

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

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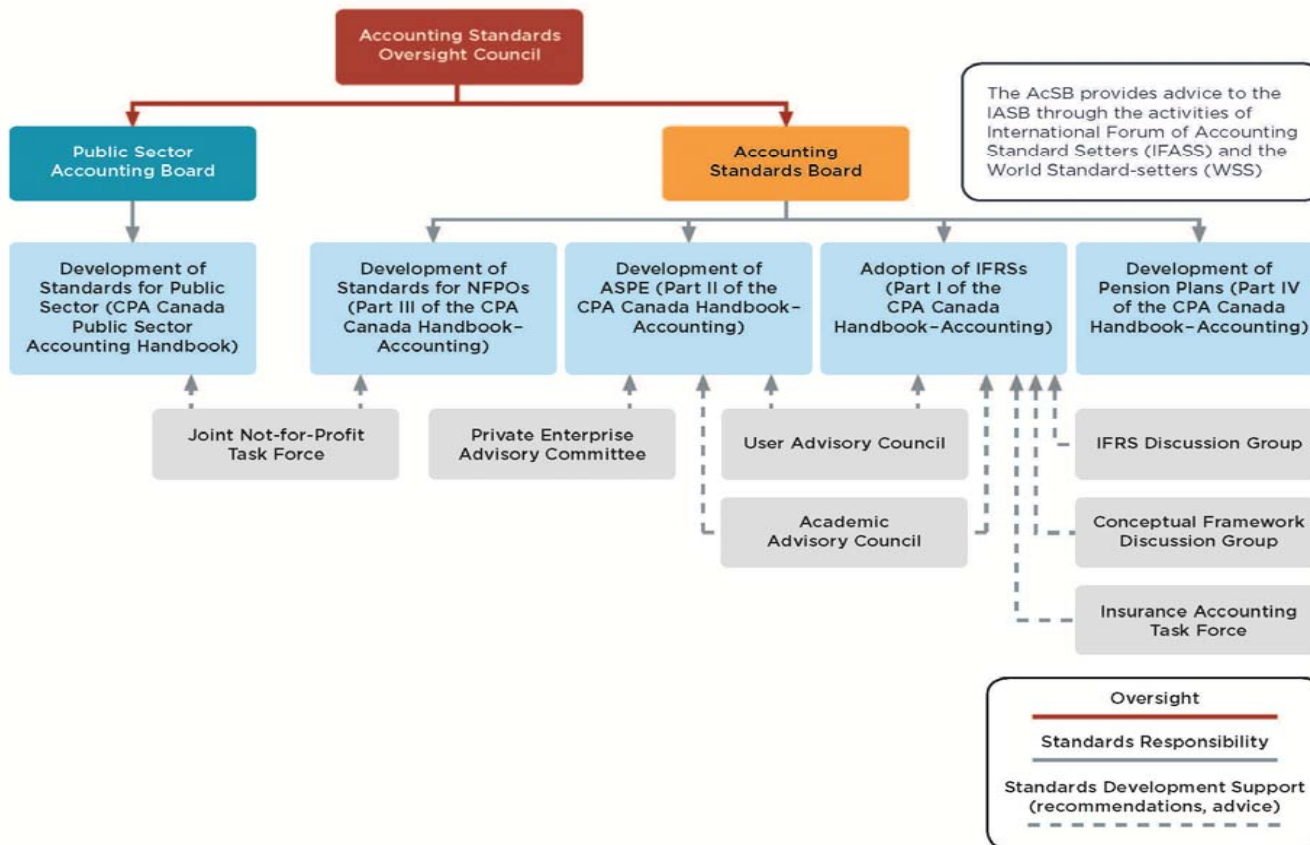
Chair, Accounting Standards Board

The views expressed in this presentation are those of the presenter, not necessarily those of the AcSB.

Overview of Outreach Conducted

- **Outreach to over 100 interested Canadian stakeholders**
 - **Financial Institutions**
 - **Insurance Companies**
 - **Oil and Gas Industry**
 - **Mining Industry**
 - **Financial Statement Users**
 - **Auditors**
 - **Academics**

Canadian Standard Setting Structure



Outreach with Financial Institutions

- **Clear interest from financial institutions due to the focus on interest rate risk**
- **Meeting with Chief Accountants Group**
- **Separate meeting with other areas within entity**
 - **Treasury Group**
 - **Risk Management Group**
- **Meeting with auditors of financial institutions**

Overall Canadian Feedback

- **Supportive of creating a standard to reflect DRM activities within an entity**
- **Reduce or eliminate hedging relationships being identified on a static basis under current hedging requirements**
- **Discussion paper focused on financial institutions**
 - **Relevance to other industries unclear**
- **Unclear if new standard or addition to current standards**

Scope

- **Risk Mitigation Approach**
 - Preferred by preparers
 - More in line with entities' risk processes
 - Reflects appropriate level of detail about risks an entity has chosen to mitigate
- **Focus on dynamic risk management**
 - Preferred by users, academics and auditors
 - Provides full transparency
 - Illustrates risks entity has chosen not to mitigate

Behavioural Factors

- **Core demand deposits**
 - **Extensive historical data is retained regarding customers' past behaviours**
- **Use of sub-LIBOR**
- **Mortgages**

Mandatory or Optional

- **Current hedging requirements are optional**
 - Inconsistent to require mandatory application
- **Define dynamic risk management**
 - Subject to interpretation within the industry and across industries

Responses to IASB questions for ASAF

In our personal views as responses have not been developed by the AcSB

Question 1- Scope of application

Focus on risk mitigation

- Useful information?
 - Provide users with insight into the risk mitigation that an entity undertakes
 - Financial Institutions are not in the business of risk avoidance but risk mitigation
 - Artificial construct to create the sub portfolio/ percentage to be used

Question 1- Scope of application

Focus on risk mitigation

- Decrease in operational complexity?
 - Reduce the need to dedesignate and redesignate
 - Tracking would be required but current systems could be modified
 - Risk management system and finance systems need to reconcile

Question 2- Revaluation

- Not a concern raised by Canadians
- Some jurisdictions manage interest rate risk on cash flow basis
 - When fixed rate products not common
 - PRA might not be appropriate for hedges of floating interest rate exposes

Question 3- Behaviouralisation

- Guidance provided should be high level
 - Flexibility should be provided to be consistent with the entity's risk management objectives
 - Consistency of factors to hedge core deposits
 - Disclosures around methodology
- Good controls over dynamic risk management processes
 - Strong requirements over extent of historical data used

Question 3- Behaviouralisation

- Pipeline transactions/ EMB
 - Preparers view as part of their dynamic risk environment
 - Interaction with the conceptual framework

Question 4- Disclosures

- Should scope disclosures differ from scope of approach?
 - Depends on approach used
 - Users want to understand the entire net interest income
 - Some want it broader to include all risks in asset/liability portfolio that is managed dynamically

Question 4- Disclosures

- Should project explore solutions based on disclosures rather recognition/measurement?
 - Conceptually easier to explain for accounting
 - Users discussed whether needs could be met by further disclosure rather than measurement