Project	**Financial Instruments (Replacement of IAS 39)—Hedge Accounting**
Topic	**Hedge accounting disclosures—Risk exposures and risk management**

Purpose of this paper

1. This paper provides the Board with a summary of possible hedge accounting disclosures that provide information on an entity's risk exposures and risk management strategies.

2. The proposals in this paper help to achieve the objectives identified in agenda paper 20. Those objectives are to provide information on:

    (a) how an entity's risk management strategy is applied to manage or transform risk; and

    (b) how the entity's hedge activities may affect the amount, timing and uncertainty of its future cash flows.

Proposed requirements

3. The disclosures proposed in agenda papers 20A and 20B summarise the effects of hedge accounting on the balance sheet, the income statement and OCI. These disclosures are done in a tabular format separating the information by risk category.

4. The proposals in this paper require disclosures about information that is not captured in the primary financial statements. The proposed disclosures provide more perspective on the information required in agenda papers 20A and 20B. The disclosures set out in this paper should be provided by the risk categories

This paper has been prepared by the technical staff of the IFRS Foundation for discussion at a public meeting of the IASB.

The views expressed in this paper are those of the staff preparing the paper. They do not purport to represent the views of any individual members of the IASB.

Comments made in relation to the application of an IFRS do not purport to be acceptable or unacceptable application of that IFRS—only the IFRS Interpretations Committee or the IASB can make such a determination.

The tentative decisions made by the IASB at its public meetings are reported in IASB *Update*. Official pronouncements of the IASB, including Discussion Papers, Exposure Drafts, IFRSs and Interpretations are published only after it has completed its full due process, including appropriate public consultation and formal voting procedures.

used for the proposed disclosures in agenda paper 20A and 20B. In other words, the entity should present the information proposed in this paper for each risk category that it has identified and used to prepare the proposed tables in agenda papers 20A and 20B.

What information should be disclosed?

Risk management strategy

5. Users of financial statements need to understand how a particular risk arises and how the entity manages that risk. Such an understanding will help place the accounting information in perspective with the entity's risk management approach.

6. The risks we are talking about here are the risk exposures the entity decided to hedge and for which hedge accounting is applied.

7. To provide users with such an understanding the entity should provide a description of what its risk management strategy is for each particular risk. This description should enable users to understand, for example (not limited to):

   (a) how the risk arises;

   (b) how the entity manages each risk; this includes whether the entity hedges the hedged item in its entirety for all risks or a risk component(s) (eg a benchmark); and

   (c) the extent of risk exposures that the entity manages.

Risk exposure managed and the extent to which it is hedged

8. Once users are provided with an understanding of the risk management strategy, the next step is to provide *quantitative* information of the extent of the risk exposure and how it is hedged. The objective of providing this information is for an entity to explain what risk exposures it manages, the extent to which it hedges and the result of the hedges.

9. To effectively describe the exposure that the entity manages and the extent to which that exposure is hedged, the entity would have to group hedging instruments and hedged items with similar characteristics (for example, similar hedging instruments that are hedging a similar exposure). However, an entity will have to use judgement to determine how it groups the information.

10. In other words, when an entity discloses information about the risk exposure and how it is managed, the entity should consider how best to present the information when there are different hedging relationships hedging a particular risk.

11. Once the entity has determined how to group the information, it should disclose:

    (a) the monetary amount or other quantity (eg tonnes, cubic metres) to which the entity is exposed for that particular risk, *identified* as part of its risk management activities (for hedges of groups or net positions, the entity will need to explain the risk exposure in the context of a group or net position);

    (b) the amount or quantity of the risk exposure being *hedged*; and

    (c) in quantitative terms how hedging has changed the exposure (ie the risk profile after hedging such as the average rate at which the entity has hedged that exposure; for example, the average forward sale contract rate for the forecasted sales designated as hedged items).

12. This table will provide the information proposed above for each period that the hedging relationship is designated as such. In other words, the entity will provide a breakdown of the risk being managed and the extent to which it is hedged for each period (subsequent to the reporting period) in which there is a risk exposure and a designated hedging relationship managing the risk (see agenda paper 20D for an example).

Additional disclosures regarding the sources of expected ineffectiveness

13. The Board has tentatively decided that the objective of testing the effectiveness of a hedging relationship should be that a hedging relationship will produce an unbiased result and minimise expected ineffectiveness[1]. To enable users to understand the reasons why there might be some ineffectiveness with relation to the hedging relationship, the entity should disclose the sources of expected ineffectiveness.

14. When there are unexpected sources of ineffectiveness, the entity should also disclose those sources and the reason why the unexpected ineffectiveness occurred.

Additional disclosures regarding forecast transactions

15. Users have indicated that they need to understand the extent to which entities are hedging forecast transactions and how accurate those forecast have been. In other words, in the event that an entity has designated a forecast transaction as a hedged item, users want to understand the extent to which those forecasts have not materialised or are no longer expected to occur.

16. Consequently, the following information might be useful:

    (a) For transactions that were forecast in previous periods to occur during the current period, information about how forecasts compare with the actual cash flow during the current period. We think that information need can best be addressed by the reconciliation of the cash flow hedge reserve. If that includes a sufficient level of granularity the effect of transactions that did occur in the period on profit or loss and transactions that were hedged before but did not occur would be transparent (see paragraph 16(e) of agenda paper 20B).

[1] See agenda paper 4A of the August 2010 IASB meeting.

(b) A description of any forecast transaction that have been designated as hedged items in the prior periods, but that are no longer expected to occur. This requirement is similar to a requirement in IFRS 7[2]. This proposals will therefore not duplicate the existing requirement in IFRS 7 but rather incorporate this into the proposed hedge accounting disclosures.

Additional disclosures regarding items that do not qualify for hedge accounting

17. It may happen that an entity enters into a transaction to manage an exposure to a particular risk. That transaction might not qualify for hedge accounting for a number of reasons (for example, it is an item not eligible to be designated as a hedged item or hedging instrument, etc.)

18. Arguably, information on such transactions might enable users to understand why an entity has entered into a transaction and how it manages the particular risk, even though it does not qualify for hedge accounting.

19. However, the Board's tentative decisions to date in this project essentially mean that hedge accounting will have to remain elective (ie a choice). Hence, we do not consider that such a disclosure requirement would in practice result in useful information. For example, an entity may decide to not even attempt to qualify for hedge accounting. The reasons why it then would not qualify would be entirely speculative. For example, not providing the required documentation of designating the hedging relationship would be an obvious reason that could be given by any entity.

20. In addition, users of financial statements can infer from information in management reports or similar information about risk management outside the financial reporting context what the entity's hedging activities are. That often gives a reasonable hint why hedge accounting might be difficult to achieve.

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[2] See IFRS 7.23(b).