CL 138

Comments on IAS 39 from Westdeutsche Landesbank (WestLB)

The IAS 39 ED prevents hedge accounting for firm commitments, including foreign currency firm commitments. This is potentially devastating for companies wishing to hedge budgeted foreign currency denominated cash flows, ie, sales or purchases. At some point, many forecasted transactions become firm commitments, which will require companies to switch their accounting from cash flow to fair value hedges midway through the hedge period. They may then switch them back to cash flow hedges when they become recognised on the balance sheet. This does not make any sense to us or to our clients.

Regarding this issue, the ED seems to be inconsistent and I'm hoping this can help encourage the IASB to at least take one more look at this issue.

The ED says that IGC Issue 137-14 is not affected by the ED, but this issue uses the words "forecasted" and "committed" for the same transaction. It describes a transaction that appears to meet the IAS 39.10 definition of a firm commitment (Company B agrees to sell goods to Company C for delivery on 31 March at a price of USD 110, payable on 30 June). It then states that this foreign currency denominated "commitment" may be hedged in a cash flow hedge.

In addition, the IGC 121-2 cash flow hedging model does not appear to Require hedge redesignation when hedged forecasted cash flows become firmly committed, nor does it emphasize a separation of forecasted from firmly committed cash flows in the defined hedged item. This has not been amended by the ED, and if the Firm commitment requirement stands, then the IGC should probably be amended as well.

As stated in the Basis for Conclusions, at least part of the reasoning for this change is alignment with US GAAP, however through FAS 138 US GAAP allows CFH for FX firm commitments, since the reporting currency denominated cash flows are still exposed to currency fluctuations, even though the foreign currency denominated cash flows are presumed to be fixed.

Finally, it seems conceptually very strange that a FX denominated balance sheet item, where cash flows are more certain than firmly committed cash flows, can be hedged in a CFH, but a firm commitment cannot.