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Mme Françoise Flores
Chair
European Financial Reporting Advisory Group
13-14 Avenue des Arts
B-1210 Brussels

Chère Mme Flores

ED/2013/2 *Novation of Derivatives and Continuation of Hedge Accounting*

ICAEW welcomes the opportunity to comment on EFRAG's draft comment letter on the International Accounting Standards Board Exposure Draft ED/2013/2 *Novation of Derivatives and Continuation of Hedge Accounting*. Our responses to the main issues highlighted by EFRAG are set out below. A copy our response to the IASB is attached to this letter. Please refer to this response for our detailed views on the IASB's proposals.

Please contact me should you wish to discuss any of the points raised in the attached response.

Yours sincerely

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ICAEW REPRESENTATION

EFRAG'S DRAFT COMMENT LETTER ON ED/2013/2 NOVATION OF DERIVATIVES AND CONTINUATION OF HEDGE ACCOUNTING

Memorandum of comment submitted in March 2013 by ICAEW, in response to EFRAG's draft comment letter on IASB's exposure draft ED/2013/2 Novation of Derivatives and Continuation of Hedge Accounting published in March 2013.

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INTRODUCTION

1. ICAEW welcomes the opportunity to comment on EFRAG's draft comment letter on the IASB's Exposure Draft ED/2013/2 *Novation of Derivatives and Continuation of Hedge Accounting*.

WHO WE ARE

2. ICAEW is a world-leading professional accountancy body. We operate under a Royal Charter which obliges us to work in the public interest. ICAEW's regulation of its members, in particular its responsibilities in respect of auditors, is overseen by the UK Financial Reporting Council. We provide leadership and practical support to over 140,000 member chartered accountants in more than 160 countries, working with governments, regulators and industry in order to ensure that the highest standards are maintained.
3. ICAEW members operate across a wide range of areas in business, practice and the public sector. They provide financial expertise and guidance based on the highest professional, technical and ethical standards. They are trained to provide clarity and apply rigour, and so help create long-term sustainable economic value.
4. The Financial Reporting Faculty is recognised internationally as a leading authority on financial reporting. The Faculty's Financial Reporting Committee is responsible for formulating ICAEW policy on financial reporting issues, and makes submissions to standard setters and other external bodies. The faculty also provides an extensive range of services to its members, providing practical assistance in dealing with common financial reporting problems.

MAJOR POINTS

We agree that change is needed

5. Like EFRAG, we are pleased that the IASB is acting quickly in response to the widespread legislative changes that are taking place in the wake of the G20's commitment to improve transparency and oversight in over-the-counter derivative markets. We agree that a discontinuation of hedge relationships in this specific situation would not provide useful information

We agree that the exception is drafted to narrowly – but suggest that the IASB widen it further than EFRAG do

6. Like EFRAG, we have some concerns about the scope of the proposed amendment. We agree that the exception to the requirement to discontinue hedge accounting is drafted too narrowly as those derivatives that are novated in advance of the mandatory date of any new law or regulation would not be within its scope of the exception.
7. However, we also believe that the exception should be extended to all voluntarily novations where only 'limited changes' to the terms occur, regardless of whether such novations are to a central counterparty or any other counterparty.

We share EFRAG's concerns about the proposed transition requirements

8. Like EFRAG, we have some concerns about the proposed transition requirements. In our view, the amendment should apply immediately.

RESPONSES TO SPECIFIC QUESTIONS RAISED BY EFRAG

Are you aware of additional novations that should also be covered by these amendments? Please describe those novations and the reasons why you believe they should qualify for the same relief.

EFRAG understands that also in circumstances where existing OTC derivatives are not required to be novated to central counterparties; there may be an economic compulsion to do so (either because of market collateral requirements or new regulatory capital requirements). Are you aware of circumstances in which OTC derivatives are novated absent a direct legal obligation (i.e. the novation is not directly required by laws or regulations)? If so, please (i) describe those voluntary novations and (ii) explain whether or not they should be covered by the proposed relief and how this would result in appropriate financial reporting.

9. In practice, there are many good reasons why a derivative might be voluntarily novated to another counterparty. As noted by EFRAG, an entity may in some circumstances feel an economic compulsion to novate as not doing so would incur an additional regulatory capital cost. Similarly, entities may simply wish to move derivatives around the group in order to facilitate a single face to an exchange
10. From a conceptual perspective, it is difficult to argue that a novation to a central counterparty is any different to any other novation. Therefore, as noted above, we believe that the exception should be extended to all voluntarily novations where only 'limited changes' to the terms occur, regardless of whether such novations are to a central counterparty or any other counterparty.

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