



Madrid, 9 March, 2011
International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

Re: Exposure Draft ED/2010/13 – “Hedge Accounting”

Dear Sirs,

Repsol is very pleased to provide comments to the International Accounting Standards Board on its request for views on the Exposure Draft ED/2010/13 – “Hedge Accounting”.

In general terms, we agree with the hedge accounting model proposed in the Exposure Draft because it provides a number of significant improvements that will make hedge accounting more flexible and accessible for preparers.

In particular, we support the proposed objective to reflect, in the financial reporting, the extent and effects of the entity's risk management activities.

However there are some issues and concerns about the proposals included in the Exposure Draft that we would like to raise in this comment letter. Even though these issues are detailed in our responses to the questions in the Exposure Draft, we would like to summarize the more relevant ones:

- Accounting and presentation criteria for synthetic hedged items (Question 3)
- Layer component of a net investment in a foreign operation as hedge item in a net investment hedge (Question 5)
- Net investment hedge accounting requirements in separate financial statements of the investor (Question 9 a-b)

- Disclosures about past transactions which are related to accounting requirements in which a material change is being proposed (Question 13).
- Fair value through profit and loss accounting for own-use contracts (Question 14)

Further information about the Repsol Group and its activities is available on our website: www.repsol.com.

If you would like to discuss any of the points we describe in this letter, please do not hesitate to contact us by e-mail to normativacontable@repsol.com.

Thank you for your attention.

Yours sincerely,

Emilio Linares-Rivas Balius

Accounting Policies and Compliance Manager

Question 1 - Objective of hedge accounting

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

Yes, we agree with the proposed objective of hedge accounting.

Current hedge accounting requirements in IAS 39 do not always reflect the economic consequences of risk management strategies. In some aspects, IAS 39 is not flexible enough to ensure that information provided in the financial statements reflects the extent and impact of the hedging activities on the economic performance of the entity.

For example, entities usually design hedging strategies that are effective from an economic perspective ("economic hedges") but fail to be reflected in the financial statements as hedging transactions because they do not meet some specific qualifying criteria. We find this circumstance to be inappropriate for preparers and also for users of financial statements.

In general, the proposals eliminate several restrictions included in the IAS 39 and would improve the correlation between risk management activities and information provided in the financial statements and involve a clear improvement in hedge accounting requirements.

Question 2 - Instruments that qualify for designation as hedging instruments

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 with the proposal for the reasons exposed in our response to Question 1.

In addition, we consider this proposal to be consistent with the principles developed in the IASB's Financial Instruments Project (Phase I).

Question 3 – Derivatives that qualify for designation as hedged items

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 with the proposal for the reasons exposed in our response to Question 1.

However, we consider it would be helpful to include additional guidance relating to the accounting and presentation criteria applicable to the components of the hedged item (synthetic hedged items). For example, to enter into an interest rate risk cash flow hedge, designating as hedged item a combination of a foreign currency loan at fixed interest rate and a fixed to floating cross currency interest rate swap (CCIRS).

Question 4 – Designation of risk components as hedged items

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?

Yes, we agree with the proposal for the reasons exposed in our response to Question 1.

Question 5 – Designation of a layer component of the nominal amount

- (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?

Yes, we agree with the proposal for the reasons exposed in our response to Question 1.

However, we would like the Board to consider not restricting this accounting treatment only to fair value hedge and cash flow hedge relationships but extending this option also to net investment hedge relationships. We think that it would be interesting to provide additional guidance in order to understand which is the conceptual basis for not allowing the definition of a certain layer of a net investment in a foreign operation as a hedged item.

Question 6 – Hedge effectiveness requirements to qualify for hedge accounting

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?

Yes, we agree that hedge effectiveness should be one of the qualifying criteria for hedge accounting. We also agree that effectiveness should be assessed on an objective basis instead of on a quantitative basis (80-125 per cent range) because it would enhance the link between hedge accounting and an entity's risk management activities.

However, we think it would be helpful to include additional guidance relating to the hedge effectiveness requirement of "*other than accidental offsetting*" concept.

Question 7 – Rebalancing of a hedging relationship

- (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?

Yes, we agree with the proposal. In our opinion "rebalancing" allows an entity to adjust a hedging relationship that continues to be consistent with its risk management strategy and avoids the obligation of discontinuing only because the effectiveness testing results are not within the 80-125 per cent range. In this regard, we agree that the 80-125 per cent range is arbitrary and its elimination is consistent with the objective of hedge accounting that is being proposed.

We also agree with the proposal of making a proactive use of rebalancing. A proactive use of rebalancing would create enough flexibility to adjust a hedging relationship that the entity considers to be consistent with its risk management strategy. This circumstance would allow entities to identify and prevent future ineffectiveness and to avoid a discontinuation and restarting of hedge relationships when the risk management strategy remains unchanged.

Despite our comments to this question we think it would be adequate to include in IFRS 9 additional guidance about "rebalancing" in order to ensure its consistent application.

Question 8 – Discontinuing hedge accounting

- (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?

As several proposals to enhance hedging accounting flexibility and to avoid discontinuations have been included in the exposure draft, we agree with the decision of not permitting 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.

Question 9 a) b) – Accounting for fair value hedges

- (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?

We support the Board's effort to simplify hedge accounting requirements. In this regard, we understand that the proposed change for fair value hedges would improve the homogeneity between all hedge accounting models.

We also understand that as a consequence of the proposals, the information of the hedged item included in the balance sheet would be improved. However, we consider this information could also be provided in the notes instead of the proposed disaggregation in the statement of financial position.

Summarizing, we are not sure that fair value hedge proposals would result in significant improvements to current requirements.

In addition, we think it would be helpful to clarify how to account for net investment hedges in the separate financial statements of an investor. Is it the investor supposed to account for net investment hedges as fair value hedges in its separate financial statements?

Question 9 c) – Accounting for fair value hedges

- (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?

Yes, we agree with the proposal because the linked presentation does not differentiate between the types of risk covered by that relationship and those that are not. Consequently, we consider linked presentation would not help to provide useful information and agree with the Board's decision of requiring detailed disclosures in the notes to the financial statements.

Question 10 – Accounting for the time value of options for cash flow and fair value hedges

- (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 (e.g. 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 (i.e. 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?

Yes, we agree with the proposal for the reasons exposed in our response to Question 1.

Question 11 - Hedges of group items: eligibility of a group of items as the hedged item

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 with the proposal for the reasons exposed in our response to Question 1.

We also agree that it should not be allowed to apply cash flow hedge accounting of net positions when risks being hedged affect profit or loss in different reporting periods. Otherwise there would be a distortion of the information provided in the financial statements of those reporting periods.

Question 12 – Hedges of group items: presentation

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 (e.g. 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?

Yes, we agree with the proposals, because if all the affected line items in the income statements were adjusted, the result would be the recognition of gross gains or losses that have not been incurred.

Question 13 - Disclosures

- (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?

In general, we agree with the proposed disclosures. Specifically, we feel that even though IFRS 7 includes an adequate set of disclosures about hedging instruments, there is no set of detailed disclosures about hedged items. In this regard, and although every disclosure being proposed should be analysed on a cost/benefit basis, we think the disclosures proposed represent an improvement from IFRS 7 current requirements.

However we consider that proposed disclosures should apply prospectively, that is, not for transactions made before the effective date. In this regard, we would like to point out that certain hedge accounting requirements in IAS 39 are quite different from the ones included

in the exposure draft (for example, effectiveness tests or discontinuation requirements). From our point of view, to provide disclosures on discontinuation of hedge accounting relationships conducted under the criteria of the current IAS 39 would not be comparable with the information on discontinuation of hedge accounting carried out with the proposed criteria to be included in the new standard (IFRS 9).

Question 14 - Accounting for a contract for a non-financial item that can be settled net in cash as a derivative

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?

The proposal would help to mitigate the distortion of certain information that is currently presented in profit or loss as a consequence of the application of IAS 39 accounting requirements.

Additionally, we think it should be clarified what "fair value-based risk management strategy" means. It would be helpful to clarify this concept, for example, by defining which type of operations are supposed to meet that definition.

Question 16 – Effective Date and Transition

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

Yes, we support the prospective application of the proposals and also the possibility of applying the new requirements before their effective date. However, and as stated in our response to Question 13, for these cases in which there would be a difference between the current IAS 39 requirements and the proposed IFRS 9 criteria, we would like to point out that we think that proposed disclosures should be applied only for transactions entered into on or after the IFRS 9 effective date.