

Brussels, 24 February 2011

Dear Sir/Madam,

Dexia (www.dexia.com) is a European bank, with 35,234 members of staff and core shareholders' equity of EUR 18.5 billion as at 31 December 2009. The Dexia Group focuses on Retail and Commercial Banking in Europe, mainly Belgium, Luxembourg and Turkey and on Public and Wholesale Banking, providing local public finance operators with comprehensive banking and financial solutions. Asset Management and Services provides asset management, investor and insurance services, in particular to the clients of the other two business lines. The different business lines interact constantly in order to serve clients better and to support the Group's commercial activity.

We welcome the opportunity to comment on the IASB's Exposure Draft Hedge Accounting.

Dexia's comments formulated in this letter are in a certain way tentative because the accounting principles to be applied on an open portfolio are not yet determined. In practice, risk components are mainly monitored based on open portfolios. We hope that the accounting principles for such portfolios will make it possible to reflect the risk management approach in the financial reporting as well. If that would be impossible, we will be obliged to apply hedge accounting either on individual items or via closed portfolios in order to reduce volatility in the statement of income but therefore we should first change our risk management approach. This is just the opposite of what is laid down by the exposure draft – an unhealthy situation.

In general, Dexia supports the IASB's direction taken in which hedge accounting in the financial reporting reflects the risk management strategy. This approach not only improves and increases the quality of information in the financial reporting but is also consistent with the business model approach in IFRS 9 Financial Instruments – classification and measurement. Dexia also welcomes a number of improvements which makes the application of hedge accounting less complex and will make hedge accounting more accessible. However, the comments made in this comment letter are tentative. Final decisions could only be made once all elements of the replacement project IAS 39 are known.

The exposure draft still contains a number of restrictions which makes that the risk management approach will not be reflected in the financial reporting or makes the application of hedge accounting still complex.

Examples are the following:

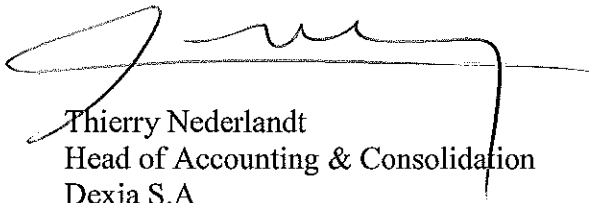
- the issue on hedging a libor on sub-libor financial instruments is not solved,
- Credit Default Swaps are excluded to be designated as hedging instruments to hedge credit risk ,
- financial instruments in which pre-payment option is embedded for which value depends on hedged risk are excluded as designated hedged items if an entity uses the layer approach,
- internal derivatives are still excluded for designation as hedging instruments which conflict with 'one window to the market'-principle applied by many financial institutions
- inflation risk embedded in financial instrument is eligible only if contractually defined,
- core deposits are still excluded to be eligible for hedged item,
- in case of a close portfolio, entity should still be able to track all underlying items.

The IASB did not explore some alternatives -or even rejected alternatives- based on defective reasoning (add complexity, would be a significant expansion of the scope, could significantly delay the project ...). Dexia believes these arguments used do not match with the objective as described in paragraph 2 of the IFRS Foundation Constitution. In addition, this is not in line with G-20 call to have a single set of high quality improved global accounting standards. In that respect, we believe that quality of the standard overrules timing.


Finally, we would like to draw your attention that the questions raised on which input is sought do not always deal with the real issues.

If you wish to discuss our comments further, please do not hesitate to contact Nico Deprez, Head of Accounting Policy Department of Dexia S.A..

Yours sincerely,



Thierry Nederlandt
Head of Accounting & Consolidation
Dexia S.A



Claude Piret
Chief Risk Officer
Dexia S.A.

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?

1. Dexia agrees that hedge accounting should not be mandatory but based on a voluntary designation even if risks are hedged by a Risk Management strategy. The main reasons are:
 - a. risk can be mitigated via offsetting positions rather than via derivatives.
 - b. despite IASB's objective to reflect Risk Management activities in an entity's financial reporting, the exposure draft still includes restrictions (for example designating core deposits as hedged items, CDS as hedging instruments, sub-libor as hedged risk, ...) that makes it impossible to translate all these strategies into hedge relationships;
 - c. from an operational point of view, it would be difficult to document all hedge relationships set up under a risk management strategy ;
2. Dexia supports the proposed objective whereby financial reporting should reflect the way an entity manages its risks. This will result in a transparent and consistent reporting which will help users to gain a better insight in the risk strategy and the performance of managing risks. Although restrictions currently included in IAS 39 are deleted, we are not convinced that the exposure draft will meet the objective mainly due to important restrictions such as: prohibition of designating internal derivatives as hedging instruments, sub-libor issue not yet solved, financial instruments with prepayment options are excluded, credit risk which is not eligible, risks relating to embedded derivatives...
3. We do not agree that only risks affecting profit or loss should be eligible for hedge accounting. We do not see any conceptual reason why for instance equity instruments measured at fair value through Other Comprehensive Income should be excluded. The arguments (adding complexity – adding another exception) put forward in BC 26 are weak. If the IASB's intention was to exclude such a hedge relationship, the consequence of the current text is that other items are excluded as well such as interest rate risk in pension obligation.

Question 2 – Do you agree that a non-derivative financial asset and 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?

4. Before answering the question whether we agree that a non-derivative financial asset/liability measured at fair value through profit or loss should be eligible hedging instruments, there must be an agreement on the classification and measurement of these financial instruments. It

is IFRS 9 financial instruments Classification and Measurement which describes the underlying accounting policies. As stated in its comment letter, Dexia believes that the IASB did not draw the line between fair value and amortised cost on the right place.

5. We do not agree with IASB's argumentation (a significant expansion of scope, significant delay of the project) to prohibit non-derivative financial instruments to be eligible for designation as hedging instruments for risk components other than foreign currency risk. If the IASB respects its Foundation Constitution and is willing to achieve the G-20 requirements, it should in the first place properly explore the alternative and secondly reject or agree based on good arguments. Dexia believes that quality overweighs timing.
6. However, if by allowing non-derivative financial instruments measured at fair value through profit or loss as eligible hedging instruments the objective could be reached, then Dexia supports such an extension.
7. We expressed our disagreement via a comment letter to the IASB's exposure draft Classification and Measurement about IASB's intention to replace for financial assets with an embedded derivative the 'closely/non-closely'-concept under IAS 39 by a new concept of cash flow characteristic. That decision did not reduce complexity but is just counterproductive as a new concept has to be launched next to the existing principles on embedded derivatives as these are still applicable for financial liabilities. On top of that, there is an accounting asymmetry for similar financial instruments depending on whether these are assets or liabilities. Now, this issue pops up in Phase III of IASB's replacement project. From a risk management perspective, risks attached to such hybrid instruments are managed as follows – if entire instrument is not classified into 'fair value through P&L': first the embedded derivative is bifurcated and risks are hedged via external derivatives (in most cases this is a perfect hedge in so far that a qualitative assessment is the most appropriate hedge effectiveness tests), secondly the interest rate attached to the host contract is designated as hedged item in a portfolio of similar financial instruments. Normally, credit risk is borne by Dexia. IFRS 9 in combination with this exposure draft will make it impossible to properly reflect in Dexia's financial reporting how risks are managed. First of all the entire financial asset will be measured at fair value because the criteria of cash flow characteristics, allowing an amortised cost measurement, are not met (despite the business model is one of collecting the contractual cash flows). Secondly, the exposure draft does not allow splitting embedded derivative and hosting contract for hedge accounting purposes. The reason is explained in BC33: '... such an approach would be a significant expansion of the scope of the hedge accounting project... and could significantly delay the project.' We believe that in both cases the IASB did not respect its objective of reflecting in the financial reporting the way risks are managed just because the IASB used arguments such as reducing complexity, expansion of scope and delaying the project. This is a missed opportunity to improve the quality of standard setting.
8. In BC 42, the IASB argues that the eligibility of internal derivatives as hedging instruments is not the root cause of misalignment between risk management and hedge accounting. Dexia believes the non-eligibility is one of major root cause why hedge accounting does not reflect

the way risks are managed. On the contrary, this principle leads to an artificial link between external derivatives and hedged items just to succeed in managing volatility in profit and loss. However, we do agree with the IASB that mitigation or transformation of risk is only relevant if it results in a transfer of risk to a party outside the reporting entity. In practice, the desk responsible to transfer internal risk externally will not be allowed to take risk positions. Therefore a situation as described in BC 44 is impossible because pervasive controls are put in place to assure there is an almost perfect risk offsetting between internal and external derivatives. The offsetting results are closely monitored by management.

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?

9. In practice, Dexia's Risk Management Department monitors synthetic risks stemming from a non-derivative and a derivative. These risks are then hedged via other derivatives. Unfortunately, IAS 39 did not allow Dexia to report such hedging activities in its financial statements. Therefore, Dexia agrees with the decision to permit the designation of a synthetic exposure as hedged item. We believe that eliminating such a restriction will facilitate the application of hedge accounting and is line with the objective - reflecting risk management practice in financial reporting.
10. Given the importance of the issue, Dexia believes that paragraph 15 together with B9 will probably not provide sufficient guidance which could lead to unnecessarily and unavoidable discussions between preparers and auditors. An illustrative example: an entity invested in a long-term fixed-rated bond for which Risk Management concludes a first swap converting the fixed-rate into a 3-month Euribor. For one reason or another, the entity decides to conclude an additional swap converting the 3-month Euribor against OIS. It is unclear whether an entity can combine the bond and the first swap and consider these two elements as an aggregate exposure.

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?

11. Dexia supports the decision that irrespective the nature of the hedged item (financial instrument or a non-financial instrument) the cash flows or fair values of an item attributable

to a specific risk can be hedged. We also agree that the risk component must be separately identifiable and reliably measurable.

12. However, we do not agree with B18 in which it is stated that inflation is not separately identifiable and reliably measurable except if that risk component is contractually specified. Such a statement is a deviation from IASB's objective to publish principle-based accounting principles. In addition, BC 18 refers only to inflation as a risk component of a financial instrument. Does that mean that an inflation risk component attached to a non-financial instruments could be considered as reliably measurable and separately identifiable ? Finally we do not agree that a difference should be made in inflation risk which is explicitly or implicitly specified. An example could be a pension liability: although inflation rate is not always explicitly mentioned in the contract, the risk component does fulfil the conditions to be eligible as hedging risk as in the actuarial calculation a specific inflation rate is used. Another example is the "livret A", one of the largest saving product in France, which has a contractual return in compliance with French legislation and is based on the variation of Euribor and French Consumer Product Inflation rate. The contract as such does not refer to the inflation rate and is thus strictly spoken not contractually specified.

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?

13. Dexia welcomes the introduction of a layer approach because this is in line with risk management practice and so it will contribute in realising the objective of reflecting that strategy into the financial reporting.

14. In BC 68, the IASB stated: “ ...If the designation of the component of a nominal amount is not aligned with the risk management strategy of the entity, it might result in profit or loss providing misleading or less useful information to users of financial statements.” Dexia fully agrees with that position and therefore regrets that restrictions formulated in the Exposure Draft results in the opposite of what the IASB said in BC 68.

15. A first restriction deals with the exclusion of financial instruments in which prepayment options are embedded for which the fair value depends on changes in the hedged risk. IASB argues in BC 69 ‘...a layer approach would be tantamount to identify a risk component that

was not separately identifiable (because the change in the value of the prepayment option owing to the hedged risk would not be part of how hedge effectiveness would be measured)'. In practice, risk management uses the difference between the net position and the under hedged position to cover prepayment, restructuring ... This rule-based principle also conflicts with B33: "This (draft) IFRS does not specify a method for assessing whether a hedging relationship meets the hedge effectiveness requirements, including determining the hedge ratio. However, an entity shall use a method that captures the relevant characteristics of the hedging relationship including the sources of hedge ineffectiveness..."

16. In addition, Dexia does not see why these are excluded for applying a layer approach while for all other situations (such as micro hedging or hedging a percentage of the nominal) this is not the case.
17. The second restriction remains unsolved: how to hedge the interest rate on sub-libor rated financial liabilities. In practice, risk management strategy includes these types of financial liabilities to determine a net position. We refer to examples developed by some banking federations on how financial institutes manage the interest rate risk relating to such sub-libor financial liabilities.

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?

18. Removing the 80-125% bright line together with the elimination of the retrospective effectiveness test are significant steps in abolishing the restrictive hedge accounting requirements under IAS 39. This decision regarding hedge effectiveness test will probably contribute to align hedge accounting closer with risk management activities but is on itself not sufficient.
19. Dexia agrees with BC 38 in which it is stated: "An entity's risk management is the main source of information to perform the assessment whether a hedging relationship meets the hedge effectiveness requirements". This means management information (or analysis) used for decision-making purposes can be used as a basis to assess whether a hedging relationship meets the hedge effectiveness requirements. In practice, risk management assesses the effectiveness of a hedge transaction next to qualitative hedge effectiveness tests also for instance via sensitivity analysis and P&L time series impact analysis. As long as the results fall between predefined levels, the transaction is considered as being effective. Unfortunately, such an effectiveness test is not sufficient for financial reporting. Therefore, an entity will have to apply a test like a dollar-offset test in order to determine the amount of (in)effectiveness. In other words, a hedge transaction considered by risk management as efficient can probably not reported as such in the financial statements. The IASB missed an

opportunity to align financial reporting with risk management activity and as a consequence departs from its objective. Therefore, the IASB should review the effectiveness principles as written down in this Exposure Draft.

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?

- 20. Dexia believes that allowing a rebalancing of the hedge ratio is fully in line with the objective set by the IASB – reflecting the risk management hedging strategy into an entity's financial reporting. We are convinced that a rebalancing will not only respect the objective but will make the application of hedge accounting easier compared to IAS 39 - whereby the principle is that first the existing hedge relationship is discontinued and then a new relationship could be established with same hedging instruments or hedged items. In practice this caused many operational problems especially because the fair value of the hedged items/hedging instruments were not equal to zero. Consequently, entities were almost forced to use hypothetical derivatives in order to be capable to determine the amount of hedge (in) effectiveness.
- 21. However, we do not agree that in case risk management changes its risk policy accounting should automatically follow by rebalancing the hedge ratio. In our view, an entity should have the choice to rebalance or to discontinue hedge accounting. Under certain circumstances an obligation to rebalance together with a prohibition to discontinue the hedge relationship could lead to an unacceptable level of administration costs. This is certainly the case when risk management actively and largely apply dynamic hedges. In addition, Dexia believes that such an accounting principle is in contradiction with the general principle – at inception an entity has the choice to apply hedge accounting but is not obliged to do so even if there is from a risk management perspective a hedge relationship.
- 22. In addition, such a deviation will lead to many discussions between preparers and auditors. In some cases, there is only a very tiny boarder line between overhauling existing hedge relationship and an important rebalancing. From an accounting perspective the conclusion will lead to a significant difference in financial reporting as the former will lead to a discontinuing while the latter will result in a rebalancing.
- 23. We do not agree with the example the IASB brought forward in BC108. Take a real case example whereby a company with a functional currency EUR attracts USD fixed rated

financing sources and invests in YEN floating bonds. Assume that all other parameters are exactly the same. From a risk management perspective, an entity will hedge all risk by concluding a CCIRS switching floating rated yen cash flows into fix rated USD flows. This perfect hedge could not be reflected in the financial statements because the entity is obliged to hedge against the functional currency, the EUR. Consequently, the basis risk YEN/ EUR plus EUR/USD will not equal to the basis risk YEN/USD. Risk management will consider that all risks are hedged on an effective way and so will not adjust its hedge ratio. But, from an accounting perspective we could face ineffectiveness due to differences in basis risk which can become so important that it can no longer be concluded that the relationship produce biased results.

24. We do agree that proactively rebalancing a hedge relationship should be allowed.

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?

25. Dexia agrees that an entity should discontinue hedge accounting when the criteria are no longer met. However, as stated in our answer to question 7, we believe that discontinuing should also be permitted in cases where the risk management strategy rebalances the hedge ratio and that for the following reasons:

- a. we do not see any conceptual reason why it should be prohibited;
- b. reduces significant degree of judgement –whether a change in hedge ratio should be considered as overhaul or rather as a rebalance;
- c. eliminates operational constraints;
- d. prohibition could lead to a negative cost/benefit balance.

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?

26. In our view, the arguments used to support IASB's initial view to eliminate the fair value hedge model and allow only a cash flow hedge model (and which are stated in BC 119) are not correct. Dexia believes the IASB took the only right decision to abandon its initial idea. We think the arguments in BC 120 justify the decision.

27. Although we agree to continue with a fair value hedge model, we can not support the presentation requirement via Other Comprehensive Income as proposed by the exposure draft. The main reason is that we do not see any added value as this is not a simplification of the accounting principles nor it will increase the usefulness of the information reported. On the contrary, for preparers this two-step approach will create operational complexity as current methodology has to be abandoned and the new accounting treatment should be developed in several IT systems. On top of that, such a two-step approach will not help users in providing a better insight in the effectiveness of the reporting entity's risk management strategy. The amounts reported in Other Comprehensive will represent:

- a. several types of hedge accounting - cash flow hedge, fair value hedge, net investment);
- b. different hedged items - financial instruments, non-financial items, non-recognised firm commitments, forecasted transactions, ...
- c. different hedging strategies - single hedged item, a closed portfolio, an open portfolio, ...
- d. different hedged risks.

We are therefore convinced that relevant and detailed information about hedging, hedging strategy and effectiveness of these strategies should be reported in disclosures rather than via a line on the balance sheet.

28. In principle, presenting the gain or loss on a hedged item attributable to the hedged risk on a separate line item could indeed increase the information. However, there is a potential risk that this objective (increasing the information) will no longer be met especially when an

entity applies several types of hedge accounting in combination with different strategies and underlying items. Such a situation will result in a considerable increase of line items on the balance sheet. Next to that, it is questionable whether the reported amount will provide useful information for the users because the amount can consist of so many different things. Finally, the presentation can add complexity for preparers (eg how will the hedging results from a portfolio be allocated to the underlying items).

29. We suggest the IASB to consider allowing one single line item on the balance sheet which represents the aggregate net amount of all fair value adjustments. Such a presentation together with an appropriate level of disclosures can overcome issues of complexity and reducing the usefulness.
30. The question whether a linked presentation should be allowed for financial instruments designated as hedged item/hedging instrument depends also on the how the IASB defines the unit of account. We are convinced that in certain situations a linked presentation would be helpful for users to better understand economic transactions. A real case example: Dexia sometimes enters into a financial package whereby a financial asset, a financial liability are concluded together with derivatives to hedge all risks. The result is a residual margin earned over the maturity of the package. Due to accounting constraints laid down by IAS 39, Dexia is not allowed to present such type of transaction as one single package. On top of that, although from a risk management perspective all risks are perfectly hedged, hedge accounting is difficult to apply. In order to properly reflect such type of transactions, we are convinced that a linked presentation would make sense. We recommend the IASB to carefully take into consideration this issue.

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?

31. Within Dexia, option and forward derivatives are used in only limited hedge transactions. Currently, changes in time value are recognised in Profit and Loss in order to respect the hedge criteria regarding effectiveness. We welcome the new proposal as long as it does not become an obligation simply because the proposed accounting treatment could be, from an operational point of view, more complex than under the existing principles.

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?

32. The IASB will only be able to achieve its objective (to reflect risk management hedging strategies in the financial reporting) when it develops an accounting framework for open portfolios. The framework should avoid any restrictions which make the achievement of the objective impossible. Some examples of such restrictions are the following:
- a. excluding financial instruments with prepayment options for which the price depends on the hedged risk;
 - b. requiring to specify each underlying hedged item iso an net position;
 - c. in case of a net position the requirement to identify the gross amounts;
 - d. excluding core deposits as hedged items;
 - e. sub-libor issue should be solved.
33. We believe once the IASB developed an accounting model for hedging open portfolios it should reconsider the accounting principles for closed portfolios described in this exposure draft. As long as we don't have an idea nor an understanding of IASB's direction it will take with respect to hedging open portfolios, our comments on this exposure draft should be considered as tentative.
34. Regarding cash flow hedges, Dexia believes the general underlying ideas and principles of IAS 39 Implementation Guidance F.6.2 and F.6.3 should form the basis of the accounting model.

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 instruments 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?

35. We believe that a general presentation principle should be developed stating that all effects of hedge accounting for a group of items are presented in one single line in both the balance sheet and the income statement. Additional disclosures could then provide detailed and

relevant information allowing users to have a better view on Risk Management Strategy's effectiveness in reducing the risks.

36. In that perspective, we are in favour of IASB's proposal to present in the income statement the hedging results on one single line but disagree with IASB's proposal requiring presenting on a separate line the fair value adjustment relating to each individual asset/liability which is part of the portfolio. In particular, it will be difficult to deal with net positions with this proposal.

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?

37. Dexia shares IASB's view on the function of disclosures: it should help users to understand the overall risk management strategies, providing insight in the effectiveness of these strategies in reducing risks but should also explain the effect of these strategies on the reporting entity's balance sheet and income statement.

38. Finding the right balance in disclosing information is a first important thing. The requirements should be written as such that it avoids a 'ticking the box' situation. In other words, if an entity has a lot of different hedging strategies the disclosures should deal with the main strategies having a significant influence on the entity's financial reporting rather than trying to be as complete as possible.

39. Consistency in the disclosures is another area. The disclosures proposed in this exposure draft regarding movements in Other Comprehensive Income should be compared with IAS 1 reporting requirements. A same exercise can be done for IFRS 7 disclosures. We support any efforts undertaken by the IASB in screening all disclosure requirements in order to achieve as much as possible consistency.

40. Dexia has to fulfil also the reporting requirements laid down by prudential regulators. The more prudential and financial information is made uniform the less unnecessary costs are incurred. Uniform disclosures will also help users because too much information or information reported in another way can kill the message.

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?

41. Such types of hedging strategies are not relevant for Dexia. However, we believe that the accounting treatment proposed will solve a practical issue.

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?
42. As already said in our previous answers, Dexia agrees with the direction of the proposed objective to reflect the entity's risk management activities in the financial reporting. We also support IASB's intention to replace the current rule-based IAS 39 by a principle-based standard.
43. In BC 219, the IASB summarised well the actual situation for financial institutions. It is correct that under some risk management strategies credit default swaps are concluded to hedge the credit risk attached a particular exposure. However, Dexia disagrees with IASB's position taken in BC 220 whereby hedge accounting of credit risk via CDSs is prohibited simply because it is difficult to isolate and measure the credit risk component- and that for the following reasons:
- a. such a prohibition is in contradiction with IASB's objective to reflect risk management strategy into the financial statements;
 - b. this makes the exposure draft rule-based rather instead of principle-based;
 - c. credit default swaps is a generic term covering contracts with different contractual features;
 - d. the IASB does not provide preparers with any valid alternative to manage the volatility of the income statement.
44. We recognise that isolating and measuring credit risk of a financial item could be much more difficult compared to other risks but this could be overcome. The arguments summed up in BC 221 indeed lead to differences between credit default swap and credit risk of a financial instrument. However, there is a correlation between both, reflecting in the way, whereby risk management deals with the assessment of the hedge.
45. We do not see why the IASB accepts hedge accounting of a foreign currency via another pegged currency while it forbids a similar situation for credit risks via credit default swaps.

46. In IFRS 7 Appendix B B4 the IASB describes how credit risk relating to a financial liability could be determined. Why does the IASB not propose to use a similar approach for situations where credit risk is hedged via a CDS ?
47. In B33 the IASB states: "This (draft) IFRS does not specify a method for assessing whether a hedging relationship meets the hedge effectiveness requirements, including determining the hedge ratio. However, an entity shall use a method that captures the relevant characteristics of the hedging relationship including the sources of hedge ineffectiveness..." Relating to CDS, the IASB is not consistent as it decides (instead of the preparers) that an entity will be unable to assess the hedge effectiveness.
48. Finally, we believe that this discussion could also be linked with the sub-libor issue. In fact, when an entity concludes a CDS to hedge the credit risk attached to a financial statement, the main objective is to hedge the variability in credit risk.

Question 16 – Do you agree with the proposed transition requirements? Why or why not? If not, what changes do you recommend and why?

49. As already explained in our Comment Letter on IASB's Request for Views, Dexia supports an effective date of 1 January 2015 for IFRS 9.
50. Although Dexia recognised that a full retrospective application probably enhances comparability between financial statements, we are convinced that for hedge accounting the IASB should allow a prospective application for operational reasons as well as to avoid too much hindsight.