

Our Ref: ER02-0014

8 October 2004

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UNITED KINGDOM

Dear Andrea

**EXPOSURE DRAFT OF PROPOSED AMENDMENTS TO IAS 39
FINANCIAL INSTRUMENTS: RECOGNITION AND MEASUREMENT AND IFRS
4 INSURANCE CONTRACTS – FINANCIAL GUARANTEE CONTRACTS AND
CREDIT INSURANCE**

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 of Queensland
- Auditor-General for Tasmania
- Auditor-General of Victoria
- 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 generally 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

**RESPONSE TO EXPOSURE DRAFT OF PROPOSED AMENDMENTS TO
IAS 39 FINANCIAL INSTRUMENTS: RECOGNITION AND MEASUREMENT
AND IFRS 4 INSURANCE CONTRACTS –
FINANCIAL GUARANTEE CONTRACTS AND CREDIT INSURANCE**

Question 1

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 accounting treatment for all contracts that in substance provide a financial guarantee, regardless of their legal form, should be accounted for in the same manner.

Question 2

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 agree with the proposed scope of the Exposure Draft.

Question 3

The Exposure Draft proposes that financial guarantee contracts, other than those that were entered into or retained on transferring financial assets of 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 agree with the proposal for subsequent measurement of financial guarantee contracts. Subsequent measurement as proposed could result in the overstatement of liabilities if the fair value less cumulative amortisation (recognised in accordance with IAS 18) is greater than the provision calculated in accordance with IAS 37. In our view, subsequent measurement should be only in accordance with IAS 37.

Question 4

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 changes do you propose, and why?

We agree that both the effective date and transition are appropriate.

Question 5

Do you have any other comments on the proposals?

We have no other comments.