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International Accounting Standards Board

This document is provided as a convenience to observers at IASB meetings, to assist them in following the Board's discussion. It does not represent an official position of the IASB. Board positions are set out in Standards.
These notes are based on the staff papers prepared for the IASB. Paragraph numbers correspond to paragraph numbers used in the IASB papers. However, because these notes are less detailed, some paragraph numbers are not used.

INFORMATION FOR OBSERVERS

Board Meeting: **21 June 2007, London**

Project: **Annual Improvements**

Subject: **IAS 39 & IFRS 4 – Accounting by holders of financial guarantee contracts (Agenda paper 12I)**

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1. The Board decided at the March 2007 Board meeting that, in most circumstances, minor issues relating to material that is not part of a standard can be resolved as an editorial change. The staff have identified that the following issue would be most appropriately resolved as an editorial change without Board discussion.

   Issue: There is an explicit statement in the introduction to IAS 39, *Financial Instruments: Recognition and Measurement*, that financial guarantee contracts <u>held</u> are not within the scope of the Standard. The scope paragraph 2(e) of IAS 39 implicitly excludes such contracts because it contains a general exclusion of all insurance contracts other than those that are <u>issued</u> by the entity and meet the definition of a financial guarantee contract. Including additional explanation in the introduction to IAS 39 would clarify that the guidance in the introduction and the scope paragraphs are consistent.

2. This paper is for information. It will not be discussed at the Board meeting unless a Board member requests.

Staff recommendation

3. The staff recommends that:

- this issue should be dealt with as an editorial change; and
- the introduction to IAS 39 is amended as proposed in paragraph 7 of this paper.

Background

4. The staff has been notified of an apparent ambiguity in the scope of IAS 39. It relates to the accounting by the holder of a financial guarantee contract. Scope paragraph 2(e) of IAS 39 implicitly excludes financial guarantee contracts held by the entity because of the general exclusion of insurance contracts from IAS 39 other than those issued by the entity that meet the definition of a financial guarantee contract.

5. The implicit exclusion by paragraph 2(e) contrasts with the explicit exclusion of such contracts by introductory paragraph IN6 of IAS 39. This states '…Financial guarantee contracts held are not within the scope of the Standard.'

6. The staff notes that the clarity of the standard would be improved by making a link between introductory paragraph IN6 and paragraph 2(e) of IAS 39. The staff proposes that this is achieved by including an additional sentence in the introduction to IAS 39.

Drafting

7. The staff recommend that IAS 39 should be amended as follows:

Scope

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IN6 The scope of the Standard includes financial guarantee contracts issued. However, if an issuer of financial guarantee contracts has previously asserted explicitly that it regards such contracts as insurance contracts and has used accounting applicable to insurance contracts, the issuer may elect to apply either this Standard or IFRS 4 to such financial guarantee contracts. Under this Standard, a financial guarantee contract is initially recognised at fair value and is subsequently measured at the higher of (a) the amount determined in accordance with IAS 37 and (b) the amount initially recognised less, when appropriate, cumulative amortisation recognised in accordance with IAS 18. Different requirements apply for the subsequent measurement of financial guarantee contracts that prevent derecognition of financial assets or result in continuing involvement. Financial guarantee contracts held are not within the scope of the Standard because they are insurance contracts and are therefore outside the scope of the Standard because of the general scope exclusion for such contracts.

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Appendix – Extracts from IAS 39 – for information

Scope

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IN6 The scope of the Standard includes financial guarantee contracts issued. However, if an issuer of financial guarantee contracts has previously asserted explicitly that it regards such contracts as insurance contracts and has used accounting applicable to insurance contracts, the issuer may elect to apply either this Standard or IFRS 4 to such financial guarantee contracts. Under this Standard, a financial guarantee contract is initially recognised at fair value and is subsequently measured at the higher of (a) the amount determined in accordance with IAS 37 and (b) the amount initially recognised less, when appropriate, cumulative amortisation recognised in accordance with IAS 18. Different requirements apply for the subsequent measurement of financial guarantee contracts that prevent derecognition of financial assets or result in continuing involvement. Financial guarantee contracts held are not within the scope of the Standard.

…

Scope

2 This Standard shall be applied by all entities to all types of financial instruments except:

...

(e) rights and obligations arising under (i) an insurance contract as defined in IFRS 4 *Insurance Contracts*, other than an issuer's rights and obligations arising under an insurance contract that meets the definition of a financial guarantee contract in paragraph 9, or (ii) a contract that is within the scope of IFRS 4 because it contains a discretionary participation feature. However, this Standard applies to a derivative that is embedded in a contract within the scope of IFRS 4 if the derivative is not itself a contract within the scope of IFRS 4 (see paragraphs 10–13 and Appendix A paragraphs AG27–AG33 of this Standard). Moreover, if an issuer of financial guarantee contracts has previously asserted explicitly that it regards such contracts as insurance contracts and has used accounting applicable to insurance contracts, the issuer may elect to apply either this Standard or IFRS 4 to such financial guarantee contracts (see paragraphs AG4 and AG4A). The issuer may make that election contract by contract, but the election for each contract is irrevocable.

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