



International Accounting Standards Board®

Press Release

FOR IMMEDIATE RELEASE

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IASB amends requirements for financial guarantee contracts

The International Accounting Standards Board (IASB) today issued amended requirements for financial guarantee contracts, in the form of limited amendments to IAS 39 *Financial Instruments: Recognition and Measurement* and IFRS 4 *Insurance Contracts*.

The amendments are intended to ensure that issuers of financial guarantee contracts include the resulting liabilities in their balance sheet. The amendments define a financial guarantee contract as a ‘contract that requires the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the original or modified terms of a debt instrument’. These contracts could have various legal forms, including a guarantee, some types of letter of credit, or a credit insurance contract.

Issuers must apply the amendments for annual periods beginning on or after 1 January 2006. Earlier application is encouraged.

Introducing the amendments, Sir David Tweedie, IASB Chairman, commented:

In making these amendments, our objective is to ensure that liabilities for financial guarantee contracts are not omitted from the financial statements. Without compromising that objective, we modified our original proposals in response to comments received, so that credit insurers can retain most aspects of their existing accounting. We expect to review accounting for credit insurance contracts and other forms of financial guarantee contract in more detail in phase II of our project on insurance contracts.

In developing these amendments, we have benefited from comments on the Exposure Draft, as well as briefings by representatives of the International Credit Insurance &

Surety Association and of the Association of Financial Guaranty Insurers at a public education session.

The primary means of publishing Standards and amendments to Standards is by electronic format through the IASB's subscriber Website. Subscribers to the IASB's Comprehensive Subscription Service are able to access the amendments issued today through the secure online services area of the IASB's Website (www.iasb.org). Those wishing to subscribe should contact:

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Printed copies of Amendments to IAS 39 Financial Instruments: Recognition and Measurement and IFRS 4 Insurance Contracts—*Financial Guarantee Contracts* (ISBN 1-904230-92-X) are available at £10.00 each, including postage, from IASCF Publications Department (order copies online through the IASCF shop: www.iasb.org).

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NOTES TO EDITORS

About the amendments

1. The amendments require the issuer of a financial guarantee contract to measure the contract:
 - (a) initially at fair value. If the financial guarantee contract was issued in a stand-alone arm's length transaction to an unrelated party, its fair value at inception is likely to equal the consideration received, unless there is evidence to the contrary.
 - (b) subsequently at the higher of (i) the amount determined in accordance with IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* and (ii) the amount initially recognised less, when appropriate, cumulative amortisation recognised in accordance with IAS 18 *Revenue*. (If specified criteria are met, the issuer may use the fair value option in IAS 39, see IASB press release of 16 June 2005. Furthermore, different requirements continue to apply in the specialised context of a 'failed' derecognition transaction.)
2. If an issuer has previously asserted explicitly that it regards such contracts as insurance contracts and has used accounting applicable to insurance contracts, the issuer may elect to apply to such contracts either IFRS 4 or the accounting described in paragraph 1 above. The IASB introduced this election in response to comments on the Exposure Draft. Respondents had expressed concerns that Exposure Draft did not give enough guidance on features of some credit insurance contracts, such as cancellation and renewal rights and profit-sharing features. The IASB will address such features in phase II of its project on insurance contracts and concluded that it could not address them in the short term.
3. As already noted, the amendment distinguishes between financial guarantee contracts on the basis of whether the issuer regards them as insurance contracts. The IASB does not view this as a robust long-term solution. However, it provides a temporary practical solution that reduces the risk of the complete omission of financial guarantee contracts from the issuer's balance sheet. When credit insurers issue credit insurance contracts, they typically recognise a liability measured initially as either the premium received or an estimate of the expected losses. Moreover, IFRS 4 requires insurers to perform a liability adequacy test. However, the IASB was concerned that some other issuers of financial guarantee contracts might argue that no recognisable liability existed at inception.

4. Phase II of the IASB's project on insurance contracts includes a comprehensive review of accounting for insurance contracts, including credit insurance contracts and other financial guarantee contracts.
5. Before these amendments, financial guarantee contracts were within the scope of IFRS 4.
6. Some credit-related guarantees do not, as a precondition for payment, require that the holder is exposed to, and has incurred a loss on, the failure of the debtor to make payments on the guaranteed asset when due. An example of such a guarantee is a credit derivative that requires payments in response to changes in a specified credit rating or credit index. These are derivatives and are not affected by the amendments. They must be measured at fair value under IAS 39.
7. The amendments address the treatment of financial guarantee contracts by the issuer. They do not address their treatment by the holder. Accounting by the holder is excluded from the scope of IAS 39 and IFRS 4 (unless the contract is a reinsurance contract). Therefore, paragraphs 10–12 of IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* apply. Those paragraphs specify criteria to use in developing an accounting policy if no IFRS applies specifically to an item.

About the IASB

8. The IASB, based in London, began operations in 2001. It is funded by contributions collected by its Trustees, the IASC Foundation, from the major accounting firms, private financial institutions and industrial companies throughout the world, central and development banks, and other international and professional organisations. The 14 IASB members (12 of whom are full-time) are drawn from nine countries and have a variety of professional backgrounds. The IASB is committed to developing, in the public interest, a single set of high quality, global accounting standards that require transparent and comparable information in general purpose financial statements. In pursuit of this objective, the IASB co-operates with national accounting standard-setters to achieve convergence of accounting standards around the world.
9. A Deloitte & Touche study indicates that 94 countries either require or permit the use of IFRSs for publicly traded companies beginning in 2005. Some other jurisdictions, including Australia, New Zealand, the Philippines and Singapore, base their national practices on international standards. In September 2002 the IASB and the

US standard-setter, the Financial Accounting Standards Board, reached an agreement to work towards the convergence of existing US and international practices and the joint development of future standards. In October 2004, the IASB and the Accounting Standards Board of Japan agreed to initiate discussions about a joint project to minimise differences between IFRSs and Japanese accounting standards towards a final goal of convergence of their standards. In January 2005 the two boards announced their agreement to launch a joint project to reduce differences between IFRSs and Japanese accounting standards, and in March the boards met to decide on the initial programme of work for the project.