FAR SRS
The institute for the accountancy profession in Sweden

International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

15th January 2008

Exposure Draft of Proposed Improvements to International Financial Reporting Standards

FAR SRS, the institute for the accountancy profession in Sweden is responding to your invitation to comment on the *Exposure Draft of Proposed Improvements to International Financial Reporting Standards*.

In general, FAR SRS agrees with the proposed amendments. Comments are therefore only given on the few items where we disagree.

FAR SRS has however two general remarks.

Some of the proposed improvements are beyond the scope of the annual improvements process that IASB has now embarked on. FAR SRS' responses to questions 4 and 30 are examples of this. FAR SRS is aware of the fact that other amendments may also be regarded as beyond the scope, but did not comment on this since we support the end result. FAR SRS suggests that the Board, based on the experience of this first set of annual improvements, duly reconsiders whether the right balance is struck between "editorial changes", "improvements" and "other changes", where the latter will require the same due process as for a major amendment of a standard.

The proposed effective date for all amendments is for annual periods beginning on or after 1 January 2009. Earlier application is allowed under the proviso that all amendments in the annual improvement project must be applied earlier. In general FAR SRS agrees with this "all or nothing" approach. However, considering our remark above, FAR SRS recommends that an exception is made in this case and that earlier application is permitted standard by standard.

FAR SRS

Jan Buisman
Chairman FAR SRS' Accounting Practices Committee

FAR SRS • Norrtullsgatan 6 • Box 6417 • SE-113 82 Stockholm, Sweden • Phone: +46 8 506 112 00 • Fax: +46 8 34 14 61 • www.farsrs.se

Attachment

Question 4 – IAS 1

Do you agree with the proposal to require an entity that cannot make an unreserved statement of compliance with IFRSs to describe how its financial statements would have been different if prepared in full compliance with IFRSs? If not, why?

FAR SRS′ response

FAR SRS agrees with the proposal in principle. Highlighting differences between IFRS as applied in financial statements that do not fully comply with IFRSs as published by the IASB is useful information for users and an important condition to ensure that the IFRS brand is protected. FAR SRS believes however, that this important change is beyond the scope of an annual improvement project. FAR SRS also notes that such a requirement can only be effectively implemented and enforced by the global regulatory community and therefore requires a thorough dialogue with the securities regulators.

Question 30 – IAS 39

Do you agree with the proposal to amend IAS 39 by removing from the definition of a derivative the exclusion relating to contracts linked to non-financial variables that are specific to a party to the contract? If not, why not?

FAR SRS′ response:

FAR SRS disagrees with the proposed amendment based on the following comments.

FAR SRS does not believe that the suggested amendment only constitutes a clarification of the current standard. The amendment gives rise to several practical potential consequences and should therefore be treated in accordance with IASB's normal due process for major changes including a more detailed analysis of the practical consequences for preparers and the increased value in information to users of financial statements. There is also a need for an analysis of potential consequential changes to be made in IAS 39. It is common practice in many industries to link payments to be received or paid to entity specific non-financial variables such as EBITDA, Net Asset value etc. Since IAS 39's current approach to the assessment of whether an embedded derivative is closely related or not to the host contract is rule-based to a full extent, there is no further guidance for how to assess the wider variety of embedded derivatives that according to the suggested amendment will exist. In FAR SRS′ view, there is a need for either a principle-based guidance on how to assess whether an embedded derivative is closely related or not to the host contract (preferable), or a continued rule-based approach for examples relevant for the new categories of derivatives not covered by the current examples (less preferable).

Under current practice EBITDA-linked return on issued bonds, where the issuer has discretion over the payments when they are contingent on the approval of the annual meeting, meets the

FAR SRS • Norrtullsgatan 6 • Box 6417 • SE-113 82 Stockholm, Sweden • Phone: +46 8 506 112 00 • Fax: +46 8 34 14 61 • www.farsrs.se

definition of an equity instrument since there is no contractual obligation to pay any amounts (until the approval of the annual meeting).

One consequence of the amendments of the standard is that EBITDA-linked payments will be classified as derivatives. IAS 32 p. 27 indicates that a derivative that can be settled net in cash is a financial liability. Hence, EBITDA-linked payments that are discretionary (e.g. payable only if the issuer has paid dividends on ordinary shares) may in the future be classified as financial liabilities since they will be settled net in cash. Currently, such EBITDA-linked payments are classified as equity. Consequently it should be considered if the EBITDA-linked payments would give rise to an embedded derivative that would need to be separated from financial debt instrument with coupons payable only if dividends are paid on the ordinary shares of the issuer (which themselves are payable at the discretion of the issuer). Compare IFRIC UPDATE March 2006 under the caption IAS 32 Financial Instruments: Presentation – Classification of a Financial Instrument. FAR SRS believes that it should be clarified whether derivative classification of EBITDA-riders affects their classification as debt or equity under IAS 32.

IFRS 4 p. B16 indicates that a contract transferring expense risk is an insurance risk. Expense risk is an ingredient in EBITDA. Thus a debt instrument with interest payments linked to EBITDA transfers expense risk and it may be argued that such a contract is an insurance contract. Since an insurance contract is not within the scope of IAS 39 contracts with EBITDA-riders may fall outside the scope of IAS 39. This appears to be a potential effect if IAS 39 applies subsidiary to IFRS 4 (i.e. first it is decided whether a contract is within the scope of IFRS 4 and, if not, IAS 39 applies). FAR SRS believes that contracts with EBITDA-riders should be within the scope of IAS 39 (unless they meet the definition of an own equity instrument). If the proposed amendments are included in IAS 39 the basis for conclusion should clarify why contracts with EBITDA-riders are not within the scope of IFRS 4.

Question 34 – IAS 39

Do you agree with the proposal to amend paragraph AG30(g) if IAS 39 to clarify that prepayment options, the exercise price of which compensates the lender for loss of interest by reducing the economic loss from reinvestment risk, as described in paragraph AG33(a), are closely related to the host contract? If not, why?

FAR SRS response:

FAR SRS agrees with the practical outcome of the suggested amendment that "*prepayment options, the exercise price of which compensates the lender for loss of interest by reducing the economic loss from reinvestment risk*", should not be bifurcated from the host contract. However, FAR SRS believes that this outcome is already reached when assessing whether this type of prepayment options meet the definition of a derivative in the first place. When the premium paid by the borrower to the lender represents the net present value of the contractual revenue stream and the current market interest rate, the prepayment option does not meet the definition of a derivative since this option does not have an intrinsic value (since the strike price is always equal to the current market price) and in consequence no time value.

FAR SRS • Norrtullsgatan 6 • Box 6417 • SE-113 82 Stockholm, Sweden • Phone: +46 8 506 112 00 • Fax: +46 8 34 14 61 • www.farsrs.se