



Paris, March 8th 2011

International Accounting Standards Board  
30 Cannon Street  
London  
EC4M 6XH  
United Kingdom

Dear Sir / Madam

**Re: Exposure Draft Hedge Accounting (ED/2010/13)**

Dear Sirs,

The French Association of Corporate Treasurers (AFTE, *Association Française des Trésoriers d'Entreprise*) wishes to thank the International Accounting Standards Board (IASB) for the opportunity to comment on the ED/2010/13 "Hedge Accounting" dated December 2010.

AFTE is made up of 1,300 members representing the 1,000 largest French firms. It is the oldest association of corporate treasurers in the world, and plays an active role in the works of the European Association of Corporate Treasurers (EACT), which it helped to found.

AFTE wishes to make clear that **this response applies to Industrial and Commercial companies only**; it does not take into consideration sectors such as Bank and Insurance, which may have different concerns.

This ED is essential for Corporates and AFTE would like to emphasise that corporate treasurers represents a larger community of preparers than banks community.

**AFTE would like to stress the importance of having reliable and constant, long-term standards.** For example, given a hedged position of ten years or longer, it would be very problematic if the rules were changed every five years.

Our answer completes the answers of the EACT which we endorse.

We welcome the IASB's project to improve and simplify IAS 39 and undertake a fundamental review of the standard. IAS 39 has widely been regarded as unduly complex and often leading to unrepresentative accounting outcomes. We believe that hedging is an economic activity and that hedge accounting should be designed to reflect the economic reality of risk management. IAS 39 hedging is rule-based whereas IFRS is, in general, principles based. Many of the rules related to hedge accounting were drafted to prevent abuse.

As a result, the treasury community has experienced a worrying trend in recent years, of risk management activities often being structured sub-optimally to fit within the strict guidelines of IAS 39.

In addition, compliance requires significant time and effort which is disproportional to the benefit obtained. Although we recognize that there have to be controls over the application of hedge accounting, we believe that this control would best be accomplished through use of professional judgment rather than rules based standards.

AFTE considers that the ED is one step in the right direction and agrees with the objectives of the Board as they bring accounting closer to the risk management strategy of non-financial companies and simplify hedge accounting rules.

However, AFTE should not support new IFRS 9 mandatory rules that are not in the line with the principles based approach.

AFTE believes that disclosures play a fundamental role in complementing financial information derived from the principles-based proposals in the ED. The proposals require application of more judgement than IAS 39. To increase transparency and comparability, we believe that the disclosures should help users to understand the overall risk management strategies.

AFTE also believes that the new standard should encourage corporates to transform the administrative burden of IAS 39 to much more analysis and not only to transfer the first one to a new one.

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Having expressed these views, AFTE has a number of concerns, the most significant of these are:

- (a) The IASB has split the revision of IAS 39 into a number of phases. However, considerable interdependencies exist among the phases of this project (particularly the amortised cost and impairment phase and macro hedging) and other projects that the IASB is concurrently working on (e.g. insurance and financial statement presentation). Therefore, we believe that the IASB will need to consider the entire package of proposals before finalising the resulting standards. We anticipate the following area for further development:
  - (i) the eligibility of embedded derivatives as hedging instruments,
  - (ii) the eligibility of equity instruments measured at fair value through other comprehensive income as hedged items.
- (b) We believe that a number of issues require further consideration. These include the eligibility of:
  - (i) non-contractually specified inflation risk as hedged item;
  - (ii) other risks not affecting profit or loss

In our view, these issues could create inconsistencies with risk management practices.

- (c) We believe that the ED should not enter into mandatory approach concerning de-designation and rebalancing rules.
- (d) We believe that the ED should not insert the reporting period concept but ED should refer to hedging management risk period which is much more correlated to the treasury activity.
- (e) We believe that the new “aligned time value” calculation adds burdensome.
- (f) The proposals rely heavily on judgement and the link to risk management. To ensure that this link is truly achieved, we believe that the IASB should conduct field-testing and outreach activities to ensure that proposals can be operationalized.
- (g) New disclosures do not give more information for users and might reach to give competitive information.

If you wish to discuss our comments further, please do not hesitate to contact us.

Yours sincerely,

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**Sébastien Tranzeat**

AFTE, IFRS Committee Chairman

## Response to IASB ED/2010/13 Financial Instruments: Hedge Accounting - response before 9<sup>th</sup> of March 2011

### 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?

### AFTE's response

AFTE agrees with the ED's objective to reflect, in the financial reporting, the extent and effects of an entity's risk management activities.

AFTE wonders why "Hedge Accounting ED" only applies to risks that affect profit or loss. Members highlighted situations where risk management is to hedge shares with impact in OCI. The ED do not accept that effect of hedging instrument should be recognized in OCI rather than P&L. Effect of IFRS 9 "rules" tends to an accounting mismatch.

*Example : Entity A invests in a listed shares X then qualifies this investment as strategic. Effect of fair value variation is recognized in OCI without any effect in P&L in the future (except dividends). Nevertheless, management decides to hedge risks on shares X with call or forward. Effect of hedging instrument is recognised in P&L.*

We also widen this remark to the risk management activity around IFRS2, IAS 19 (pension...).

**We encourage the IASB to reconsider carefully why it is necessary to prohibit hedge accounting for items that affect other comprehensive income or equity as well.**

### 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?

### AFTE's response

AFTE fully supports that a non-derivative financial asset and a non-derivative financial liability measured at fair value through profit or loss should be eligible as hedging instruments.

**We encourage IASB to give implementation guidance to designate component risk of non-financial that will be eligible as hedge item.** Should Risk component be clearly identified in a index formula into contracts or only be correlated to a risk that can be hedge in respect to risk management documentation?

We do not believe that IASB has to give place to judgment on that subject.

In connexion to Q1, we also believe that non-derivative instruments other than those at fair

value through profit or loss should be eligible as hedging instruments.

### 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?

#### **AFTE's response**

**AFTE agrees that a synthetic exposure may be designated as a hedged item and represent a positive step to match accounting with corporate risk management purposes.**

**We encourage IASB to give implementation guidance to designate a global exposure (combination of a hedge item and hedging instrument) as hedged item.**

**Example :**

**Interest Rate Risk management policy is to have a fixed debt in a range of 70% to 80%. In order to respect this guideline, treasurer transforms a fixed interest rate bond to a variable rate to obtain a synthetic variable interest rate bond. Then, treasurer uses a fix pay swap or purchase cap to obtain a global exposure in risk management guideline.**

**Exposure draft do not give guidance on how to consider accounting mechanism when global exposure is a combination of a Fair Value hedge and a Cash Flow Hedge ?**

### 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 (i.e. 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?

#### **AFTE's response**

**AFTE fully supports the proposal to allow the designation of a risk component as a hedged item if it is separately identifiable and measurable (like contractually specified).**

**We question why an inflation risk should not be able to follow hedge accounting rules.**

#### 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?

#### **AFTE's response**

**AFTE fully agrees that an entity should be allowed to designate a layer of the nominal amount of an item as the hedged item that reduces hedge accounting complexity.**

**AFTE do not support in its entirety that an entity could not designate as hedge item a contract with a prepayment option, because :**

- (a) a distinction should be made between purchased and written prepayment options : when an entity controls the exercise of the option, the designation of a layer component should be allowed since the entity is able to demonstrate that the option is not affected by the hedged risk (e.g. interest rate).
- (b) if entity use a hedging instrument with a symmetric prepayment option, entity should be authorized to use hedged accounting.

#### 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?

#### **AFTE's response**

**AFTE fully approved the removal of the 80 to 125 per cent test for assessing and measuring hedge effectiveness and the introduction of an objectives-based assessment. But, we think that this removal only eliminates the undue sanction to fully impact P&L when under IAS39 test will be not respect due to unintentional matters. Ineffectiveness calculation remains same as IAS 39.**

But, we are also concerned that the proposed guidance may create inconsistencies between risk management and accounting as explained below :

- i) management consider that any ineffectiveness should be accounted if treasurer respect defined policy but for accounting purpose ED impose to put on P&L this ineffectiveness
- ii) We want also to emphasis problem when hedging activity will be not due to an

entity risk management policy determined in its sole discretion but it due to respect to financing constraints, like into finance project contract (as infrastructure). In that type of activity, balance sheet and P&L are impacted with fair value that give to users a “wrong” view of infrastructure business project. IASB should make some exceptions.

#### 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?

#### AFTE's response

**(a) AFTE agrees with the notion of ‘rebalancing’ hedging relationships, because this enables an entity to reflect in hedge accounting the changes in hedge ratio that it makes for risk management purposes (see example Q4).**

**Nevertheless, notion of rebalancing is not yet well understood** and we therefore suggest the IASB to undertake the necessary field-testing to ensure that the proposals can be operationalized and give implementation guidance. If not, this could raise operational difficulties since:

- (i) Rebalancing is mandatory and could lead to review hedging accounting in each reporting period that is not to reduce complexity.
- (ii) Several rebalancing lead to new burdensome administrative work without any value added to management reporting

We understand in example Q4 that entity does not have to rebalance. Entity has to aggregate all fair value impact on “OCI” with non-significant ineffectiveness impact. If not AFTE suggest that IASB gives some guidance.

**(b) AFTE agrees, that if so, to allow entity to make prospective rebalancing.**

#### 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?

**AFTE's response**

**(a) While we refer to Q7a regarding the lack of clarity regarding the interactions between rebalancing and discontinuation**, AFTE agrees 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.

**AFTE do not agree with the mandatory** approach that an entity should not be permitted to discontinue voluntary hedge accounting for a hedging relationship that still meets the risk management objective and strategy and that continues to meet the qualifying criteria.

**(b) AFTE agrees to allow entity to make discontinuation prospectively.**

**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?

**AFTE's response**

AFTE acknowledges that the proposed presentation of fair value hedges would show the effect of hedging transactions in a single place of the financial statements. However, we fail to see what additional information that this would provide to users of financial statements.

**AFTE wants to emphasise that many corporate treasurer have invested (i) in new Treasury Information system to comply with IAS 39 rules and reporting (ii) in process and control reengineering.**

Nevertheless, AFTE believes that IASB was right in abandoning its original proposal to replace the fair value hedge accounting mechanics with the cash flow hedge mechanics for the same reasons as those stated in paragraph BC120 of the ED



**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?

**AFTE's response**

**AFTE welcomes the proposals, which address the issue of ineffectiveness due to the time value component in options and provide a solution to an important practical issue.**

**(a) AFTE does not support mandatory approach on the proposed basis adjustment. AFTE encourages IASB to leave preparers to take the appropriate approach to recognize option time value accumulated in OCI.** For example, apply basis adjustment for retail business is quite impossible.

AFTE believes that an allocation over the relevant period on a rational basis would be the most appropriate method.

(b) AFTE agrees that time value that relates to the current period should be transferred from accumulated other comprehensive income to profit or loss on a rational basis. However, AFTE do not understand the value added of the use of a "hypothetical" aligned time value as proposed in the ED. The new rule of "aligned time value" is burdensome.

Therefore, if ED maintains "aligned time value concept", we ask IASB to give some guidance.

( c ) see response (b)

AFTE believes that IASB should allow corporates to amortize the impact of the time value (bakwardation...) of FX forward.

**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?

**AFTE's response**

AFTE will not be able to have a global view on these proposals because it is more a bank concern than corporate one even if this possibility allows sometimes hedges accounting.

AFTE waits the macro hedging new standards to complete its response.

**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?

**AFTE's response**

AFTE agrees with the proposals regarding the presentation in profit or loss of the effects of hedge accounting for groups of items.

AFTE disagrees with the way gains or losses from fair value hedges of net positions are proposed to be presented. Rather than requiring presentation on a gross and disaggregated basis in the statement of financial position, we would recommend that all fair value changes be aggregated into a single item in the statement of financial position and to provide details in the notes.

AFTE highlights that IAS 39 is already complex to understand by users (credit banks analyst, financial and rating analyst). AFTE urge IASB that new standards do not create new accounting mechanism.

**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?

**AFTE's response**

AFTE are concerned about the prescriptive nature of the disclosure requirements and the interaction with the disclosure requirements of IFRS 7.

AFTE understands that disclosures play a fundamental role in providing users with an understanding of an entity's risk management strategy and hedging activities. In order to justify the use of hedge accounting in accordance with their risk management policies, we consider that entities should refine the description of their risk management policies and strategies.

**IFRS 7 is already wide and corporate has to keep the choice of data of the additional information. Besides, the ED information is too precise. Then users can redo the implicit calculation by crossing of IFRS 7 tables.**

**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?

**AFTE's response**

**AFTE understand that IASB wants to simplify accounting for "own use" commodity contract. Hence, AFTE agrees that the proposals are a step in the right direction, but demand to the IASB to investigate this issue further in finalising the proposals.**

**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?

**AFTE's response**

**AFTE believes that, where the hedged item is credit risk, there is not any inherent obstacle to achieving hedge accounting and hedge accounting should be permitted provided that the hedging relationship meets the general requirements for qualification and is consistent with the risk management activities.**

**We acknowledge this may be difficult to achieve in practice. Therefore, we support the IASB in its efforts to investigate further the development of the proposed accounting alternatives.**

**Question 16**

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

**AFTE's response**

**AFTE supports an effective date of 1 January 2015 for all phases of IFRS 9 and the other major projects currently under the consideration of the IASB. If IASB maintain 1 January**

**2013 as transition date, corporate treasurer have only 1,5 years to comply with this 2 years conception IFRS new standards.**

**AFTE supports only prospective application of the proposals. Therefore, IASB should give guidances on how treat transition application for IFRS 9 new time value option accounting.**