-----Original Message-----
From: janhughes@hsbc.com [mailto:janhughes@hsbc.com] On Behalf Of douglasflint@hsbc.com
Sent: Thursday, April 13, 2006 11:43 AM
To: Director - FASB; Bob Wilkins
Cc: Sir David Tweedie
Subject: File Ref: 1250-001 Fair Value Option

Letter of Comment No: 23A
File Reference: 1250-001
4-13-06

Dear Mr Wilkins

Further to our formal response of 10 April, I attach for your interest an extract from today's FT noting the anomaly between results reported in Korea to those reported by HSBC in its IFRS accounts.

I draw this to your attention because the principal difference between IFRS and Korean GAAP (the latter matching US GAAP in this area) is in the area of structured deposits where under the Fair Value Option within IAS 39 the economics of the structured deposit business are captured whereas under Korean and US GAAP, which do not have the benefit of the Fair Value Option, the structured deposit is accrual accounted and the hedging derivative is marked to market, leading to asymmetrical accounting which prompts the sort of headlines in the attached article. The introduction of FAS 155 will not eradicate this GAAP difference since, for these structured deposits, the embedded derivative is closely related and, hence, would not be bifurcated under FAS 133.

The importance of introducing a Fair Value Option within US GAAP is reinforced by this confusion.

Yours sincerely

Douglas J Flint
Group Finance Director
(See attached file: ft_20060413155216.pdf)

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FT Back

THURSDAY APRIL 13 2006

THE LEX COLUMN

South Korean banking

Earnings numbers released yesterday make one wonder why foreign banks set up shop in South Korea. The 32 banks operating in the country – excluding Citigroup and Standard Chartered, which control local lenders – earned an aggregate $90m last year. That is roughly what HSBC earns globally in a couple of days.

Last year was particularly horrible. Foreign banks' net income slumped 69 per cent, according to Korea's financial regulator. HSBC, Deutsche Bank and Credit Suisse were among those falling into the red. There are some good reasons for that. Trading income, a big part of foreign banks' profits, was ripped apart by volatility in Korean markets. Interest rates were a particularly tough call, as the Bank of Korea caught the market on the hop with a series of increases. Traders at foreign banks were not the only ones misreading the central bank; some local banks also recorded weaker trading contributions.

That said, the earnings numbers are deceptive. Once Citigroup and Standard Chartered are removed, most of the foreign banks have only one branch or office.

Earnings are naturally lumpy and more vulnerable to big swings; last year, for instance, the derivatives market was damped by a government-sponsored investigation into possible breaches concerning risk management. More important, global banks choose where to book profits based on several criteria, including tax and domicile of the counter-party. Income from buying or selling the Korean won for a foreign institution may be booked in Singapore; a cross-border acquisition could go in either jurisdiction. Accountancy standards further distort the numbers. Differing treatment of structured deposits, a big swing factor for HSBC, means its loss becomes a profit of nearly $100m under IAS39. That makes the numbers pretty arbitrary. The better barometer is the growing ranks of foreign banks on the ground.