01 July 2010

Mr Kevin Stevenson
Chairman
Australian Accounting Standards Board
PO Box 204
Collins Street West
Melbourne VIC 8007
AUSTRALIA

By email: standard@aasb.gov.au

Dear Mr Stevenson

Comments on Exposure Draft 196 Fair Value Option for Financial Liabilities

Thank you for the opportunity to comment on the Exposure Draft 196 Fair Value Option for Financial Liabilities. CPA Australia, the Institute of Chartered Accountants (the Institute), and the National Institute of Accountants (the Joint Accounting Bodies) have jointly considered the above exposure draft (ED) and our comments follow.

The Joint Accounting Bodies represent over 180,000 professional accountants in Australia. Our members work in diverse roles across public practice, commerce, industry, government and academia throughout Australia and internationally.

The Joint Accounting Bodies support the ED's proposed solution to the objections to own credit risk being reported in profit or loss as an interim measure only, subject to resolution through the Conceptual Framework project as well as the International Accounting Standards Board (IASB) reaching an agreement with the Financial Accounting Standards Board on a consistent financial instruments standard. Our response to matters on which the Australian Accounting Standards Board has requested specific comment is included in the attached Appendix. Our submission to the IASB is attached.

If you have any questions regarding this submission, please do not hesitate to contact either Mark Shying (CPA Australia) at mark.shying@cpaaustralia.com.au, Kerry Hicks (the Institute) at kerry.hicks@charteredaccountants.com.au or Tom Ravlic (NIA) at tom.ravlic@nia.org.au.

Yours sincerely

Alex Malley	Graham Meyer	Andrew Conway
Chief Executive Officer	**Chief Executive Officer**	**Chief Executive Officer**
CPA Australia Ltd	**Institute of Chartered Accountants in Australia**	**National Institute of Accountants**

a. Are there any regulatory issues or other issues arising in the Australian environment that may affect the implementation of the proposals, particularly any issues relating to:
   i. not-for-profit entities; and
   ii. public sector entities?

The Joint Accounting Bodies are not aware of any regulatory issues or other issues arising in the Australian environment that would affect the implementation of the proposals.

b. Overall, would the proposals result in financial statements that would be useful to users?

The Joint Accounting Bodies believe that as an interim measure, the solution offered by the ED that changes in the credit risk of the liabilities designated under the fair value option should not affect profit or loss will result in financial statements that would be useful to users.

c. Are the proposals in the best interests of the Australian and New Zealand economies?

The Joint Accounting Bodies believe that as an interim measure, the proposals are in the best interests of the Australian and New Zealand economies.

d. Are there any implications for GAAP/GFS harmonisation?

The Joint Accounting Bodies understand that the ED proposal to report changes in the credit risk of the liabilities designated under the fair value option as Other Comprehensive Income and to not affect profit or loss aligns with the Government Finance Statistics reporting that revaluation are to be reported separately from "crystallised" transactions. Accordingly, GAAP/GFS harmonisation will be improved.

01 July 2010

Sir David Tweedie
International Accounting Standards Board
30 Cannon Street
LONDON EC4M 6XH
United Kingdom

By: "Open to comment" page on www.iasb.org

Dear Sir David

Comments on Exposure Draft ED/2010/4 Fair Value Option for Financial Liabilities

Thank you for the opportunity to comment on the IASB Exposure Draft Fair Value Option for Financial Liabilities. CPA Australia, The Institute of Chartered Accountants (the Institute), and the National Institute of Accountants (the Joint Accounting Bodies) have jointly considered the above exposure draft (ED) and our comments follow.

The Joint Accounting Bodies represent over 180,000 professional accountants in Australia. Our members work in diverse roles across public practice, commerce, industry, government and academia throughout Australia and internationally.

The Joint Accounting Bodies acknowledge that during the global financial crisis, some entities reported in profit or loss substantial gains on their financial liabilities measured at fair value because of increases in the liabilities' credit risk – an outcome that many commentators (including some regulators) see as counter intuitive. We acknowledge the efforts of the International Accounting Standards Board to improve the relevance to users of the financial statements for this situation.

The Joint Accounting Bodies note the ED proposals to require the use of Other Comprehensive Income (OCI) in the circumstances specified establish a further exception to the all-inclusive approach to measuring income. We strongly suggest that as part of the conceptual framework project the IASB and the Financial Accounting Standards Board (FASB) work together to agree the purpose of OCI, the attributes that distinguish profit or loss items from OCI items and the status of recycling gains or losses to profit or loss (on derecognition of the liability or otherwise). Moreover, the ED proposes an approach different to that proposed by the FASB Exposure Draft Accounting for Financial Instruments and Revisions to the Accounting for Derivative Instruments and Hedging Activities. We strongly suggest that the IASB and the FASB agree on what variables are a change in own credit.

Notwithstanding our concerns noted above, we support the proposals as an interim solution to address the objections to own credit risk being reported in profit or loss. Our response to matters on which specific comment is requested is included in the attached Appendix.

If you have any questions regarding this submission, please do not hesitate to contact either Mark Shying (CPA Australia) at mark.shying@cpaaustralia.com.au, Kerry Hicks (the Institute) at kerry.hicks@charteredaccountants.com.au or Tom Ravlic (National Institute of Accountants) at tom.ravlic@nia.org.au.

Yours sincerely

Alex Malley
Chief Executive Officer
CPA Australia Ltd

Graham Meyer
Chief Executive Officer
Institute of Chartered Accountants in Australia

Andrew Conway
Chief Executive Officer
National Institute of Accountants

Question 1
Do you agree that for all liabilities designated under the fair value option, changes in the credit risk of the liability should not affect profit or loss? If you disagree, why?

The Joint Accounting Bodies' position is that an entity's own credit risk will always be included in the fair value measurement of a financial liability – thus, the statement of financial position will be affected. Therefore, the outstanding issue to be resolved is the 'other side of the double entry'. We do not support the presentation of effects of the change in equity for the reasons described in paragraph BC34 to the IASB Exposure Draft *Fair Value Option for Financial Liabilities* (IASB ED) - a change in own credit risk ought to affect the entity's performance. We agree that changes in the credit risk of the liabilities designated under the fair value option should not affect profit or loss. However, we see this solution as an interim measure only, subject to resolution through the Conceptual Framework project as well as reaching an agreement with the FASB on a consistent financial instrument standard.

The Joint Accounting Bodies strongly suggest that as part of the conceptual framework project the IASB and the Financial Accounting Standards Board (FASB) work together to determine the purpose of OCI, whether profit or loss items and OCI items can be distinguished on some basis that would enhance the relevance to users of the financial statements and the status of recycling gains or losses to profit or loss (on derecognition of the liability or otherwise). Possible distinguishing attributes might include items that have different predictive values or risk profiles. We consider it important that this work is done.

Moreover, the ED proposes an approach different to that proposed by the FASB Exposure Draft *Accounting for Financial Instruments and Revisions to the Accounting for Derivative Instruments and Hedging Activities*. The IASB ED requires that the amount to be eliminated from profit or loss and presented in OCI include changes in the price of credit that are not specific to the entity in that they relate solely to changes in market conditions. We understand that under IFRS 7 *Financial Instruments: Disclosure* changes in fair value other than changes related to a change in the benchmark rate are generally attributed to a change in the credit risk. The Basis for Conclusions paragraph BC164 to the FASB Exposure Draft *Accounting for Financial Instruments and Revisions to the Accounting for Derivative Instruments and Hedging Activities* states the FASB "...believes that the change in fair value attributable to the change in an entity's credit spread does not accurately reflect the change in an entity's own credit because it also measures the change in the price of credit, which affects not just the individual entity, but also other entities in the industry and the economy.".

Conceptually, we agree with the FASB rationale. However, whether the FASB concept can be operationalised will require further research. Accordingly, we encourage the IASB and FASB to undertake this research, work through this difference and to agree on what variables are a change in own credit.

Question 2
Or alternatively, do you believe that changes in the credit risk of the liability should not affect profit or loss unless such treatment would create a mismatch in profit or loss (in which case, the entire fair value change would be required to be presented in profit or loss)?

No, the Joint Accounting Bodies do not agree and would like the issue fully explored in conjunction with FASB to reach a common outcome in the standards.

Question 3
Do you agree that the portion of the fair value change that is attributable to changes in the credit risk of the liability should be presented in other comprehensive income? If not, why?

Yes, the Joint Accounting Bodies agree that the best interim solution to addressing the objections to own credit risk being reported in profit or loss is that the change in credit risk of any liability designated under the fair value option not affect profit or loss.

Question 4
Do you agree that the two-step approach provides useful information to users of financial statements? If not, what would you propose instead and why?

Yes. As an interim solution, the Joint Accounting Bodies find some intuitive appeal in the two-step approach.

We expect that two outcomes of the conceptual framework project will be clarity as to the purpose of OCI and specificity around the attributes that differentiate profit or loss items from OCI items. At that time, we would no longer expect the proposed two-step approach to faithfully represent the activities of the entity or to deliver information that is relevant to user decision making.

Question 5
Do you believe that the one-step approach is preferable to the two-step approach? If so, why?

No. The Joint Accounting Bodies believe that as an interim solution, the two-step approach has greater intuitive appeal.

Question 6
Do you believe that the effects of changes in the credit risk of the liability should be presented in equity (rather than in other comprehensive income)? If so, why?

No, the Joint Accounting Bodies consider a change in own credit risk ought to affect the entity's performance. Accordingly, we do not support the presentation of the effects of the change in equity.

Question 7
Do you agree that gains or losses resulting from changes in a liability's credit risk included in other comprehensive income (or included in equity if you responded 'yes' to Question 6) should not be reclassified to profit or loss? If not, why and in what circumstances should they be reclassified?

As an interim solution, the Joint Accounting Bodies agree with the IASB's view at paragraph BC37 to the IASB ED that gains or losses on liabilities should be recognised only once and not reclassified.

We strongly suggest that the conceptual framework project establish whether gains or losses can be recycled to profit or loss (on derecognition of the liability or otherwise).

Question 8
For the purposes of the proposals in this exposure draft, do you agree that the guidance in IFRS 7 should be used for determining the amount of the change in fair value that is attributable to changes in a liability's credit risk? If not, what would you propose instead and why?

The Joint Accounting Bodies response to Question 1 notes the ED proposes an approach different to that proposed by the FASB ED. Conceptually, we agree with the FASB that changes in the prices of credit that affect not just the individual entity, but also other entities in the industry and the economy are not part of own credit risk and should therefore affect profit or loss. Whether the concept can be operationalised will require further research.

Accordingly, we encourage the IASB and FASB to undertake this research, work through this difference and to agree on what variables are a change in own credit.

Question 9
Do you agree with the proposals related to early adoption? If not, what would you propose instead and why? How would those proposals address concerns about comparability?

Yes, the Joint Accounting Bodies agree with the proposals to require that all previously adopted requirements in IFRS 9 have to be implemented when the entity adopts the amendments addressed in the ED.

Question 10
Do you agree with the proposed transition requirements? If not, what transition approach would you propose instead and why?

Yes, the Joint Accounting Bodies agree with the proposed transitional provisions to apply the requirements retrospectively. Further, as the ED proposals modify the accounting treatment we believe entities should be allowed to redesignate liabilities previously designated under the fair value option, and thereby enable those entities the opportunity to make a knowing election based upon the standards that will be applied going forward and not the standards that were in place when the initial election was made.