

# Rådet för **finansiell rapportering**

## The Swedish Financial Reporting Board

RFR-rs 2008:3

International Accounting Standards Board  
30 Cannon Street  
London EC4M 6 XH  
United Kingdom

### EXPOSURE DRAFT OF PROPOSED **Amendments to IAS 39 Financial Instruments: Recognition and Measurement Exposures Qualifying for Hedge Accounting**

We appreciate the opportunity to respond to the International Accounting Standard Board's Exposure Draft of Proposed Improvements to International Financial Reporting Standards. This letter represents the views of the Swedish Financial Reporting Board.

The exposure draft provides a detailed list over which exposures that qualify for hedge accounting. We do not support this approach due to the following:

1. A rules based approach is not in line with the principles based approach that the IASB has as an objective to follow.
2. It will provide restrictions, which will result in costly and unnecessary structuring activities to achieve hedge accounting.
3. Already now the requirements to achieve hedge accounting are seen as being very extensive, when from a risk management standpoint a hedging situation is considered to exist. To further increase these requirements will be seen as unnecessary and restrictive.
4. A rules based approach will not reflect the inevitable future developments in businesses, financial practices and products.
5. A consequence of the above comments is that a principles based approach is more robust and better supports a corporation's business activities.

Despite the fact that we prefer a principles based approach we respond to your questions. As a result we comment on certain proposals in the exposure draft where the rules based approach has resulted in what we consider to be unintended effects.

Question 1 – Specifying the qualifying risks  
**The proposed amendments restrict the risks qualifying for designation as hedged risks to those identified in paragraph 80Y.**

# Rådet för finansiell rapportering

**Do you agree with the proposal to restrict the risks that qualify for designation as hedged risks? If not, why? Are there any other risks that should be included in the list and why?**

We do not agree with the proposal. Our view is that all risk components that exist in an agreement should be possible to use in a hedge relationship if certain requisites are fulfilled. These are:

- The risk component should be possible to identify separately as a risk component in the contract,
- The risk component should be possible to carve out from the other components of the contract, and
- The risk component should be possible to measure objectively

If these requisites are fulfilled, it should not matter if they are separately mentioned in an agreement or not. E.g. if inflation is an important risk component in a contract, it should not matter if that component is separately mentioned in the contract, it should still be possible to identify it as a separate component and it should therefore be possible to separately define it as a hedged item.

Question 2 – Specifying when an entity can designate a portion of the cash flows of a financial instrument as a hedged item

**The proposed amendments specify when an entity can designate a portion of the cash flows of a financial instrument as a hedged item.**

**Do you agree with the proposal to specify when an entity can designate a portion of the cash flows of a financial instrument as a hedged item? If you do not agree, why?**

**Are there any other situations in which an entity should be permitted to designate a portion of the cash flows of a financial instrument as a hedged item? If so, which situations and why?**

We agree that IAS 39 should specify when an entity is able to define a portion of a risk as a hedged item.

However we do not agree with the proposals presented in the exposure draft. We think that there are at least two requirements that need to be reconsidered:

1. That a risk component needs to be mentioned separately in a contract if it should be possible to use hedge accounting for that separate component
2. That a risk component could not be larger than the total.

See our answer on question 1 for our comment on the first requirement.

Our main concerns regarding the second requirement are the following:

If a certain risk component is present in a contract it should be possible to define it as a hedged item if the requirements proposed in our answer to question 1 is fulfilled. We believe that the IASB has been too eager to prevent abuse when restricting a component approach to hedge accounting. E.g. if changes in an interest rate are directly linked to an interbank interest rate (e.g. Libor), it should be possible to define

# Rådet för finansiell rapportering

the Libor component as the hedged item. The present requirement, that forces those companies that have a funding rate below the interbank interest rate to define the whole instrument as the hedged item is inconsistent and unbalanced. The requirement makes it extremely difficult for good quality companies to fulfil the effectiveness criteria's in IAS 39.

All companies that have funding rates below the interbank interest rates have those difficulties while all companies that are of higher credit risk (i.e. those that have a funding rate exceeding the interbank interest rates) are permitted to define the interbank interest rate as the hedged item. This lack of equality is strange since all other parameters, except the margin to the interbank interest rate are the same.

The market developments after June this year has highlighted this problem since the lack of liquidity in the financial markets have created a large volatility in margins around the interbank interest rates. That volatility proves the need for the IASB to reconsider its present standpoint.

We believe that the IASB should focus more on the principles behind a component approach to hedge accounting, than trying to list all possible components in the standard. The principles should instead make it clear that the components have to be directly present in the contract. E.g. if the interest rates on a current account does not change with movements in interbank interest rates, that component is not directly present in the contract and does therefore not qualify for a components approach to hedge accounting.

## Question 3 – Effect of the proposed amendments on existing practice

**The aim of the proposed amendments is to clarify the Board's original intentions regarding what can be designated as a hedged item and in that way to prevent divergence in practice from arising.**

**Would the proposed amendments result in a significant change to existing practice? If so, what would those changes be?**

A possibly unintended effect of listing portions in par 80z is that it limits the possibility for non financial hedging. The proposal says that "one sided risks" are included in "portions". The effect of the proposal would be to restrict the use of hedge accounting, for instance when using options for hedging non financial items, a practice which is common. We consider that the same principles should be used for both financial and non-financial items and therefore do not agree with the proposal as it will result in restrictions with respect to the financial management techniques that a company can apply.

## Question 4 – Transition

**The proposed changes would be required to be applied retrospectively.**

**Is the requirement to apply the proposed changes retrospectively appropriate?**

**If not, what do you propose and why?**

The requirements are in our opinion not appropriate. An entity has several different alternatives when using IAS 39. The one's chosen are those which create the most relevant effects on the income statement and on the balance sheet. To implement new requirements for hedge accounting and thereafter require an entity to redefine its old hedging relationships and restate previous year's figures may lead to several irrelevant restatements. The reason for that is that

# Rådet **för** finansiell rapportering

the entities probably would have chosen other possibilities in IAS 39 if the requirements would have existed at the inception of the previous hedging relationships, e.g. using the fair value

option, or may have documented the agreements with the counterpart differently to make them fit into the new documentation requirements.

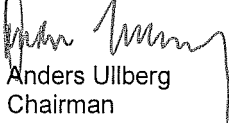
Therefore, if the IASB chooses to require restatement, it has to be possible for the entities to choose if it they still want to use hedge accounting or some other alternative. Such possibilities

will, however, create a risk of hindsight. We therefore propose that if the IAS 39 is changed, the changes should be implemented without a requirement to restate.

If you have any questions concerning our comments please address our Executive member Carl-Eric Bohlin by e-mail to: [carl-eric.bohlin@radetforfinansiellrapportering.se](mailto:carl-eric.bohlin@radetforfinansiellrapportering.se).

Stockholm, January, 28, 2008

THE SWEDISH FINANCIAL REPORTING BOARD

  
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