21 May 2010

Mr Kevin Stevenson
Chairman
Australian Accounting Standards Board
PO Box 204
Collins Street West Victoria 8007

Via email: standard@aasb.gov.au

Dear Mr Stevenson

Comments on Exposure Draft 189 Financial Instruments: Amortised Cost and Impairment

Thank you for the opportunity to comment on the AASB Exposure Draft 181 Fair Value Measurement. CPA Australia, the Institute of Chartered Accountants (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.

We are unable to support the ED, and we have attached our submission to the IASB which explains our reasons. We understand you are in the process of 'outreaching' to the Australian and Asian banking communities, asking them to provide you with more information on applying the current model. We commend you on these efforts as we consider that more guidance on the current model would be preferable as in interim solution until full convergence with the US can be achieved in this area. Given this, we do not consider the expected loss proposals would result in useful financial statements to users and would not be in the best interests of the Australian and New Zealand economies.

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

Alex Malley
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

21 May 2010

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

Via "Open to comment" page on www.iasb.org

Dear Sir David

Comments on Exposure Draft ED/2009/12 Financial Instruments: Amortised Cost and Impairment

Thank you for the opportunity to comment on the IASB Exposure Draft Financial Instruments: Amortised Cost and Impairment. CPA Australia, The Institute of Chartered Accountants (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 and academia throughout Australia and internationally.

One result of the global financial crisis was a call to accounting standard setters from various international groups and bodies such as the G20 to improve the accounting for financial instruments, in particular impairment. We acknowledge the efforts of the IASB to deliver a suitable response. However, the proposals in the ED do not achieve convergence with US GAAP and as a result we are unable to support it at this time. The proposals appear to be inconsistent with a true amortised cost measurement model and inconsistent with other IFRS standards and projects.. It is for these reasons the IASB should defer its own consideration the of current exposure draft and work with the Financial Accounting Standards Board (FASB) to expose for public comment a comprehensive articulation of an agreed proposed approach to impairment. We offer the following observations on the content of the ED and hope the IASB finds them useful in understanding our concerns.

Convergence
We are disappointed that the FASB and IASB have gone their separate ways and are producing different requirements for financial instruments when an acknowledged objective of joint work is to eliminate differences between the two bodies of accounting literature. The FASB will soon issue its exposure draft on accounting for financial instruments, which along with being different to the IASB's final decisions on classification and measurement will propose an incurred loss model. It is unfortunate timing as it would have been useful for constituents to have had the time to fully understand the FASB proposals before commenting on the IASB's proposals for impairment. Once again we strongly urge the boards to work more closely together in coordinating their work on joint projects and on the issuance of pronouncements.

Proposals not true to the Framework and other projects
The ED refers to amortised cost as a cost-based measurement however the way it is described in the proposals does not appear to be a true reflection of a cost-based measurement for the reasons outlined below.

In the conceptual framework project, one of the measurement approaches tentatively decided on (in January 2009) was "actual past entry prices adjusted for interest accruals, depreciation, amortization, impairments, and similar things". In the report to the boards in April 2007, this measurement approach was referred to as 'modified past amount' and defined as 'the remainder of an asset's (or a liability's) original past entry price ...after assigning some of that price to subsequent accounting periods, according to an accounting rule for amortization..." The proposals do not appear to fit this definition, given that the proposals require amortised cost to reflect current inputs regarding cash flow estimates at each measurement date. Paragraph BC 47 of the ED states the fact that the effective interest rate is set at initial recognition and is used as the discount rate (instead of using a current market rate) means that amortised cost is a cost-based measurement. We consider the fact that forward looking information is required in the measurement suggests that this is not a cost-based measurement as defined in the current position of the conceptual framework project.

There are also inconsistencies noted with other projects. The revenue recognition project focuses on contractual rights, whereas the focus of the ED is on expectations and mixes revenue recognition with expense recognition. The liabilities project (amendments to IAS 37) focuses on present obligation and reliable measurement, and has removed the probability criterion so that the focus shifts from predicting the likely outcome to judging whether the entity has an obligation. The expected loss model however is proposing the opposite – it removes the judgement of whether a loss event has occurred to instead require predicting a likely outcome.

The current framework defines income and expenses as increases/decreases in future economic benefits *during* the accounting period. This would be contrary to the ED which would require an entity to book *future* expected losses into the *current* accounting period. This would also be contrary to the requirement in IAS 37 that future operating losses cannot be provided for. The expected loss model is also inconsistent with the way in which other assets are assessed for impairment under IAS 36 *Impairment of assets*, which requires the identification of impairment indicators. The existence of two different impairment models for assets is unsupported and further highlights the need for the conceptual framework to be completed so new or revised standards are consistent with a core set of principles and with each other.

Cost
Despite acknowledging that the expected loss model would be costly to apply given the responses from the ITC, it appears that the IASB has ignored this in paragraph BC30. We do not consider the arguments put forward in BC30 to be valid, as the degree of estimation and uncertainty that these proposals would introduce would be at a very high level, as noted in the alternative views, paragraph AV2.

Smoothing
We are also concerned that the expected loss model would give management a way to manipulate profit. Paragraphs BC 35-36 note that an entity is required to revise its estimates which can give rise to gains even if no impairment had been previously recognised and impairment reversals. Given that the expected loss model relies on expectations only and not on more substantial evidence such as a debtor defaulting, will allow entities to take advantage of it in order to get the result they are after. Paragraph BC30 notes that estimation uncertainty and the use of assumptions is not new however the increased focus on fair values and other areas where estimation and assumptions are required will ultimately have an impact on how and whether these items can be audited.

We do not believe the expected loss model would provide useful information to users either as it attempts to project what the financial impact will be in some future period instead of reporting on what the present current financial impact is. Where there is evidence to suggest that a debtor is impaired, then surely this is more relevant and reliable information to users than what management considers might happen in the future? The role of financial statements should not be to predict future events but to provide relevant and reliable information based on current or historical data.

Non-financial institutions
The proposals are overly complex, not just for financial institutions, but more so for other entities having few financial assets other than non-interest bearing receivables. As noted earlier, the ED mixes revenue recognition with expense recognition, which is even more of a concern for these other entities given that impairment of debtors is typically treated as an operating expense and accounted for separately from revenue. Not only would the proposals be difficult for financial institutions to apply in practice, but it will also be an unnecessary burden on other entities. We consider it important that a separate section for receivables such as trade receivables be developed that makes clear that simple calculation of losses will suffice as there are no interest payments.

Concluding comments
Australia's experience with applying the incurred loss model is generally positive but we can understand that each jurisdiction may interpret the existing requirements differently. An interim solution (with the final goal being convergence with US GAAP) may be to provide additional guidance that better articulates the existing model (as opposed to providing examples to illustrate the application of the existing model), instead of replacing it with a complex model that will be extremely difficult to implement and apply, will not provide users with reliable and relevant information and does not achieve convergence.

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 (National Institute of Accountants) at tom.ravlic@nia.org.au.

Yours sincerely

Alex Malley	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