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Melbourne Victoria 3000
AUSTRALIA

31 January 2011

Sir David Tweedie
Comment Letters
International Accounting Standards Board
1st Floor 30 Cannon Street
London EC4M 6XH
UNITED KINGDOM

Dear Sir David,

Effective Dates and Transition Methods

We are pleased to have the opportunity to comment on the Request for Views on Effective Dates and Transition Methods (Request for Views) in respect of the new International Financial Reporting Standards (IFRSs).

National Australia Bank (NAB) is one of the four major banks in Australia. Our operations are predominately based in Australia, New Zealand, the United Kingdom, the United States and Asia. In our most recent annual results we reported net profit after tax of A$4.2 billion and total assets of A$686 billion.

We prefer a single date approach for the implementation of the new IFRSs mainly based on the following reasons:

- minimise the period of change and disruption to the business;
- appropriate focus, time and resources will be directed to establishing a project for planning and implementation given scale;
- reduce the need for ongoing communication of accounting policy changes to analysts and investors; and
- improve comparability across entities.

We propose that the mandatory effective date for all new standards should be set for annual reporting periods commencing at least after 1 January 2015 for the adoption of all new IFRSs, subject to final standards being completed by June 2011, to enable sufficient time for implementation given the number and significance of the proposed changes in accounting requirements. However, it is difficult to be definitive on a proposed effective date as the final standards for some projects subject to the Request for Views are yet to be published and certain aspects still need to be addressed (e.g. macro hedge accounting and impairment). Accordingly there is still some uncertainty around the full impact these projects will have on entities and the degree of effort and time required for implementation. In addition, there will be a number of potential regulatory capital and tax implications arising from these changes that need to be appropriately addressed once the final standards are published. As a result, the effective date of 1 January 2015 should be viewed as a date that could be further extended once final standards are published and should be reviewed further once the constituents have a complete understanding of the extent of effort required for implementation.

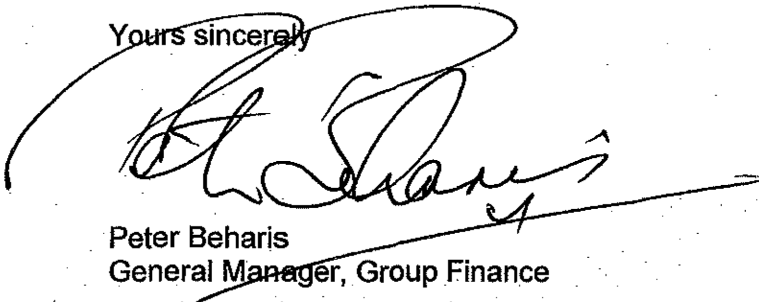
We further propose that an option for early adoption be permitted to allow entities to report information under an improved accounting framework earlier and provide some scope for entities to manage the timing, resource requirements and costs of implementation. Whilst we appreciate that permitting early adoption reduces comparability across entities, we believe that the disclosure requirements provide sufficient transparency to address this concern.

In respect to the transition method proposed for each project, please refer to our comment letters submitted for the various projects. Our views on the transition method proposed for each project remain the same irrespective of whether it is considered in the context of a broad implementation plan or in isolation. In general, we consider retrospective application to be the most appropriate transition method where it is possible and practical to do so. We support a limited retrospective method that adopts a simplified approach for transition as a practical expedient if it achieves a reasonable and appropriate outcome.

The Appendix to this letter outlines our responses to questions within the Request for Views.

Should you have any queries regarding our comments, please do not hesitate to contact Marc Smit, Head of Group Accounting Policy at marc.smit@nab.com.au.

Yours sincerely



Peter Beharis
General Manager, Group Finance

Detailed Answers to Questions

BACKGROUND INFORMATION

Question 1 – Please describe the entity responding to this Request for Views.

National Australia Bank (NAB) is one of the four major banks in Australia and is publicly listed on the Australian Stock Exchange. Our operations are predominately based in Australia, New Zealand, the United Kingdom, the United States and Asia. In our most recent annual results we reported net profit after tax of A$4.2 billion and total assets of A$686 billion. NAB and its subsidiaries mainly prepare its financial statements in accordance with IFRS. One of the subsidiaries prepares audited financial information in accordance with US GAAP.

Based on the current status of the projects, the proposed new IFRSs will have a pervasive impact on the organisation given the nature of our operations. Significant time and resources will need to be dedicated for implementation as a substantial volume of transactions and data would need to be assessed and collected, systems and processes to be adapted or newly developed, and personnel will need to be trained in order to implement and apply the new accounting requirements. Specifically, the following projects would have the greatest impact:

- Consolidation – NAB sponsors and transacts with many structured entities requiring consolidation conclusions to be reassessed and a considerable amount of information on those entities to be collated to comply with the proposed substantive disclosure requirements;

- Financial instruments – assessment of a significant volume of transactions, adapting measurement approaches and quantification of the impact on transition will be required. In addition, we expect considerable changes to systems and models would be required to adopt the new impairment and hedge accounting model once it is finalised;

- Insurance contracts – through our wealth management division, MLC, we provide investment, superannuation and insurance solutions to corporate and institutional customers. MLC is a leading provider of life insurance in Australia and holds the number one position for personal insurance annual inforce premiums. Significant financial and administration system changes would be required to implement the proposals. In particular, modelling of risk adjustments, understanding cohort measurement and considering the impact of increased maintenance costs on assumption setting; and

- Leases – we have a substantial number of leasing arrangements in place, both as a lessee and lessor, for which underlying information will be required for ongoing calculations and reassessment of assumptions throughout the period of each lease contract under the current proposals. As an indication we estimate that we are party to approximately 157,000 leases as lessor in our Australian region alone (there are further leases in other countries that we operate in), in addition to leases where we are the lessee.

Whilst the other projects within the scope of the Request for Views would not have the same degree of impact as the abovementioned projects, we believe that necessary time and resources will still be required for transition and adapting systems and processes for ongoing

implementation. Therefore, sufficient lead time will be required to plan investment activities including assessing technology requirements, and acquiring the appropriate expertise and capabilities to manage and implement change. Australian financial institutions are already undergoing significant changes in the regulatory environment with the introduction of the National Consumer Credit Protection Act and the new international regulatory framework for banks (Basel III), which will absorb considerable time and resources.

Further, since the final standards for these projects have yet to be published and certain aspects still need to be addressed (e.g. macro hedge accounting and impairment), there is still some uncertainty around the full impact these projects will have and the degree of effort and time required for implementation. In addition, there will be a number of potential regulatory capital and tax implications arising from these changes that needs to be appropriately addressed once the final standards are published.

Consequently, it is our view that the 1 January 2013 effective date set for IFRS 9 will be extremely challenging to achieve given the current status of standards development and the number and significance of the changes being introduced. In our opinion, the mandatory effective date for all new standards including IFRS 9 should be set for annual reporting periods commencing at least after 1 January 2015, subject to final standards being completed (and assuming that the final standards do not include significant unknown issues not already in the exposure drafts) by June 2011, to give entities adequate time to plan for and implement the new requirements appropriately.

PREPARING FOR TRANSITION TO THE NEW REQUIREMENTS

Question 2(a) - Which of the proposals are likely to require more time to learn about the proposal, train personnel, plan for, and implement or otherwise adapt?

The projects that will likely to require more time and effort for training, planning and implementation are financial instruments, insurance contracts, consolidation and leases based on the main reasons highlighted above.

Question 2(b) – What are the types of costs you expect to incur in planning for and adapting to the new requirements and what are the primary drivers of those costs? What is the relative significance of each cost component?

The type of costs expected to be incurred and main drivers can be broadly summarised as follows:

- Personnel – extensive personnel time will be required for learning, training, planning and implementing the changes arising from the new standards within our core business, finance and IT processes and internal controls framework.
  In addition, effort and time will be required for education and messaging to internal and external stakeholders including our front line bankers and analysts for the expected changes in accounting treatment and its impact on customers' behaviour, profit or loss patterns, key financial ratios and performance measures.

- Consultancy – it is expected that external consultants will be engaged to assist with implementation efforts. The level of engagement will largely be dependent on the final versions of the standards, implementation approach, together with the time frame for implementation (a tight timeframe is likely to require greater engagement of consultants to assist).

- Technology – given the major changes being proposed with the new projects, it is expected that changes to, or development of, new business systems and models will be required in order to apply the new standards. For example, we anticipate the following key changes based on the current drafting of the new projects:

  - Financial instruments – development of new expected loss impairment models; and modification or development of systems for the application of hedge accounting;

  - Insurance – modification or development of systems that can account for separate risk margins and residual margins, in addition, systems or models to capture valuation inputs and perform calculations; and

  - Leases – sourcing of new systems or modifications to existing systems will be required to capture the required data and perform lease calculations on an ongoing basis.

  We envisage that technology related costs would have a significant impact to the organisation in the implementation of the new requirements.

Question 3 – Do you foresee other effects on the broader financial reporting system arising from these new IFRSs? For example, will the new financial reporting requirements conflict with other regulatory or tax reporting requirements? Will they give rise to a need for changes in auditing standards?

The proposed new standards will have some potential regulatory capital and tax implications, namely:

- Leases – In respect of regulatory capital, there is a possibility that Australian banks may be required to hold regulatory capital in respect of right-of-use assets if they are considered intangible assets, and not viewed in conjunction with the liability to make lease payments by our local regulator.

- Insurance – in the absence of change to Australian tax laws, there would be a significant cash flow impact from the proposed transitional requirements from a tax payment which is effectively brought forward by the transfer of future planned profits to retained earnings. We note that the previous transition from Australian GAAP to IFRS, relief was not provided from tax consequences of transferring amounts to retained earnings on adoption of new or revised accounting standards. In addition, a significant tax payment would result in an additional capital requirement under Australia's prudential regulation regime.

- Financial instruments – Australian tax law has recently been amended allowing the taxation of financial arrangements to be largely in line with current accounting standards (i.e. IAS 39). The implementation of IFRS 9 will therefore have taxation implications for Australian companies where the accounting treatment for a financial arrangement under IFRS 9 and IAS 39 differs. The Australian tax law will be required to be further amended in order realign accounting and tax and this is likely to take some time to accomplish.

Question 4 – Do you agree with the transition method as proposed for each project, when considered in the context of a broad implementation plan covering all the new requirements? If not, what changes would you recommend, and why? In particular, please explain the primary advantages of your recommended changes and their effect on the cost of adapting to the new reporting requirements.

Please refer to our comment letters submitted for the various projects in respect to our views on the proposed transition methods. Our views on the transition method proposed for each project remain the same irrespective of whether it is considered in the context of a broad implementation plan or in isolation.

In general, we consider retrospective application to be the most appropriate transition method where it is possible and practical to do so. We support a limited retrospective method that adopts a simplified approach for transition as a practical expedient if it achieves a reasonable and appropriate outcome. For example, the proposed transition method for the lease project adequately balances the need for comparable information with the effort and costs associated with full retrospective application. This is achieved by simplifying the measurement of assets and liabilities arising from leases to be based only on the remaining lease payments.

We strongly disagree with the proposed transitional requirements for the insurance project as discussed in our comment letter. The proposed transitional requirements are to measure insurance contracts at the present value of fulfilment cash flows, which in effect results in the residual margin being transferred to retained earnings. Setting the residual margin to zero on transition will result in mature and profitable life insurance businesses reporting little profit or loss for several years until the business written after transition becomes a significant proportion of the portfolio. Such a representation of the underlying performance of the business is not considered appropriate and is not in line with market expectations of the life insurance industry particularly as there is future benefit in the portfolio.

We also disagree with the transitional method for IFRS 9 requiring retrospective application only for assets that have not been derecognised at the date of initial application. This approach would reduce the meaningfulness of comparative figures since it will be a mix of two accounting models. In addition, the implementation of the transitional requirements will be extremely challenging as comparative data cannot be determined until after the date of initial application and will require significant amount of time and effort to make the necessary calculations and adjustments. We propose that entities should have the option to present comparative figures for all financial assets under IFRS 9.

Further, given the final standards for some projects subject to the Request for Views are yet to be developed and published, we believe the effective date for IFRS 9 should be deferred to annual reporting periods commencing at least after 1 January 2015. Consequently, the period for which early adoption is permitted without the requirement to restate comparatives should be extended.

EFFECTIVE DATES FOR THE NEW REQUIREMENTS AND EARLY ADOPTION

Question 5 (a) – Do you prefer the single date approach or the sequential approach? Why? What are the advantages and disadvantages of your preferred approach? How would your preferred approach minimise the cost of implementation or bring other benefits? Please describe the sources of those benefits (for example, economies of scale, minimising disruption, or other synergistic benefits).

We prefer a single date approach for the implementation of the new IFRSs mainly based on the following reasons:

- minimise the period of change and disruption to the business;
- appropriate focus, time and resources will be directed to establishing a project for planning and implementation given scale;
- reduce the need for ongoing communication of accounting policy changes to analysts and investors; and
- improve comparability across entities.

We propose that the mandatory effective date for all new standards should be set for annual reporting periods commencing at least after 1 January 2015 for the adoption of all new IFRSs to enable sufficient time for implementation given the number and significance of the proposed changes in accounting requirements. Please refer to question 5 (b) below for further details.

However, we propose that an option for early adoption be permitted to allow entities to report information under an improved accounting framework earlier and provide some scope for entities to manage the timing, resource requirements and costs of implementation. Whilst we appreciate that permitting early adoption reduces comparability across entities, we believe that the disclosure requirements provide sufficient transparency to address this concern.

Question 5 (b) – Under a single date approach and assuming the projects noted in the introduction are completed by June 2011, what should the mandatory effective date be and why?

We propose that the mandatory effective date for all new standards should be set for annual reporting periods commencing at least after 1 January 2015 to give entities adequate time to plan and implement the new requirements appropriately given the number and significance of the proposed changes in accounting requirements. However, it is difficult to be definitive on a proposed effective date as the final standards for some projects subject to the Request for Views are yet to be published and certain aspects still need to be addressed (e.g. macro hedge accounting and impairment). Accordingly there is still some uncertainty around the full impact these projects will have on entities and the degree of effort and time required for implementation. In addition, there will be a number of potential regulatory capital and tax implications arising from these changes that need to be appropriately addressed once the final standards are published. As a result, the effective date of 1 January 2015 should be viewed as a date that could be further extended once final standards are published and should be reviewed further once the constituents have a complete understanding of the extent of effort required for implementation.

Question 5(c) – Under the sequential approach, how should the new IFRSs be sequenced (or grouped) and what should the mandatory effective dates for each group be? Please explain the primary factors that drive your recommended adoption sequence, such as the impact of interdependencies among the new IFRSs.

We do not support the sequential approach.

Question 5 (d) – Do you think another approach would be viable and preferable? If so, please describe that approach and its advantages.

No, please refer to our response in question 5 (a).

Question 6 – Should the IASB give entities the option of adoption some or all of the new IFRSs before their mandatory effective date? Why or why not? Which ones? What restrictions, if any, should there be on early adoption (for example, are there related requirements that should be adopted at the same time)?

Yes, please refer to our response in question 5 (a).

INTERNATIONAL CONVERGENCE CONSIDERATIONS

Question 7 – Do you agree that the IASB and FASB should require the same effective dates and transition methods for their comparable standards? Why or why not?

Yes, however we believe that convergence efforts should not impact the IASB's timeline with issuing the new IFRSs and should not prevent entities early adopting the new accounting standards prior to their effective dates.

CONSIDERATION FOR FIRST-TIME ADOPTERS OF IFRSs

Question 8 – Should the IASB permit different adoption dates and early adoption requirements for first-time adopters of IFRSs? Why, or why not? If yes, what should those different adoption requirements be, and why?

No, we believe that the mandatory effective dates and early adoption requirements should be consistent for current preparers and first-time adopters of IFRSs. This should be undertaken on the basis that the option for early adoption is available immediately after the final standards have been issued by the IASB and endorsed by the local accounting standard setter.