



The South African Institute of Chartered Accountants

29 June 2007

Mr Allan Cook
IFRIC Coordinator
International Financial Reporting Interpretations Committee
First Floor, 30 Cannon Street
London EC4M 6XH
United Kingdom

Dear Mr Cook

IFRIC Tentative Agenda decision: IAS 39 *Financial Instruments: Recognition and Measurement* – paragraph AG33(d)(iii)

We are responding to your invitation to react to the above Tentative Agenda Decision, published in the May 2007 edition of IFRIC Update.

We note that the IFRIC was asked about paragraph AG33(d)(iii) of IAS 39, particularly to interpret the meaning/population/interpretation of the term “economic environment”. The IFRIC decided not to take the issue on to its agenda because it felt that any guidance developed would be more in the nature of application guidance than an interpretation.

We do not support the proposed rejection as we believe that the decision does not validly apply to all aspects of the request. We support the view that it is not appropriate for principle-based IFRSs to interpret the term “common” or to assign a specific percentage to the term. We do however strongly support the staff’s recommendation to ask the Board to clarify what an “economic environment” is through its Annual Improvement Process.

The reasons for our view (besides those set out in our original submission) can be summarised as follows:

- It seems to be accepted that IAS 39 is not clear on what the ‘population’ of an economic environment could comprise.
- IAS 39 either *requires* or *prohibits* the bifurcation of embedded derivatives depending on the interpretation of the application guidance. As such the impact of an incorrect or inconsistent interpretation is significant.
- In the South African experience, there are a variety of views on the interpretation of these paragraphs and, consequently, there is diversity and significant inconsistencies between and amongst preparers, academics, users and auditors (both locally and internationally, large and small).
- We have encountered “economic environment” being interpreted in the following ways:



- The country of the reporting entity (for example entities in South Africa commonly uses the US dollar in all trade). This could be supported by reference to IAS 39 IG C.7;
- The internal or external trade environment (for example entities in South Africa commonly uses the US dollar in all external trade, but not in internal trade). This could be supported by the reference to 'internal or external' in IAS 39 paragraph AG33(d)(iii);
- The internal or external trade environment in a specific industry (for example entities in the motor industry in South Africa commonly use the US dollar for external trade but not in internal trade).
- The internal or external trade environment of a specific company (for example a particular entity may commonly use the US dollar for external trade with particular countries).
- The economic foreign currency risk in the host contracts is often economically hedged, which creates different accounting opportunities depending on whether the embedded derivatives are bifurcated or not.

We also support the staff's comment that were the Board to clarify what an "economic environment" is, we would not expect significant demand for interpreting the term "common".

Please do not hesitate to contact me should you require any further input.

Yours sincerely

Sue Ludolph