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Mr Bruce Porter
The Chairman
Australian Accounting Standards Board
PO Box 204
COLLINS STREET WEST VIC 8007

1 December 2008

Our Ref: DH:EL

Dear Bruce,

Re: ED 169 *Improving Disclosures about Financial Instruments: Proposed amendments to AASB 7*

Thank you for the opportunity to comment on the Australian Accounting Standards Board's (AASB) Exposure Draft 169 *Improving Disclosures about Financial Instruments: Proposed amendments to AASB 7* ('ED 169'). This letter sets out our principal comments on ED 169. Our responses to the specific matters for comment are contained in the Appendix to the letter.

Overall, we support the proposals and welcome the AASB and IASB's efforts in responding to the current market crisis.

Due to the later IASB submission deadline for its Exposure Draft *Improving Disclosures about Financial Instruments: Proposed amendments to IFRS 7*, the global firm of Deloitte Touche Tohmatsu has not finalised its views in relation to the matters raised in the IASB's Exposure Draft. Therefore, the views presented in this document in relation to ED 169 should be read in this context and may not necessarily represent the views of the global firm of Deloitte.

If you have any questions concerning our comments, please contact Debbie Hankey on (02) 9322 7665.

Yours sincerely

Debbie Hankey
Partner
Deloitte Touche Tohmatsu

APPENDIX

SPECIFIC MATTERS FOR COMMENT RAISED BY THE AASB

(a) **whether there are 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;**
  (ii) **public sector entities**

We are not aware of any regulatory issues or other issues arising in the Australian environment that may affect the implementation of the proposals.

(b) **whether, overall, the proposals would result in financial statements that would be useful to users**

We believe that the proposals will result in financial statements that would be useful to users.

(c) **whether the proposals are in the best interests of the Australian economy**

We believe that the proposals are in the best interests of the Australian economy through issuance of an equivalent Australian Accounting Standard to ensure full convergence with IFRSs.

SPECIFIC MATTERS FOR COMMENT RAISED BY THE IASB

Question 1 – Do you agree with the proposal in paragraph 27A to require entities to disclose the fair value of financial instruments using a fair value hierarchy? If not, why?

We agree with the proposal in paragraph 27A to require entities to disclose the fair value of financial instruments using a fair value hierarchy. We comment further on the proposed additional disclosures in Question 3 below.

If the proposed amendments are approved, in our opinion, it is necessary for paragraph 27A to be accompanied by application guidance, or, where appropriate, commentary within the body of the accounting standard, explaining the different levels of the hierarchy to avoid preparers, regulators and auditors referring to US GAAP to interpret the requirements. Further, as the proposed amendments have been referred to in the exposure draft as being similar to those required by SFAS 157 *Fair Value Measurements* we believe it would be appropriate for the IASB basis of conclusions to discuss any differences between the fair value hierarchy and disclosures required of SFAS 157 and the amended accounting standard, especially given the wording (and guidance) proposed by the IASB does not exactly mirror that of the SFAS.

Question 2 – Do you agree with the three-level fair value hierarchy as set out in paragraph 27A? If not, why? What would you propose instead, and why?

For the purposes of short-term convergence with another widely recognised GAAP in current market conditions, we agree with the three-level hierarchy proposed in paragraph 27A. However, in our opinion before adopting a hierarchy and disclosures that are similar to those in SFAS 157, sufficient due process should be undertaken to determine whether the objectives of the disclosures have been met by US companies and to identify any practical issues with the disclosures and/or application of the hierarchy.

Question 3 – Do you agree with the proposals in:

(a) paragraph 27B to require expanded disclosures about the fair value measurements recognised in the statement of financial position? If not, why? What would you propose instead, and why?

We disagree with the proposed disclosure in paragraph 27B(b).

In our opinion, the requirement in paragraph 27B(b) to disclose a reconciliation by class of Level 3 financial assets and financial liabilities will require for some entities significant additional effort. We question whether the additional costs required for entities to comply with this disclosure outweigh the additional benefits – we are also unsure what additional benefits there are to having this information. In our opinion, the information required by paragraph 27B(c) would be sufficient to address the needs of users concerned with the impact on the profit and loss of financial assets and financial liabilities that are measured using valuation techniques that are not based on observable market data. Further, we consider that it would be sufficient and appropriate to require entities to disclose narrative information explaining reasons for movements between different levels of the hierarchy; that is, the information required by paragraph 27B(e).

If the proposed disclosure requirement is retained in a resultant accounting standard, in our opinion, the resultant accounting standard should allow as a transitional provision, the information required by paragraph 27B(b) to be disclosed prospectively.

Also, if the proposed disclosure requirement is retained in a resultant accounting standard, we believe it should include the relief available to derivative financial assets and derivative financial liabilities under SFAS 157. SFAS 157 permits the reconciliation to be presented net for derivative financial assets and derivative financial liabilities.

We have a number of other comments in relation to the proposed disclosures in paragraph 27B. We comment on these in the section headed 'Other comments' below.

(b) paragraph 27C to require entities to classify, by level of the fair value hierarchy, the disclosures about the fair value of the financial instruments that are not measured at fair value? If not, why? What would you propose instead, and why?

We agree with the proposal, however we believe it should be accompanied by application guidance, and that the disclosure should be made separately from the disclosures specified by paragraph 27B(a).

We also note that there is an inconsistency between the disclosure requirements of paragraph 25 and paragraph 27C that should be addressed. Paragraph 27C requires disclosure of the fair value of all financial instruments not measured at fair value separately categorised into the three levels of the fair value hierarchy. However, paragraph 25 does not require fair values of certain financial assets and financial liabilities to be provided as it refers to the exclusions in paragraph 29 (whereas paragraph 27C does not).

Question 4 – Do you agree with the proposal in paragraph 39(a) to require entities to disclose a maturity analysis for derivative financial liabilities based on how the entity manages the liquidity risk associated with such instruments? If not, why? What would you propose instead, and why?

We agree with the proposal in paragraph 39(a) to require entities to disclose a maturity analysis for derivative financial liabilities based on how the entity manages the liquidity risk associated with such instruments.

Proposed paragraph B11C discusses the maturity analysis for derivative financial liabilities, and provides examples of manners by which an entity includes items in its maturity analysis. In our opinion, it would be useful for the paragraph to also include examples of how:

(a) a gross-settled forward contract to sell listed shares held

(b) a gross-settled cross currency interest rate swap

could be managed and included in the maturity analysis. We also query why BC11C(b) refers only to the expected net cash flows, and believe the IASB should clarify whether this is the accounting disclosure irrespective of whether the interest rate swap is contractually gross settled or net settled.

Various guidance paragraphs in the accounting standard relating to derivative instruments have been proposed for deletion. In our opinion, the application of the requirements of the accounting standard to derivative instruments is not well understood, and we believe that rather than deleting requirements, further application guidance is necessary to promote consistent interpretation and application of the liquidity risk disclosures. It would also be useful to include examples of how the disclosures could be crafted to provide meaningful information to users.

Question 5 – Do you agree with the proposal in paragraph 39(b) to require entities to disclose a maturity analysis for non-derivative financial liabilities based on remaining expected maturities if the entity manages the liquidity risk associated with such instruments on the basis of expected maturities? If not, why? What would you propose instead, and why?

We agree with the proposal in paragraph 39(b) to require entities to disclose a maturity analysis for non-derivative financial liabilities based on remaining expected maturities if the entity manages the liquidity risk associated with such instruments on the basis of expected maturities.

Question 6 – Do you agree with the amended definition of liquidity risk in Appendix A? If not, how would you define liquidity risk, and why?

We agree with amending the definition of liquidity risk in Appendix A to the accounting standard, however are concerned that the proposed wording may lead to ambiguity in treatment of instruments that may be settled in either equity instruments or in cash (or another financial asset).

For example, it is unclear whether convertible notes that will mature at a specified future date but may be converted into ordinary shares of the entity at the holder's option before that time, should be included in the maturity analysis under the proposed amendments as while they may be settled in equity instruments, this is not within the control of the issuer

In our opinion, the definition of liquidity risk should also capture those instruments that may potentially be settled, at the holder's option, in cash or another financial asset, to avoid ambiguity in treatment in relation to instruments that *may* result in the outflow of cash or another financial asset. We suggest that the definition be amended as follows:

> "The risk that an entity will encounter difficulty in meeting obligations associated with financial liabilities that ~~are~~ will, or may (at the option of the holder), be settled by delivering cash or another financial asset."

Further, we understand from Introduction paragraph 5(a) and Basis of Conclusions paragraph BC9 to the IASB's exposure draft that the proposed amendments to the definition of liquidity risk are intended to clarify that the liquidity risk disclosures specified by AASB 7.39 are required only in respect of financial liabilities that will result in the outflow of cash or another financial asset. However, we do not believe that the proposed amendments clearly articulate this link, and suggest amending paragraph 39 in the following manner:

> "An entity shall disclose:
> (a) a maturity analysis for derivative financial liabilities that is based on how the entity manages the liquidity risk associated with such instruments.
> (b) a maturity analysis for non-derivative financial liabilities that shows the remaining contractual maturities for such financial liabilities. If the entity manages liquidity on the basis of expected maturities, it also shall disclose the remaining expected maturities for those financial liabilities.
> (c) a description of how it manages the liquidity risk inherent in (a) and (b).
> These disclosures need only be provided in respect of financial liabilities that will, or may, be settled by delivering cash or another financial asset."

Question 7 – Do you agree with the proposed effective date? If not, why? What would you propose instead, and why?

We agree with the proposed effective date.

Question 8 – Are the transition requirements appropriate? If not, why? What would you propose instead, and why?

Other than as noted in Question 3 above in respect of paragraph 27B(b), we agree that no specific transitional provisions are required.

OTHER COMMENTS

Terminology
Paragraph 27B and 27C should clearly indicate that the disclosures apply in respect of financial assets and financial liabilities and not also to equity instruments of the entity.

Classification into different levels
Paragraph 27B(a) should be reworded to address that a class of financial assets or financial liabilities can include individual instruments in different levels of the hierarchy; for example as follows:

> "the level(s) in the fair value hierarchy into which the fair value measurements are categorised in their entirety."

Illustrative examples
The illustrative examples included in IG13A and IG13B show the disclosures by category of financial assets. The text to IG13A further notes that "Disclosures by class of financial instruments would **also** be required ..." (emphasis added). In our opinion, the illustrative examples, and the accompanying text, are not consistent with the requirement in paragraph 27B to make the disclosures by class of financial instrument. Further, the illustrative examples include totals of various amounts – we do not believe that totals are required by the disclosure specified in paragraph 27B(a) or (b). In our opinion, it would be inappropriate for the examples not to be revised before being made in amendments to the Illustrative Guidance accompanying IFRS 7.