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1 MARCH, 2011

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

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

Dear Sir/Madam:

Bank Of China welcomes the opportunity to comment on the Exposure Draft: **Hedge Accounting(ED/2010/13)**. We support the principle-based approach for hedge accounting brought by the exposure draft (ED), which focuses more on actual risk management practices. The responses to the specific questions are as follows:

**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?*

**Comments**

We generally support the proposed objective. We think hedge accounting should cover all the activities related to risk management practices. We suggest that equities measured at fair value through OCI should be allowed to include within the scope of hedge accounting to avoid fluctuation in reserve and to reflect the reporting entity's risk management activities. This may be achieved by taking the effective portion of the fair value change of the hedging instrument to OCI and offset with the fair value change of the equity instrument there.

**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?*

**Comments**

We agree with the proposals for allowing a non-derivative financial asset and a non-derivative financial liability, measured at fair value through profit or loss, to be

eligible hedging instruments. It will extend the flexibility for an entity to designate hedging instruments in hedging relationships.

### **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?*

### **Comments**

We support the proposal that an aggregated exposure that is a combination of another exposure and a derivative (a synthetic exposure) may be designated as a hedged item. It will extend the flexibility for an entity to designate a hedged item in hedging relationships and be good for managing the different risk exposures.

### **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?*

### **Comments**

We agree with the proposal.

### **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?*

### **Comments**

We agree that an entity should be allowed to designate a layer of the nominal amount of an item as the hedged item. In addition, we 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.

### **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?*



### **Comments**

We support the decision to eliminate the effectiveness threshold of a range of 80%-125%. However, we suggest that certain quantity criterion for hedge accounting should be still set, which could contain the behavior of manipulating accounting information and improve the reliability and comparability of accounting information.

### **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?*

### **Comments**

We suggest that rebalancing should be permitted, but not required. This will better match hedge accounting with the entity's risk management objectives. Mandatory rebalancing effectively limits the ability of an entity to voluntarily discontinue a hedging relationship.

### **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?*

### **Comments**

We agree that an entity should discontinue hedge accounting prospectively when the hedging relationship (or part of a hedging relationship) ceases to meet the qualifying criteria. However, we think that even if the hedging relationship (or part of a hedging relationship) still meets the qualifying criteria, an entity should have option to discontinue hedge accounting. It can be more closely with the risk management objective and accord with the requirements of objective of hedge accounting.

### **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?*

### **Comments**

We 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.

We do not 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. Given the potential diversity of hedged items, this could result in a significant expansion of the requirements for the face of the statement of financial position. It is suggested that the gain or loss on the hedged item attributable to the hedged risk be disclosed in the footnotes.

We agree that linked presentation should not be allowed for fair value hedges.

### **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?*

### **Comments**

We 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. From an operational

perspective, It's better to use a unique treatment for both the cases above.

We 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.

We 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.

#### **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?*

#### **Comments**

We agree with the criteria for the eligibility of groups of items as a 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?*

#### **Comments**

We disagree. It is suggested to be disclosed in the footnote.

#### **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?*

#### **Comments**

We largely agree with the proposed disclosure, as the requirements are too specific, we suggest IASB to make further improvements.

#### **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?*

#### **Comments**



We agree with the proposal but subject to the condition that the hedged risk component is separately identifiable and reliably measurable.

**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?*

**Comments**

We 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.

**Question 16**

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

**Comments**

We agree with the proposed transition requirements but we do not agree with the proposed transition date of 1 January 2013. The proposals will require the entity to undertake a fundamental review of their hedging strategies, hedge documentation and associated accounting. In addition, all existing hedge relationships will need to be reviewed to ensure that they continue to qualify for hedge accounting at transition. It will need a longer period for preparation.

We hope the above comments can be helpful. Should you wish to discuss the contents of this comment paper further, please do not hesitate to contact us.

Yours sincerely,

Xiao Wei

(Signed)



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