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Hans Hoogervorst
Chairman
International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

Dear Hans,

On behalf of the Austrian Financial Reporting and Auditing Committee (AFRAC), the privately organised standard-setting body for financial reporting and auditing standards in Austria, I appreciate the opportunity to comment on Exposure Draft the ED/2013/2 Novation of Derivatives and Continuation of Hedge Accounting – Proposed amendments to IAS 39 and IFRS 9 (ED). Principal authors of this comment letter were Peter Bitzyk, Florian Botschen, Peter Häfliger, Michael Hammer, Heiner Klein, Philip Kudrna, Caroline Pranzl, Raoul Vogel, Alexander Schiebel and Roland Nessmann.

AFRAC appreciates the opportunity to comment on the questions raised by the proposed changes in hedge accounting because of their importance for the whole financial industry. Our comments deal especially with the questions raised with respect to the scope, which in our view is too narrow.

General remarks

AFRAC considers that the scope of application of the ED is too narrow. One of the conclusions drawn from the financial crisis was that the stability of the financial markets should be strengthened by having derivative transactions in interbank business cleared through central counterparties (CCP), so that markets and regulatory authorities would more quickly recognise any imbalances and be able to take the necessary remedial action. It was quickly recognised that this would only lead to early success if existing derivatives were also included in the process.

The purpose of the present ED is to ensure that this measure to promote economic stability does not result in balance sheet instability, that derivative transactions that up until now were concluded without CCPs and to which hedge accounting under IAS 39 was applied now no longer satisfy the requirements for hedge accounting under IAS 39 because of the necessary change in counterparties. Such changes in counterparties, therefore, are to be disregarded under the rules for

hedge accounting in IAS 39 and IFRS 9. This is the only way to present a true and fair view of the activities of the reporting entity in its financial reporting.

In our view, however, the present ED too narrowly limits the scope of this good and correct new rule and thus puts achievement of the amendment's objective at risk. In AFRAC's view, there are also the following two important points.

1. All changes in counterparties in connection with the transfer of an existing derivative to a CCP should be entitled to this relief, not just those required under statutory regulations, since every transfer of an existing derivative to a CCP contributes to the desired financial stability.
2. As the ED stands at present, transactions would need to be concluded directly with the CCP in order for the relief to be available: It is, however, not in any way foreseen that every financial institution will contract directly with a CCP; what is foreseen is that certain major banks will act as Clearing Members (CM), through which the majority of other financial institutions (Clients and Indirect Clients) will bring their derivatives into the CCP system. In our view, it is absolutely necessary both in the interests of financial markets stability and for a true and fair view of the entity's economic activities that transactions that are passed on by Clients and Indirect Clients via transactions with a CM to the CCP should also be entitled to the relief proposed by the ED.

Specific remarks

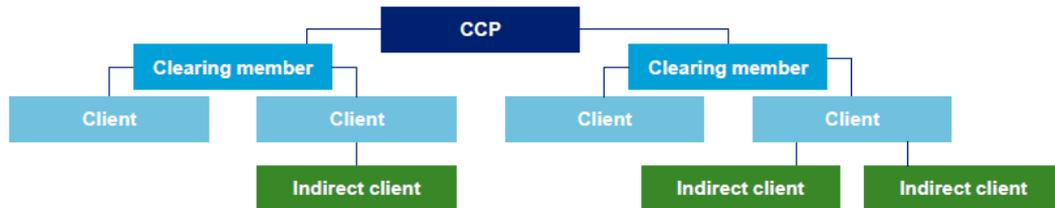
Question 1: The IASB proposes to amend IAS 39 so that the novation of a hedging instrument does not cause an entity to discontinue hedge accounting if, and only if, the following conditions are met:

- (i) the novation is required by laws or regulations;
- (ii) (ii) the novation results in a central counterparty (sometimes called 'clearing organisation' or 'clearing agency') becoming the new counterparty to each of the parties to the novated derivative; and
- (iii) The changes to the terms of the novated derivative arising from the novation of the contract to a central counterparty are limited to those that are necessary to effect the terms of the novated derivative. Such changes would be limited to those that are consistent with the terms that would have been expected if the contract had originally been entered into with the central counterparty. These changes include changes in the collateral requirements of the novated derivative as a result of the novation; rights to offset receivables and payables balances with the central counterparty; and charges levied by the central counterparty.

Do you agree with this proposal? If not, why? What criteria would you propose instead, and why?

As explained under *General remarks*, we see the scope of application as being too limited. As only major financial institutions can or will succeed in becoming CMs, it is necessary both for financial markets stability and for a true and fair view of the economic activities of reporting entities that all financial institutions should have the opportunity to transfer – either directly or indirectly – their derivatives to CCP, without that having negative effects on their hedge accounting.

The diagram below should help to explain how we think the system should work:



Every derivative transferred directly or indirectly by a financial institution to a CCP should be covered by the new rule proposed in the ED, since this will help make the financial system more stable.

Question 2: The IASB proposes to address those novations arising from current changes in legislation or regulation requiring the greater use of central counterparties. To do this it has limited the scope of the proposed amendments to a novation that is required by such laws or regulations. Do you agree that the scope of the proposed amendment will provide relief for all novations arising from such legislation or regulations? If not, why not and how would you propose to define the scope?

See our answer to Q1 and in the *General remarks* above.

Question 3: The IASB also proposes that equivalent amendments to those proposed for IAS 39 be made to the forthcoming chapter on hedge accounting which will be incorporated in IFRS 9 Financial Instruments. The proposed requirements to be included in IFRS 9 are based on the draft requirements of the chapter on hedge accounting, which is published on the IASB's website(a)

Do you agree? Why or why not?

(a) See the draft of the forthcoming hedge accounting requirements posted on the IASB website on 7 September 2012 (<http://go.ifrs.org/Draft-of-forthcoming-IFRS-general-hedge-accounting>)

To strengthen the stability of financial markets as well as to present a true and fair view on the business activities of the reporting entity it necessary that as a matter of principle the exemption always applies, both under IAS 39 and in future under IFRS 9. With respect to the narrowness of scope, see our answer to Q1 and in the *General remarks* above.

Question 4: The IASB considered requiring disclosures when an entity does not discontinue hedge accounting as a result of a novation that meets the criteria of these proposed amendments to IAS 39. However, the IASB decided not to do so in this circumstance for the reason set out in paragraph BC13 of this proposal.

Do you agree? Why or why not?

We agree.

Please do not hesitate to contact me if you wish to discuss any aspect of our comment letter in more detail.

Kind regards,

Romuald Bertl

Chairman