



**Australian Government**  
**Australian Accounting  
Standards Board**

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26 May 2005

Mr Gilbert Gélard  
Acting Chairman – IFRIC  
International Accounting Standards Board  
30 Cannon Street  
London EC4M 6XH  
United Kingdom

Dear Sir,

**IFRIC Draft Interpretation D15**  
***Reassessment of Embedded Derivatives***

The Urgent Issues Group (UIG) has considered the proposals in Draft Interpretation D15, prepared by the International Financial Reporting Interpretations Committee (IFRIC). The UIG is pleased to provide its principal views in respect of the proposals for consideration by the IFRIC. The UIG supports the general principles articulated by Draft Interpretation D15.

The UIG considers that the finalised Interpretation would be improved if it clarified some issues that Draft Interpretation D15 leaves unresolved. The Draft Interpretation appears not to cover all situations involving host contracts and their embedded derivatives. In particular, a situation in which a non-financial host contract is closely related to an embedded derivative at inception results in the two contracts being accounted for as one non-financial instrument, placing the instrument outside the scope of International Accounting Standard IAS 39 *Financial Instruments: Recognition and Measurement*, hence negating the relevance of the guidance proposed by the Draft Interpretation. Therefore, the UIG considers that the reassessment of an instrument deemed to be non-financial at inception should be addressed in any Interpretation.

Paragraph 4 of the Draft Interpretation states that “subsequent reassessment is prohibited unless there is a change in the terms of the contract, in which case it is required”. The UIG considers that this guidance is limited because a “change in the terms of the contract” and the term “contract” are not adequately defined. If a situation arises wherein a hybrid contract is separated into two distinct components at inception, these two components (i.e. the host contract and the embedded derivative) are both deemed to be contracts. Hence it is unclear to which contract the guidance refers where there is a “change in the terms of the contract”, or whether it is to both contracts.

Furthermore, the question arises whether a change in the terms of the contract gives rise to a reassessment per se, or rather to the creation of a different and new contractual situation (e.g. where previously an embedded derivative and its host contract were deemed to be closely related and recognised as one, a change in the terms of the contract may require derecognition of some component of the financial instrument). The UIG considers that clarification regarding the status of a contract when its terms have been changed and whether such a change qualifies for derecognition under IAS 39 is necessary. In the event that derecognition applies, the issue may not be one of reassessment, but rather of re-recognition.

Please contact us if further information or clarification is required.

Yours faithfully,

A handwritten signature in black ink that reads "David Boymal," with a comma at the end. The signature is written in a cursive, slightly slanted style.

David Boymal  
Chairman, AASB and UIG