Exposure Draft Hedge Accounting

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?

We agree with EFRAG's position on this matter. We believe that hedge accounting should not be restricted to risks that affect profit or loss and entities should be able to use hedge accounting in order to better reflect how the entity manage the risks that the entity is exposed to. Taking this in consideration, the entity should give information, regardless if hedge accounting is used, about the risks that entity is exposed to. This information is important to investor`s knowledge about the risks that the investment is directly or indirectly exposed and how the entity manages that exposures.
Additionally we believe that it is urgent, also to this matter, that IASB should define what can be understood as performance of an entity, because, we believe that at least, hedge accounting could be used in order to eliminate or reduce the risks that affects the performance of the entity and not only the profit or loss.

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?

We agree that non-derivative financial asset and non-derivative financial liability measured at fair value through profit or loss should be eligible hedging instruments.

Question to constituents

17 Do you believe there is in effect an inconsistency between (i) the irrevocable designation of a financial instrument as at fair value through profit or loss and (ii) hedge accounting that may be discontinued if that is in accordance with an entity's risk management strategy?

We agree that there is an apparent inconsistency between the irrevocable designation of a financial instrument as at fair value through profit or loss and hedge accounting that may be discontinued if that is in accordance with an entity's risk management strategy, and this inconsistency should be clarified by IASB.

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?

Yes, we agree.

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?

We agree with EFRAG on this issue. However, we must draw your attention to the fact that the designation by the entity of hedging relationship in cash-flows or fair values will lead to different applications according to each entity risk management policies and activities, and according to judgment that each entity takes. In order to allow the comparability among entities and management policies, disclosures on this issue should be mandatory as well guidance in this issue should be given.

Questions to constituents

33 Do you have any concerns regarding inflation as a non-contractually specified risk component of financial instruments? If so, please provide examples.

We think that if the component of inflation can be separately identifiable and reliably measured than hedge accounting should be allowed, even if inflation is 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?

a) Yes, we agree that a layer of nominal amount of an item could be designated as hedged item.

b) Concerning this issue, we believe that it should be more clearly explained why the prepayments options cannot be eligible as hedge item even if they are traded instruments where prepayment risks are observable in the market or modelling techniques for prepayment risk at portfolio level.

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?

We agree with the removal of the thresholds set out in IAS 39, although we still believe like IASB that the hedge effectiveness continues to be an important qualifying criterion for hedge accounting.

We also welcome the removal of retrospective testing as a qualification criterion, as well the possibility of rebalancing the hedge relationship.

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?

We agree with the concept of rebalancing as explained in the ED, although we believe the ED lacks enough guidance on this issue especially concerning the distinction between rebalancing and discontinuance. We believe that this issue is extremely judgemental and in practice may lead to a free choice from issuers to choose between rebalancing and discontinuance, when an entity elects to retrospectively change the management risk policies or strategies. In order to avoid this it is important that entities should be obliged to document risk management strategies that impact the entity's approach on hedging accounting as well as disclosed their approach in the Financial Statements.

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?

We agree with EFRAG on this issue.

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?

We believe that previously to the discussion on where the fair value changes should be recognized, IASB should clarify what is considered "performance" and what should be recognized in profit or loss and what should be classified in OCI and Equity. The project on this issue is not yet schedule and is urgent that IASB takes this issue on his agenda, since this issue relates not only to hedge accounting but also other projects ongoing.

Having said that, CNC thinks that our answer is biased by the above position. Nevertheless, we agree with EFRAG's view on the fact that ineffectiveness should be recognized directly to profit or loss, although we believe that more disclosures shall be mandatory in order to assure that users understand clearly the movements that are recognized in profit or loss, their origin and the different type of hedging and hedging transactions.

CNC considers appropriated to present the gain and losses on the hedged item separately from the hedged item that shall be presented next to the hedged item. We also believe that the presentation of the aggregated of all the fair value adjustments is appropriated, as long as the disclosures related to them shall be mandatory and with the appropriated disaggregation. We believe, however that all adjustments should be presented in financial position statement gross between assets and liabilities and presented separately on each side of the balance sheet.

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?

We agree with the proposals of the ED related to recognition on the time value in options. However, we draw your attention to what was previously said with relation to what is considered performance and the recognition of the changes in time value options in profit or loss and OCI.

We welcome the solution presented in ED to the ineffectiveness of time value component to financial options, however we alert that there are still some concerns regarding the fact that proposals presented in ED takes into consideration that a premium is paid for an option, when there are certain derivatives where no premium is paid, for example "Zero cost collar".

We stress out, as well, the situations where it is important to establish interactions between this project and the other Standards. In this regard we alert the possible inconsistencies between IAS 41 and IAS 40 (when fair value option is exercised) and hedging accounting regarding the time of value included as costs transactions in non-financial assets.

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?

We agree with IASB proposal for eligibility of groups of items to be hedged as long as the aggregation is consistent with the risk management strategies. For cash flow hedges we believe that the offsetting cash-flows should affect profit and loss in the same period.

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?

We agree with ED proposals on this issue and accordingly, we disagree with EFRAG's view which considers the aggregation in the same line of all the fair value changes regardless of the origin (assets or liabilities);

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?

We agree with EFRAG's view that disclosures play a fundamental role in providing users with an understanding of an entity's risk management strategies and hedging activities, consequently, we think that ED should provide more information that in our opinion is important to comply with the objective of hedge accounting.

In this regard we think that disclosures about the following aspects should be taken into account:

- An entity should provide information about the main risks that it is exposed to, regardless the use of hedge accounting.
- Definition of hedge effectiveness and details of risks hedge.
- Details regarding the changes in risk management strategies;
- Disclosures regarding the main judgements involved in hedge accounting;
- Quantitative and qualitative disclosures taking into consideration what was previously stated in questions 7 and 9.

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?

We agree with EFRAG.

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?

We agree with EFRAG.

Question 16

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

We agree with EFRAG.

Lisbon, 2nd March 2011