



Australian Government
**Australian Accounting
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Hans Hoogervorst
Chairman
International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
UNITED KINGDOM

Dear Hans

ED/2013/2 Novation of Derivatives and Continuation of Hedge Accounting

The Australian Accounting Standards Board (AASB) welcomes the opportunity to provide comments on *ED/2013/2 Novation of Derivatives and Continuation of Hedge Accounting*. In formulating its comments, the AASB sought and considered the views of Australian constituents through comment letters and other consultation. The comment letters received are published on the AASB's website.

The AASB supports the proposals in *ED/2013/2*. The AASB understands that the proposal in the ED is intended as a narrow scope exception from mandatory discontinuation of hedge accounting in IAS 39 *Financial Instruments: Recognition and Measurement* when novation occurs as a consequence of laws or regulations.

IAS 39 already permits that replacement or rollover of a hedging instrument into another hedging instrument does not trigger discontinuation of hedge accounting when such replacement or rollover is part of the entity's documented hedging strategy. Some may consider that this can apply to novations of derivatives in the absence of changes in laws or regulations.

The AASB does not support the view that the exception should be expanded to other forms of novation of hedging instruments.

If you have any queries regarding any matters in this letter, please contact Sue Lightfoot (slightfoot@asb.gov.au).

Yours sincerely

A handwritten signature in black ink that reads "K.M. Stevenson".

Kevin M. Stevenson
Chairman and CEO

**AASB's Specific Comments on the IASB Exposure Draft
ED/2013/2 *Novation of Derivatives and Continuation of Hedge Accounting***

The AASB's views on the questions in the Exposure Draft are as follows:

Question 1: The IASB proposes to amend IAS 39 so that the novation of a hedging instrument does not cause an entity to discontinue hedge accounting if, and only if, the following conditions are met:

- (i) the novation is required by law or regulations;
- (ii) the novation results in a central counterparty (sometimes called 'clearing organisation' or 'clearing agency') becoming the new counterparty to each of the parties to the novated derivative; and
- (iii) the changes to the terms of the novated derivative arising from the novation of the contract to a central counterparty are limited to those that are necessary to effect the terms of the novated derivative. Such changes would be limited to those that are consistent with the terms that would have been expected if the contract had originally been entered into with the central counterparty. These changes include changes in the collateral requirements of the novated derivative as a result of the novation; rights to offset receivables and payables balances with the central counterparty; and charges levied by the central counterparty.

Do you agree with this proposal? If not, why? What criteria would you propose instead, and why?

- 1 The AASB supports the proposal and considers that the criteria are appropriate. However in practice, the AASB expects that the amendment would have little effect. Most novations arising from changes in legislation or regulation are prospective for new derivatives only, so there would be no benefit in the amendment for such derivatives. Derivatives which are novated on a voluntary basis would not be captured by the amendment.

Question 2: The IASB proposes to address those novations arising from current changes in legislation or regulation requiring the greater use of central counterparties. To do this it has limited the scope of the proposed amendments to a novation that is *required* by such laws or regulations. Do you agree that the scope of the proposed amendment will provide relief for all novations arising from such legislation or regulations? If not, why not and how would you propose to define the scope?

- 2 The AASB agrees with the limited scope. IAS 39 and the proposed draft of IFRS 9 already permit that a rollover or replacement or a hedging instrument into another hedging instrument does not trigger discontinuation if such a replacement or rollover is part of the entity's documented hedging strategy. Some may consider that this can apply to novations of derivatives in the absence of changes in laws or regulations. The AASB therefore does not consider that a broader scope is necessary.

- 3 It is not clear whether the scope of the proposed amendments will provide relief for all novations arising from such legislation or regulations. However, the AASB considers that if the terms of the novated derivative are not sufficiently similar to the original hedging instrument then hedge accounting should be discontinued.

Question 3: The IASB also proposes that equivalent amendments to those proposed for IAS 39 be made to the forthcoming chapter on hedge accounting which will be incorporated in IFRS 9 Financial Instruments. The proposed requirements to be included in IFRS 9 are based on the draft requirements of the chapter on hedge accounting, which is published on the IASB's website.

Do you agree? Why or why not?

- 4 The AASB agrees that equivalent amendments should also be included in the hedge accounting chapter of IFRS 9 to align the forthcoming standard with IAS 39.

Question 4: The IASB considered requiring disclosures when an entity does not discontinue hedge accounting as a result of a novation that meets the criteria of these proposed amendments to IAS 39. However the IASB decided not to do so in this circumstance for the reason set out in paragraph BC13 of this proposal.

Do you agree? Why or why not?

- 5 The AASB agrees with the rationale given in paragraph BC13 of the ED that specific disclosure would not be appropriate. The AASB agrees that from the users' perspective, if the novation of the hedging instrument meets the proposed criteria, the hedging relationship is a continuation and no additional information is required. However, an entity would not be prohibited from providing additional disclosure if it considered it to be useful.