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Stockholm 14 October 2004

International Accounting Standards Board
Att: Sandra Thompson
Senior Project Manager
30 Cannon Street
London EC4M 6XH
United Kingdom

Dear Sirs,

Cash flow hedge accounting of forecasted intra-group transactions

We disagree with the draft amendment and the current standard because it does not correspond to how many corporations manage foreign exchange exposure. It does not acknowledge the currency exposure that arises from forecasted intra-group transactions in foreign currency. Furthermore the draft amendment and the current standard diverge from US GAAP.

The exposure

Forecasted intra-group transactions result in foreign currency exposure within many multi-national corporations (MNC).

Many MNCs manage the group on an operating unit basis and a common operational model is to concentrate manufacturing of goods in countries other than those where they generate a significant proportion of their sales revenue. As a result these entities may be exposed to foreign currency risk due to the fact that they incur costs in currencies other than those in which they earn much of their revenue.

The application of the functional currency concept (IAS 21) means that MNCs will have different functional currencies for manufacturing and selling subsidiaries. The transfer of the manufactured goods from one subsidiary to another will give rise to intra-group transactions as a result of which one subsidiary will be exposed to foreign currency risk arising from forecasted intra-group transactions denominated in the functional currency of the other.

Consider a MNC where the group has EUR as the functional currency. A European manufacturing entity sells internally in USD to an US foreign entity.

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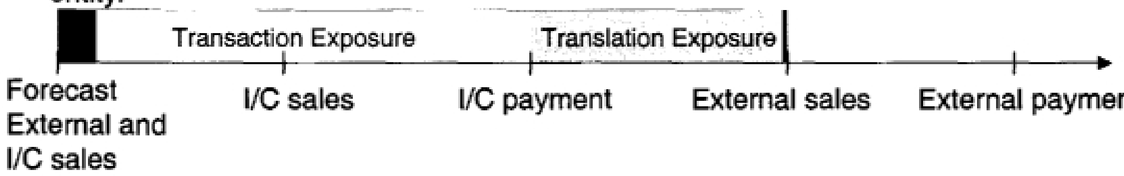
Example: An European entity sells internally in USD to an US foreign entity. The US foreign entity sells externally in USD. EUR is the functional currency of the group and the European entity.



On consolidation, the intra-group transactions are eliminated, leaving an FX exposure only where the forecasted transactions has given rise to an intra-group monetary item.

The exposure, for the European entity and the group arises when the intra-group transaction is forecasted. The forecasted can consist of highly probable intra-group transactions or intra-group firm commitments.

For the group the transaction exposure arises when the intra-group transaction is forecasted and stops when the intra group payment in USD is exchanged into EUR.

Hedging

The subsidiaries do normally hedge the forecasted transactions independent of whether it arises from an intra-group or external transaction. The hedges of the subsidiaries are normally transacted with the group's treasury center and are thus internal derivatives that are eliminated on consolidation. The treasury center executes the hedges externally and the group's exposure is thereby hedged.

Implication

If entities are unable to obtain hedge accounting for these hedges, the consolidated sales margin will show the impact of currency fluctuations and the requirement to fair value the derivatives will introduce additional volatility to the income statement.

Current risk management strategies where forecasted intra-group transactions are hedged are prudent and have proved to be efficient in managing a group's transaction exposure.

A consequence can be that entities will have to adopt different processes for risk management and hedge accounting whether it is an external or internal transaction even though both transactions affect the consolidated income statement.

It is inconsistent that an intra-group monetary item may qualify as a hedged item but not allow cash flow hedges of the same risk when forecasted.

Furthermore, the modification creates a further divergence from US GAAP, which explicitly permits hedge accounting for foreign currency risk on intra-group forecasted transactions.

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Suggested solution

We request re-instatement of the possibility to hedge forecasted intra-group transactions and possibility to achieve hedge accounting on theses transactions. Both internal and external transactions should qualify for hedge accounting as both give rise to real currency exposures that MNCs want to hedge.

Even though this letter was sent after 8 October 2004, when comments were to be received, we are convinced that you are interested in our view on this issue.

Best regards

Vidar Mohammar

Group Treasurer