

Accounting Standards Advisory Forum

Accounting for Dynamic Risk Management: a Portfolio Revaluation Approach to Macro Hedging

July 2015

The views expressed in this presentation are those of the presenter,
not necessarily those of the IASB or IFRS Foundation

Objective of the meeting

- During February and March 2015, the IASB discussed the feedback received to its Discussion Paper (DP) *Accounting for Dynamic Risk Management: a Portfolio Revaluation Approach to Macro Hedging*.
- At its May 2015 meeting, the IASB discussed the next steps of its project on accounting for Dynamic Risk Management (DRM).

The IASB acknowledged that any solution needs to consider the **information needs of constituents concerning DRM activities**. It tentatively decided to:

- first consider how the **information needs** of constituents concerning **DRM activities** could be addressed through **disclosures** before considering areas that need to be addressed through recognition and measurement; and
- prioritise the consideration of **interest rate risk** and consider other risks at a later stage in the project.

Objective of the meeting—*continued*

- Comment letters and outreach activities, albeit not complete, provided valuable insight into the information that is thought to be useful to constituents concerning DRM activities (see slides 4–7 for feedback received).

We would like your views on:

- any **additional information needs** concerning an entity's DRM activities for interest rates not identified in slides 4–7;
- **additional information sources** that could help us understand information needs of constituents other than:
 - ✓ comment letters to the DP;
 - ✓ the usual channels such as outreach with users, preparers, regulators, national standard-setters and academics; and
 - ✓ reviewing existing GAAP and non-GAAP measures and regulatory requirements.

Key messages from comment letters

- The DP successfully captured the key characteristics of DRM.
- The DP succeeded in identifying the challenges in accounting for open portfolios and comprehensively analysed key features such as behaviouralisation and deemed exposures.
- There is a need to address the limitations of current IFRS hedge accounting requirements when applied to DRM scenarios.
- There is a lack of clarity in the information provided about DRM activities in the financial statements.

However:

- The feedback received also highlighted **significant diversity** in views among constituents regarding the objectives of the project, which translates into differences in their information needs.

- The project should address the challenges in applying hedge accounting for the purposes of managing volatility in profit or loss arising from accounting mismatches.
 - Preparers do not believe that volatility in profit or loss arising from unhedged risk exposures provides useful information.
- Preparers would generally like to have the flexibility to apply either fair value or cash flow hedge accounting, the Portfolio Revaluation Approach (PRA) or the fair value option.

Feedback—Needs and challenges from preparers— *continued*

- Preparers are willing to convey the information arising from their DRM activity and its effects in line with their risk management practices and techniques, including behaviouralisation. For example, they think behaviouralisation of core demand deposits should be accepted, in spite of the conceptual challenges.
- Current accounting requirements present significant challenges to represent DRM activities directly; entities have to rely on indirect methods (for example, proxy hedging), which is not an optimal solution.
- It was also noted by preparers that the current disclosure requirements under IFRS 7 *Financial Instruments: Disclosures* do not appropriately cover DRM activities.

Users generally support the project and the concept of the PRA.

- They are interested in information about:
 - Net Interest Income (NII) by profit source (customer margin vs the result of taking open risk positions);
 - Derivatives by their use (ie trading and hedging); and
 - Hedged and unhedged exposures.
- Expressed a concern about the lack of comparability, if the accounting for DRM is optional.
- Users prefer direct representation of economic hedges in principle. However, they expressed concerns over behaviouralisation concerning applicability of judgement and earnings management.

Questions or comments?—Thank you

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