11 November, 2003

Ms. Sandra Thompson
Senior Project Manager
International Accounting Standards Board
30 Cannon Street
London
EC4M 6XH

Dear Ms. Thompson:

<u>Proposed amendments to IAS 39 Financial Instruments: Recognition and Measurement – Fair value hedge accounting for a portfolio hedge of interest rate risk</u>

MBNA Europe Bank Limited ("MBNA Europe") thanks the International Accounting Standards Board (the "Board") for the opportunity to comment on the above exposure draft. MBNA Europe is a bank authorised and supervised in the United Kingdom by the Financial Services Authority, specialising in the issuance of bank credit cards in the Visa and MasterCard systems, with branches in Spain and the Republic of Ireland. MBNA Europe is currently the third largest issuer of bank credit cards in the United Kingdom, with total accounts of 7.1 million and total managed loans of £9.4 billion. It is regulated by the Financial Services Authority. MBNA Europe is a wholly owned subsidiary of MBNA America Bank, N.A. ("MBNA America"), the principal operating subsidiary of MBNA Corporation.

MBNA Corporation is the largest independent credit card issuer in the world. At 30 September 2003 MBNA Corporation reported assets net of securitisations totalling $58.7 billion; managed assets, including securitised loans were approximately $141.1 billion. The Office of the Comptroller of the Currency and the Federal Reserve Board are the primary regulatory agencies for MBNA America and MBNA Corporation, respectively.

We welcome the proposed amendments to IAS 39 insofar as they establish the principle that fair value hedge accounting is not excluded for certain commercially effective portfolio hedges of interest rate risk. However, we would like to express our concern over some apparent inconsistencies in the exposure draft.

We believe that there are practical and conceptual difficulties when allowing portions of financial assets or liabilities to be designated as hedged items where a prepayment option is present and the associated derivative is designed to match the expected prepayment. This is because the changes in fair value of the derivative could not be expected to be highly effective in offsetting the changes in fair value of the underlying financial assets or liabilities if the expected prepayment dates change.

For example, assume an entity owns a portfolio of €100 million of fixed-rate debt securities. Further assume the securities have a remaining contractual term of ten years, but are callable by the issuer and it is expected that the securities will be called in three years. If an entity wished to hedge this portfolio for fair value changes caused by movements in the benchmark rate, it may use a three year interest rate swap (receive LIBOR and pay fixed-rate) with a notional amount of €100 million. Assume that at the next reporting period, based on increases in the benchmark interest rate, the entity now believes the expected call date will be in five years instead and there will be no debt securities expected to mature on the date originally estimated. How should ineffectiveness be measured?

Paragraph A36 of the exposure draft appears to suggest that the entire change in the fair value of the derivative would be ineffective since there are now no debt securities expected to mature within the originally designated period. This interpretation appears to be inconsistent with our interpretation of paragraphs 128A, A32, and especially A33 which appear to suggest that the ineffectiveness should be calculated based on the change in the expected repricing date of the originally designated hedged item (i.e. the portfolio consisting of €100 million of fixed-rate debt securities). If this were the case, the contractual cash flows of the debt securities would be measured based on the new expected cash flows (now over a five-year period) discounted back at the contractual rate plus the increase in the benchmark rate. If this were the intention, the recognised ineffectiveness would be different. In fact, the hedge, using a euro-offset to measure effectiveness, may not be highly effective for the period (i.e. there would be no basis for expecting that the change in that swap's fair value would be highly effective in off-setting the change in the fair value for the five-year asset for only the first three years).

In addition, IAS 39 as currently drafted is in our view ambiguous in the standards to be met in measuring hedge effectiveness where critical terms match, as between paragraph 151 and IGC 147-1. It is not clear in our minds whether the "short cut" method is available or not. The exposure draft contains no reference to this topic, but the availability or otherwise of the "short cut" method is very relevant to macro hedging.

We feel that clarification by the IASB of these two points would significantly enhance the quality of the final standard.

We appreciate the opportunity to provide these comments to the IASB. If you have any questions regarding this submission or if we can provide further information, please contact Vernon Wright directly on 001 302 453 2074 (e-mail at **vernon.wright@mbna.com**) or Robin Russell on 01244 672251 (e-mail at **robin.russell@mbna.com)**.

Yours sincerely,

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