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Project update

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

Accounting Standards Advisory Forum

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Project update

- In **May 2015** the IASB discussed the next steps of the project. The IASB tentatively decided to:
  - first consider the **information needs of constituents concerning DRM activities** as a basis for determining how we may approach recognition, measurement and disclosure; and
  - prioritise the consideration of **interest rate risk** and consider other risks at a later stage in the project.

  The project will **not** be a disclosures-only project. The objective is to produce a comprehensive solution that would include recognition, measurement and disclosure requirements.

- In **July 2015** the IASB decided that the project should remain in the Research Programme, with the aim of publishing a **second Discussion Paper**.

  At the July meeting, the IASB also discussed the completeness and appropriateness of the **process for identifying information needs** of constituents relating to dynamic risk management activities for interest rate risk.

Project update

Following those public discussions, the IASB staff held discussions with some banks for the purposes of understanding their management of interest rate risk.

In particular, these discussions and further research has allowed us to gain a better understanding of how those banks model their core demand deposits (CDDs).

While we explored CDDs in the Discussion Paper, our conversations have shown that there are other nuances involved, which would be worthwhile to look at during the development of the project.

Core demand deposits—What we are learning

Our initial understanding was that banks managed the deemed interest rate risk on CDDs based on behaviour of deposits.

Customer behaviour is considered mainly in the process of identifying the ‘core’ portion of demand deposits.

Once the ‘core’ part is defined, banks typically construct replicating portfolios for the purposes of measuring the interest rate risk inherent in this funding source.

The terms of the replication portfolio of CDDs (eg tenor, coupons, number/width of tranches etc) are often a reflection of a bank’s risk management / board strategies and their view on the yield curve rather than a mere reflection of customer behaviour.

Project update

Following these discussions with banks and considering that CDDs are an integral part of the banks' risk management of Net Interest Income (NII), we are currently working on the following aspects:

- How should the accounting reflect banks' risk management activities regarding CDDs?
- If the accounting model incorporates the banks' CDD modelling, how should changes in the assumptions made in those models be accounted for?
- How should ineffectiveness be determined?

In addition to the work already done, we have learnt that the EFRAG Secretariat is exploring undertaking an outreach exercise with a group of European banks to gain a better understanding of the key drivers and parameters that banks use in their CDDs modelling. If this outreach is confirmed, we expect to participate as observers.

Questions or comments?—Thank you

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