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Beyond the GAAP

Mazars' newsletter on accounting standards

Contents

Editors in chief:
Michel Barbet-Massin, Edouard Fossat

Columnists:
Vincent Guillard, Egle Mockaityte, Arnaud Verchère and Mathieu Vincent.

Contact us:
Laurence Warpelin, Head accounting standards
laurence.warpelin@mazars.ch
Tél. : +41 21 310 49 03

Denise Wipf, Director
denise.wipf@mazars.ch
Tél. : +41 44 384 93 75

www.mazars.com

Editorial

November 2013 saw the publication of the final standard on hedge accounting that constitutes phase 3 of IFRS 9, and which is explained in full detail in this issue of Beyond the GAAP. This standard represents a significant new direction for IFRSs, with a greater focus on entities' operational risk management policy. From now on, the accounting treatment must be adapted to fit the management policy, rather than the other way around. This is the first step towards a "business model" approach that many have called for, and that is currently being discussed as part of the *Conceptual Framework* project.

In addition, the IASB launched a *Post-Implementation Review* to gather information on the relevance and usefulness of the financial information resulting from application of IFRS 3 - *Business Combinations.* Stakeholders are asked for their opinion on separate recognition of intangible assets at fair value, recognition of non-controlling interests, step acquisitions and partial disposals, among other things. However, it is not yet known how the information gathered will be used, as IFRS 3 is a US GAAP converged standard.

Happy reading!

Michel Barbet-Massin Edouard Fossat

IFRS Standards

FAF to fund completion of joint FASB and IASB projects

On 28 January 2014, the FAF (Financial Accounting Foundation), which oversees the FASB (Financial Accounting Standards Board), announced that it would make a one-off contribution of $3m to the IFRS Foundation to aid the completion of the four main convergence projects which the FASB is undertaking jointly with the IASB. The joint projects cover revenue recognition, leases, insurance contracts and financial instruments.

IASB launches post-implementation review of IFRS 3

On 30 January 2014, the IASB launched the public consultation phase of the post-implementation review of IFRS 3 - *Business Combinations*, by publishing a Request for Information (RfI). The comment period is open until 30 May 2014.

The IASB wants to gather feedback on application of the standard, any difficulties or costs involved in implementing it, and whether it provides useful information for users of financial statements.

The IASB also announced in the RfI that it will undertake outreach activities internationally to gather more detailed information on the effect of IFRS 3.

The RfI is available on the IASB's website via the following link:
http://www.ifrs.org/Current-Projects/IASB-Projects/PIR/PIR-IFRS-3/Request-for-Information-January-2014/Documents/RfI_PIR_IFRS3-Business-Combinations.pdf

IFRS/US GAAP convergence on financial instruments seems unlikely following latest FASB decisions

Plenary meetings in December 2013 and January 2014 saw the US standard-setter (FASB) reverse the decisions made last year on the classification of financial assets. It has now decided not to use the "principal and interest" (P&I) and "business model" criteria that were developed jointly with the IASB.

The FASB also decided at these meetings to retain the existing US GAAP rules on the bifurcation of derivatives embedded in hybrid assets. The US standard-setter has announced that it will work alone on the remaining issues relating to the classification of financial assets under the current US accounting framework. The FASB will be looking particularly at the new classification criteria based on the contractual cash flows characteristics assessment for non-derivative financial instruments.

Attempts to achieve convergence between IFRS and US GAAP on impairment of financial instruments (Phase 2 of IFRS 9) had already failed in 2013 after the FASB decided to develop its own model, under which the impairment allowance takes account at the outset of full lifetime expected credit losses. However, the latest FASB decisions seem to have finally sounded the death knell for convergence between the IFRS and the US GAAP on financial instruments.

IASB approaching completion of IFRS 9 project

At its plenary meeting in January 2014, the IASB discussed the transition requirements and disclosures to be made in the notes for Phase 1 – *Classification and Measurement* and Phase 2 – *Impairment* of the IFRS 9 project. Readers will remember that the future standard will eventually replace the current IAS 39 requirements on financial instruments.

In particular, the IASB has decided to clarify the rules on early application of IFRS 9 (cf. our Highlights item on the subject in issue 72 of Beyond the GAAP). They can be summarised as follows:

- The various phases of IFRS 9 may be applied early as they are published;
- However, entities will not be permitted to early apply a previous version of IFRS 9 if their date of initial application is six months or more after the completed version of IFRS 9 is issued. This means that once the complete final standard has been published for six months, early application of IFRS 9 will only be permitted as long as all phases of the project are applied early in their entirety;
- Entities which have early applied a previous version of IFRS 9 before the "6-month window" expires may continue with their existing approach until the completed version of IFRS 9 becomes mandatorily effective (scheduled for 2017 *a priori*).

However, the macro-hedging chapter will have its own standard. Until it is completed, the hedge accounting requirements of IFRS 9 will remain optional. This means that companies may opt to retain the hedge accounting requirements of IAS 39 during the transition period.

Finally, readers should also remember that the European Union has not yet made any announcements regarding the adoption of this standard or the relevant effective dates.

The publication of final standard IFRS 9 is scheduled for the second quarter of 2014 (assuming that the *Impairment* phase is not re-opened for comment).

IASB publishes interim standard on rate-regulated activities

On 30 January 2014, the IASB published an interim standard on rate-regulated activities, entitled IFRS 14 - *Regulatory Deferral Accounts*.

The goals of this interim standard are:

- to allow first-time adopters to continue to use local standards when recognising regulatory assets and liabilities;
- to require entities to present regulatory deferral account balances as a separate line item in the statement of financial position, and movements over the period as a separate line item in the statement of profit or loss and other comprehensive income;
- to require entities to disclose information that enable users to understand the nature of, and the risks associated with, the rate regulation that has given rise to the recognition of regulatory deferral accounts, and to assess the effects of that rate regulation on the financial statements.

Aside from the fact that this standard targets rate-regulatory activities, it is of limited scope in that it only affects first-time adopters. It may not be used by entities that already present their financial statements under IFRS, even if local accounting standards require the recognition of regulatory assets and liabilities.

It should also be noted that this interim standard is not mandatory. A first-time adopter may opt not to apply it when transitioning to IFRS, in which case it will not recognise any regulatory assets or liabilities in its initial IFRS financial statements.

Finally, the IASB has set the effective date for this standard at 1 January 2016. Early application is permitted.

Concurrently with the publication of this standard, the IASB is continuing to work on the IFRS accounting treatment for rate-regulated activities. A *Discussion Paper* is scheduled for the second quarter of 2014.

Europe

EFRAG publishes results of field test on *Insurance Contracts* exposure draft

On 15 January 2014, the EFRAG published the results of its field test on the impact in practice of applying the draft standard on insurance contracts, which was published by the IASB last June. The field test was carried out in conjunction with the French, German, Italian and British standard-setters (the ANC, ASCG, OCI and FRC, respectively).

The report can be accessed on the EFRAG's website via the following link:
http://www.efrag.org/Front/n1-1255/EFRAG-s-report-on-the-findings-from-the-field-test-on-the-revised-IASB-ED-Insurance-Contracts.aspx

A Closer Look

Revision of hedge accounting under IFRS: publication of IFRS 9 final standard on general hedge accounting

After five years in the pipeline, the IASB has completed the hedge accounting phase of its project to replace IAS 39. The concrete evidence of progress appeared on 19 November 2013 in the form of an amendment to IFRS 9 to integrate the section on the general hedge accounting model (micro-hedging).

The publication of the IFRS 9 final standard comes just over a year after the IASB published a review draft on micro-hedging on its website (7 September 2012).

A review draft is an optional stage in the IASB's due process, with the three main goals of:

- giving stakeholders the opportunity to comment on the clarity and intelligibility of the document;
- allowing the US standard-setter (FASB) to study the IASB's proposals on general hedge accounting with a view to convergence; and
- giving the IASB itself the time required to complete outreach activities with stakeholders.

Beyond the GAAP has identified the key changes introduced by IFRS 9 in comparison with the current IAS 39. This article will also identify changes made from the review draft published on 7 September 2012.

1. What is the stated objective of IFRS 9?

The stated objective of IFRS 9 is to ensure that hedge accounting reflects the reporting entity's risk management policy. To this end, the standard proposes several positive changes for entities, including:

- An increase in the range of hedged items which are eligible;
- More flexible criteria for effectiveness;
- The introduction of the concept of "rebalancing";
- Treating time value, forward elements and FX basis spreads as hedging costs;
- Extension of the fair value option when hedge accounting is not applicable.

IFRS 9 states that, despite the goal of ensuring that hedge accounting reflects the risk management policy, the designation of hedging relationships for accounting purposes does not have to be identical to risk management in practice. Thus, for example, hedge accounting will remain optional. However, hedge accounting designations must be "directionally consistent" with the actual risk management policy.

Readers will remember that the review draft already had the stated objective of ensuring that hedge accounting reflected the reporting entity's risk management policy. However, some stakeholders queried whether this would in practice prevent entities from designating hedging relationships under IFRS if the accounting designation differed slightly from the actual risk management. For example:

- *designating the hedged risk on a gross basis when the risk management is carried out on a net basis (hedging on a net basis is limited to foreign exchange risk in the case of cash flow hedges under IFRS 9);*
- *applying hedge accounting to the entire fair value of a hedged item when the risk management approach applies to only one risk component (which is not eligible for hedge accounting individually).*

The new IFRS 9 standard clarifies these issues.

2. What are the criteria for using hedge accounting under IFRS 9?

Under IFRS 9, hedge accounting remains optional and is subject to certain conditions. As under IAS 39, IFRS 9 requires the following five criteria to be met in order for hedge accounting to be used:

- condition 1: The type of hedging relationship must be eligible;
- condition 2: The hedging instrument must be eligible;
- condition 3: The hedged item must be eligible;
- condition 4: The effectiveness criteria must be met; and
- condition 5: The hedging relationship must be documented from inception.

The broad approach therefore remains identical to IAS 39, but some changes have been made within this general context.

3. The impact of IFRS 9 on types of hedging relationship and their accounting treatment

What is the impact of IFRS 9 on types of hedging relationship?

IFRS 9 retains the same three types of hedging relationship as IAS 39:

- fair value hedge (FVH);
- cash flow hedge (CFH); and
- hedge of a net investment in a foreign operation (NIH).

These three types of hedging relationships will continue to be applicable in the same situations as under the current IAS 39.

What is the impact of IFRS 9 on the accounting treatment for hedging relationships?

In most cases, the accounting treatment will also remain the same as under IAS 39.

It should however be noted that basis adjustment[1] is now required for cash flow hedges when the hedged transaction involves recognising a non-financial asset or liability in the statement of financial position; this was optional under IAS 39.

[1] Basis adjustment involves including the hedging gain or loss in the initial carrying amount of the hedged non-financial asset or liability in the statement of financial position.

4. The impact of IFRS 9 on eligible hedging instruments

What impact does IFRS 9 have on the eligibility of derivatives as hedging instruments?

IFRS 9 does not change the conditions under which a derivative may be designated as a hedging instrument (provisions related to internal derivatives, written options, etc.).

However, the future standard does clarify that a combination of two separate options – a purchased and a written option – constitutes an eligible hedging instrument as long as the combination of the two options does not constitute a net written option[2]. As long as this condition is met, a combination of a purchased cap option and written floor option may be designated as a hedging instrument under IFRS 9, even if the two options are separate contracts with different inception dates.

[2] Readers will remember that under IAS 39, combinations of options are not eligible as hedging instruments if one of the contracts is a written option.

What impact does IFRS 9 have on the eligibility of non-derivative financial instruments as hedging instruments?

Under IAS 39, non-derivative financial instruments were only eligible as hedging instruments for foreign exchange hedges.

IFRS 9 introduces the option of designating any non-derivative financial instrument as a hedging instrument, as long as it is measured at fair value through profit or loss.

The following points should also be noted:

- debts measured at fair value using the fair value option in IFRS 9 are not eligible as hedging instruments, as their credit risk component is adjusted through OCI rather than through profit or loss;
- IFRS 9 also clarifies that an intragroup foreign currency loan may not be designated as a hedging instrument for foreign exchange risk.

5. The impact of IFRS 9 on eligible hedged items

Hedging risk components (non-financial instruments)

Under IAS 39, a non-financial instrument could be designated as a hedged item in its entirety or for its foreign exchange risk only. IFRS 9 relaxes these rules significantly by permitting a risk component to be designated as a hedged item, as long as it is:

- separately identifiable; and
- reliably measurable.

We believe that this significantly expands the possibilities for commodity risk hedging (e.g. the lead element of a battery, in certain situations).

Hedging aggregated exposures

IFRS 9 permits the option of hedging aggregated exposures composed of an exposure and a derivative.

This means that the accounting treatment can better reflect the entity's risk management each time that a treasurer adds a derivative to an existing strategy.

Hedging on a net basis

IFRS 9 permits the option of hedging on a net basis, once again allowing for a better match between accounting treatment and risk management for entities which frequently use this type of arrangement in order to reduce hedging costs.

However, this new option is strictly limited to specific situations:

- in the case of cash flow hedges, hedging on a net basis is only permissible if it is a hedge of foreign exchange risk. The hedging documentation must specify the cash flows which make up the net position and the reporting periods in which the hedged items are expected to have an impact on profit or loss;
- the performance of the hedging instrument must be presented in a separate line item in the statement of profit or loss; in other words, recognition of hedged cash flows on a net basis at the hedged rate is not permitted.

Layer approach extended to fair value hedges

IFRS 9 permits the use of a layer approach on condition that:

- the "layer" can be identified; and
- the designation of the "layer" component reflects the entity's operational risk management.

Thus, for example, an entity may wish to hedge the last €20m of a debt with a nominal amount of €100m. If this debt includes a prepayment option, the layer approach is permitted as long as the effectiveness calculation takes account of this option.

Hedging risks which have no impact on profit or loss is still forbidden

Under IFRS 9, it is still forbidden to hedge risks which have no impact on profit or loss. However, the standard does introduce one exception, permitting fair value hedges of investments in equity instruments measured at fair value through other comprehensive income as set forth in IFRS 9.

The following types of exposure are still not eligible for hedge accounting under IFRS:

- the entity's own treasury shares (notably shares repurchased in the context of share-based payments under IFRS 2);
- future dividends from subsidiaries; and
- IAS 19 actuarial gains and losses.

Hedging closed portfolios: more flexibility and new criteria

The current criteria for designating a group of instruments as a hedged item under IAS 39 are as follows:

- each item in the portfolio shares the same hedged risk; and
- the change in fair value attributable to the hedged risk for each individual item in the group shall be expected to be approximately proportional to the hedged risk of the group of items.

IFRS 9 eliminates these criteria and replaces them with the following:

- each item is individually eligible to be a hedged item; and
- the items in the group are managed together on a group basis as part of the entity's risk management.

The removal of the "approximately proportional" criterion is a big step forward, particularly for fair value hedges of equity portfolios using index-linked derivatives.

Sub-LIBOR issue still not resolved

IFRS 9 still forbids the hedging of a risk component which could generate cash flows greater than the total flows of the hedged item (known as the "sub-LIBOR issue"). This rule lies at the heart of the European carve-out of IAS 39.

IFRS 9 stipulates that this applies to both financial and non-financial items:

- Financial items: it is not possible to hedge the LIBOR component of a debt instrument which bears interest of LIBOR minus 20 basis points with a floor at zero basis points.
- Non-financial items: it is not possible to hedge the MATIF component of a grain that is priced at MATIF minus €10 with a floor at €15.

Hedging inflation risk

IFRS 9 no longer contains an outright ban on hedging an inflation risk component which is not contractually specified.

However, the standard points out that there is a strong presumption that inflation risk is not separately identifiable and reliably measurable. It is therefore incumbent on the entity to prove the opposite with reference to specific characteristics of the market environment.

For example, a sufficiently liquid inflation-linked bond market may in certain cases mean that the inflation risk is separately identifiable and reliably measurable.

Hedging credit risk

IFRS 9 introduces a more flexible fair value option so that an instrument's credit risk hedging can be reflected in the entity's financial statements. Thus, for example, an entity using a credit derivative (such as a CDS) to hedge the credit risk on a financial instrument may optionally measure the entirety of the hedged instrument at fair value through profit and loss. This is subject to the following conditions:

- the entity's counterparty risk management approach is actually based on use of the credit derivative;
- the name of the credit exposure matches the reference entity of the credit derivative[3]; and
- the seniority of the hedged instrument matches that of the instruments that can be delivered in accordance with the credit derivative.

This fair value option, which is restricted to credit risk hedges, may be exercised prospectively at any time and is not limited to the date of initial recognition of the instrument. It will also cease prospectively if the criteria are no longer met.

[3] Thus, this option does not permit hedging using a portfolio or index-linked CDS.

Hedging commodity risk on own-use contracts

"Own-use" contracts are those which involve purchasing or selling of non-financial items (goods) resulting in the physical receipt or delivery of goods in order to meet the entity's production requirements. These contracts fall outside the scope of IAS 39, meaning they are not accounted for as derivatives.

Some industrial companies use derivatives to hedge these contracts for the purchase or sale of goods, as part of their risk management strategy. The high volume of transactions and the constant changes in net exposure mean it is very difficult to apply hedge accounting. To make things easier, IFRS 9 has extended the fair value option for own-use contracts.

Using the fair value option allows an entity to reduce the accounting mismatch between:

- own-use contracts which are off-balance-sheet commitments; and
- hedging derivatives which are recognised at fair value through profit or loss.

6. The impact of IFRS 9 on effectiveness criteria

IFRS 9 makes big improvements to the criteria for effectiveness and reduction of volatility in profit or loss linked to hedging operations.

What are the new effectiveness criteria under IFRS 9?

The 80%-125% range, which was often felt to be arbitrary, has been eliminated. It has been replaced by three effectiveness criteria which take greater account of the entity's risk management policy:

- criteria 1: There is an economic relationship between the hedged item and the hedging instrument (inverse correlation);
- criteria 2: Changes in the value of the derivative are not primarily due to changes in the credit risk of the parties to the derivative transaction[4];
- criteria 3: The hedge ratio[5] corresponds to the ratio which is actually used by the entity in its operational risk management, and does not show an obvious imbalance (e.g. an imbalance which would create structural hedge ineffectiveness).

[4] In practice, this makes it difficult to designate as a hedging instrument a derivative entered into with a party with severe financial difficulties.

[5] Hedge ratio: the relationship between the quantity of hedged items and the quantity of hedging instruments.

These criteria should be considered at the inception of the hedging relationship and at each closing date. In addition, the entity must also carry out an effectiveness test if a significant event changes the balance of the hedging relationship during the reporting period.

These assessments are only carried out prospectively. Retrospective effectiveness tests have been removed from the standard. However, readers should note that it will still be necessary to quantify hedge ineffectiveness for the period and recognise it in profit or loss.

What is rebalancing?

Rebalancing involves adjusting the hedge ratio of an existing hedging relationship to bring it back into line with the effectiveness criteria (cf. criterion 3 above). In our opinion, rebalancing will primarily apply to hedging relationships which operate on a proxy basis.

Let us take the example of an entity which is hedging an MXN (Mexican peso) exposure, using USD derivatives.

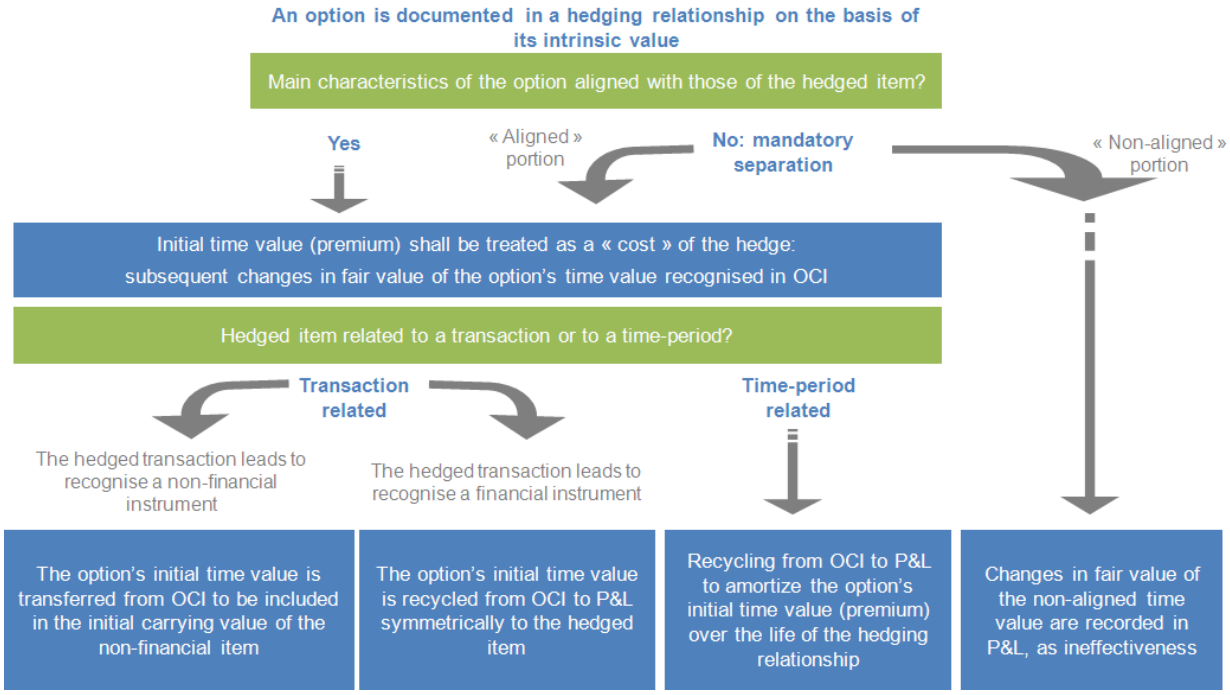
- The entity has made this decision for cost reasons (the USD derivatives market is more liquid);
- It is also able to identify a stable relationship (correlation) between the two currencies;
- The entity will therefore use its correlation analysis to determine the quantity of USD required to hedge its MXN exposure with a view to minimising ineffectiveness;
- The relationship between the quantity of USD and the quantity of MXN constitutes the hedge ratio;
- Rebalancing allows the entity to adjust the hedge ratio in the event of a subsequent change in the correlation between USD and MXN.

Rebalancing is obligatory when the hedge ratio is such that the hedging relationship no longer meets the effectiveness criteria, but the objectives of the hedging relationship remain the same. The purpose of rebalancing is to correct structural changes in the hedge ratio. Temporary variations in the current ratio do not necessarily require adjustment of the ratio. It will often be necessary to resort to subjective judgement in this domain.

For accounting purposes, rebalancing is treated as an extension to an existing hedging relationship. Adjusting the ratio does not entail a discontinuation of the existing hedging relationship. It should however be noted that the entity must calculate the ineffectiveness of the hedging relationship and recognise it in profit or loss before changing the hedge ratio.

How is the time value of options accounted for under IFRS 9?

The effectiveness of a hedging relationship may be maximised by designating only the intrinsic value (and not the time value) of an option as the hedging instrument. This meant that under IAS 39, the time value of options generated volatility in profit or loss that was not connected to the entity's risk management. Under IFRS 9, if an option is designated as a hedging instrument on the basis of its intrinsic value alone, its time value must be treated as a "cost" of hedging for accounting purposes.



How is the forward element of forward contracts accounted for under IFRS 9?

IFRS 9 introduces an option which permits entities to account for the forward element of a forward contract as a "cost" of hedging, when the forward contract is designated as a hedging instrument on the basis of its spot element alone. The forward element of a forward contract is therefore accounted for in the same way as the time value of options.

The entity may decide whether or not to do this on a transaction by transaction basis.

We feel that this significantly expands the possibilities for commodity risk hedging (e.g. the lead element of a battery, in certain situations).

As a reminder: the review draft stated that, if an entity opted to account for the forward element of a forward contract as a "cost" of hedging, it must then amortise the forward element over the lifetime of the hedging relationship. The review draft did not distinguish between transaction-related hedged items and time-period-related hedged items.

How are FX basis spreads accounted for under IFRS 9?

FX basis spreads represent market participants' relative preference for a given currency (e.g. investors favour USD over EUR).

Since the financial crisis in 2008, market participants have taken this risk component into account when measuring

currency derivatives. This risk component is present in derivatives but not necessarily in hedged items: it is therefore a potential source of hedge ineffectiveness.

IFRS 9 explicitly prohibits entities from taking FX basis spreads into account when determining the hypothetical derivative to be used in effectiveness tests (the hypothetical derivative may not be used to include risk components which are not present in the hedged item).

However, IFRS 9 allows entities to account for FX basis spreads as a "cost" of hedging (like the forward element of a forward contract or the time value of options). In practice, this means that entities should recognise changes in the value of the hedging derivative relating to the FX basis spread in other comprehensive income rather than in profit or loss.

As with forward elements, the entity may decide whether or not to do this on a transaction by transaction basis.

Readers will remember that the review draft did not permit entities to account for FX basis spreads as a "cost" of hedging.

7. Other changes introduced by IFRS 9

Documentation requirements retained and updated

Entities are still required to document hedging relationships. IFRS 9 stipulates that hedging documentation must include the following elements:

- The strategy and objectives of the hedging policy;
- Identification of the hedged item;
- Identification of the hedging instrument;
- Identification of the risk being hedged;
- A description of the methods used for prospective effectiveness tests;
- An analysis of the sources of hedge ineffectiveness (new requirement);
- The method of determining the hedge ratio (new requirement, cf. paragraph on rebalancing).

An entity may not simply choose to discontinue a hedging relationship

IFRS 9 stipulates that an entity may not discontinue a hedging relationship if:

- the hedging relationship still meets the entity's management objective for the hedging relationship; and
- the hedging relationship still meets the eligibility criteria (after mandatory rebalancing has been taken into account).

Henceforth, all other things being equal, an entity may only choose to discontinue a hedging relationship if the objective of the hedging relationship has changed. It should be noted that IFRS 9 distinguishes between the hedging "strategy", which refers to the entity's general risk management principles, and the hedging "objectives", which are decisions taken at an operational level. Thus, in practice, the objectives may change more frequently than the strategy.

Finally, if the entity decides to settle the hedging derivative in cash, the relationship will *de facto* be prospectively discontinued.

What disclosures shall be made in the notes?

Given that the effectiveness criteria have been made more flexible in order to take greater account of the entity's risk management policy, it is necessary to provide more information on this policy in the notes to the financial statements.

Therefore, IFRS 9 also introduces amendments to IFRS 7, in the form of additional disclosures required in the notes:

- The risk management strategy;
- The amount, timing and uncertainty of future cash flows (new requirement);
- The impact of hedge accounting on the financial statements;
- Specific information on dynamic hedges (new requirement); and
- Specific information on credit risk hedges (new requirement).

These disclosures are only required if the entity uses hedge accounting. The information may be presented in the notes to the financial statements or incorporated by cross-reference.

8. Date of initial application and transition requirements

What is the date of initial application for the hedging section of IFRS 9?

The mandatory effective date of 1 January 2015 has been cancelled following the publication of the amendment to IFRS 9 in November 2013. No new date has been set yet.

At its plenary meeting in November 2013, the IASB:

- clarified that it will not be able to set a new date for initial application of IFRS 9 until phases 1 (classification and measurement) and 2 (impairment) are completed; and
- confirmed that the mandatory effective date for IFRS 9 will be no earlier than 1 January 2017, to allow preparers of financial statements to better plan the transition.

However, the publication of the IFRS 9 final standard will allow preparers of financial statements to start considering the impact on their risk management policy, the organisation of their treasury department and the accounting treatment of their hedging operations.

Readers will remember that the review draft stipulated that the standard would be mandatory for financial periods starting on or after 1 January 2015.

The relationship between micro- and macro-hedging under IFRS 9

The IASB has chosen to break down its proposals on hedge accounting into two parts:

- The general hedge accounting model (micro-hedging), which is the subject of the 19 November 2013 amendment to IFRS 9 presented above; and
- Hedging in the context of open portfolios (macro-hedging).

The IASB has decided to address macro-hedging in a separate standard so as not to delay the completion of IFRS 9. A *Discussion Paper* on macro-hedging is scheduled for the first quarter of 2014.

The IFRS 9 final standard will introduce a choice of two different accounting methods that can be used for all hedging relationships. The two options are:

- To apply hedge accounting as set out in IFRS 9, while retaining the option of using IAS 39 for the specific case of fair value hedges of a portfolio's interest rate risk exposure; or
- To continue applying the principles of IAS 39 until the macro-hedging project is completed.

In practice, this choice of accounting methods may lead some companies to delay first-time application of the hedge accounting section of IFRS 9.

It should be noted that the new disclosures on hedge accounting required in the notes will be incorporated into IFRS 7. The new requirements will therefore apply to all entities, whether they use IAS 39 or IFRS 9 for their hedge accounting.

As a reminder: the review draft removed all the paragraphs of IAS 39 which related to hedge accounting, except those relating to fair value hedging of a portfolio's interest rate risk exposure (81A, 89A and AG113-AG132). The draft stipulated that issuers of financial statements could continue to apply these provisions until the future standard on macro-hedging became available.

What are the transition requirements?

IFRS 9 specifies prospective application with a limited-scope exception for the rules on the accounting treatment for the time value of options and the forward element of forward contracts, which shall (or may, in certain cases) be applied retrospectively.

In addition, to avoid a phase-in transition period during which two accounting methods could co-exist for the same type of contract, IFRS 9 allows entities to use the fair value option for existing own-use contracts at the date of initial application of IFRS 9, as long as the option is applied to all contracts of the same type.

Readers will remember that the review draft did not specify any particular transition requirements for own-use contracts. Thus, in practice, the fair value option was only available for contracts signed after the date of initial application of IFRS 9 (as the fair value option must be applied from the inception of a contract).

Events & FAQ

Frequently asked questions

IFRS

- Partial sale of securities: IFRS 5 accounting treatment at the closing date and control held subsequently.
- Substance of a deadlock clause and impact on the conclusion in terms of control.
- Identification of joint control over an entity under IFRS 11 when one of the two partners is not a shareholder immediately, but has rights due to a convertible debt security.
- Hedging investments in OATi inflation-linked government bonds.
- Accounting treatment of planned termination of a business activity under IFRS 5.
- The accounting impact of implementing a profit-sharing plan.

Upcoming meetings of the IASB, IFRS Interpretations Committee and EFRAG

IASB	Committee	EFRAG
19 - 20 February 2014	25 - 26 March 2014	26 - 28 February 2014
14 - 21 March 2014	13 - 14 May 2014	2 - 4 April 2014
22 - 25 April 2014	15 - 16 July 2014	7 - 9 May 2014