

30 Cannon Street, London EC4M 6XH, United Kingdom Tel: +44 (0)20 7246 6410 Fax: +44 (0)20 7246 6411 E-mail: iasb@iasb.org Website: www.iasb.org

International Accounting Standards Board

This observer note is provided as a convenience to observers at IFRIC meetings, to assist them in following the IFRIC's discussion. Views expressed in this document are identified by the staff as a basis for the discussion at the IFRIC meeting. This document does not represent an official position of the IFRIC. Decisions of the IFRIC are determined only after extensive deliberation and due process. IFRIC positions are set out in Interpretations.

Note: The observer note is based on the staff paper prepared for the IFRIC. Paragraph numbers correspond to paragraph numbers used in the IFRIC paper. However, because the observer note is less detailed, some paragraph numbers are not used.

INFORMATION FOR OBSERVERS

IFRIC meeting:	March 2008, London
Project:	Situation 3B: Hedging instruments held by Parent — Forwards (Agenda Paper 2I)

On 1 January 2005, Parent entity, which presents consolidated financial statements in € holds a 100% investment in Subsidiary B (£500m). Subsidiary B also holds a 100% investment in Subsidiary C (\$300m). Parent entity has a functional currency of € Subsidiary B has a functional currency of Pound Sterling (£) and Subsidiary C has a functional currency of \$. Parent entity wishes to hedge its foreign exchange exposures from its investment in Subsidiary C and Subsidiary B. On 1 January 2005 the Parent entered into two external forward contracts. The first contract sells \$300m for €238m in one year's time. The second forward sells £500m for €751m in one year's time. The net assets of Subsidiary B on 1 January 2005 are £500m including an amount in respect of the net assets of Subsidiary C which are equal to \$300m on this date. The Parent's net assets comprise the investment in Subsidiary B and the two forwards. The Parent designates the \$300m forward as a hedge of the forward foreign exchange risk associated with its net investment in the first \$300m net assets of Subsidiary C in its consolidated financial statements. The Parent also designates the £500m forward as a hedge of £341m of its net investment in the net assets of Subsidiary B in its consolidated financial statements. Although \notin \$ risk from a net investment in Subsidiary C between Parent and Subsidiary C is different risk from \notin £ risk from a net investment in Subsidiary B between Parent and Subsidiary B, hedging the remaining £159m of net assets in Subsidiary B, which represent the net investment in Subsidiary C, would amount to hedging the same net assets, those of Subsidiary C, twice for the same risk, ie retranslation into \notin It would result in an overhedge of a net investment in Subsidiary B in Parent's consolidated financial statements.

As the external forward contracts are not within the consolidated financial statements of Subsidiary B, the question of designation at that level is not applicable.



Results of hedge effectiveness

Step-by-step method of consolidation

Hedged risk	In which financial statemer	nts?
	In Parent's consolidated	In Sub B's consolidated
	F/S	F/S
①Euro/\$ exposure from a	Spreadsheet No. 3B-1	N/A
net investment in	Forwards	
Subsidiary C between		
Parent and Subsidiary C	100% effective	
3 Euro/£ exposure from a	Spreadsheet No. 3B-1	
net investment in B	Forwards	
between parent and	100% effective	
Subsidiary B		

Direct method of consolidation

Hedged risk	In which financial stateme	nts?
	In Parent's consolidated	In Sub B's consolidated
	F/S	F/S
①Euro/\$ exposure from a	Spreadsheet No. 3B-2	N/A
net investment in	Forwards	
Subsidiary C between	100% effective	
Parent and Subsidiary C		
③Euro/£ exposure from a	N0. 3B-2	
net investment in B	100% effective	
between parent and		
Subsidiary B		

IFRIC MEETING LONDON, MARCH 08 AGENDA PAPER 21 APPENDIX 1 PAGE1

> helper 0.318 0.682

USD JPY EUR GBP	Year 0 1 118 0.8 0.53										
Investment in A Investment in B Investment in C Other assets	P (EUR) 755 0	A(JPY)	A(EUR)	C(USD) 300	C(GBP)	B(GBP) 159 341	consol adj -159	BC(GBP)	BC(EUR) pre-acq	-755	BC(EUR) 0 0 755 755
Opening FCTR Income Closing	-755	0	0	-300	-159	-500	159	-500	-755	755	-755
Equity Fwd #1 68.2% of Fwd #2 31.2% of Fwd #2 Fwd #4 # 2	-755 0 0 0	0	0	-300	-159	-500		0	-755		-755
Check	0	0	0	0	0	0		0	0	0	0
USD JPY EUR GBP	Year 1 a 1 125 0.88 0.58	verage 1 121.5 0.84 0.555		P accounts Forward #1 Forward #1 P/L	Year 0 Year 1	EU	R 0 -26 -26	P accounts Forward #2 Forward #2 P/L	Year 0 Year 1	68 EU	3.2% Fwd 31.8% Fwd JR EUR 0 0 -5 -2 -5 -2
USD JPY EUR GBP Investment in A Investment in B Investment in C Other assets	Year 1 a 1 125 0.88 0.58 P (EUR) 755 0 755	verage 1 121.5 0.84 0.555 A(JPY)	A(EUR)	P accounts Forward #1 Forward #1 P/L C(USD) 300	Year 0 Year 1 C(GBP) 174 174	EU 	R 0 -26 -26 consol adj hedg -159	P accounts Forward #2 P/L e BC(GBP) 515 515	Year 0 Year 1 BC(EUR) pre-acq 781 781	consol adj 0 -755	2.2% Fwd 31.8% Fwd JR EUR 0 -5 -2 -5 -2 -5 -2 PABC(EUR) 0 0 781 781
USD JPY EUR GBP Investment in A Investment in B Investment in C Other assets Opening FCTR (Entity B)*2 FCTR (Entity C)*3 Income (USD forward Income (£341 forward Income (£159 forward Closing	Year 1 a 1 125 0.88 0.58 P (EUR) 755 0 755 -755 26 5 2 26 5 2	verage 1 121.5 0.84 0.555 A(JPY) 0	A(EUR)	P accounts Forward #1 Forward #1 P/L C(USD) 300 -300 -300	Year 0 Year 1 C(GBP) 174 174 -159 -15	EU B(GBP) 159 341 500 -500	R 0 -26 -26 consol adj hedg -159 159	P accounts Forward #2 P/L e BC(GBP) 515 515 -500 -15	Year 0 Year 1 BC(EUR) pre-acq 781 -755 -4 -23	68 EL consol adj -755	2.2% Fwd 31.8% Fwd JR EUR 0 -5 -2 -5 -2 -5 -2 -5 -2 -5 -2 0 0 0 781 -755 -4 -23 26 5 2
USD JPY EUR GBP Investment in A Investment in B Investment in C Other assets Opening FCTR (Entity B)*2 FCTR (Entity C)*3 Income (JSD forward Income (£341 forward Income (£159 forward Closing Fwd #1 68.2% of Fwd #2 51.2% of Fwd #2 Fwd #1 & #2	Year 1 a 1 125 0.88 0.58 P (EUR) 755 0 755 -755 26 5 2 26 5 2 -721 -26 -5 -2 -34	verage 1 121.5 0.84 0.555 A(JPY) 0 0 0	A(EUR) 0	P accounts Forward #1 Forward #1 P/L C(USD) 300 -300 -300 -300 0	Year 0 Year 1 C(GBP) 174 174 -159 -15 -174 -174 0	EU B(GBP) 159 341 500 -500 -500	R 0 -26 -26 consol adj hedg -159 159	P accounts Forward #2 P/L e BC(GBP) 515 515 -500 -15 -515 0 0	Year 0 Year 1 BC(EUR) pre-acq 781 -755 -4 -23 -781 -781 0	68 EL consol adj -755 755	22% Fwd 31.8% Fwd JR EUR 0 -5 -2 -5 -2 -5 -2 -5 -2 -75 -2 -75 -2 -75 -2 -75 -2 -781 -781 -781 -785 -4 -23 -26 5 2 -748 -26 -5 -2 -34

SITUATION 3B - 1 FORWARD (step-by-step method): designate \$/Euro exposure from Entity C and £/Euro exposure from Entity B as hedged risks

IFRIC MEETING LONDON, MARCH 08 AGENDA PAPER 2I APPENDIX 1 PAGE2

SITUATION 3B - 1 FORWARD (step-by-step method): designate \$/Euro exposure from Entity C and £/Euro exposure from Entity B as hedged risks

26 EUR	5 EUR
USD300m forward	GBP341m forward
-26 Euro	-5 EUR
USD 300m	GBP341m
	USD/EUR exposure from C USD 300m -26 Euro USD300m forward 26 EUR

*2 EUR-4=-(GBP515/0.58*0.88-EUR755-EUR23)		
*3 GBP-15=GBP159-\$300*0.58 EUR-23=GBP-15/0.58*0.88		

The following entries would be recorded	for hedging instruments		
(P's separate F/S)			
Dr) Profit and loss	EUR 26	Cr) Forward	EUR 26
being profit/loss arising from US\$ for	ward		
Dr) Profit and loss	EUR 5	Cr) Forward	EUR 5
being profit/loss arising from 68.2% o	f the ∉ GBP forward		
Dr) Equity (FCTR-Entity C)	EUR 26	Cr) Profit and loss	EUR 26
being the hedge accounting entry for	the net investment in Er	ntity C	
Dr) Equity (FCTR-Entity B)	EUR 5	Cr) Profit and loss	EUR 5
being the hedge accounting entry for	the net investment in Er	ntity B	
The following entries would be recorded	for hedged item		
(P's consolidated F/S)			
Dr)Other assets	EUR 23	Cr)FCTR(EntityC)	EUR 23
retranslation of exchange difference a	rising from Entity C		
Dr)Other assets	EUR 4	Cr)FCTR(EntityB)	EUR 4
retranslation of exchange difference a	rising from Entity B		

EUR

	Defensible data		A 44
<arter entry="" nedge=""></arter>	Before heage		After hedge
	PABC(EUR)	hedge	ABC(EUR)
Investment in A	0		0
Investment in B	0		0
Investment in C	0		0
Other assets	781		781
	781		781
	701		701
Oponing	765		755
COPERING	-755	-	-755
FUTR (Entity B)"2	-4	5	1
FCTR (Entity C)*3	-23	26	4
Income (USD forward)	26	-26	0
Income (£341 forward)	5	-5	0
Income (£159 forward)	2		2
Closing			
g	-7/8		-748
	-740		-740
	00		00
Forward (USD 300m)	-26		-26
Forward (GBP 341m)	-5		-5
Forward (GBP 159m)	-2		-2
Forward	-34		-34
Check	0		0

Equity (FCTR)

Check:

IFRIC MEETING LONDON, MARCH 08 AGENDA PAPER 21 APPENDIX 2 PAGE1

> helper 0.318 0.682

L J E C	JSD IPY UR BBP	Year 0 1 118 0.8 0.53									
		P (EUR)	A(JPY)	A(EUR)	C(USD)	C(EUR)	B(GBP)	B(EUR)	consol adj pre-acq	PABC(EUR)	
li li C	nvestment in A nvestment in B nvestment in C Dther assets*1	755 0 755	0	0	<u>300</u> 300	<u>240</u> 240	159 341 500	240 515 755	-755 -240	0 0 755 755	
C F II	Dpening -CTR ncome Diosing	-755			-300	-240	-500	-755	995	-755	
		-755	0	0	-300	-240	-500	-755		-755	
F 6 3	Fwd #1 \$8.2% of Fwd #2 \$1.2% of Fwd #2	0 0 0			0	0			0	0	
F	-wd #1 & #2	0			0	0	0	0	U	0	
C	Check	0	0	0	0	0	0	0		0	
L J E	JSD JPY EUR BBP	Year 1 a 1 125 0.88 0.58	iverage 1 121.5 0.84 0.555		P accounts Forward #1 Forward #1 P/L		Year 0 Year 1	EUR 0 -26 -26	P account Forward # Forward # P/L	s Year 0 2 Year 1	68.2% Fwd 31.8% Fwd EUR EUR 0 0 -5 -2
L J C	JSD JPY EUR BBP	Year 1 a 125 0.88 0.58 P (EUR)	Average 1 121.5 0.84 0.555 A(JPY)	A(EUR)	P accounts Forward #1 Forward #1 P/L C(USD)	C(EUR)	Year 0 Year 1 B(GBP)	EUR 0 -26 -26 B(EUR)	P account Forward # Forward # P/L consol adj ore-acg hedge	S Year 0 2 Year 1 PABC(EUR)	68.2% Fwd 31.8% Fwd EUR EUR 0 0 -5 -2 3B-1(Step) PABC(EUR)
	JSD JPY UR SBP nvestment in A nvestment in B nvestment in C Dther assets	Year 1 a 1 125 0.88 0.58 P (EUR) 755 0 755	1 121.5 0.84 0.555 A(JPY) 0	A(EUR)	P accounts Forward #1 P/L C(USD) 300 300	C(EUR) 264 264	Year 0 Year 1 B(GBP) 159 341 500	EUR 0 -26 -26 B(EUR) 240 517 757	P account Forward # P/L consol adj pre-acq hedge -755 -240	S 2 Year 0 2 Year 1 PABC(EUR) 0 0 0 0 781 781	68.2% Fwd 31.8% Fwd EUR EUR 0 0 -5 -2 -5 -2 3B-1(Step) 0 PABC(EUR) 0 0 0 0 0 0 0 0 0 781 0
U 3 3 4 5 5 7 7 7 7 7 7 7 7 7 7 7 7 7 7 7 7 7	JSD JPY EUR SBP nvestment in A nvestment in B nvestment in C Dther assets Dpening CTR (Entity B)*2 CTR(Entity C)*3 ncome (USD forward ncome (£159 forward Dissing	Year 1 a 1 125 0.88 0.58 P (EUR) 755 0 755 0 755 26 5 2	verage 1 121.5 0.84 0.555 A(JPY) 0	A(EUR)	P accounts Forward #1 P/L C(USD) 300 -300	C(EUR) 264 264 -240 -24	Year 0 Year 1 B(GBP) 159 341 500 -500	EUR 0 -26 -26 -26 -26 -240 517 517 -755 -3	P account Forward # P/L consol adj ore-acq hedge -755 -240 995 26 -26 -26	S 2 Year 0 2 Year 1 PABC(EUR) 0 0 0 781 781 -755 2 2 2 0 0 0 2	68.2% Fwd 31.8% Fwd EUR EUR 0 -5 -5 -2 -5 -2 3B-1(Step) PABC(EUR) 0 0 0 0 0 0 781 0 781 0 1 1 4 -1 0 0 0 0
L J J E E C C I I I I I I I I I I I I I I I I	JSD JPY EUR 3BP nvestment in A nvestment in B nvestment in C Dther assets Depening CTR (Entity B)*2 :CTR(Entity C)*3 ncome (USD forward ncome (£159 forward Distribution (£159 forward	Year 1 a 1 125 0.88 0.58 P (EUR) 755 0 755 26 5 26 5 2 -721	verage 1 121.5 0.84 0.555 A(JPY) 0 0 0	A(EUR) 0	P accounts Forward #1 P/L C(USD) 300 300 -300 -300	C(EUR) 264 -240 -240 -24	Year 0 Year 1 B(GBP) 159 341 500 -500	EUR 0 -26 -26 B(EUR) 240 577 -755 -3 -755 -3	P account Forward # P/L consol adj ore-acq hedge -755 -240 995 26 -26 -26 -26	S 2 Year 0 2 Year 1 PABC(EUR) 0 0 0 0 781 781 -755 2 2 2 0 0 0 2 2 -748	68.2% Fwd 31.8% Fwd EUR EUR 0 -5 -5 -2 -5 -2 -5 -2 3B-1(Step) 0 PABC(EUR) 0 0 0 781 0 -755 0 1 1 4 -1 0 0 0 0 0 0
L J J E G G H H H H H G G G F F F H H H H G G F F F F	JSD JPY EUR SBP nvestment in A nvestment in B nvestment in C Dther assets Depening CTR (Entity B)*2 :CTR(Entity C)*3 ncome (LSD forward ncome (£159 forward closing :Wd #1 38.2% of Fwd #2 :L2% of Fwd #2 :Wd #2 :Wd #1	Year 1 a 1 125 0.88 0.58 P (EUR) 755 0 755 26 5 26 5 2 -721 -26 -5 -2 -34	verage 1 121.5 0.84 0.555 A(JPY) 0 0	A(EUR) 0	P accounts Forward #1 P/L C(USD) 300 300 -300 -300	C(EUR) 264 264 -240 -24 -240 -24	Year 0 Year 1 B(GBP) 159 341 500 -500 -500	EUR 0 -26 -26 B(EUR) 240 577 -755 -3 -757 -757	P account Forward # P/L consol adj ore-acq hedge -755 -240 995 <u>5</u> 226 -26 -26	S 2 Year 0 2 Year 1 PABC(EUR) 0 0 0 0 781 781 -755 2 2 0 0 0 2 2 -748 -26 -5 -2 -34	68.2% Fwd 31.8% Fwd EUR EUR 0 -6 -5 -2 -5 -2 -5 -2 3B-1(Step) PABC(EUR) 0 0 0 0 0 0 781 0 7755 0 1 1 4 -1 0 0 -748 0 -26 -5 -2 -34
U J E C M H H H C C F F H H H H C C F F F H H H H	JSD JPY EUR 3BP nvestment in A nvestment in B nvestment in C Dher assets Depening CTR (Entity B)*2 CTR(Entity C)*3 ncome (LSD forward ncome (£159 forward) ncome (£159 forward)	Year 1 a 1 125 0.88 0.58 P (EUR) 755 0 755 26 5 26 5 2 -721 -26 -5 -2 -2 -3	verage 1 121.5 0.84 0.555 A(JPY) 0 0 0		P accounts Forward #1 P/L C(USD) 300 -300 -300 -300	C(EUR) 264 -240 -240 -24 -264 -264	Year 0 Year 1 B(GBP) 159 341 500 -500 -500	EUR 0 -26 -26 -26 -26 -26 -26 -26 -755 -3 -755 -3 -755 -3 -757 0 0	P account Forward # P/L consol adj ore-acq hedge -755 -240 995 26 -26 -26 -26	S 2 Year 0 2 Year 1 PABC(EUR) 0 0 0 0 781 781 781 -755 2 2 2 0 0 0 2 2 -748 -26 -5 -2 -2 -34	68.2% Fwd 31.8% Fwd EUR EUR 0 -5 -5 -2 -5 -2 -5 -2 3B-1(Step) PABC(EUR) 0 0 0 0 0 0 0 0 781 0 781 0 0 0 -755 0 1 1 4 -1 0 0 -748 0 -26 -5 -2 -34

SITUATION 3B - 2 FORWARD (direct method): designate \$/Euro exposure from Entity C and £/Euro exposure from Entity B as hedged risks

IFRIC MEETING LONDON, MARCH 08 AGENDA PAPER 2I APPENDIX 2 PAGE2

SITUATION 3B - 2 FORWARD (direct method): designate \$/Euro exposure from Entity C and £/Euro exposure from Entity B as hedged risks

change in value of net assets at forward rates (as per IE 15 of D22) Hedging instrument	-26 Euro SD300m forward	-5 EUR GBP341m forward
Hedging instrument U	SD300m forward	GBP341m forward
		obi o miniomaid
Change in P/L	26 EUR	5 EUR
Hedge effectiveness	100%	100%

The following entries would be recorded	for bedging instruments		
The following chales would be recorded	for neuging instruments		
(P's separate F/S)			
Dr) Profit and loss	EUR 26	Cr) Forwa	EUR 26
being profit/loss arising from US\$ for	ward		
Dr) Profit and loss	EUR 5	Cr) Forwa	EUR 5
being profit/loss arising from 68.2% of	f the ∉GBP forward		
Dr) Equity (FCTR-Entity C)	EUR 26	Cr) Profit a	EUR 26
being the hedge accounting entry for	the net investment in Entity	C	
Dr) Equity (FCTR-Entity B)	EUR 5	Cr) Profit a	EUR 5
being the hedge accounting entry for	the net investment in Entity I	B	

The following entries would be reco	orded for hedged	d item		
(P's consolidated F/S)				
Dr)Other assets	EUR 24	Cr)FCTR(EntityC)	EUR 24	
retranslation of exchange differe	nce arising fro	m Entity C		
Dr)Other assets	EUR 3	Cr)FCTR(EntityB)	EUR 3	
retranslation of exchange differe	nce arising fro	m Entity B		

Check: Equity (FCTR) EUR

IFRIC MEETING LONDON, MARCH 08 AGENDA PAPER 2I APPENDIX 3

SITUATION 3B FORWARD Forward Calculation Sheet

Forward #1 matures in one year time, ie. 1/1/02					
Buy	€	237.725.118.48			
Sell	\$	300.000.000.00			
	•				
Fair Value @ 31/12/00	Leg in EUR				
Buy €	227,488,151.66	227,488,151.66			
Sell \$	284,360,189.57	227,488,151.66			
TOTAL		0.00			
Fair Value @ 31/12/01	Leg				
Buy €	237,725,118.48	237,725,118.48			
Sell \$	300,000,000.00	264,000,000.00			
TOTAL		-26,274,881.52			
<u></u>		<u> </u>			
Forward #2 matures in one	year time, ie. 1/1/02				
Buy	€	751,123,090.75			
Sell	GBP	500,000,000.00			
Fair Value @ 31/12/00	Leg in	in EUR			
Buy €	718,778,077.27	718,778,077.27			
Sell GBP	476,190,476.19	718,778,077.27			
TOTAL		0.00			
Fair Value @ 31/12/01	Leg				
Buy€	751,123,090.75	751,123,090.75			
Sell GBP	500,000,000.00	758,620,689.66			
TOTAL		-7,497,598.91			

NB: all hedges assume that both the spot and forward component are designated

		5	Spot rates		
	<i>t</i> €		£	Yen	\$
	1	0.8	0.53	118	
	0	0.88	0.58	125	
		Int	erest rates		•
	t€		£	Yen	\$
	0	4.50%	5.00%		5.50%
	1	4.70%			5.70%
Exchange ra	ates			1	
Period		0	1		
\$/Yen		118	125		
\$/GBP		0.53	0.58		
\$/€		0.8	0.88		
Yen/\$		0.008474576	0.008		
Yen/GBP		0.004491525	0.00464		
Yen/€		0.006779661	0.00704		
GBP/\$		1.886792453	1.724137931		
GBP/Yen		222.6415094	215.5172414		
GBP/€		1.509433962	1.517241379		
€/\$		1.25	1.136363636		
€/Yen		147.5	142.0454545		
€/GBP		0.6625	0.659090909		
	(- (*)			•	
Forward rate	(E/\$)		Forward rate (E/GBP)		
	1.26		0.67		

IFRIC MEETING LONDON, MARCH 08 AGENDA PAPER 2I APPNEDIX 4

SITUATION 3B FORWARD

Net assets (\$)	300,000,000.0000
\$/€ spot rate @ 31/12/00	0.8000
\$/€ spot rate @ 31/12/01	0.8800
€/\$1-y forward rate @ 31/12/00	1.2620
Change in hedged item at forward rates*	-26,274,881.5166

Net assets (GBP)	341,000,000.0000
GBP/€ spot rate @ 31/12/00	1.5094
GBP/€ spot rate @ 31/12/01	1.5172
€/GBP 1-y forward rate @ 31/12/00	0.6657
Change in hedged item at forward rates*	-5,113,362.4562

* this calculation involves retranslating the net assets at the forward rate to 31/12/01 @ 31/12/00 and then again at the forward rate to that date at 31/12/01 itself (ie at the spot rate) this is consistent with the methodology used in IE 15 of IFRIC D22