27

Ms. Andrea Pryde
Assistant Project Manager
International Accounting Standards Board
30 Cannon Street, London EC4M 6XH
United Kingdom

Dear Ms. Andrea Pryde:

The International Accounting Standards Review Committee (IASRC) of the Korea Accounting Standards Board (KASB) sends you its comments on the Exposure Draft of Proposed Amendments to IAS 39 Financial Instrument: Recognition and Measurement and IFRS 4 Insurance Contracts, *Financial Guarantee Contracts and Credit Insurance*. I would appreciate your including our comments in your summary of analysis that will be presented to the IASB.

The enclosed comments are those of the IASRC and do not represent an official position of the KASB. The official position of the KASB is determined only after extensive due process and deliberation, to which this letter has not been subjected.

Please do not hesitate to contact us if you have any inquiries regarding our comments. You may forward your inquiries either to Mr. Jae-ho Kim (jhkim@kasb.or.kr) or Mr. Kyoung-chun Yu (yukc@kasb.or.kr), both of whom are full-time research staff of the KASB.

Best regards,

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Dr. Suk Sig Lim
Chairman, International Accounting Standards Review Committee
Vice Chairman, Korea Accounting Standards Board

Encl: IASRC comments on the Exposure Draft of Proposed Amendments to IAS 39 Financial Instrument: Recognition and Measurement and IFRS 4 Insurance Contracts, *Financial Guarantee*

IASRC Comments on the ED of Proposed Amendments to IAS 39 Financial Instrument: Recognition and Measurement and IFRS 4 Insurance Contracts,
Financial Guarantee Contracts and Credit Insurance

■ Question 1 – Form of contract

> The Exposure Draft deals with contracts that require the issuer to make specified payments to reimburse the holder for a loss it incurs if a specified debtor fails to make payment when due under the original or modified terms of a debt instrument (financial guarantee contracts). These contracts can have various legal forms, such as that of a financial guarantee, letter of credit, credit default contract or insurance contract. Under the proposals in the Exposure Draft the legal form of such contracts would not affect their accounting treatment (see paragraphs BC2 and BC3).
>
> Do you agree that the legal form of such contracts should not affect their accounting treatment?
>
> If not, what differences in legal form justify differences in accounting treatments? Please be specific about the nature of the differences and explain clearly how they influence the selection of appropriate accounting requirements.

We agree that the legal form of such contracts should not affect their accounting treatment. Although financial guarantee contracts take various legal forms, the principle of substance over form should be applied to all forms of such contracts.

■ Question 2 - Scope

> The Exposure Draft proposes that all financial guarantee contracts should be within the scope of IAS 39 (see paragraph 2 of IAS 39 and paragraph 4 of IFRS 4), and defines a financial guarantee contract as "a contract that requires the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the original or modified terms of a debt instrument"(see paragraph 9 of IAS 39).

Is the proposed scope appropriate?

If not, what changes do you propose, and why?

We believe that the proposed scope is appropriate. If financial guarantee contracts are accounted for by the substance-over-form principle, IAS 39 that deals with the accounting treatments of financial liabilities should also deal with the accounting treatments of all forms of financial guarantee contracts.

■ Question 3 – Subsequent measurement

The Exposure Draft proposes that financial guarantee contracts, other than those that were entered into or retained on transferring financial assets or financial liabilities within the scope of IAS 39 to another party, should be measured subsequently at the higher of:

(a) the amount recognised in accordance with IAS 37 Provisions, Contingent Liabilities and Contingent Assets; and
(b) the amount initially recognised (ie fair value) less, when appropriate, cumulative amortisation recognised in accordance with IAS 18 Revenue (see paragraph 47(c) of IAS 39).

Is this proposal appropriate? If not, what changes do you propose, and why?

We do not believe that the proposal is appropriate. In IAS 39, financial assets and financial liabilities are in principle measured at fair value on initial recognition, and financial guarantee contracts are also measured at fair value on initial recognition. The fair value of liabilities of financial guarantee contracts could fluctuate subsequently due to the changes in economic conditions. Therefore, the subsequent measurement of financial guarantee contracts should reflect those fair value changes.

■ Question 4 – Effective date and transition

The proposals would apply to periods beginning on or after 1 January 2006, with earlier application encouraged (see paragraph BC27). The proposals would be applied retrospectively.

Are the proposed effective date and transition appropriate? If not, what do you propose, and why?

We believe that the proposed effective date and transition are appropriate.

■ Question 5 – Other comments

Do you have any other comments on the proposals?

We have no other comments on the proposals.