Fax

To:	Mr Kevin Stevenson	**From:**	Jeremy Robson, ANZ
Fax:	9617 7608	**Pages:**	5
Phone:		**Date:**	19 May 2010
Re:	ED /2010 / 1 Measurement of liabilities in IAS 37	**cc:**	

● **Comments:**

Copy of ANZ submission to IASB on ED /2010 / 1 Measurement of liabilities in IAS 37 follows.

Group Finance
Level 9A, 833 Colllins Street
Melbourne Vic 3008
Phone 03 8654 6580
Fax 03 8654 9944
Robsonj1@anz.com
www.anz.com

Jeremy Robson
Deputy Chief Financial Officer

18 May 2010

Sir David Tweedie
Chairman
International Accounting Standards Board
First Floor, 30 Cannon Street
London EC4M 6XH
UNITED KINGDOM

Submitted electronically through the IASB Internet site (www.iasb.org)

Dear Sir David

Exposure Draft ED/2010/1: Measurement of Liabilities in IAS 37

Thank you for the opportunity to comment on this Exposure Draft (ED).

Australia and New Zealand Banking Group Limited (ANZ) is listed on the Australian Securities Exchange and remains one of a select group of banks who continue to be AA rated. Our operations are predominantly based in Australia, New Zealand and Asia and our most recent annual results reported profits of USD2.7 billion and total assets of USD438 billion.

Summary
Whilst one of the stated objectives of the project on liabilities is to clarify their measurement under IAS 37, in our view the proposed measurement requirements for liabilities will result in more complexity in accounting for liabilities.

In summary, our concerns are as follows:

- The requirements in Appendix B lack clarity and result in potential measurement inconsistency between obligations fulfilled by making cash payments compared to those fulfilled by undertaking a service (notably that a profit margin is built into one but not the other).
- The removal of the 'probability' recognition criterion and the concept of contingent liabilities will result in a further widening of the gap between the accounting treatment of assets and liabilities. To obtain a 'balanced' view of the financial position and performance of an entity, we consider that consistent principles should be applied as far as possible to assets and liabilities. The proposed approach further widens the criteria for assets and liabilities to the extent we believe it would no longer fairly present an entity's financial position, because of the additional liabilities recognised (although assets with equivalent probabilities remain unrecognised).
- We note that the Application Guidance of the proposed standard specifies recognition criteria for restructurings which are difficult to reconcile with the general criteria for recognition of liabilities in the standard. For example, paragraph C4 of the Application Guidance precludes the recognition of a restructuring provision 'even when an entity announces or starts to implement a restructuring plan' on the grounds that the entity could avoid these costs by changing or recalling the plan. In our view the public announcement or commencement of a restructuring plan is sufficient evidence that

an entity has incurred a present obligation for which the recognition of a liability should be required. We consider it inconsistent that the proposed standard would preclude the recognition of a liability in these circumstances yet require recognition of contingent liabilities for which the likelihood of settlement is much less certain.

Our comments in the attached Appendix to this letter also set out our concerns regarding the introduction of an arbitrary "profit estimate" into liability measurement. In our view this will result in entities recognising a profit on activities which, in most cases, they fully intend to carry out themselves.

We are also concerned with the practicality of the probability-weighted average approach to recognising and measuring liabilities and are not supportive of all the additional disclosure requirements in the proposed Standard. In particular the requirement to provide a reconciliation of each class of recognised liability merely adds another mandated disclosure with little obvious benefit to the users of financial statements.

Detailed comments on select questions raised in the ED are attached to this letter. Should you have any queries on our comments, please contact Rob Goss, Head of Accounting Policy, Governance and Compliance at Rob.Goss@anz.com.

Yours sincerely

JEREMY ROBSON
Deputy Chief Financial Officer

Copy: Chairman, Australian Accounting Standards Board (AASB)

Appendix

Question 1

The proposed measurements requirements are set out in paragraphs 36A-36F. Paragraph BC2-BC11 of the Basis for Conclusions explain the Board's reasons for these proposals. Do you support the requirements in paragraphs 36A-36F? If not, with which paragraphs do you disagree, and why?

Whilst we are generally supportive of the requirements in paragraphs 36A-36F, we have a number of concerns regarding the implementation of these requirements in Appendix B. In particular:

- A profit margin will be required to be included in the measurement of obligations fulfilled by providing a service whereas our understanding is that this margin will not be included in measuring obligations fulfilled by making a cash payment. In our view, this results in inconsistency in the measurement of provisions.
- Where obligations are fulfilled by making payments to the counterparty, the ED states that the amount of the obligation are the relevant outflows including "payments to the counterparty" and "associated costs, such as external legal costs or the costs of an in-house legal department attributable to that obligation" (para. B7). Further clarification of the costs permitted to be included in the relevant outflows should be provided. For example, should only incremental costs be included or is it permissible to allocate other employee costs in addition to the cost of an in-house legal department and, if so, on what basis should such costs be included?
- We consider that the use of a probability-weighted average approach:
    - Is not suitable for many liabilities covered by the proposed IAS 37, such as legal claims and restructuring provisions. Such obligations tend to be one-off or unique in nature and therefore it can be very difficult to reliably assign probabilities to various outcomes which may (or may not) arise. We prefer that probability weighting be done according to the most probable outcome.
    - Will require a liability to be recognised even when the probability of an outflow is considered remote (e.g. less than 10% chance). In our view this results in information which is nonsensical and at odds with the general concept of a liability. We consider that liabilities for which the probability of an outflow is remote should not be required to be recognised, consistent with current well-established practice.

If the current proposals are pursued we concur with the alternative views expressed by members of the IASB in paragraphs AV5 and AV6 that further practical guidance is needed on the circumstances in which the risk adjustment should be included in the measurement of a liability and how it should be determined. It may be useful to include further guidance or examples to illustrate the determination of the risk adjustment. We also note that a risk adjustment may result in an amount which is higher than the alternative measures specified in the proposed standard, i.e. higher than the amount that the entity would rationally pay to cancel or transfer the obligation.

Question 2

Some obligations within the Scope of IAS 37 will be fulfilled by undertaking a service at a future date. Paragraph B8 of Appendix B specifies how entities should measure the future outflows required to fulfil such obligations. It proposes that the relevant outflows are the amounts that the entity would rationally pay a contractor at a future date to undertake the service on its behalf. Paragraphs BC19-BC22 of the Basis for Conclusions explain the Board's rationale for this proposal. Do you support the proposal in paragraph B8? If not, why not?

We disagree that obligations fulfilled by undertaking a service should be measured by reference to the amount the entity would rationally pay a contractor to undertake the service on its behalf.

We note that the arguments advanced in favour of the 'contractor price' approach include the view that there is a market for most types of services. In our view, many service obligations are unique to each entity, therefore estimates of the price a contractor would charge for undertaking the service will frequently not be readily available. This will require entities to make estimates of the price a contractor would charge for providing a service which will be very subjective and impose additional costs of accounts preparation for little apparent benefit. We are also concerned that some provisions may involve both cash payments and undertaking a service and that the measurement of provisions in these circumstances will be complex and result in different measurement practices being applied to various components of the overall provision.

We concur with the alternative views expressed by members of the IASB in paragraphs AV2 to AV4 of the ED that the measurement of the obligation should not include a profit margin.

In our view the most relevant and reliable measure for service obligations covered by the proposed IAS 37 is the minimum cost expected to be incurred by the entity to satisfy the obligation. The cost model has proved workable and effective in measuring provisions under current IAS 37 as well as other standards that permit use of the cost basis. By contrast, measuring liabilities inclusive of a profit margin would not provide more useful information to users.

Question 3

Paragraph B9 of Appendix B proposes a limited exception for onerous contracts arising from transactions within the scope of IAS 18 Revenue or IFRS 4 Insurance Contracts. The relevant future outflows would be the costs of the entity expects to incur to fulfil its contractual obligations, rather than the amounts the entity would pay a contracted to fulfil them on its behalf. Paragraphs BC23-BC27 of the Basis for Conclusions explain the reason for this exception. Do you support the exception? If not, propose instead and why?

If all liabilities were measured using a single cost principle there would be no need for these exemptions. However, if the proposals are pursued we have no objection to this limited exemption pending the development of new standards to replace IAS 18 and IFRS 4.

We note that the effect of this exemption would allow onerous contracts arising under the abovementioned standards to be measured using the cost basis. In our view, this exemption adds further weight to the retention of the cost basis as the preferred measurement model for all liabilities.