



Spanish Banking Association

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Subject: *Exposure Draft Hedge Accounting*

Dear Madam,

The AEB¹ welcomes the opportunity to comment you on the proposals set out in the Exposure Draft on “Hedge Accounting” the efforts of the IASB to undertake a review and replacement of IAS 39 with the aim of simplifying the accounting for financial instruments.

In this sense, we are pleased with the steps taken by the IASB in terms of more flexibility, nevertheless we would like to stress some points relevant for the Spanish Banks we represent. Those points are as follows:

- We notice also that the proposed standard prohibits hedging for equity investments designated at fair value through other comprehensive income. From a risk management perspective, nothing precludes an institution to hedge such investment. So, this accounting prohibition conflicts obviously with the stated objective for hedge accounting. That means that the general objective designated from hedge accounting, to translate adequately in financial statements the risk management strategy of entity is not the basic principle supporting the whole text. BC 23 to BC 26 highlight some technicalities arisen from the decision not to recycle in P& L, the realized value of such investments, but in our view, they are not convincing to justify the de facto prohibition of hedging those securities. Furthermore, as BC 27 pinpoints that a forecast dividend from such investments

¹ The Spanish Banking Association (AEB) is the voice of the Spanish banking sector representing and defending the collective interests of banks operating in Spain (94 member banks: 59 Spanish and 35 credit entities' branches of foreign banks operating in Spain), with total consolidated assets of € 2,110 billion as of December 2010 and 109,996 employees in Spain.



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could be an eligible hedged item, it is illogical to preclude from this status, the sum of the discounted forecast dividend, which is the recorded fair value of these securities.

- Many entities have subsidiaries in foreign countries whose operations are performed in a functional currency which differs from the parent company's functional currency. Regarding profit and loss, the annual results in local currencies of these entities are translated to the consolidated profit and loss account using the average exchange rate of the period (this is for practical reasons. However, if exchange rates fluctuate significantly the exchange rate of each transaction should be used).

Then, the variability of the exchange rate of the local currency in respect to the functional currency of the parent company, give rise to a foreign exchange risk exposure in the consolidate financial statements, and entities want to hedge this risk, sometimes 2-3 years ahead.

According to paragraph 14, if a hedged item is a forecast transaction, that transaction must be highly probable. From our point of view, a portion of predicted revenues, normally those expected in the short term, will meet the "high probable" criterion. Additionally, 2-3 years forecast results in a retail banking business which is very stable and forecast results are based on historical information, could be also predictable with a high probable criterio. This hedging relationship will have to meet all the hedge effectiveness requirements according to paragraphs B27-B39.

Finally, we want to point out that the current uncertainty in the other areas of financial instrument accounting and the interaction of the different consultations (e.g. financial statements presentation, derecognition, consolidation) makes it difficult to provide final comments. Therefore the views expressed in this letter may be subject to change as a more complete picture emerges on all of financial instrument accounting.

Best regards,