



International Accounting Standards Board®

Press Release

For immediate release

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INTERNATIONAL ACCOUNTING STANDARDS BOARD FINALISES MACRO HEDGING AMENDMENTS TO IAS 39

The International Accounting Standards Board (IASB) today issued an Amendment to IAS 39 Financial Instruments: Recognition and Measurement on *Fair Value Hedge Accounting for a Portfolio Hedge of Interest Rate Risk*. The amendments simplify the implementation of IAS 39 by enabling fair value hedge accounting to be used more readily for a portfolio hedge of interest rate risk (sometimes referred to as a macro hedge) than under previous versions of IAS 39.

The publication of this amendment is a direct response to concerns expressed by the banking community about the potential difficulty of implementing the requirements of IAS 39. Many constituents had sought fair value hedge accounting treatment for portfolio hedging strategies, which was not previously permitted under IAS 39. In the light of these concerns, the IASB launched intensive discussions with representatives of the banking industry to determine whether a way could be found within the existing principles of IAS 39 to allow fair value hedge accounting treatment to be applied to a macro hedge.

The publication of this amendment means that macro hedging will be part of the IASB's set of standards to be adopted in 2005. The IASB notes that discussions will continue on another aspect of IAS 39, namely an additional hedging methodology and the balance sheet presentation of certain hedges—issues of particular concern to some banking institutions. Furthermore, in April, the IASB will publish a proposed limited amendment to restrict the existing fair value option in response to concerns raised by banking supervisory authorities.

With today's publication of the macro-hedging amendment, the IASB announced its intention to set up an international working party to examine the fundamentals of IAS 39 with a view to replacing the standard in due course. (A similar working party will be established on the IASB's long-term insurance project.) The financial instruments working party will assist in improving, simplifying and ultimately replacing IAS 39 and examine broader questions

regarding the application and extent of fair-value accounting—a topic on which the IASB has not reached any conclusion. Although any major revision of IAS 39 may take several years to complete, the IASB is willing to revise IAS 39 and IFRS 4 *Insurance Contracts* in the short term in the light of any immediate solutions arising from the working parties' discussions. The IASB plans to announce details of these two working parties in the coming weeks.

Introducing the amendment to IAS 39, Sir David Tweedie, IASB Chairman, commented:

This amendment is a further step in our project to ease the implementation of IAS 39 for the thousands of companies required to implement international standards in 2005 and those companies already using IFRSs. The IASB has made it clear that any amendments must be within the basic principles of hedge accounting contained in IAS 39, but that we will work within those principles to simplify the application of the standard. This amendment does not mark the end of the Board's work on the subject of financial instruments. The Board remains open to all suggestions for improvement of the standard and is taking active steps in both the immediate future and in the medium term to that end.

The primary means of publishing International Financial Reporting Standards is by electronic format through the IASB's subscriber Website. Subscribers are able to access the amendment published today through "online services". Those wishing to subscribe should contact:

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United Kingdom. Tel: +44 (0)20 7332 2730, Fax: +44 (0)20 7332 2749,
email: publications@iasb.org Web: www.iasb.org.

Printed copies of Amendment to IAS 39 Financial Instruments: Recognition and Measurement: *Fair Value Hedge Accounting for a Portfolio Hedge of Interest Rate Risk* (ISBN 1-904230-58-X) will be available shortly, at £15 each including postage, from IASCF Publications Department.

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NOTES TO EDITORS

Summary of Amendments to IAS 39 Financial Instruments: Recognition and Measurement: *Fair Value Hedge Accounting for a Portfolio Hedge of Interest Rate Risk*

The amendments improve the implementation of IAS 39 by enabling fair value hedge accounting to be used more readily for a portfolio hedge of interest rate risk (sometimes referred to as macro hedging) than under previous versions of IAS 39. In particular, for such a hedge, the amendments allow:

- (a) the hedged item to be designated as an amount of a currency (eg an amount of dollars, euro or pounds) rather than as individual assets (or liabilities).
- (b) the gain or loss attributable to the hedged item to be presented either:
 - (i) in a single separate line item within assets, for those repricing time periods for which the hedged item is an asset, or
 - (ii) in a single separate line item within liabilities, for those repricing time periods for which the hedged item is a liability.
- (c) prepayment risk to be incorporated by scheduling prepayable items into repricing time periods based on expected, rather than contractual, repricing dates. However, when the portion hedged is based on expected repricing dates, the effect that changes in the hedged interest rate have on those expected repricing dates are included when determining the change in the fair value of the hedged item. Consequently, if a portfolio that contains prepayable items is hedged with a non-prepayable derivative, ineffectiveness arises if the dates on which items in the hedged portfolio are expected to prepay are revised, or actual prepayment dates differ from those expected.
- (d) a reduction in implementation and compliance costs, because previously institutions would have to set up systems to track the relationship between either individual assets and liabilities and the hedging derivative.

Summary of due process

Accounting for financial instruments is a difficult and controversial subject. The International Accounting Standards Board's predecessor body, the International Accounting Standards Committee (IASC) began its work on the issue some 15 years ago in

1988. During the next eight years it published two exposure drafts, culminating in the issue of IAS 32 on disclosure and presentation in 1995. IASC decided that its initial proposals on recognition and measurement should not be progressed to a standard, in view of

- the critical response they had attracted,
- evolving practices in financial instruments and
- the developing thinking by certain national standard-setters.

In the meantime, IASC concluded that a standard on the recognition and measurement of financial instruments was needed urgently. It noted that whilst financial instruments were widely held and used throughout the world, few countries apart from the United States had any recognition and measurement standards for them. In addition, IASC had agreed with the International Organization of Securities Commissions (IOSCO) that it would develop a set of 'core' International Accounting Standards that could be endorsed by IOSCO for the purposes of cross-border capital raising and listing in all global markets. Those core standards included one on the recognition and measurement of financial instruments.

In March 1997, IASC, jointly with the Canadian Institute of Chartered Accountants, published a comprehensive Discussion Paper *Accounting for Financial Assets and Financial Liabilities* and invited comments on the proposals therein. IASC held a series of special consultative meetings about those proposals with various national and international interest groups and in numerous countries. Those meetings and analysis of comment letters on the Discussion Paper confirmed that IASC faced controversies and complexities in seeking a way forward. While some acceptance existed of the view put forward in the Discussion Paper—that measurement of all financial assets and liabilities at fair value was necessary to obtain consistency and relevance to users—application of that concept to some industries and to some kinds of financial assets and liabilities continued to present difficulties. Concerns focused on reliability, volatility, and the presentation of the effects of changes in values—issues that still exist. Widespread unease was also evident about the prospect of including unrealised gains, particularly on long-term debt, in income as proposed in the Discussion Paper. Furthermore, while several national standard-setters had undertaken projects to develop national standards on various aspects of recognition and measurement of financial instruments, no country had in place or proposed standards that were similar to the proposals in the Discussion Paper.

Completion of a single comprehensive International Accounting Standard on financial instruments based on the Discussion Paper for inclusion, before the end of 1998, in the core standards to be considered by IOSCO was not a realistic possibility. Nonetheless, the ability to use International Accounting Standards for investment and credit decisions and securities offerings and listings was urgent for both investors and business enterprises. Moreover, while financial instruments are widely held and used throughout the world, only a very few countries had any national recognition and measurement standards at all for financial instruments.

Accordingly, in 1997 IASC decided:

- (a) to join with nine national standard-setters to form a Joint Working Group (JWG) to develop the proposals in the 1997 discussion paper. The ultimate aim was an integrated and harmonised standard on financial instruments that would reflect the best research and thinking on the subject worldwide. IASC recognised that this would

take several years to develop. The JWG took the first step in the form of a draft standard published in 2000, before the IASB had been constituted.

- (b) at the same time, to develop an International Accounting Standard on the recognition and measurement of financial instruments that would serve until an integrated comprehensive standard was completed. This standard would be based on US GAAP—the only major GAAP with comprehensive requirements for financial instruments. The result was IAS 39, issued in 1999 after a period of exposure and comment.

In August 2001 the International Accounting Standards Board (IASB) announced, as part of its initial agenda, that it would undertake a project to improve IAS 32 and IAS 39 to simplify application and implementation of the Standards.

The Board invited the IAS 39 Implementation Guidance Committee (IGC) to function as an Advisory Committee to the Board in identifying and reviewing issues that should be addressed. The IGC consisted of senior experts in financial instruments with backgrounds as accounting standard-setters, auditors, bankers, and preparers from a range of countries as well as observers from the Basel Committee on Banking Supervision, the International Organization of Securities Commissions (IOSCO), and the European Commission.

In June 2002 the IASB published an Exposure Draft of proposed improvements to IASs 32 and 39. In response to the Exposure Draft the IASB received over 170 comment letters. In view of this response, the IASB decided to extend the consultation by conducting a series of roundtable discussions.

Roundtables are not a routine part of the IASB's due-process procedures. Rather, the Board decides to hold these public discussions with constituents when it appears that the development of an accounting standard would benefit from a fuller public discussion of the issues involved. The Board decided to use the roundtable format to allow a free and open exchange of views between the Board and respondents and among respondents who may hold differing views. The Board's ultimate goal was to determine whether there were better alternative applications of the principles underlying IASs 32 and 39, or whether these existing applications could be simplified. Because of time constraints imposed by the 2005 adoption in some jurisdictions, the IASB did not have sufficient time to reassess the fundamental principles behind existing practices. The roundtable participants included 108 of the over 170 individuals, companies, regulatory bodies, and other organisations that had commented on the Exposure Drafts of proposed amendments to IAS 32 and IAS 39.

Following the roundtable discussions the Board began the process of public discussions by reviewing the roundtable material with its Standards Advisory Council and with its partner national standard-setters.

In March 2003 the IASB began its deliberations, in open Board meetings, of the issues raised on the Exposure Draft, keeping in view the insights obtained from the consultation process. There was one issue that had emerged from the consultation process for which the Board decided warranted further debate. Many constituents, particularly in the banking industry, expressed concern that portfolio hedging strategies they regarded as effective hedges would not qualify for fair value hedge accounting under IAS 39.

In light of these concerns, the IASB launched intensive discussions with the banking industry, represented by the European Banking Federation (FBE) to see if a way could be

found within the principles of IAS 39 to accommodate macro hedging. As a result, in August 2003, the IASB published a second Exposure Draft, *Fair Value Hedge Accounting for a Portfolio Hedge of Interest Rate Risk*, on this one aspect of IAS 39, proposing an important advance by permitting macro hedging. More than 120 comment letters were received.

However, in order to help those companies preparing to adopt the revised IAS 32 and IAS 39 in 2005, the Board decided not to delay the finalisation of the rest of the Standards for this one issue. Accordingly, the Board issued the revised Standards, subject to any amendments it might make for macro hedging, in December 2003.

About the IASB

The International Accounting Standards Board (IASB), based in London, began operations in 2001. It is funded by contributions collected by its Trustees, the IASC Foundation, from the major accounting firms, private financial institutions and industrial companies throughout the world, central and development banks, and other international and professional organisations. The 14 Board members (12 of whom are full-time) reside in nine countries and have a variety of functional backgrounds. The Board is committed to developing, in the public interest, a single set of high quality, global accounting standards that require transparent and comparable information in general purpose financial statements. In pursuit of this objective, the Board cooperates with national accounting standard-setters to achieve convergence in accounting standards around the world.

Upon its inception the IASB adopted the body of International Accounting Standards (IASs) issued by its predecessor, the International Accounting Standards Committee.