IASB publishes Discussion Paper on accounting for macro hedging

The International Accounting Standards Board (IASB) today published for public comment a Discussion Paper exploring an approach to better reflect entities’ dynamic risk management activities in their financial statements, otherwise known as macro hedging.

Many financial institutions and other entities manage risks, such as interest rate risk, dynamically on a portfolio basis rather than on an individual contract basis. Dynamic risk management is a continuous process because the risks that such entities face evolve over time, as does their approach to managing those risks. However, the existing accounting requirements of IAS 39 Financial Instruments are generally considered to be difficult to apply when accounting for such transactions.

As part of its comprehensive response to the global financial crisis, the IASB is replacing IAS 39 with an entirely new financial instruments accounting Standard, known as IFRS 9 Financial Instruments. That project is in the final stages of completion. However, the IASB decided to treat as a separate project the macro hedging component of these reforms in order to elicit views from a broader range of constituents. The Discussion Paper published today represents the first stage in this project, by seeking public comment on a possible approach to accounting for an entity’s dynamic risk management activities, the portfolio revaluation approach (PRA). Under the PRA:

- Exposures that are risk-managed dynamically would be revalued for changes in the managed risk through profit or loss.
- Fair value changes arising from risk management instruments that are used to manage this risk (derivatives) would also be recognised in profit or loss.
- The success of an entity’s dynamic risk management is captured by the net effect of the above measurements in profit or loss.
- Fair valuation of the risk exposures that are dynamically managed is not required.

The PRA also addresses the needs of users by providing a more comprehensive set of disclosures concerning an entity’s dynamic risk management activities.

Commenting on the publication of the Discussion Paper, Hans Hoogervorst, Chairman of the IASB said:

Current requirements make it difficult to faithfully represent dynamic risk management in entities’ financial statements and can increase operational complexity.

This Discussion Paper sets out preliminary views on an accounting approach that better reflects the economics of dynamic risk management as compared to the current accounting requirements. Users of financial statements will also benefit from presentation that shows how dynamic risk management has affected an entity’s profit or loss.

The Discussion Paper: Accounting for Dynamic Risk Management: a Portfolio Revaluation Approach to Macro Hedging is available for comment until 17 October 2014. In addition to seeking input in the form of comment letters, the IASB will undertake an outreach programme designed to obtain feedback on the areas covered in the Discussion Paper. Further information is available on the project page.
A high level ‘Snapshot’ summary of the Discussion Paper is available here. On 29 April 2014 the IASB will hold two live webcasts taking place at 10am and 2pm (both London time).

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About the International Accounting Standards Board

The IASB was established in 2001 and is the standard-setting body of the IFRS Foundation, an independent, private sector, not-for-profit organisation.

The IASB is committed to developing, in the public interest, a single set of high quality, global accounting Standards that provide high quality, transparent and comparable information in general purpose financial statements.

In pursuit of this objective the IASB conducts extensive public consultations and seeks the co-operation of international and national bodies around the world.

The IASB has 16 full-time members drawn from 11 countries and a variety of professional backgrounds. Board members are appointed by, and accountable to, the Trustees of the IFRS Foundation, who are required to select the best available combination of technical expertise and diversity of international business and market experience.

In their work the Trustees are accountable to a Monitoring Board of public authorities.