



**AUTORITÉ DES NORMES COMPTABLES**  
**5, PLACE DES VINS DE FRANCE**  
**75573 PARIS CÉDEX 12**

**Phone 33 1 53 44 28 53**

**Internet <http://www.autoritecomptable.fr/>**

**Mel [jerome.haas@anc.gouv.fr](mailto:jerome.haas@anc.gouv.fr)**

**Chairman**

**JH**

**n°145**

Paris, the 11<sup>th</sup> december 2012

**Monsieur Hans HOOGERVORST**  
**Chairman**  
**IASB**

**30 Cannon Street**  
**LONDON EC4M 6XH**  
**UNITED KINGDOM**

**Re: IASB Review Draft IFRS 9 - Chapter 6 - Hedge accounting**

Dear Mr Hoogervorst,

I am writing on behalf of the Autorité des Normes Comptables (ANC) to express our views on the Review Draft (RD) of the phase III of IFRS 9 related to hedge accounting released by the IASB in September 2012.

The ANC welcomes the improvements made to hedge accounting requirements which will be better aligned with risk management.

We wish to draw your attention to the following critical issues, which are further developed in the Appendix:

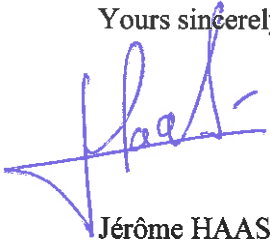
- Hedge of credit risk
- Hedge of sub-libor cash flows
- Hedge of commodity risk of cash flows on a net basis

Furthermore, we consider that it is necessary to specify that all macro-hedging transactions, including both macro-fair value hedge and macro-cash flow hedge transactions, may still apply current IAS 39 requirements.

All our detailed comments have been included in the Appendix attached to this letter.

We hope you find these comments useful and would be pleased to provide any further information you might require.

Yours sincerely,



Jérôme HAAS

## Appendix

The ANC welcomes the improvements made to the Exposure draft (which already aligned more closely hedge accounting with risk management) on the following topics:

- The extension of eligible hedged items to equity instruments measured at fair value through OCI;
- The possibility to designate not contractually specified inflation risk as an eligible risk component for financial instruments, under certain circumstances;
- The removal of the restrictions regarding cash flow hedge (CFH) of a net position (for foreign currency risk);
- The possibility to amortise the forward element of forward contracts in a fair value hedge relationship;
- The retention of the current presentation rules in the fair value hedge;
- The removal of the proposed new accounting mechanism for fair value hedges based on a two-step approach (OCI and transfer in profit or loss) and new presentation rules in the statement of financial position.

However, the review draft still raises the following major issues that the IASB should address:

- **Hedging of credit risk:** the alternative to hedge accounting allowed by the Board is not satisfactory since it is based on the fair value option which implies to recognise all changes in fair value in profit or loss, including components that may not be hedged by the entity, such as the interest rate risk. Moreover, the pre-requisites for being able to resort to the Fair Value Option on credit risk are too restrictive (for instance, banks do not use only single-name, credit default swaps (CDS) in practice to hedge their credit risks).

Moreover, asserting (BC6.382) that credit risk is not an eligible hedged component (i.e. separately identifiable and reliably measurable) in a hedge relationship is consistent neither with risk management activities (compliant with regulatory requirements) nor with IFRS 9 itself (par. 6.4.1.(c) (ii)) which requires, in order to meet the qualifying effectiveness criterion, to assess whether credit risk “*dominates*” the changes in fair value (thus implicitly requires a specific measurement). We also note that IFRS 13 on fair value measurement refers to credit adjustment (par. 48-52).

Therefore, we consider that hedge accounting must be eligible for credit derivatives hedging the credit risk component of financial instruments (see also our detailed comments in the letter on the ED *Hedge accounting*).

- **Sub-libor issue:** the prohibition from designating a risk component that exceeds the total cash flows of the hedged item is not consistent with well established risk management practices, both for financial (e.g. highly-rated sovereign bonds held) and non-financial hedged items (e.g. commodities markets that trade at a benchmark minus a spread). Moreover, the RD should clarify that this rule would not be applied for macro-hedges (when this phase will be added to IFRS 9) as it directly contradicts risk management principles that underlie macro-hedge accounting.
- **CFH on a net basis:** we welcome the Board’s decision to relax the proposed restrictions regarding CFH of net positions over different periods but disagree with limiting the eligibility

of such group of items to hedge of foreign currency risk. This restriction is rule-based and not consistent with risk management activities of many entities exposed to commodity risk for instance. The fact that “foreign currency risk was the risk most commented on by respondents” (BC6.332) seems a weak argument to explain the Board’s decision. If the Board maintained this restriction, we would recommend that the Board clarifies that the designation, for accounting purposes, of a hedged relationship on a gross basis is still available under IFRS 9 when risk management activities (such as hedging commodity cash flows risks on a net basis) does not fit with the new hedge accounting framework.

- **Implementation guidance:** the section F “Hedging” of the IAS 39 implementation guidances (IG) will be fully deleted by IFRS 9 although some IGs may be still relevant under IFRS 9 or need a slight update. Those IGs are very useful in practice (e.g. partial term hedge; “all in one” hedge,...) and we recommend that the Board releases updated guidance in the time between the publication of IFRS 9 phase III and its mandatory date of application.
- **Intragroup monetary items as hedging instruments against foreign exchange risk:** BC6.60 states that “*in the Board’s view, considering intragroup monetary items for eligibility as hedging instruments would require a review of the requirements in IAS 21 at the same time as considering any hedge accounting requirements. [...] Hence, it decided that it should not address this issue as part of its project on hedge accounting.*” This statement is not satisfactory since there is no rationale to prevent intragroup monetary items for which translation gains or losses impact the consolidated statement of profit or loss from being designated as hedging instruments. Therefore, we consider that the Board should address this issue as soon as possible (for instance in the time between the publication of IFRS 9 phase III and its mandatory date of application) and if necessary amend IAS 21.
- **Hedge of risks that do not impact the P&L:** while we welcome the extension of eligible hedged items to equity instruments at FV through OCI, we do not understand why IFRS 9 is still prohibiting hedge accounting for other risk exposures that do not impact the P&L, such as a forecast transaction to purchase or sell a non-controlling interest, which impacts net equity.
- **Aligned time value vs actual time value of options:** while we fully support the new accounting treatment of the time value of options (as a cost of the hedge), the detailed treatment seems operationally complex (dual pricing process, different treatments depending on whether the actual time value is higher or lower than the aligned time value,..) and should be simplified.

In addition, the review draft raises the following fatal flaws:

- **Hedge of open portfolios (or macro hedges):** we welcome the retention of IAS 39 requirements for fair value hedges of the interest rate exposure of a portfolio of financial assets or liabilities (“macro-FVH”). However,
  - We ask the Board to clarify in par. 6.1.3 that all IAS 39 requirements on hedge accounting will be maintained for macro-FVH and that entities will not be allowed to apply only paragraphs 81A, 89A and AG114-132 of IAS 39 as some may interpret. For instance, we note that AG99C (which was impacted by the European carve-out) is not listed in par. 6.1.3. This may be seen by some as an impediment to macro-FVH;
  - We do not have a clear understanding of the concept of open portfolio which is scoped out from the general hedge accounting requirements stated in the review draft as per IN8c) and BC6.9-6.12. However, according to par. 6.1.3. only macro-FVH as defined above is scoped out of the review draft. Consequently, we understand that hedge accounting of an open portfolio of future cash flows (“macro-CFH”) is within the scope of the review draft although the Implementation guidance on macro-CFH (see IAS 39 IG F.6.1, F.6.2 and F.6.3.) is not carried forward in IFRS 9.

However, we consider that both macro-FVH and macro-CFH must be addressed through the specific project that is still in progress. As explained in IAS 39 IG F.6.2. (a), “*in economic terms, it does not matter whether the derivative instrument is regarded as a fair value hedge or as a cash flow hedge. Under either perspective of the exposure, the derivative has the same economic effect of reducing the net exposure*”. In other words, Macro-hedge strategies, whether designated as FVH or CFH, are both managed in the same way by the risk management (at a level that aggregates open portfolios) and should follow the same hedge accounting framework. Consequently, they should both be scoped out from the general hedge accounting model, waiting for the macro-hedging separate standard.

- **Hypothetical derivatives:** we welcome the reference to a “hypothetical derivative” as a possible way of measurement of hedge ineffectiveness, i.e. “*to calculate the change in the value of the hedged item an entity may use a derivative that would have terms that match the critical terms of the hedged item*” (B6.5.5). However, the last sentence which prevents from imputing “*a charge for exchanging different currencies for a cross-currency interest rate swap*” in the hypothetical derivative is not consistent with valuation methodologies. The concept of “hypothetical derivative” should refer to a derivative contract that it exists or could exist on capital markets providing it matches the critical terms of the hedged item. It does not seem economically sound to prohibit the incorporation of key valuation inputs from the modelling. For instance, the basis spread for a cross-currency interest rate swap is a marked pricing component that should be imputed in the hypothetical derivative. In order to avoid unintended consequences or over-interpretation, we recommend that the Board removes this example from the application guidance B.6.5.5.
- **Hedging FX risk with a non-derivative instrument:** according to par. 6.2.4. (c), for a hedge of FX risk, the foreign currency component of a non-derivative financial asset or liability may be designated as a hedging instrument provided that it is not an investment in an equity instrument at fair value through OCI. However, par. 6.2.2. provides that a non-derivative financial asset or liability at fair value through profit or loss may be designated as a hedging instrument, (with an exception for financial liabilities). Therefore, it is not clear from the wording whether a non-derivative asset or liability at amortised cost denominated in a foreign currency may be eligible as a hedging instrument. The current provisions under IAS 39 would qualify such instrument as a hedging instrument. We consider that par. 6.2.2. should be redrafted to remove this inconsistency.

Moreover we consider that the Board should review *in fine* the consistency of these hedge accounting requirements with those of the future standard on insurance contracts in the light of the necessity to reflect appropriately the economic model of insurers in the financial statements. In addition, we still believe that IFRS 9 and IFRS 4 phase 2 should be applied at the same date; however would IFRS 9 be mandatory in 2015 and IFRS 4 later, insurers should be able to revisit the accounting choices made while applying IFRS 9 for the first time when implementing later IFRS 4 phase 2 standard.