
| | |
|---------|--|
| Project | Financial Instruments: Replacement of IAS 39 |
| Topic | Cover note – hedge accounting presentation: basis adjustments and hedging FX risk of firm commitments |

Introduction

1. IAS 39 *Financial Instruments: Recognition and Measurement* provides different presentation choices for particular hedging transactions. At this meeting, the following papers will be discussed in relation to these presentation choices¹:
 - (a) agenda paper 16A: basis adjustments (ie the treatment of the hedged item in hedges of forecast transactions that subsequently result in the recognition of non-financial items, or hedges of forecast transactions for non-financial items that become firm commitments);
 - (b) agenda paper 16B: hedges of foreign currency (FX) risk of firm commitments;
 - (c) agenda paper 16C: interaction between basis adjustments and hedges of FX risk of firm commitments; and
 - (d) agenda paper 16D: illustrative examples.

¹ Some of these presentation choices also affect the measurement of hedge ineffectiveness because the 'lower of test' that applies to cash flow hedges.

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.

IASB Staff paper

Agenda paper 16A

2. Agenda paper 16A discusses the *accounting policy choice* in IAS 39 today for cash flow hedges of forecast transactions that result in the recognition of non-financial items. When such a non-financial item is recognised, IAS 39 today allows entities to either:
 - (a) adjust the initial carrying amount of the hedged item for the hedging gain or loss (basis adjustment); or
 - (b) leave the hedging gain or loss in other comprehensive income (OCI) and transfer it to profit or loss when the hedged item affects profit or loss.
3. Agenda paper 16A discusses this accounting policy choice, set outs alternatives for how the Board could proceed, a staff analysis and a staff recommendation.

Agenda paper 16B

4. Agenda paper 16B discusses the *choice* (on a hedge by hedge basis) in IAS 39 today for hedges of FX risk of firm commitments.
5. Under IAS 39 today, hedges of FX risk of a firm commitment can be accounted for as a fair value hedge or as a cash flow hedge.
6. Agenda paper 16B discusses this accounting choice, sets out alternatives for how the Board could proceed, a staff analysis and a staff recommendation.

Agenda paper 16C – interaction between issues in AP16A and AP16B

7. Agenda paper 16C discusses the implications for FX hedges of the interaction between the alternatives set out in agenda papers 16A and 16B. The interaction is illustrated in the diagram in Appendix A of this paper.
8. That diagram illustrates when an entity hedges its FX exposure from t0 to t2.

IASB Staff paper

9. Agenda paper 16A discusses the presentation choice at t1 where the FX hedge of a highly probable forecast transaction becomes a FX hedge of a firm commitment. Agenda paper 16A also discusses the presentation at t2 if the FX hedge of a firm commitment is accounted for as a cash flow hedge throughout the hedge.
10. Agenda paper 16B discusses the presentation choices from t1 to t2 for which the hedge is an FX hedge of a firm commitment.

Agenda paper 16C

11. Agenda paper 16C contains questions to the Board and asks the Board for decisions on whether to retain the current presentation choices in:
 - (a) paragraph 98 of IAS 39 for hedges of forecast transactions that subsequently result in the recognition of non-financial items or hedges of forecast transactions for non-financial items that become firm commitments; and
 - (b) paragraph 87 of IAS 39 for hedges of FX risk of firm commitments.

Agenda paper 16D

12. Agenda paper 16D contains illustrative examples of the different scenarios and interactions addressed in agenda papers 16A, 16B and 16C.
13. **The staff strongly encourages the Board to consider the examples in agenda paper 16 D side-by-side with the other agenda papers in this series.**

Appendix A (print in colour)

14. This diagram illustrates:

- (a) a FX hedge of a forecast transaction that turns into a FX hedge of a firm commitment that results in recognition of a non-financial item; and
- (b) the choices available between fair value and cash flow hedge accounting;
- (c) the presentation choices available for a designated cash flow hedge (basis adjustment); and
- (d) a hedge designated as a fair value hedge is equivalent to the basis adjustment presentation in a cash flow hedge.

