Project **Financial Instruments: Hedge Accounting**

Topic **Presentation – Linked presentation**

Introduction

1. At the April 27th IASB meeting, the Board tentatively decided not to allow linked presentation for fair value hedges. However, the Board asked the staff to do some further outreach to determine if there were any perspectives that were not captured in the deliberations of the Board up to this point.
2. This paper provides the Board with the feedback of the discussions that the staff and some Board members had on linked presentation.
3. This paper asks the Board the Board to confirm its decision not to allow linked presentation for fair value hedges.

Background

4. Linked presentation is a way of presenting information so that it shows how particular assets and liabilities are related. Linked presentation is technically not the same as offsetting. This is because linked presentation displays the 'gross' amount of related items in the statement of financial position (while the net amount is included in the total for assets and liabilities).
5. In its exposure draft, the Board proposed not to allow linked presentation. The Board noted that linked presentation could provide some useful information about a particular relationship between an asset and a liability. However, it does not differentiate between the types of risk covered by that relationship and those that are not. Consequently, linked presentation could result in one net amount for an asset

and liability that are 'linked' even though that link (ie the relationship) affects only one of several risks underlying the asset or liability (eg only currency risk but not credit risk or interest rate risk).

6. At the April 27th 2011 meeting the staff provided the Board with feedback on responses to this proposal in the exposure draft (refer to Agenda Paper 3 of that meeting). Essentially the feedback received supported the proposal in the exposure draft not to allow linked presentation for fair value hedges. However, it was noted that one respondent representing a specific industry strongly disagreed with the proposal in the exposure draft. Consequently, while the Board tentatively confirmed their original decision they asked the staff to do some additional outreach on this issue.

Feedback from the additional outreach

7. The staff confirmed that the need for linked presentation was driven by specific regulatory requirements in a specific jurisdiction. The regulation in question requires that entities calculate a total debt ratio (debt/equity). If entities exceeded the specific total debt ratio threshold set by the regulator, the entity would have to be restructured. Because fair value hedges for foreign exchange risk can result in extremely large liabilities being recognised (sometimes as much as 30% of total liabilities) for the entities in the industry in question, it can result in breaches of the specific limits set by regulators in that specific jurisdiction. However, if linked presentation is applied in this situation, the 'net' number in the liabilities section results in a lower debt ratio. This in turn means that the entities do not run the risk of exceeding the limit set by the regulator (which means no forced restructuring is necessary). Linked presentation is viewed by entities in that jurisdiction as more accurately representing their leverage position.

8. It is difficult to address needs specific to individual jurisdictions. However, the staff notes that the affected entities could provide additional information in their note disclosure to better explain their economic position.

9. The staff confirmed that users do not necessarily view linked presentation more useful. Users view additional information in the notes as being sufficient to explain the relationships that exist between the hedged items and the hedging instrument. Without a clear principle behind linked presentation the users spoken to indicated that they do not want the Board to introduce a new concept for a specific situation such as a jurisdictional regulation.

Staff recommendation

10. While the staff are sympathetic to the issues faced by the jurisdiction in question, the information obtained from the additional outreach is consistent with the staff's arguments in previous papers[1]. Therefore, the staff recommends that the Board confirms that linked presentation not be allowed for fair value hedges.

Question
Does the Board agree with the staff recommendation in paragraph 10? If not, why not and what would the Board prefer instead and why?

[1] Refer to agenda papers 9 of the April 2011 IASB meeting and 8B of the July 2010 IASB meeting.