

## STAFF PAPER

22 – 26 April 2013

## REG IASB Meeting

<b>Project</b>	<b>Hedge Accounting (IFRS 9)</b>		
<b>Paper topic</b>	Due process summary for the hedge accounting project		
<b>CONTACT(S)</b>	Tiernan Ketchum	<a href="mailto:tketchum@ifrs.org">tketchum@ifrs.org</a>	+44 (0)20 7246 6937
	Martin Friedhoff	<a href="mailto:mfriedhoff@ifrs.org">mfriedhoff@ifrs.org</a>	

This paper has been prepared by the staff of the IFRS Foundation for discussion at a public meeting of the IASB and does not represent the views of the IASB or any individual member of the IASB. Comments on the application of IFRSs do not purport to set out acceptable or unacceptable application of IFRSs. Technical decisions are made in public and reported in IASB *Update*.

## Introduction

1. This paper analyses the IASB's compliance with due process requirements over the course of the general hedge accounting project, and considers whether the requisite steps to proceed from the draft hedge accounting requirements for IFRS 9 *Financial Instruments*<sup>1</sup> to the Ballot Draft of the new IFRS 9, incorporating the final version of Chapter 6 *Hedge Accounting*, have been met. In doing so, it presents:
  - (a) the background of the general hedge accounting project;
  - (b) the present status of due process;
  - (c) an analysis of compliance with due process steps; and
  - (d) the staff's view on whether compliance was achieved.
2. The IASB's due process requirements, as set out in the *IASB and IFRS Interpretations Committee Due Process Handbook* issued February 2013, describe the mandatory and optional steps to be taken before the publication of an IASB document. In considering the finalisation of an IFRS, the objective of due process is to ensure that the IASB is satisfied that it has undertaken sufficient consultation and analysis to justify its decisions.

---

<sup>1</sup> See draft of the forthcoming hedge accounting requirements posted on the IASB website on 7 September 2012 (<http://www.ifrs.org/Current-Projects/IASB-Projects/Financial-Instruments-A-Replacement-of-IAS-39-Financial-Instruments-Recognitio/Phase-III-Hedge-accounting/Pages/Draft-of-IFRS-General-Hedge-Accounting.aspx>). This paper refers to this as "draft requirements" or "draft IFRS 9".

## Project background

3. The draft Chapter 6 *Hedge Accounting* (to be included in IFRS 9) is the third phase of the project to improve the accounting for financial instruments by replacing IAS 39 *Financial Instruments: Recognition and Measurement*.

## Pre-Exposure Draft

4. In March 2008 the IASB published for comment the discussion paper (DP) *Reducing Complexity in Reporting Financial Instruments*. The comment period for the DP lasted until 7 September 2008. A total of 162 comment letters were received on the DP, which were analysed with results presented to the IASB. The DP identified hedge accounting as a source of complexity in financial reporting, and introduced proposals for simplifying hedge accounting requirements. The two general approaches put forward were:
  - (a) to eliminate (and possibly replace) existing hedge accounting; and
  - (b) to maintain and simplify the existing hedge accounting requirements.
5. During its post-DP deliberations to prepare for the Exposure Draft the IASB engaged in extensive consultation with preparers, auditors, regulators, and users of financial statements for views on the hedge accounting requirements of IAS 39. Of all the phases of the project to replace IAS 39, hedge accounting elicited the highest number of requests from constituents for meetings with the staff and IASB members. The staff spent a considerable amount of time satisfying these requests for meetings including actively reaching out to parties to understand how users view hedging and how an entity's hedging activities affect their analysis and decisions. The staff consulted with over 30 individual analysts and various user groups including the Analyst Representative Group (ARG) and the Corporate Reporting Users Forum (CRUF). A broad variety of responses were received, which the staff took into consideration during the development of the proposals.
6. During outreach it became clear that constituents wanted the Board to fully consider the hedge accounting issues rather than to simply 'patch' existing requirements. To accomplish this, the staff's approach was to reform the hedge accounting requirements (rather than simply amending IAS 39) to develop a hedge accounting

model with less reference to arbitrary requirements that would result in more useful information. The main issues addressed in IASB public meetings during this period prior to the Exposure Draft (ED) were:

- (a) Overall objective and purpose of hedge accounting.
- (b) Eligibility of hedged items and hedging instruments.
- (c) Hedging effectiveness requirements and measurement thereof.
- (d) Discontinuation of hedge accounting.
- (e) Mechanics of fair value hedge accounting.
- (f) Presentation and disclosure.
- (g) Effects on other project phases.

### ***Exposure Draft***

7. On 9 December 2010 the IASB issued the Exposure Draft *Hedge Accounting*, which built on the proposals in the DP, and incorporated input received from comment letters and outreach performed during deliberations. The ED proposed requirements with the objective of better enabling entities to align hedge accounting with risk management activities that are undertaken when hedging financial and non-financial exposures. The draft had a three-month comment letter deadline of 9 March 2011. The three-month period was approved based off the timeline for IFRS 9 at the time. The IASB had received 177 comment letters by the comment letter deadline and 216 letters as of the March public meeting. A total of 247 comment letters were ultimately received on the ED.
8. During the 3-month consultation period for the Exposure Draft IASB members and staff conducted extensive outreach. It was our most intensive outreach programme for any project to date. Participants were consulted across all major geographical regions, with a total of 145 meetings held in Africa, Asia Pacific, Europe, North America, Central America and South America (illustrated in the table below). More than 2,500 individuals participated in the IASB's outreach activities. Examples of parties from which feedback was received include auditors, regulators, users, national standard setters, treasurers, risk management experts and academics.

<b>Geographic Region</b>	<b>Number of meetings</b>
Africa	10
Asia-Pacific	44
Europe	47
North America	10
Central America	14
South America	20
<b>TOTAL</b>	<b>145</b>

9. Feedback on the outreach was positive, with many participants stating that they appreciated the extent and geographical coverage of the outreach efforts made by the IASB. Most group meetings consisted of between 20 to 50 participants, with the largest being attended by over 200. The majority of meetings were face-to-face interactive sessions, with meeting time balanced between providing an explanation of proposals and receiving feedback from participants.
  
10. In general, there was strong support for the proposals in the ED, and many commented that they thought that the proposals would resolve many practice problems in applying IAS 39. Respondents were supportive of an objective to better link risk management with hedge accounting, and of particular proposals such as the changes to hedge effectiveness qualification requirements. Because the proposals introduced various new concepts, the most common request was for additional clarification and examples to explain certain areas. A number of respondents also requested that the IASB address ‘macro hedging’, which they emphasised would form a vital part of the overall hedge accounting model.

### **Present status of due process**

11. The IASB completed its redeliberations on the Exposure Draft *Hedge Accounting* at the September 2011 public meeting. At that meeting, the IASB tentatively decided that re-exposure would not be necessary. However, the IASB decided to post a staff (review) draft of the requirements on our website for a period of 90 days to enable

stakeholders to become more familiar with the document prior to its finalisation<sup>2</sup>. During the interim period the IASB undertook a detailed fatal flaw review and an outreach process.

12. A draft for editorial review of the forthcoming general hedge accounting requirements was posted on the IASB's website on 07 September 2012. This draft was posted for a period of three months with the intention to finalise the document after the December 2012 Board meeting. This period was part of an extended fatal flaw process, and was intended to capture essentially editorial issues to assist in drafting. Given that it was part of the fatal flaw process—and not part of the exposure process—it did not involve seeking comments from stakeholders. In particular, it was not intended to be an opportunity to get further comments about the decisions made by the Board during redeliberations.
13. The IASB has a formal comment letter process that incorporates permission to post comments on the IFRS Foundation website. In contrast to that process, the comments we received on the hedge accounting review draft were intended to be the comments of individuals to assist in drafting rather than providing 'opinions' on a proposal (as is the case for an exposure document). Based on this, we did not attempt to obtain permission to—nor have we posted—comment letters for the review draft on the IASB website. Issues arising from the extended fatal flaw process that are drafting points will be addressed during the finalisation of the document.
14. Those issues resulting from the fatal flaw process which were more substantive (and not purely disagreements with IASB decisions, which was not the purpose of the process) were discussed by the IASB in the January 2013 public meeting, after the close of the three month review period ending in December 2012. The issues discussed during this meeting were:
  - (a) using 'hypothetical derivatives' to measure the change in the value of the hedged item;
  - (b) the transition requirement for designation of 'own use' contracts as at fair value through profit or loss; and

---

<sup>2</sup> At the time as the timing of the FASB's redeliberations on hedge accounting was unclear it was also designed to enable the FASB to consider the draft in their redeliberations. However, the FASB have not yet recommenced their redeliberations.

- (c) the scope of the draft requirements and the interaction with macro hedging activities.
15. The IASB agreed to make amendments to the hedge accounting requirements to address the first two issues and to clarify the application of IFRS 9 to certain macro hedging activities.
  16. The European Financial Reporting Advisory Group (EFRAG) issued a finalised comment letter on the review draft on 18 January 2013. Points in this comment letter were addressed during the January Board meeting. Subsequently, EFRAG issued a draft second comment letter on 22 January—with a comment period ending 21 February—focussing on the interaction between the review draft and the current treatment of macro hedging activities under IAS 39. As a result of the issues raised in this draft comment letter the IASB decided at the January Board meeting to postpone finalising the hedge accounting requirements. The IASB requested that the staff undertake additional targeted outreach to understand the concerns raised by EFRAG, and the need for and nature of possible solutions.
  17. The IASB has conducted additional outreach with EFRAG staff and audit firms during the interim period since the January meeting. In so doing, to obtain feedback as quickly as possible the staff requested that the audit firms obtain feedback from banks in Europe. Outstanding issues will be addressed at this Board meeting. An agenda paper on the impact of the draft requirements on existing macro hedging relationships under IAS 39 will be included in these deliberations.

### **Analysis of compliance with due process steps**

18. The following section presents the mandatory, non-mandatory “comply-or-explain”, and other optional steps performed during the general hedge accounting project. These steps are listed in the *IASB and IFRS Interpretations Committee Due Process Handbook*, as issued in February 2013, in paragraphs 3.41 to 3.45.
19. This section should be considered in conjunction with Appendix A of this document.

## **Mandatory steps**

### *Debating any proposals in one or more public meetings*

20. The IASB has held public meetings on the hedge accounting project from September 2009 to this meeting. Staff papers for these meetings have been posted on the website prior to meeting dates. All decisions have been made in those public meetings, and summaries of the decisions reached were posted on the website after each meeting.

### *Exposing for public comment a draft of any proposed new Standard—with minimum comment periods*

21. The IASB exposed for comment the Exposure Draft *Hedge Accounting* in December 2010. The ED had a three-month comment letter period ending 9 March 2011.
22. The three-month comment period was agreed upon by the IASB in October 2010, when the staff were asked to proceed with drafting and balloting the ED. In reaching that decision the IASB acknowledged that the issues addressed in the Exposure Draft are complex, but also noted the extensive outreach activities by the staff and board members that helped to ensure that constituents had been able to follow the project.

### *Considering in a timely manner those comment letters received on the proposals*

23. The IASB received a total of 247 comment letters on the ED. The initial comment letter summary was presented to the IASB in the 14 March 2011 public meeting, covering the 216 letters received by the posting date of that paper. Any additional points raised in comment letters after that date were analysed and incorporated in later agenda papers.
24. All comment letters have been posted on the hedge accounting project page of the IFRS Foundation website.

### *Considering whether the proposals should be exposed again*

25. At the September 2011 public meeting the IASB tentatively decided that re-exposure of the proposed IFRS would not be necessary. That question will again be asked of the IASB at this public meeting taking into consideration the feedback received on the draft of the final chapter.

### ***Non-mandatory steps***

#### *Publishing a discussion document (eg a Discussion Paper) before an Exposure Draft is developed*

26. In March 2008 the IASB published for comment the discussion paper *Reducing Complexity in Reporting Financial Instruments*, which identified hedge accounting as a source of complexity in financial reporting, and introduced proposals for simplifying hedge accounting requirements. A comment letter summary was presented to the board in October 2008, covering the 157 comment letters received by the 19 September 2008 comment letter deadline. In March 2009 the staff presented another analysis of the total 162 comment letters received.

#### *Establishing consultative groups or other types of specialist advisory groups*

27. The IASB created a Financial Instruments Working Group (FIWG) in 2004 to address issues related to financial instruments projects.
28. The IASB did not form a consultative group specifically for hedge accounting. Rather we relied upon practical input through the extensive outreach activities.

#### *Holding public hearings*

29. The hedge accounting project has been discussed during meetings in London with:
- (a) the Capital Markets Advisory Committee; and
  - (b) the Global Preparers Forum.

Meeting papers and audio webcasts are available for these meetings on the IASB's website.

#### *Undertaking fieldwork*

30. The IASB has performed extensive outreach with a wide sample of participants during the project and has received and considered a significant amount of feedback. In addition, some of this feedback included results received on fieldwork done by national standard setters. Through this process we have obtained a thorough understanding of the practical implications of the new hedge accounting requirements.



**Other steps**

31. Throughout the hedge accounting project, the IASB has performed a significant amount of outreach and consultation with constituents in order to understand concerns and inform constituents of the project's progression. IASB members and staff have:
- (a) held a large number of meetings with individuals and groups of auditors, industry representatives, preparers, regulators, national standard-setters, and users of financial statements;
  - (b) maintained lines of communication with industry groups, regulators, and national standard-setters; and
  - (c) appeared at public events to exchange views with constituents.
32. The staff have made use of the IASB's website to regularly update constituents on the status of the project. In addition to the standard posting of the ED, comment letters, draft IFRS, meeting agenda papers, IASB *Updates*, and board meeting webcasts, the website has included such material as:
- (a) Project webcast and podcast recordings.
  - (b) Snapshot, outreach summary, and FAQ document for the ED.
  - (c) Summary of tentative decisions at completion of redeliberations.
  - (d) Multiple pages of additional detailed explanatory information on the ED, including numerous technical examples and comprehensive links to relevant staff papers.
33. Interested parties have received updates for major project news items through subscriber email alerts. Over 22,000 participants are registered for IAS 39 Project Update email alerts.

***IASB sets an effective date for the standard***

34. An entity shall apply IFRS 9, Chapter 6 *Hedge Accounting* for annual periods beginning on or after 1 January 2015.<sup>3</sup> Earlier application is permitted. However, if an entity elects to apply this IFRS it must apply all of the requirements in this IFRS at the

---

<sup>3</sup> The recently published Exposure Draft on impairment asks constituents for their view on whether the effective date of IFRS 9 of 01 January 2015 should be reconsidered.

same time. If an entity applies this IFRS in its financial statements for a period beginning before 1 January 2015, it shall disclose that fact and at the same time apply the amendments in Appendix C, IFRS 9, Chapter 6.

### *Analysis of likely effects of the forthcoming IFRS*

35. The IASB is committed to assessing and sharing knowledge about the likely costs of implementing proposed new requirements and the likely on-going associated costs and benefits of each new IFRS—the costs and benefits are collectively referred to as ‘effects’. The IASB gains insight on the likely effects of the proposals for new or revised IFRSs through its formal exposure of proposals and through its fieldwork, analysis and consultations with relevant parties through outreach activities.
36. The draft requirements are accompanied by an extensive Basis for Conclusions that sets out what issues the Board sought to address, how it addressed them, and the expected effect of the changes.
37. Other consultative steps are documented in Appendix A.

### **Considerations for the post-implementation review**

38. IFRS 9 *Financial Instruments*, incorporating Chapter 6 *Hedge Accounting*, if finalised, will be subject to a two-phase post-implementation review as required by IFRS Foundation due process. This is generally performed after the new requirements have been applied internationally for two years—normally 30 to 36 months after the effective date. The first phase involves identifying and assessing the matters to be examined, and then subjecting them to public consultation in a Request for Information. The second phase is an analysis of comments and feedback received through the public consultation and other outreach activities. This is followed by the IASB presenting its findings and plans for further steps, if any, to be taken.

### **Summary**

39. In the staff’s view the IASB has complied with the requirements of the *IASB and IFRS Interpretations Committee Due Process Handbook* in the development of the draft of the new IFRS 9, incorporating the final version of Chapter 6 *Hedge*

*Accounting*, and the staff are prepared to begin the balloting process for the final IFRS.

**Questions for the IASB**

Does the IASB agree with the staff's view that due process requirements have been met?

Are there any further due process steps that the IASB thinks are necessary before the balloting process?

Do any members of the IASB dissent from the staff's view of compliance with due process? If so, why?

## Appendix A: Due process steps

Step	Required/Optional	Metrics or evidence	Protocol for and evidence provided to DPOC	Action
<b>Consideration of information gathered during consultation</b>				
IASB posts all comment letters received in relation to the Exposure Draft on the project pages	Required if request issued	Letters posted on project pages	IASB reports on progress as part of the quarterly report at Trustee meetings, including summary statistics of respondents	Comment letters for the ED have been posted on the IASB website's project page.
Round-table meetings between external participants and members of the IASB	Optional	Number of meetings held	DPOC receives a report on outreach activities	No round-tables were held because the nature of the topic is not suitable for that way of soliciting input. Instead we relied on supplementing comment letter input through extensive outreach.
Board meetings held in public, with papers available for observers. All decisions are made in public session	Required	<p>Number of meetings held to discuss topic</p> <p>Project website contains a full description with up-to-date information on the project</p> <p>Meeting papers posted in a timely fashion</p> <p>Number of meetings with consultative group and confirmation that critical issues have been reviewed with consultative group</p>	<p>IASB discusses progress on major projects, in relation to the due process being conducted, with DPOC</p> <p>IASB and DPOC reviews its due process over the project life cycle, and how many issues regarding due process have been/are being addressed</p> <p>DPOC meets with the Advisory Council to understand perspectives of stakeholders</p> <p>DPOC reviews and responds to comments on due process as appropriate</p>	<p><b>IASB Meetings</b></p> <p>The IASB has held public meetings on general hedge accounting from September 2009 to the current meeting.</p> <p><b>Project website</b></p> <p>A project page has been in place over the course of the project. The page is current and features comprehensive project links and information.</p> <p><b>Meeting papers</b></p> <p>Agenda papers for meetings have been posted on the IASB website prior to meeting dates.</p>
Analysis of likely effects of the forthcoming IFRS or major amendment, for example, costs or on-going associated costs	Required	Publication of effect analysis	IASB reviews with DPOC results of effect analysis and how it has considered such findings in proposed IFRS IASB provides a copy of the effect analysis to the DPOC at the point of standard's publication	The draft requirements are accompanied by an extensive Basis for Conclusions that sets out what issues the Board sought to address, how it addressed them, and the expected effect of the changes.
Email alerts are issued to registered recipients	Optional	Evidence that alerts have occurred	DPOC receives a report on outreach activities	Over 22,000 participants are registered for IAS 39 email alerts. Since December 2008 eight alerts have been directly related to hedge accounting.

Step	Required/Optional	Metrics or evidence	Protocol for and evidence provided to DPOC	Action
Outreach meetings to promote debate and hear views on proposals published for public comment	Optional	Number of meetings, including efforts aimed at investors	DPOC receives a report on outreach activities	During the 3-month consultation period for the Exposure Draft IASB members and staff conducted extensive outreach. Participants were consulted across all major geographical regions of the world. More than 2,500 individuals participated in the IASB's outreach activities.
IASB organise regional discussion forums organised with national standard-setters	Optional	Number of meetings held	DPOC receives a report on outreach activities	A significant part of the outreach on hedge accounting was conducted in co-operation with national standard-setters, including discussion forums.
<b>Finalisation</b>				
Need for re-exposure of standard considered	Required	An analysis of the need to re-expose is considered at a public IASB meeting, using the agreed criteria	IASB discusses its thinking on the issue of re-exposure with the DPOC	In the September 2011 public meeting the IASB tentatively decided that re-exposure of the proposed IFRS would not be necessary. This decision will be reassessed at this IASB meeting considering feedback on the draft hedge accounting chapter.
IASB sets an effective date for the standard, considering the need for effective implementation, generally providing at least a year	Required	Effective date set, with full consideration of implementation challenges	The IASB and DPOC discuss any proposed shortening of the period for effective application	Consistent with IFRS 9 generally, an entity shall apply this IFRS for annual periods beginning on or after 1 January 2015. Earlier application is permitted. However, if an entity elects to apply this IFRS it must apply all of the requirements in this IFRS at the same time.
Drafting quality assurance steps are adequate	Required	Translations team included in review process	DPOC receives summary report on due process steps followed before an IFRS is issued	The IFRS Foundation translations staff has been consulted as part of the balloting process to take into account the need for language in the proposed document that is translatable into other languages.
Drafting quality assurance steps are adequate	Required	XBRL team included in review process	DPOC receives summary report on due process steps followed before an IFRS is issued	The IFRS Foundation XBRL staff has been consulted as part of the balloting process to take into account the need for language in the proposed document that is translatable into the IFRS XBRL Taxonomy.

Step	Required/ Optional	Metrics or evidence	Protocol for and evidence provided to DPOC	Action
Drafting quality assurance steps are adequate	Optional	Review draft made available to members of IFASS and comments collected and considered by the IASB  Review draft posted on project website	DPOC receives summary report on due process steps followed before an IFRS is issued	A draft of the forthcoming general hedge accounting requirements was posted on the IASB website on 7 September 2012.
Due process steps reviewed by IASB	Required	Summary of all due process steps discussed by the Board before an IFRS is issued	DPOC receives summary report on due process steps followed before an IFRS is issued	This document presents the project's compliance with due process, and is to be reviewed during the present IASB meeting.
<b>Publication</b>				
Press release to announce final standard	Optional	Press release announced in timely fashion Amount of media coverage of press release	DPOC receives a copy of the press release and a summary of media coverage	To be completed in due course.
Feedback statements provided, which provide high level executive summaries of the standard and explains how the IASB has responded to comments received	Required	Publication of feedback statement	IASB provides a copy of the feedback statement to the DPOC at the point of standard's publication	A feedback statement for the project will be provided in due course when the standard is finalised.
Podcast to provide interested parties with high level updates or other useful information about the standard	Optional	Number of podcasts held	DPOC receives a report on outreach activities	Seven podcasts dedicated to hedge accounting were held. These podcasts are available on the IASB website. Other podcasts addressing the entirety of IFRS 9 were also held.
IFRS published	Required	Official release	DPOC informed of release	The staff are requesting permission to prepare the Ballot Draft of the final IFRS 9, Chapter 6 Hedge Accounting at the present IASB meeting.