8 July 2009

Mr Kevin Stevenson
Chairman
Australian Accounting Standards Board
PO Box 204
COLLINS STREET WEST VIC 8007

By email: standard@aasb.gov.au

Dear Kevin

ED 177: Derecognition

Thank you for the opportunity to comment on the AASB Exposure Draft 177 Derecognition. CPA Australia, The Institute of Chartered Accountants in Australia (The Institute) and the National Institute of Accountants (the Joint Accounting Bodies) have 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, academia throughout Australia and internationally.

The Joint Accounting Bodies do not support the approach proposed in the ED. We are not convinced that the removal of the existing risks and rewards test results in better financial reporting. Further, we are not aware of users, preparers, auditors and/or regulators opining that the current derecognition model has resulted in inappropriate financial reporting. That does not mean that the current IAS 39 *Financial Instruments: Recognition and Measurement*, including the derecognition model cannot be improved. We do see some merit in the alternative approach, however it is difficult for us to give it our complete support, given the incompleteness of its discussion in the ED. Adding to our difficulty is the absence of a comprehensive shared vision for the accounting for financial instruments from the International Accounting Standards Board (IASB) and the Financial Accounting Standards Board (FASB).

The Joint Accounting Bodies strongly encourage the IASB and the FASB to use the opportunity presented by the global financial crisis to deliver a principles-based financial instruments standard that is relatively less complicated but still satisfies the needs of preparers and their auditors and the needs of users of financial statements. We think the decisions of the IASB and FASB to not commit to a joint project are not making full use of this opportunity – a joint project would seem more capable of delivering a more permanent global solution. We are concerned the ED proposals are overly concentrated on responding to the accounting issues identified by the G20 and other international bodies. We think this over-concentration will result in a 'quick-fix' to the derecognition requirements of IAS 39, in the absence of adequate consideration of the 'unit of account', the purpose of the statement of financial position, and the requirements for initial recognition and measurement of financial assets and financial liabilities.

Accordingly, the Joint Accounting Bodies strongly encourage the IASB to not proceed. Instead, we suggest the IASB and FASB agree to jointly undertake a project to deliver a principles-based standard.[1] If this is not feasible, then we think the IASB should not finalise any amendments to the derecognition requirements ahead of finalising other aspects of the improvements to IAS 39.

Our response to matters on which specific comment is requested is included in the attached Appendix. Also attached is our submission to the IASB which includes our responses to the specific IASB questions for comment.

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

Geoff Rankin	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**

[1] We acknowledge that adoption of our suggestion would affect the IASB's proposal to issue three financial instruments: recognition and measurement EDs in the next 5 months.

Appendix: Issues 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; and
(ii) public sector entities.

Because we do not support these proposals for the private sector, we are similarly unable to support them for not-for-profit and public sector entities.

(b) Whether, overall, the proposals would result in financial statements that would be useful to users; and

The proposals as currently drafted will not result in financial statements that will be useful to users, as they may in some circumstances not accurately reflect the true position of the entity.

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

The proposals as currently drafted are not in the best interests of the Australian economy as due to the decisions of the IASB and FASB to not commit to a joint project, we are concerned that we will not see the emergence of a more permanent global solution through a principles-based financial instrument standard. Our cover letter is strong in our encouragement of the IASB to not proceed. Instead, we suggest the IASB and FASB agree to jointly undertake a project to deliver a principles-based standard. If this is not feasible, then we think the IASB should not finalise any amendments to the derecognition requirements ahead of finalising other aspects of the improvements to IAS 39.

8 July 2009

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

Email: CommentLetters@iasb.org

Dear Sir David

Comments on ED 2009/3 Derecognition (Proposed amendments to IAS 39 and IFRS 7)

Thank you for the opportunity to comment on the IASB Exposure Draft 2009/3 *Derecognition (Proposed amendments to IAS 39 and IFRS 7)*. CPA Australia, The Institute of Chartered Accountants in Australia (The Institute) and the National Institute of Accountants (the Joint Accounting Bodies) have 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, academia throughout Australia and internationally.

The Joint Accounting Bodies do not support the approach proposed in the ED. We are not convinced that the removal of the existing risks and rewards test results in better financial reporting. Further, we are not aware of users, preparers, auditors and/or regulators opining that the current derecognition model has resulted in inappropriate financial reporting. That does not mean that the current IAS 39 *Financial Instruments: Recognition and Measurement*, including the derecognition model cannot be improved. We do see some merit in the alternative approach; however it is difficult for us to give it our complete support, given the incompleteness of its discussion in the ED. Adding to our difficulty is the absence of a comprehensive shared vision for the accounting for financial instruments from the International Accounting Standards Board (IASB) and the Financial Accounting Standards Board (FASB).

The Joint Accounting Bodies strongly encourage the IASB and the FASB to use the opportunity presented by the global financial crisis to deliver a principles-based financial instruments standard that is relatively less complicated but still satisfies the needs of preparers and their auditors and the needs of users of financial statements. We think the decisions of the IASB and FASB to not commit to a joint project are not making full use of this opportunity – a joint project would seem more capable of delivering a more permanent global solution. We are concerned the ED proposals are overly concentrated on responding to the accounting issues identified by the G20 and other international bodies. We think this over-concentration will result in a 'quick-fix' to the derecognition requirements of IAS 39, in the absence of adequate consideration of the 'unit of account', the purpose of the statement of financial position, and the requirements for initial recognition and measurement of financial assets and financial liabilities.

Accordingly, the Joint Accounting Bodies strongly encourage the IASB to not proceed. Instead, we suggest the IASB and FASB agree to jointly undertake a project to deliver a principles-based standard.[1] If this is not feasible, then we think the IASB should not finalise any amendments to the derecognition requirements ahead of finalising other aspects of the improvements to IAS 39.

Notwithstanding our comments above, our response to matters on which specific comment is requested are 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 (NIA) at tom.ravlic@nia.org.au.

Yours sincerely

Geoff Rankin
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

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[1] We acknowledge that adoption of our suggestion would affect the IASB's proposal to issue three financial instruments: recognition and measurement EDs in the next 5 months.

Question 1—Assessment of 'the Asset' and 'continuing involvement' at reporting entity level
Do you agree that the determination of the item (ie the Asset) to be evaluated for derecognition and the assessment of continuing involvement should be made at the level of the reporting entity (see paragraphs 15A, AG37A and AG47A)? If not, why? What would you propose instead, and why?

The Joint Accounting Bodies agree with the proposal that the determination of the asset to be evaluated for derecognition and the assessment of continuing involvement should be made at the level of the reporting entity. We think the proposal is a better expression of the requirement in the current IAS 39 *Financial Instruments: Recognition and Measurement*.

We would also like to bring to the Board's attention the link with the its discussion paper on the reporting entity, the Exposure Draft ED 10 *Consolidated Financial Statements* and this ED. In our submissions dated 1 September 2008 and 24 February 2009, we have suggested there is a need to include guidance on the boundaries of a reporting entity. The same is true of the current ED. We suggest that the IASB literature provide such guidance.

Question 2—Determination of 'the Asset' to be assessed for derecognition
Do you agree with the criteria proposed in paragraph 16A for what qualifies as the item (ie the Asset) to be assessed for derecognition? If not, why? What criteria would you propose instead, and why?
(Note: The criteria proposed in paragraph 16A are the same as those in IAS 39.)

The Joint Accounting Bodies do not agree with the criteria proposed in paragraph 16A that a part of a financial asset (or a part of a groups of financial assets) qualifies as the "Asset" to be assessed for derecognition only if it represents a right to specifically identified cash flows or a proportionate share of the cash flows from that asset (or group of assets).

We agree with the Dissenters' comment that the proposed approach does not have a strong conceptual foundation. We think that financial assets are bundles of rights and obligations and the right to receive any of the cash flows of a financial asset qualifies as the "Asset" to be assessed for derecognition.

Question 3—Definition of 'transfer'
Do you agree with the definition of a transfer proposed in paragraph 9? If not, why? How would you propose to amend the definition instead, and why?

The Joint Accounting Bodies support the principle of "substance over form". Therefore, we are supporters of the proposal to broaden the definition of "transfer" if it does result in all qualifying transactions irrespective of their form being assessed for derecognition.

Question 4—Determination of 'continuing involvement'
Do you agree with the 'continuing involvement' filter proposed in paragraph 17A(b), and also the exceptions made to 'continuing involvement' in paragraph 18A? If not, why? What would you propose instead, and why?

The Joint Accounting Bodies do not support the proposal.

The role of the 'continuing involvement' filter in the proposed derecognition model is significant. The Joint Accounting Bodies think its purpose in many simple types of transactions is to enable entities to avoid the application of the more complex requirements of proposed derecognition model. The purpose of the 'continuing involvement' filter is not unlike that of the 'risks and rewards' filter in the existing derecognition model – when the entity has transferred substantially all risks and rewards, the other requirements of the existing model are not applied.

We understand that in recent years the concept of the 'risks and rewards' filter has become well understood and is operationally robust. We are not aware of issues arising from its operation in the global financial crisis – to the contrary, some commentators have suggested that the 'risks and rewards' filter has resulted in more appropriate financial reporting. Accordingly, we do not favour its replacement. Some of our members have suggested that they would like to see the IASB and the FASB explore the operation of the alternative approach in conjunction with a 'risks and rewards' filter.

Question 5—'Practical ability to transfer for own benefit' test
Do you agree with the proposed 'practical ability to transfer' derecognition test in paragraph 17A(c)? If not, why? What would you propose instead, and why?
(Note: Other than the 'for the transferee's own benefit' supplement, the 'practical ability to transfer' test proposed in paragraph 17A(c) is the same as the control test in IAS 39.)

Do you agree with the 'for the transferee's own benefit' test proposed as part of the 'practical ability to transfer' test in paragraph 17A(c)? If not, why? What would you propose instead, and why?

The Joint Accounting Bodies do not support the 'practical ability to transfer for own benefit' test.

As stated in our response to Question 4 we think the current 'risks and rewards' filter is operationally robust. We note that the Basis for Conclusions paragraph BC80 states "...that users generally support an approach that would not permit derecognition of a part of a financial asset when the transferor retains substantial risks of ownership of the underlying asset." – a statement we think is supportive of the retention of the 'risks and rewards' filter. In our submission to ED 10, we recommended the need for the inclusion in the Application Guidance of the [proposed] Standard of a discussion of risks and rewards in the context of identifying powers to direct activities. We think any such discussion may usefully inform a similar discussion in the context of the derecognition model in IAS 39.

Further, we are not convinced that the accounting for the sale and repurchase agreements of readily obtainable securities (repo transactions) under the proposals is an improvement. We are not aware of global financial crisis problems with the existing requirements whereby the arrangement is accounted for as a secured borrowing. We note the outcomes of the proposed change are not likely to be consistent with the expectations of the G20 and other international bodies.

Question 6—Accounting for retained interests
Do you agree with the proposed accounting (both recognition and measurement) for an interest retained in a financial asset or a group of financial assets in a transfer that qualifies for derecognition (for a retained interest in a financial asset or group of financial assets, see paragraph 21A; for an interest in a financial asset or group of financial assets retained indirectly through an entity, see paragraph 22A)? If not, why? What would you propose instead, and why?
(Note: The accounting for a retained interest in a financial asset or group of financial assets that is proposed in paragraph 21A is not a change from IAS 39. However, the guidance for an interest in a financial asset or group of financial assets retained indirectly through an entity as proposed in paragraph 22A is new.)

Given that we do not support the proposed approach, the Joint Accounting Bodies also do not agree with this particular aspect of the proposal.

Some of our members have suggested that any further work on the alternative approach should also explore measurement methods in addition to the measurement of the new asset at fair value on initial recognition (that is, the retained interest in the asset transferred).

Question 7—Approach to derecognition of financial assets
Having gone through the steps/tests of the proposed approach to derecognition of financial assets (Questions 1–6), do you agree that the proposed approach as a whole should be established as the new approach for determining the derecognition of financial assets? If not, why? Do you believe that the alternative approach set out in the alternative views should be established as the new derecognition approach instead, and, if so, why? If not, why? What alternative approach would you propose instead, and why?

The Joint Accounting Bodies do not support the approach proposed in the ED, nor can we give our complete support to the alternative approach, although we believe it has some merit.

We are not convinced that the removal of the existing risks and rewards test results in better financial reporting. We understand that market regulators and others have expressed their criticism about the quantum of off-balance sheet securitisations under US financial reporting. However, we are not aware of a similar concern being directed at financial reporting in accordance with IFRS.

That does not mean that the current IAS 39, including the current derecognition model, cannot be improved. We would like to see the IASB and the FASB work together to deliver a principles-based financial instruments: recognition and measurement standard that is relatively less complicated but still satisfies the needs of preparers and their auditors and the needs of users of financial statements. We do not want to see a 'quick-fix' solution. Accordingly, the work of the IASB and the FASB should also include adequate consideration of the 'unit of account', the purpose of the statement of financial position, and the requirements for initial recognition and measurement of financial assets or financial liabilities.

Question 8—Interaction between consolidation and derecognition
In December 2008, the Board issued an exposure draft ED 10 Consolidated Financial Statements. As noted in paragraphs BC28 and BC29, the Board believes that its proposed approach to derecognition of financial assets in this exposure draft is similar to the approach proposed in ED 10 (albeit derecognition is applied at the level of assets and liabilities, whereas consolidation is assessed at the entity level). Do you agree that the proposed derecognition and consolidation approaches are compatible? If not, why? Should the Board consider any other aspects of the proposed approaches to derecognition and consolidation before it finalises the exposure drafts? If so, which ones, and why? If the Board were to consider adopting the alternative approach, do you believe that that approach would be
compatible with the proposed consolidation approach?

An aspect the Board should consider is including a 'risks and rewards' filter in both the approach to consolidation and the two approaches to derecognition. Intuitively, this would result in increased similarity.

However, without detailed analysis, the Joint Accounting Bodies are not in a position to opine on the degree of similarity of the proposed approach to consolidation and the proposed or alternative approaches to derecognition.

Question 9—Derecognition of financial liabilities
Do you agree with the proposed amendments to the principle for derecognition of financial liabilities in paragraph 39A? If not, why? How would you propose to amend that principle instead, and why?
The Joint Accounting Bodies support the amendment of the approach to derecognition of financial liabilities to more closely align it with the definition of a liability in the *Framework*.

However, we are concerned that the IASB has proposed to use the Application Guidance paragraph AG57 to articulate the discharge requirement. We do not think this is helpful to users of the [proposed] Standard who would expect such detail in the Standard itself.

Question 10—Transition
Do you agree with the proposed amendments to the transition guidance in paragraphs 106 and 107? If not, why? How would you propose to amend that guidance instead, and why?

The Joint Accounting Bodies have no comment.

Question 11—Disclosures
Do you agree with the proposed amendments to IFRS 7? If not, why? How would you propose to amend those requirements instead, and why?

Conceptually, the Joint Accounting Bodies think it important that the IASB and FASB not use disclosures as a solution to deficient recognition (derecognition) and measurement requirements.

We are concerned that the increased quantum of disclosure requirements can obscure the quality of the reported financial information. For example, we are not certain that the quality of the financial information is improved by the proposed disclosures about transferred financial assets that have been derecognised. In addition, some of our members have indicated that they will incur significant additional costs to obtain this information.