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Wayne Upton
Chairman of the
IFRS Interpretations Committee
30 Cannon Street
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United Kingdom

Berlin, 23 November 2012

Dear Wayne,

IAS 39 – Income and expenses arising on financial instruments with a negative yield – presentation in the statement of comprehensive income

On behalf of the Accounting Standards Committee of Germany (ASCG) I am writing to comment on the IFRSIC's tentative agenda decision, published in the September 2012 *IFRIC Update*, not to add the issue to its agenda.

We disagree with the IFRSIC's tentative agenda decision for the following reasons:

- The interest yield of a financial asset can contain several components, some of which can be negative;
- interest cash flows with a negative yield component or even a total negative yield are, intuitively and economically, still considered part of (net) interest income;
- interest cash flows from a financial asset can be negative as a temporary and exceptional phenomenon – but are still interest revenue;
- adding positive with negative yield components of the same origin (same instrument) is not a matter of offsetting but of aggregation;
- the definition of revenue is interpreted too narrow in the context of IAS 18 but not as a financial instrument's issue.

Our rationale for the above is as follows: Firstly, we agree that interest cash flows of an asset resulting in a negative yield cannot be considered interest expenses, thus, we agree with the argument that interest expenses can arise on liabilities only. Secondly, we also agree that interest revenue and interest expenses must not be offset. However, we consider both positive and negative interest cash flows from a financial asset being revenue, hence, adding (temporarily) negative interest cash flows (i.e. negative yield) with positive interest cash flows does not violate offsetting constraints.

Let us consider two examples:

- A financial asset with a low coupon issued with a high premium would lead to recognising the interest rate coupon as a positive yield component and the amortisation of the premium as a negative yield component, with the effect that the sum of both components may lead to a (total) negative yield.
- A high quality government bond issued with a coupon that resets at, for instance, three months LIBOR minus credit spread, where the discount from LIBOR for the credit risk of the bond is higher than the prevailing LIBOR rate may lead to a negative yield for certain periods.

In the first example, the negative (amortisation) yield component would be presented as part of interest revenue, probably not even separate from the positive (coupon) yield component. In the second case, during "positive" periods the yield would obviously be presented as interest revenue. In both cases, it would be counter-intuitive, even impracticable, to present cash flows of the same nature and origin as interest revenue during one period (e.g. first quarter of a year), but as any other (non-interest) expense during the next period (e.g. second quarter of the same year).

Finally, considering a negative yield as "fee for custody" seems inappropriate to us since it is neither implicitly/explicitly agreed upon nor is it empirically approved; it is merely an assertion. If presuming so, any yield of any financial asset/liability would implicitly be split into a "pure interest" component and a "custody fee" component – e.g. deposits, current accounts (usually having a low interest rate) – with both being presented separately. For obvious reasons, we would deny this assertion.

Therefore, we suggest that the IFRSIC reconsider and change its tentative decision such that interest cash flows can exceptionally and temporarily be negative with the nature of interest revenue still being preserved. As argued above, negative interest yield from a financial asset should be presented as part of interest revenue, thus, being part of interest (net) income.

If you would like further clarification of the issues set out in this letter, please do not hesitate to contact me.

With best regards,

Liesel Knorr

President