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Sir David Tweedie
Chairman of the
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Group Accounting

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8th March 2011

Re: ED/2010/13 Hedge Accounting

Dear Sir David,

We appreciate the opportunity to comment on the above mentioned exposure draft.

RWE is one of the leading utilities in Europe, focussing on the electricity and gas sector. Our activities cover all of the major elements of the energy value chain. Headquartered in Germany and with external revenues amounting to 53 bn. EUR we are providing work for more than 70.000 full-time employees (figures as of 31 December 2010).

We strongly support the IASB's intent to align risk management and accounting by proposing a more principle-based approach for hedge accounting. In the energy industry this will help to present the economic characteristics of the business more adequately and thus improve the information presented in the financial statements. This is in particular true with regard to the following issues:

- Eligibility of hedged items and hedging instruments, in particular
 - designation of specific risk components in non-financial items,
 - designation of a combination of an exposure and a derivative as a hedged item;
- Groups of items and net positions, i.e. permitting hedge accounting for relationships other than between a single hedging instrument and a single hedged item;

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- Effectiveness testing, in particular
 - elimination of retrospective effectiveness testing,
 - elimination of the 80 – 125 %-bright line,
 - strong link between effectiveness testing and risk management;
- Accounting for the time value of an option that qualifies for hedge accounting; the proposals will help to avoid income volatility that is only accounting-driven, but does not exist economically.

We also welcome the continuation of the IASB's discussions with regard to open portfolios and macro hedges in a later phase of the project. Nevertheless, we think that the present exposure draft is an important step in improving the presentation of business models and risk management strategies in the financial statements of entities so that we support the IASB's intent to issue the new requirements for hedge accounting even without having finished the deliberations on macro hedging if this is not possible in the short term.

Further to this general approval, we would like to point out the following issues where we think that the board's approach could be improved by making it even more principle-based and by solving some pending issues that are of high importance for the users of financial statements:

- As a general statement, we believe that all economic hedge strategies should be eligible to hedge accounting on the basis of adequate documentation. We have noticed that some items/instruments (even if deemed to be economic hedges) do not qualify for hedge accounting (e.g. instruments designated as at fair value through other comprehensive income under IFRS 9 are not eligible hedged items, written options are not eligible hedging instruments).
- Since hedge accounting will not be available for all economic hedges, we believe that hedge accounting should remain optional and hence revocation of hedge accounting should still be based on a voluntary basis as well ("scope of hedge accounting", "optionality of hedge accounting" and "voluntary revocation" are interdependent and cannot be considered separately).
- Regarding the application of fair value accounting on own use contracts, in our opinion the issue is not adequately solved and the following should be considered for the final standard:
 - Derivative accounting should be allowed as an option only, because otherwise the requirement could produce significant accounting mismatches; and
 - it should be considered that contracts may be composed of two or more separate contracts for the purpose of IFRS 9 under certain conditions.

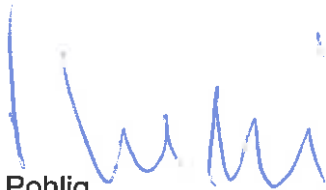
- With regard to the disclosure requirements, we are concerned that they will lead to the publication of sensitive information about the entities' business strategies. This is in particular true with regard to the provisions concerning the amount, timing and uncertainty of future cash flows, which require to disclose detailed quantitative information about the risk exposures of the entities.

On the following pages we comment on the questions posed in the invitation to comment on the exposure draft in detail.

We hope that our comments are helpful for your considerations. We would also like to refer to the comment letter of the International Energy Accounting Forum (IEAF) that contains more details and examples regarding hedge accounting in the energy industry. If you have any questions please do not hesitate to contact Fred Riedel, Head of Group Accounting (fred.riedel@rwe.com), or Britta Leippe, Head of IFRS Competence Center (britta.leippe@rwe.com) of RWE AG.

Sincerely yours,

RWE Aktiengesellschaft



Pöhlig
(CFO)



Riedel
(Head of Group Accounting)

Question 1

*Do you agree with the proposed objective of hedge accounting? Why or why not?
If not, what changes do you recommend and why?*

As indicated in our cover letter, we strongly support the IASB's intent to align risk management and accounting by proposing a more principle-based approach for hedge accounting.

However, we believe that a non-economically justified restriction is still pending in the exposure draft. There are numerous examples where the risk management strategy is to hedge one or more risks attributable to items that do not affect profit or loss. Imagine e.g. a company that issues hybrid capital denominated in a foreign currency which is classified as equity according to IAS 32. The company is exposed to a foreign currency risk because it has to pay interests in a foreign currency. If the company aims to hedge itself against this exposure, the company may conclude cross currency swaps. Although the company is not exposed to any risk afterwards, there will be income volatility because of recognising the derivatives at fair value through profit or loss. As the derivatives are, however, meant to assure a certain level of equity, fair value measurement of the derivatives should also be reflected in equity by applying hedge accounting.

Another example refers to equity instruments that will (in accordance with IFRS 9) be designated as at fair value through other comprehensive income. Under the current proposals, these instruments would not be eligible for hedge accounting, although they can represent economic hedges.

In these cases, it is not possible to represent risk management strategies adequately in the financial statements. We therefore ask the IASB to reconsider this issue so that hedge accounting is not restricted by a rule-based measure.

Question 2

Do you agree that a non-derivative financial asset and a non-derivative financial liability measured at fair value through profit or loss should be eligible hedging instruments? Why or why not? If not, what changes do you recommend and why?

Yes, we agree.

Question 3

Do you agree that an aggregated exposure that is a combination of another exposure and a derivative may be designated as a hedged item? Why or why not? If not, what changes do you recommend and why?

Yes, we agree and again strongly support the intent of the IASB to align risk management and accounting by removing inconsistent rule-based measures from IAS 39.

Question 4

Do you agree that an entity should be allowed to designate as a hedged item in a hedging relationship changes in the cash flows or fair value of an item attributable to a specific risk or risks (ie a risk component), provided that the risk component is separately identifiable and reliably measurable? Why or why not? If not, what changes do you recommend and why?

Yes, we agree. We strongly support the IASB's intent to align hedge accounting requirements for both financial and non-financial items. In the energy industry, this will help to achieve hedge accounting for economic hedges that have not been eligible for hedge accounting under IAS 39. The example used in ED/2010/13 par. B15 with regard to gas supply contracts is a common example for the industry which shows that applying hedge accounting for risk components in non-financial contracts improves the information quality of the financial statements of the energy industry.

Question 5

- (a) *Do you agree that an entity should be allowed to designate a layer of the nominal amount of an item as the hedged item? Why or why not? If not, what changes do you recommend and why?*
- (b) *Do you agree that a layer component of a contract that includes a prepayment option should not be eligible as a hedged item in a fair value hedge if the option's fair value is affected by changes in the hedged risk? Why or why not? If not, what changes do you recommend and why?*

Yes, we agree that an entity should be allowed to designate a layer of the nominal amount of an item as hedged item since this improvement ensures that risk management policy will be adequately translated into accounting.

We are, however, concerned that although the IASB intends to apply a principle-based approach it has nevertheless introduced new restrictions in its proposed guidance. We would rather propose a positive principle-based approach explaining that a layer component including a prepayment option is eligible to hedge accounting only to the extent that the risk component can be separately identifiable and meets all the requirements to be accounted for as such.

Question 6

Do you agree with the hedge effectiveness requirements as a qualifying criterion for hedge accounting? Why or why not? If not, what do you think the requirements should be?

We strongly welcome the removal of the 80-125% bright line test to assess whether the hedging relationship qualifies for hedge accounting. We also support the IASB's view to link risk management objectives with hedging documentation in ED/2010/13 par. 19.

Furthermore, the ED requires that the hedging relationship should meet the objective of the hedge effectiveness assessment and *is expected to achieve other than accidental offsetting*. The objective of the hedge effectiveness assessment is to ensure that the hedging relationship will produce an unbiased result and *minimise expected hedge ineffectiveness*.

On that topic, we believe that the IASB should clarify that since the entity should rely on its risk management to determine the hedging instrument, the hedging instrument will not necessarily be the most effective but could be an alternative instrument (because it will be traded in a more liquid market or is less expensive).

Otherwise, some could believe that minimising ineffectiveness is not achieved if other more effective instruments exist on the market.

The fundamental objective of any risk management policy is *risk reduction*, as it is not always possible to know 'ex-ante' whether hedging strategies adopted by the risk management will actually succeed in minimising expected hedge ineffectiveness. Therefore, minimising hedge ineffectiveness should be presumed when the transaction is part of the risk management strategy.

Question 7

- (a) *Do you agree that if the hedging relationship fails to meet the objective of the hedge effectiveness assessment an entity should be required to rebalance the hedging relationship, provided that the risk management objective for a hedging relationship remains the same? Why or why not? If not, what changes do you recommend and why?*
- (b) *Do you agree that if an entity expects that a designated hedging relationship might fail to meet the objective of the hedge effectiveness assessment in the future, it may also proactively rebalance the hedge relationship? Why or why not? If not, what changes do you recommend and why?*

We strongly support the IASB in its efforts to align risk management objectives with hedge accounting and therefore agree with the proposed approach subject to what follows.

Even if we feel that the rebalancing principle is intended to reduce complexity in applying hedge accounting and we support this principle because it is a means to react to the dynamics of risk management, we would like to ask the IASB to clarify this principle with respect to the application guidance that is provided in B46-60 and that should follow the way we interpret it (see below). Our remarks will mainly focus on cash flow hedging.

We have noted that concepts such as risk management policy/objective or change in risk management policy/objective are nowhere defined in the proposal. Since we believe that entities should use their adequate internal documentation to assess whether the risk management objective does remain or not the same for the hedging relationship and should rely on strong internal controls to make sure that (and how) risk management objectives are put in place, we ask the IASB to confirm that this assessment is subject to judgement.

According to us, a change of the risk management is likely to be a sustainable change of the risk management structure or strategy and not only a slight change due to operational events or marginal (and not lasting) market movements. This

statement would avoid that the documentation becomes much more complex than necessary because of a misinterpretation of the rebalancing principle.

With regard to the accounting consequences, we would like to ask the IASB to more adequately describe and illustrate the requirements on rebalancing. The following example shall help to illustrate our questions:

In the electricity business, risk management hedges the power plants as “real options” based on market prices. Generation forecasts therefore vary with forward market prices; and this is why the resulting hedge cover ratio needs to be adapted frequently: buying back when the forecast production (based on prevailing market prices) decreases and selling again when forecasts are going up again (hence, frequent rebalancing of the hedge cover ratio).

However since all power plants are not pure merchant¹ (i.e. production will not be based only on prevailing market prices²), it is important to emphasize that this hedging strategy entails **increases/decreases** in the hedge cover ratio, as a defined percentage of the forecast production, but that the forecast production is still highly probable (all other things remaining constant) and that this has to be seen as rebalancing, hence continuation of the hedging relationship.

If, for any reason, a portion of the forecast production should disappear, discontinuation of part of the hedging strategy must be considered.

It is assumed that when the hedged item's and the hedging instrument's characteristics are matched, the hedge should be fully effective.

It is our understanding that, provided that the forecast production is still highly probable and considering that elective dedesignation (see our answer to question 8 below) is not permitted as long as the risk management criteria are met, the accounting impacts of the above described strategy will be fully booked in other comprehensive income, i.e. all the hedging derivatives, including any subsequent accreting or offsetting derivatives that belong to the designated hedging strategy.

¹ Pure merchant power plants will run if the (dark or spark) spread is positive and will not run if it is negative.

² Because of technical constraints (e.g. no or little generation flexibility for other than gas-fired assets) and end-customers demand (final electricity demand is rather inelastic in many circumstances).

Question 8

- (a) *Do you agree that an entity should discontinue hedge accounting prospectively only when the hedging relationship (or part of a hedging relationship) ceases to meet the qualifying criteria (after taking into account any rebalancing of the hedging relationship, if applicable)? Why or why not? If not, what changes do you recommend and why?*
- (b) *Do you agree that an entity should not be permitted to discontinue hedge accounting for a hedging relationship that still meets the risk management objective and strategy on the basis of which it qualified for hedge accounting and that continues to meet all other qualifying criteria? Why or why not? If not, what changes do you recommend and why?*

We agree that an entity should discontinue hedge accounting when the hedging relationship ceases to meet the qualifying criteria.

We also agree that the introduction of rebalancing would help to achieve more flexible accounting requirements and would help to better reflect the developments of the entity's risk management activities in the financial statements.

However, since hedge accounting will not be available for all economic hedges (e.g. hedging an instrument designated as at fair value through other comprehensive income, use of written options, macro hedging), it will not be possible to represent all risk management strategies in the financial statements. That would lead to the conclusion that the revision of hedge accounting is still incomplete to offer a full consistent principle-based approach to apply hedge accounting to all existing economic hedges.

As a consequence of what precedes, we do believe that applying hedge accounting should remain optional and therefore the revocation of hedge accounting should be based on a voluntary basis as well. We think that the scope and the optionality of hedge accounting as well as the voluntary revocation are interdependent and cannot be considered on a stand-alone basis.

Furthermore, we do not think that the prohibition of a voluntary revocation is necessary as an anti-abuse measure since

- it is generally not the aim of entities to avoid application of hedge accounting when it is allowed, because applying hedge accounting would reduce in many cases non-economically justified volatility in its profit and loss (the entity is likely to rebalance its hedging relationship and would therefore not revoke its designation);
- the voluntary revocation of hedge accounting (when all criteria are otherwise still met) is not an incentive to generate profit or loss effects since it does not

lead to a reclassification of fair value gains or losses previously recognised in other comprehensive income into profit or loss.

A voluntary revocation of hedges may, however, be helpful in situations where hedge accounting becomes more and more complex over the lifetime of a hedging relationship. This shall be explained with the help of the following example:

In the context of the building of new power plants, currency risks arise when components are supplied by foreign suppliers and denominated in a foreign currency. These risks are hedged with the help of foreign currency forward contracts. In the financial statements, this hedge is reflected as a cash flow hedge of highly probable forecast transactions (= the foreign currency amount that has to be paid after delivery of the components).

During the construction period it happens that the delivery of components is delayed. In this case, new currency forwards are entered into which fall due at the date of expected delivery. As it is very difficult to predict the exact delivery dates in a complex project like the construction of a power plant, hedge accounting for the exposures described above may become complex and error-prone over time. The difficulty lies in particular in the allocation of the components of other comprehensive income to the hedged items when they realise. In order to avoid errors arising from the complexity of hedge accounting in such a situation an entity might decide to forego hedge accounting for the future and therefore revoke the hedging relationship.

Question 9

- (a) *Do you agree that for a fair value hedge the gain or loss on the hedging instrument and the hedged item should be recognised in other comprehensive income with the ineffective portion of the gain or loss transferred to profit or loss? Why or why not? If not, what changes do you recommend and why?*
- (b) *Do you agree that the gain or loss on the hedged item attributable to the hedged risk should be presented as a separate line item in the statement of financial position? Why or why not? If not, what changes do you recommend and why?*
- (c) *Do you agree that linked presentation should not be allowed for fair value hedges? Why or why not? If you disagree, when do you think linked presentation should be allowed and how should it be presented?*

As a general comment, we strongly support the intent of the IASB to retain a dedicated accounting treatment for fair value hedges. Indeed, we believe that the underlying fundamentals of fair value hedges are quite different from cash flow hedges since

- cash flow hedges are related to highly probable transactions that are not yet accounted for in the financial statements,
- while fair value hedge accounting (except for unrecognised firm commitments) applies to items that are already recognised in the financial statements.

We believe, however, that the introduction of a two-step approach (recognising all changes in fair value of both hedged items and hedging instruments and then recycling immediately the ineffectiveness into profit or loss) does not add any value. Furthermore:

- There is no rationale/principle that supports the recognition of the gain or loss of the hedged items and hedging instruments in other comprehensive income;
- the immediate reclassification of ineffectiveness from other comprehensive income to profit or loss is in substance not a change compared to IAS 39 which has already required to recognise ineffectiveness in profit or loss.

We furthermore do not believe that the proposed approach has eliminated the mixed measurement for the hedged item since the total amount that would be accounted for according to IFRS 9 (hedged item + the gain or loss on the hedged item attributable to the hedged risk) is not different from the amount recognised under IAS 39.

As a consequence, we ask the IASB to reconsider the cost-benefit of this measure that does not depart significantly from IAS 39 (we believe that IAS 39 mechanics should remain) and that would not reduce complexity in applying hedge accounting.

Even if we agree that the proposal intends to avoid a measurement attribute that is neither at amortised cost nor at fair value, we however ask the IASB to reconsider the use of a separate line for the following reasons:

- We fear that most of these separate assets and liabilities (those related to the gain or loss on the hedged items attributable to the hedged risk) would not meet the definition of an asset or a liability according to the framework in themselves but should rather be related to another asset or liability;
- this information in itself (i.e. on the face of the balance sheet) is not necessary to understand the risk management policy of an entity since it is redundant with the information provided in the disclosures. On the contrary, in the case of an entity that uses hedge accounting for several asset and liability

items, it would lead to a huge number of additional line items which would make the statement of financial position look complex and confusing.

Additionally, we agree that linked presentation should not be allowed for fair value hedges. Linked presentation would not reduce complexity in preparing financial statements when the risk policy is complex and would be redundant with the information provided in the disclosures.

Question 10

- (a) Do you agree that for transaction related hedged items, the change in fair value of the option's time value accumulated in other comprehensive income should be reclassified in accordance with the general requirements (eg like a basis adjustment if capitalised into a non-financial asset or into profit or loss when hedged sales affect profit or loss)? Why or why not? If not, what changes do you recommend and why?*
- (b) Do you agree that for period related hedged items, the part of the aligned time value that relates to the current period should be transferred from accumulated other comprehensive income to profit or loss on a rational basis? Why or why not? If not, what changes do you recommend and why?*
- (c) Do you agree that the accounting for the time value of options should only apply to the extent that the time value relates to the hedged item (ie the 'aligned time value' determined using the valuation of an option that would have critical terms that perfectly match the hedged item)? Why or why not? If not, what changes do you recommend and why?*

As a general comment, we strongly support the IASB in its intent to align optimal business decisions with accounting. Indeed, the accounting treatment of time value under IAS 39 has often prevented the entities from using option derivatives for the benefit of linear derivatives such as forward contracts or swaps that were often considered less suitable economically (giving away upside as well as protecting downside risk), but preferable from an accounting perspective.

In addition, we feel that the proposed accounting treatment is sometimes complex and we would propose the IASB to eventually reconsider it with respect to DIG issue G20 in US GAAP that actually deals with options well and that could be used as a framework.

Furthermore, we assume that the guidance applicable to the time value of an option will also be applicable for the time value of a forward contract (interest element). However, we believe that this clarification is not straightforward in the

proposal. Therefore we propose that ~~the~~ guidance related to the accounting treatment of the time value of an option should be applied by analogy to the interest element of a forward contract.

Question 11

Do you agree with the criteria for the eligibility of groups of items as a hedged item? Why or why not? If not, what changes do you recommend and why?

Yes, we agree and strongly support the overall proposal of the IASB to extend hedge accounting to groups of items and net positions.

However, as we have said before, we think that in order to achieve an even better alignment of risk management and accounting it would be necessary to extend hedge accounting to open portfolio and macro hedging as these strategies are fully part of the risk management and risk mandates of the companies. We therefore welcome the continuation of the IASB's discussions with regard to these issues as indicated in our cover letter.

Furthermore, we are concerned about the fact that the IASB – while it has intended to fully align risk management and hedge accounting – continues to pursue an accounting approach based on individual items. According to ED/2010/13 par. BC178 an entity would “need to designate a *combination of gross positions* if it were to apply the hedge accounting mechanics to the hedged position.”

We instead believe that an entity would designate a *net position*, but for internal control purposes, it would need to document the items that constitute this net position. Indeed, we feel that our proposed statement will avoid confusion about the intent of the IASB to allow net position as eligible hedged item.

Question 12

Do you agree that for a hedge of a group of items with offsetting risk positions that affect different line items in the income statement (eg in a net position hedge), any hedging instrument gains or losses recognised in profit or loss should be presented in a separate line from those affected by the hedged items? Why or why not? If not, what changes do you recommend and why?

We agree with the proposal to present on a net basis in a separate line the gains or losses attributable to the hedging instruments. That would indeed avoid artificial grossing up of gains or losses (that do not exist).

We are however concerned that this principle does not apply to fair value hedges where the proposal requires that the gain or loss shall be presented on a gross

basis next to each line item that includes the related asset or liability. Since the disclosures provide the users with sufficient information about the risk management policy (and its consequences in the financial statements), we believe and ask the IASB that the change in fair value should be aggregated into a single line in the statement of financial position.

Question 13

- (a) *Do you agree with the proposed disclosure requirements? Why or why not? If not, what changes do you recommend and why?*
- (b) *What other disclosures do you believe would provide useful information (whether in addition to or instead of the proposed disclosures) and why?*

We agree that disclosures play a fundamental role in understanding the risk management policy of an entity.

As indicated in our cover letter, we are, however, concerned that the proposed provisions require the publication of sensitive information. This is in particular true with regard to the disclosures required on the amount, timing and uncertainty of future cash flows, which require to disclose detailed quantitative information about the risk exposures of the entities.

Moreover, we would like to draw the attention of the IASB on the importance of the use of judgement and therefore would like to emphasise the following:

- Leaving the disclosures up to the judgement of the entity is crucial since disclosing all existing information directly or indirectly linked to hedge accounting would “drown” the users of financial statements especially in a situation when the entity has many and often complex activities.
- Using judgement will also enable the entity to make a trade-off between existing disclosures already foreseen in its reference document (that includes consolidated financial statements but also – due to regulatory reasons like the requirement to present management commentary in Germany – disclosures on risk management) so that some information do not become redundant because of a rule-based approach on disclosures.

In addition, we would rather have included paragraphs 44-52 in the application guidance (and not in the standard itself). This would avoid a rule-based interpretation of the requirements (these paragraphs being understood as a checklist to be fully filled in by each entity) and would rather enable the entity to prepare relevant information to the users of financial statements.

At last, we are concerned about the wording used by the IASB and which reinforces this “checklist” approach, i.e. the wording “shall” is used instead of “may or may not”.

Question 14

Do you agree that if it is in accordance with the entity's fair value-based risk management strategy derivative accounting would apply to contracts that can be settled net in cash that were entered into and continue to be held for the purpose of the receipt or delivery of a non-financial item in accordance with the entity's expected purchase, sale or usage requirements? Why or why not? If not, what changes do you recommend and why?

We basically welcome the IASB's intent to simplify the accounting for portfolios that are managed on a fair value basis by providing for a full fair value approach and thus avoid complex hedge accounting.

However, we think that this issue is not adequately solved since – if we understand the proposal correctly – it results from the proposal that fair value accounting would apply mandatorily to any own use contracts that are managed based on fair value. This would inevitably result in higher artificial volatility in the financial statements, which would not be beneficial for users. It would also increase complexity for preparers in a number of industries which currently make use of the own use exemption.

As an alternative, we believe that this issue would be more adequately solved if

- derivative accounting would be allowed as an option only; and
- it can be considered that contracts may be composed of two or more separate contracts for the purpose of IFRS 9 under certain conditions.

Applying derivative accounting for contracts that otherwise meet all requirements for application of the own use exception should be left as an option since automatic application of fair value accounting for contracts managed at fair value would lead to profit and loss mismatch and volatility in some situations. This is especially occurring when contracts are managed together with assets that are not in the scope of IAS 39 and are not fair valued (example: power plants accounted for according to IAS 16).

For example, in the energy industry, it is a common practice to manage power plants and related electricity sales on a fair value basis. In this case, the fair valuation of the sales contracts would lead to an accounting mismatch and therefore “artificial” volatility in profit or loss, as the power plants are still subject to

accrual accounting according to IAS 16 (or fair value measurement through other comprehensive income).

On the other hand, there are cases where it can make sense to apply the same accounting treatment for all contracts within a portfolio. This could be the case when for example electricity or gas supply contracts have to be fair valued because part of the volume is economically managed by using derivatives. In this case, it could be appropriate to fair value physical sales contracts to end-customers that actually qualify for own use accounting under IAS 39 as well in order to avoid accounting mismatches.

Against this background, we propose to introduce a fair value option for own use contracts in particular for the purpose of avoiding accounting mismatches that is similar to the fair value options for financial assets and financial liabilities as governed by IFRS 9 par. 4.1.5 and 4.2.2.

Furthermore, commodity contracts often contain volume flexibilities, and in some circumstances³ it would be appropriate to consider them separately from the rest of the contract. For long term commodity purchase or sales contracts, it can also be appropriate to consider different blocks of volumes within one single contract.

The separate treatment can be adequate because of different business purposes (so that accrual accounting for one part and fair value accounting for another part is possible), or because of a different hedging strategy that will be applied to the different components of a contract.

A contract has two (or more) components that could have been the subject of two (or more) separate contracts in the following examples:

Example 1

An energy sales contract with a volume of 100, of which a minimum quantity of 75 and a flexibility of 25, can be considered as a combination of two separate contracts: a forward sale of 75 and a written option that allows the customer to purchase a quantity of 25.

Example 2

A long term gas purchase contract with an annual volume of 1,000 take or pay, a price indexed on fuel and a term of 10 years, can be considered as a combination of two separate contracts: one with a volume of 800, and one with a volume of 200. The business intention of both contracts may be different. For example: 800 in accordance with the entity's expected purchase, sale or usage requirements, and 200 for trading activities.

³ This separation should be analysed on case-by-case basis since volume flexibilities can comply with different management intentions, i.e. one being made for own use purposes and others being concluded for optimization purposes (and managed therefore based on its fair value).

Split designation of such contracts, based on volumes, should be possible at the inception of the contracts and provided that the entity can ensure that the volumes sold to the market do not exceed the volumes designated as financial instruments.

We have noted that the IFRIC received in January 2010 a (quite similar) request to add an item to its agenda on providing guidance on whether a contract that can be seen as two separate contracts for the purpose of applying paragraphs 5-7 of IAS 39. At that time, the IFRIC decided not to add this issue to its agenda arguing that the IASB would answer it through its project to replace IAS 39. This request has not been taken into account in the IFRS 9 proposal.

We would therefore like to propose that the IASB clarifies that composed contracts to buy or sell a non-financial item can be considered as two (or more) separate contracts under the following conditions:

- The contract has two (or more) components that could have been subject of two (or more) separate contracts, which together would have had exactly the same impact as the composed contract.
- The cash flows and the risks of the separate components can be clearly identified and measured.

In our opinion, this would lead to an economically appropriate and informative presentation of such contracts in the financial statements.

Question 15

- (a) *Do you agree that all of the three alternative accounting treatments (other than hedge accounting) to account for hedges of credit risk using credit derivatives would add unnecessary complexity to accounting for financial instruments? Why or why not?*
- (b) *If not, which of the three alternatives considered by the Board in paragraphs BC226–BC246 should the Board develop further and what changes to that alternative would you recommend and why?*

We believe that prohibiting hedge accounting for credit risk is a rule-based measure that does not fit to the objectives followed by the IASB. Rather, we would propose that hedge accounting should be applied if all criteria are otherwise met (i.e. eligibility of hedged item, consistency with risk management etc.).

However, we acknowledge that it may be difficult to achieve hedge accounting in practice for the reasons raised in the ED (hedged item cannot be reliably identified and measured). Therefore, we support the IASB in its efforts to investigate further in the development of the proposed alternatives.

Question 16

Do you agree with the proposed transition requirements? Why or why not? If not, what changes do you recommend and why?

Yes, we agree with the proposed transition requirements.

With regard to the effective date, we would, however, like to point out that 1 January 2013 – this would give the entities 18 months provided that the final standard is issued by mid of 2011 at the latest – is too early for the implementation of the new requirements, because they will lead to fundamental changes compared to IAS 39. We would therefore propose that IFRS 9 will become mandatory not earlier than 2015 (cf. also our comment letter to the “Request for Views on Effective Dates and Transition Methods”). Nevertheless we recommend to retain that earlier application is permitted.