



Australian Government

Australian Accounting
Standards Board

Level 7, 600 Bourke Street
MELBOURNE VIC 3000
Postal Address
PO Box 204
Collins Street West VIC 8007
Telephone: (03) 9617 7600
Facsimile: (03)9617 7608

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Mr Gavin Francis
Director of Capital Markets
International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

Dear Mr Francis,

Exposure Draft Improving Disclosures about Financial Instruments: Proposed amendments to IFRS 7

The Australian Accounting Standards Board (AASB) is pleased to submit its comments on the Exposure Draft *Improving Disclosures about Financial Instruments: Proposed amendments to IFRS 7*. In formulating these comments, the AASB considered the views of Australian constituents.

The AASB is broadly supportive of the proposed amendments particularly because they result in greater IASB/FASB convergence and respond to user needs. However, the AASB is concerned that the narrowness of the scope of the proposed changes to IFRS 7 *Financial Instruments: Disclosures* means that other potential improvements to IFRS 7 are overlooked. Therefore, the AASB encourages the IASB to undertake a post-implementation review of IFRS 7 to confirm whether the disclosures are relevant for the purposes of decision making and whether there are other areas of IFRS 7 that can be made more relevant by incorporating other disclosures or amending existing disclosures. The AASB is also concerned that the current drafting has some inconsistencies and can be improved. Areas that are currently unclear are noted in the attached, together with comments on the IASB Exposure Draft specific questions.

If you have any queries regarding this submission, please contact Raymond Yu (ryu@asb.gov.au) or me.

Yours sincerely


Bruce Porter
Acting Chairman

**Exposure Draft *Improving Disclosures about Financial Instruments:*
*Proposed amendments to IFRS 7***

Specific comments

Fair value disclosures

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?

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?

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?
- (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?

Question 1

The AASB agrees with the proposal in paragraph 27A and the rationale for it in paragraph BC4. In addition to the advantages noted in paragraph BC4, the AASB notes that proposed paragraph 27A would give informational value to investors on the subjectivity inherent in the measurements. Measurement of financial instruments with an active market would be less subjective than measurement of financial instruments with no active market.

Question 2

While the AASB broadly agrees with the approach of a fair value hierarchy, it notes the following areas for improvement:

- (a) Level 2 of the proposed hierarchy itself consists of two levels that, if distinguished, would provide useful information for users. One level is “quoted prices in active markets for similar assets or liabilities” and the other level is “other valuation techniques for which all significant inputs are based on observable market data”. The AASB is of the view that the former would be regarded as less subjective than the latter. The disclosure for the latter should be similar to the proposed Level 3 disclosure;
- (b) the term ‘in its entirety’ in paragraph 27A may be unclear to some readers. The AASB thinks that this could be resolved by stating that the level(s) of the fair value

hierarchy must be determined based on the lowest level input that is significant to the fair value measurement in its entirety (as is done in SFAS 157 paragraph 21); and

- (c) consistent with the comment about a post-implementation review of a revised IFRS 7 in the covering letter to these comments, the AASB believes that it would be informative for the IASB to undertake research to determine whether the proposed disclosures have met their objectives in the US (under SFAS 157).

Question 3(a)

The AASB broadly agrees with paragraph 27B but has the following concerns:

- (a) the second last sentence of paragraph 27B specifies that an entity must provide information in a tabular format unless another format is more appropriate. The AASB notes that this approach seems to be inconsistent with the IASB's more principle-based approach to drafting standards;
- (b) some of the proposed disclosures are by class, but the illustrative examples (IG13A and IG13B) are disclosed by IAS 39 measurement category. Although the IASB acknowledges through paragraph IG13A that disclosures by class would also be required, but are not included in the example, the AASB thinks that it would be more helpful to users if by-class were illustrated;
- (c) the AASB believes that the expanded disclosures required by paragraph 27B may be potentially burdensome in some respects. The AASB thinks that some relief should be provided by permitting the reconciliation required by paragraph 27B(b) to be presented net for derivative financial assets and derivative financial liabilities, consistent with SFAS 157; and
- (d) paragraph 27B (and paragraph 27C) should clearly indicate that the disclosures apply in respect of financial assets and financial liabilities only and not to equity instruments of the entity.

Question 3(b)

The AASB broadly agrees with paragraphs 27C but notes that there is an inconsistency between paragraph 25 and proposed paragraph 27C. Paragraph 25 states that:

Except as set out in paragraph 29, for each class of financial assets and financial liabilities (see paragraph 6), an entity shall disclose the fair value of that class of assets and liabilities in a way that permits it to be compared with its carrying amount. [emphasis added]

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, but does not provide the paragraph 29 exception.

Liquidity risk disclosures

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?

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?

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?

Questions 4

The AASB believes that the derivative liquidity risk disclosure requirement should be applicable to derivative financial assets and derivative financial liabilities. This is because derivatives may move from being financial assets to financial liabilities, and vice versa, over time and the asset and liability positions are typically managed together. Therefore, requiring entities to disclose a maturity analysis for only derivative financial liabilities would be insufficient. The AASB's preferred approach would align IFRS 7 closer to SFAS 157, as SFAS 157 allows the reconciliation of fair value measurement of financial assets and financial liabilities to be presented net.

Paragraph B11C provides some examples for scenarios by which an entity includes items in its maturity analysis. In addition to the example in B11C(b), the AASB thinks that it would be useful to include similar examples of gross-settled financial instruments.

As a general comment, the AASB notices that the following examples of factors for disclosure in paragraph 39(c) are proposed for deletion (see deleted paragraph IG3, only some of which has been relocated to paragraph B11E):

- expects some of its liabilities to be paid later than the earliest date on which the entity can be required to pay (as may be the case for customer deposits placed with a bank);
- expects some of its undrawn loan commitments not to be drawn;
- holds financial assets for which there is a liquid market and that are readily saleable to meet liquidity needs; and
- holds financial assets for which there is not a liquid market, but which are expected to generate cash inflows (principal or interest) that will be available to meet cash outflows on liabilities.

The AASB thinks that, since they are examples that are not binding, it would be more helpful to retain the examples.

Questions 5

The AASB broadly agrees with the proposal in paragraph 39(b) but feels that it would be helpful if the IASB provides an explanation regarding the difference in treatment between derivatives and non-derivatives in the Basis for Conclusions.

Question 6

The AASB is of the opinion that the definition of liquidity risk can be improved by amending it to read along the following lines as shown in mark up:

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

In this way, the definition would provide clarity in relation to those instruments (e.g. convertible bonds) that may be potentially settled in either equity instruments or in cash or another financial asset.

Effective date and transition

Question 7

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

Question 8

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

Question 7 and 8

The AASB broadly agrees with the proposed effective date. However in relation to the transition requirements addressed in Question 8, the AASB thinks that it would be onerous to require disclosure of comparative fair value information in the first year of application.

Drafting issues

Std/Para.	Current text (relevant words are highlighted)	Suggestion/comments
IFRS 7.27B(a)	the level in the fair value hierarchy into which the fair value measurements are categorised in their entirety.	Consistent with AASB's comment in Question 2(b), 'level' should be pluralised as 'level(s)' to indicate that a class of financial assets or financial liabilities can include individual instruments in different levels of the hierarchy.
IFRS 7.27B(b)(i)	total gains or losses for the period (realised and unrealised) recognised in profit or loss, and a description of where they are presented in the statement of comprehensive income;	'for the period' should be deleted as it adds no value to the sentence, given that the lead-in refers to 'during the period'.
IFRS 7.27B(b)(ii)	total gains or losses recognised in other comprehensive income;	It is unclear if the reference is <u>net</u> gains or losses when read with IFRS 7.27B(b)(iii)
IFRS 7.27B(b)(iii)	purchases, sales, issues and settlements (net); and	It is unclear if '(net)' refers to settlements only or to purchases, sales, issues and settlements.
IFRS 7.27B(c)	the total amount of unrealised gains or losses for the period in (b)(i) included in profit or loss for those assets and liabilities still held at the end of the reporting period and a description of where those unrealised gains or losses are presented in the statement of comprehensive income.	<ul style="list-style-type: none"> ○ 'total amount of' should be deleted as it adds no value to the sentence. ○ Paragraph reference to '(b)(i)' should be changed to be consistent with the style of paragraph reference in IFRS 7.27B(e)
IFRS 7.27B(d)	... For this purpose, significance shall be judged with respect to profit or loss, and total assets or total liabilities, or, when changes in fair value are recognised in other comprehensive income, total equity.	The 'or' in the phrase 'total assets or total liabilities' leaves it unclear as to when to use total assets and when to use total liabilities.
IFRS 7.27C	An entity shall disclose the fair value, by level of the fair value hierarchy into which the financial instruments are categorised in their entirety, of the financial instruments or the classes of financial instruments that are not measured at fair value in the statement of financial position.	'not measured' should be changed to 'not recognised' to better capture the essence of the sentence.
IFRS 7.39(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.	<ul style="list-style-type: none"> ○ It is unclear if 'liquidity' actually refers to 'liquidity risk', which is the term used more generally in the Exposure Draft. ○ Paragraph B11D clarifies that for disclosure of contractual maturities, the cash flows are undiscounted (paragraph B11D). However, there is no reference to whether the cash flows referred to in paragraph 39(b) of the ED are discounted or undiscounted where the disclosure relates to expected maturities.
IFRS 7 Appendix B Application guidance B11E(c)	has very diverse funding sources;	'very' should be deleted as it adds no value to the sentence.