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by email and post

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Dear Jim

**IAS 39; ADOPTION OF INTERNATIONAL ACCOUNTING STANDARDS FOR USE
WITHIN THE EUROPEAN UNION**

I write following our recent meeting and correspondence with yourself and Wayne Upton.

The ACT recognises that IAS 39 addresses a very complex area. The ACT has long supported the concept of marking to market for many types of financial assets and liabilities and the need for there to be good criteria for application of hedge accounting in company accounts.

We also accept that given limits of time and resource a standard like IAS 39 will not be able to reflect all parties' needs from the outset.

From the point of view of treasury operations in non-financial corporations the principal area remaining outstanding in IAS 39 is that of the practice of treasury-centre net hedging of forecast currency exposures. Foreign exchange is, of course, the main area of financial price risk where corporations may face offsetting exposures, thereby permitting netting. In the standard as drafted, hedging treatment will not be available in this area.

Netting of forecast transactions prior to externally hedging the net exposure is clear best practice – reducing the operational and credit risks from transacting and reducing the direct costs and overhead costs involved. The “work-around” of dealing gross with a third party – i.e. adding net nil transactions - is manifestly absurd: a net-nil transaction (ignoring the costs incurred and risks introduced) should not change reported accounts. Such transactions occurring, absent IAS 39, would of course be a signal for urgent investigation of the treasury operation by internal audit and security.

All of this indicates that a more fundamental review is needed of the principles which have led the IASB to its conclusions so far in respect of this type of netting.

However, despite our specific concerns, we believe that, more widely, IAS 39 provides a valuable framework for the treatment of derivative financial instruments and hedging and important topics like de-recognition.

Even more broadly, the ACT has long supported the move to internationally accepted accounting standards. The long-run advantages to corporations, and more generally in financial markets, of international accounting standards as part of a wider programme of improvements in the fields of audit and corporate governance, are clear.

To adopt international standards without IAS 39 would fail to provide a framework for accounting of many transactions and such a régime would fail to achieve many of the advantages, and thus wide acceptance, of such standards.

Accordingly, the ACT will let it be known that it believes that the European Union should adopt international financial reporting standards as they stand, including IAS 39, for use from 2005 in accordance with its standing plan. Such adoption will provide a base from which to move forward as international standards themselves evolve and are reviewed.

All of which said, we look forward to the process of review of IAS 39 which you have told us is likely to be an iterative process that will begin later this year.

The ACT will be posting a copy of this letter on its website.

Yours sincerely

A handwritten signature in black ink, appearing to read "Richard Raeburn". The signature is fluid and cursive, with a large initial 'R'.

Richard Raeburn.
Chief Executive