

Via email: www.iasb.org

September 14, 2009

International Accounting Standards Board

Re: Exposure Draft ED/2009/7

The Accounting Principles and Auditing Standards Committee (the AP&AS “Committee”) of the California Society of Certified Public Accountants (CalCPA) is please to provide our comments to the International Accounting Standards Board (the “Board”) on this proposed standard.

The AP&AS Committee is the senior technical committee of CalCPA. CalCPA has approximately 32,000 members. The Committee is comprised of 50 members, of whom 67% are from local or regional accounting firms, 23% are sole practitioners in public accounting, 5% are employed by industry and 5% are employed in academia.

Following are the Committee’s comments in response to the questions posed by the Board in its invitation to comment:

Classification approach (paragraphs 3–5)

Question 1

Does amortised cost provide decision-useful information for a financial asset or financial liability that has basic loan features and is managed on a contractual yield basis? If not, why?

Amortized cost can provide decision useful information. However, as described in response to Question 2, we do not find the reference to “managed on a contractual yield basis” to be operational.

Question 2

Do you believe that the exposure draft proposes sufficient, operational guidance on the application of whether an instrument has ‘basic loan features’ and ‘is managed on a contractual yield basis’? If not, why? What additional guidance would you propose and why?

We have three suggestions concerning “basic loan features”:

- **Some loans that would otherwise meet the requirements of paragraph B3 seem to be excluded. These are loans that reference two quoted or observable interest rates, for example LIBOR and Prime, and permit the borrower to chose which rate will be used, or alternatively, mandate the use of one or the other depending on which rate is higher. Provisions such as these are relatively common and should be included in “basic loan features”**

- **Paragraphs B7 and B8 are unclear, both in application and purpose. In application, any tranche below the most senior is subordinate and would not have “basic loan features.” If that is how the example is to be interpreted, it should be stated clearly. The purpose of the provision is questionable; the buyer of a subordinate tranche is in effect buying a loan of lower quality than the senior tranche, and is being compensated for that, no differently than if he bought a subordinated obligation directly from a borrower. We suggest that the proposal be amended to state that the transactions in paragraphs B7 and B8 do have basic loan features.**
- **The application to principal and interest “strips” is unclear. It would appear that they have “basic loan features”; inclusion in the Application guidance would be helpful.**

The meaning of “managed on a contractual yield basis” is unclear. In the first instance, contractual yield will always be a factor in managing a financial instrument, whether it is acquired or issued for investment or trading. It seems a clearer distinction is whether the instrument was, based on the decision of management personnel, consistent with their business model, designated for trading or non-trading purposes. This distinction is familiar to most. The “non-trading purposes” should be substituted for “managed on a contractual yield basis.”

We have two other specific suggestions:

- **Paragraph B11 would ban reclassification between fair value and amortized cost categories. Such reclassification should be permitted if management makes a change in the purpose of the financial instrument. The instrument should be adjusted to fair value at transfer date, with any gain or loss to net income. Failure to do the reclassification would cause the financial statements to fail to reflect the new purpose for the financial instrument.**
- **The provision of paragraph B13(b) concerning a financial asset acquired at a discount that reflects incurred credit losses should be clarified or deleted. What is an “incurred credit loss” can be unclear at any time until the ultimate discharge or payment of the instrument. Financial instruments may be issued at substantial discounts by borrowers with poor credit, but would the same speculative intent referred to in paragraph BC29 affect their classification? From the acquirer’s view, it may make little difference whether the instrument is acquired new or in an aftermarket.**

Question 3

Do you believe that other conditions would be more appropriate to identify which financial assets or financial liabilities should be measured at amortised cost? If so,

- (a) what alternative conditions would you propose? Why are those conditions more appropriate?

(b) if additional financial assets or financial liabilities would be measured at amortised cost using those conditions, what are those additional financial assets or financial liabilities? Why does measurement at amortised cost result in information that is more decision-useful than measurement at fair value?

(c) if financial assets or financial liabilities that the exposure draft would measure at amortised cost do not meet your proposed conditions, do you think that those financial assets or financial liabilities should be measured at fair value? If not, what measurement attribute is appropriate and why?

See response to Question 2.

Embedded derivatives (paragraphs 6–8)

Question 4

(a) Do you agree that the embedded derivative requirements for a hybrid contract with a financial host should be eliminated? If not, please describe any alternative proposal and explain how it simplifies the accounting requirements and how it would improve the decision-usefulness of information about hybrid contracts.

The Committee agrees with the proposed paragraphs 6 through 8.

(b) Do you agree with the proposed application of the proposed classification approach to contractually subordinated interests (ie tranches)? If not, what approach would you propose for such contractually subordinated interests? How is that approach consistent with the proposed classification approach? How would that approach simplify the accounting requirements and improve the decision-usefulness of information about contractually subordinated interests?

The Committee does not agree with the proposed application of the proposed classification approach to contractually subordinated interests (i.e., tranches). See Question 2 comments on paragraphs B7 and B8.

Fair value option (paragraph 9)

Question 5

Do you agree that entities should continue to be permitted to designate any financial asset or financial liability at fair value through profit or loss if such designation eliminates or significantly reduces an accounting mismatch? If not, why?

The Committee sees no need to retain this provision in view of the proposed new classification approach. Similar transactions should be accounted for by all entities in a consistent manner, and an optional designation would undermine such consistency.

Question 6

Should the fair value option be allowed under any other circumstances? If so, under what other circumstances should it be allowed and why?

No.

Reclassification (paragraph 10)

Question 7

Do you agree that reclassification should be prohibited? If not, in what circumstances do you believe reclassification is appropriate and why do such reclassifications provide understandable and useful information to users of financial statements? How would you account for such reclassifications, and why?

No. See Question 2 response re: paragraph B11.

Investments in equity instruments that do not have a quoted market price and whose fair value cannot be reliably measured

Question 8

Do you believe that more decision-useful information about investments in equity instruments (and derivatives on those equity instruments) results if all such investments are measured at fair value? If not, why?

The Committee believes that more decision-useful information about investments in equity instruments results if all such investments are measured at fair value, but is concerned that measurement of certain non-traded equity instruments may not be sufficiently reliable as to provide decision-useful information.

Question 9

Are there circumstances in which the benefits of improved decision-usefulness do not outweigh the costs of providing this information? What are those circumstances and why? In such circumstances, what impairment test would you require and why?

See response to Question 8. The Committee believes an impairment test similar to that in Statement of Financial Accounting Standards No. 144 *Accounting for the Impairment of Long-Lived Assets* should be required.

Investments in equity instruments that are measured at fair value through other comprehensive income (paragraphs 21 and 22)

Question 10

Do you believe that presenting fair value changes (and dividends) for particular investments in equity instruments in other comprehensive income would improve financial reporting? If not, why?

Yes.

Question 11

Do you agree that an entity should be permitted to present in other comprehensive income changes in the fair value (and dividends) of any investment in equity instruments (other than those that are held for trading), only if it elects to do so at initial recognition? If not,

(a) how do you propose to identify those investments for which presentation in other comprehensive income is appropriate? Why?

(b) should entities present changes in fair value in other comprehensive income only in the periods in which the investments in equity instruments meet the proposed identification principle in (a)? Why?

The Committee believes that an entity should be required to present in other comprehensive income changes in the fair value (and dividends) of all investments in equity instruments (other than those that are held for trading) other than those for which fair value cannot be measured reliably.

Effective date and transition (paragraphs 23–33)

Question 12

Do you agree with the additional disclosure requirements proposed for entities that apply the proposed IFRS before its mandated effective date? If not, what would you propose instead and why?

The Committee has no comment.

Question 13

Do you agree with applying the proposals retrospectively and the related proposed transition guidance? If not, why? What transition guidance would you propose instead and why?

Yes.

An alternative approach

Question 14

Do you believe that this alternative approach provides more decision-useful information than measuring those financial assets at amortised cost, specifically: (a) in the statement of financial position? (b) in the statement of comprehensive income? If so, why?

No.

Question 15

Do you believe that either of the possible variants of the alternative approach provides more decision-useful information than the alternative approach and the approach proposed in the exposure draft? If so, which variant and why?

No.

We thank you for the opportunity to comment on this matter. We would be glad to discuss our opinions with you further should you have any questions or require additional information.

Very truly yours,

A handwritten signature in black ink, appearing to read "JoAnn Guattery". The signature is written in a cursive style with a large initial "J" and "G".

JoAnn Guattery, Chair
Accounting Principles and Auditing Standards Committee
California Society of Certified Public Accountants