IASB daily staff *Update*—30 January 2013

The International Accounting Standards Board began its public meetings for this month on Tuesday 29 January, 2013, at the IASB offices in London, UK. The meetings will conclude on Thursday 31 January.

This staff update is a draft summary of decisions taken by the IASB at today's meeting. These decisions are tentative and may be subject to change in future meetings. A final summary will be published in IASB *Update* shortly after the January meetings conclude.

The topics discussed at today's IASB meeting were:

- **Financial Instruments: Hedge Accounting**
- **Matters arising from the IFRS Interpretations Committee: Hedge Accounting**
- **Revenue Recognition**
- **Insurance Contracts**
- **Leases**

Previous sessions

Rate regulated Activities (IASB-only education session)

The IASB held an education session on 29 January 2013 to continue its discussions about a proposal for an interim IFRS for Rate-regulated Activities that would allow entities adopting IFRS to continue to use their local GAAP requirements for rate-regulated activities until the main project is completed. The IASB discussed proposals for the scope of the [draft] interim Standard, as well as proposals for grandfathering, impairment, presentation, disclosure and transition.

No decisions were made.

Next steps

The IASB will continue its discussions on the proposals for the [draft] interim Standard for Rate-regulated Activities at their meeting on Thursday 31 January 2013.

Leases (IASB-only education session)

The IASB held an education session on 29 January 2013 to discuss questions that have arisen during the drafting of the revised *Leases* Exposure Draft about the identification of lease components and the unit of account when applying the classification guidance.

No decisions were made.

Next steps

The IASB will discuss the above issues in a joint meeting with the FASB on 30 January 2013.

Today's sessions

Financial Instruments: Hedge Accounting

On 7 September 2012 a draft of the forthcoming hedge accounting requirements (draft requirements) was posted on the IASB website. This was part of an extended fatal flaw process.

At this meeting the IASB discussed three issues that were raised in comments on the draft requirements:

1. Using 'hypothetical derivatives' to measure the change in the value of the hedged item.
2. The transition requirement for designation of 'own use' contracts as at fair value through profit or loss.
3. The scope of the draft requirements and the interaction with macro hedging activities.

Using 'hypothetical derivatives' to measure the change in the value of the hedged item

The IASB discussed what use of 'hypothetical derivatives' was appropriate for hedge accounting purposes. The discussion focused in particular on the nature of FX basis spreads and whether they can be considered to represent costs of hedging. The IASB noted that the appropriate use of a 'hypothetical derivative' is to represent the hedged item (instead of representing the 'perfect hedge'). The IASB retained this notion of a 'hypothetical derivative' that was included in the draft requirements but tentatively decided to expand the notion of 'costs of hedging' so as to accommodate FX basis spreads by:

a. expanding the existing draft requirement regarding the forward elements of forward contracts so that it also covers FX basis spreads; and
b. aligning the structure with that used for the accounting for the time value of options.

The IASB was concerned that using a broader principle for costs of hedging could result in some types of hedge ineffectiveness being inappropriately deferred in other comprehensive income as costs of hedging. Consequently, the IASB limited its decision to FX basis spreads.

Fourteen IASB members agreed, one abstained.

The transition requirement for designation of 'own use' contracts as at fair value through profit or loss

The IASB discussed the draft requirements for the transition of the designation of 'own use' contracts. The IASB noted that because under the draft requirements the election of accounting as at fair value through profit or loss can only be made at inception of a contract, the transition to the new scope of IAS 39 *Financial Instruments: Recognition and Measurement* for 'own use' contracts would in effect be 'prospective' in that the election would not be available for contracts that already exist on the date on which an entity applies the new scope for the first time. This would result in an effect on financial statements that could involve a prolonged 'phasing in' of the new accounting treatment, which would make comparative information less useful. Consequently, the IASB tentatively decided to change the draft transition requirements so that an entity makes the election for all 'own use' contracts that already exist on the date on which it applies the new scope for the first time on an 'all-or-none' basis for all similar contracts. The IASB also decided to make a consequential amendment to IFRS 1 *First-time Adoption of International Financial Reporting Standards* that provides the same approach on transition to IFRSs.

Fourteen IASB members agreed, one abstained.

The scope of the draft requirements and the interaction with 'macro hedging' activities

The IASB discussed the scope of the new hedge accounting model and its interaction with 'macro hedging' activities. The draft requirements allow entities to apply IAS 39 instead of the new hedge accounting model for a fair value hedge of the interest rate exposure of a portfolio of financial assets or financial liabilities (and only for such a hedge). Conversely, cash flow hedging relationships must be accounted for under the new hedge accounting model even if they relate to 'macro hedging' activities. The IASB discussed whether IAS 39 should continue to be applied for some cash flow hedges and whether it should clarify how the new hedge accounting model relates to hedging relationships that result from macro hedging activities.

The IASB tentatively decided:

- not to include any additional guidance from IAS 39 or the accompanying implementation guidance in the draft requirements;
- to clarify that designations for hedge accounting purposes do not have to be the *same* as the actual risk management view but must be directionally consistent with it. This relates to designations of hedging relationships that do not *exactly* represent the actual risk management (colloquially referred to as 'proxy hedging');
- to expand the example of when to discontinue hedge accounting (paragraph B6.5.24(b) of the draft requirements); and
- to add an explicit explanation that not carrying forward implementation guidance of IAS 39 does not mean that the IASB rejected it.

Fourteen IASB members agreed, one abstained.

The IASB also asked the staff to provide at a future meeting some analysis of how an election to apply IAS 39 instead of the new hedge accounting model might be designed and the consequences that might have. The IASB emphasised that this was to be investigated but that no decision had yet been made to adopt such an approach.

Next steps

The IASB will discuss the staff analysis regarding the scope of the new hedge accounting model at a future meeting.

Matters arising from the IFRS Interpretations Committee: Hedge Accounting

The IASB discussed an issue that has been raised from the IFRS Interpretations Committee (the Interpretations Committee) regarding hedge accounting. The issue is whether hedge accounting should be discontinued in a circumstance in which an over-the-counter (OTC) derivative, which has been designated as a hedging instrument, is novated from one counterparty to a central counterparty (CCP) following the introduction of new regulations.

Matters arising from the IFRS Interpretations Committee

The IASB discussed whether the current IFRS standards should be amended to require such a novation to be deemed to be a continuation of the existing hedging relationship and, if so, how to determine the scope of the amendment. The IASB also discussed how long the comment period for the Exposure Draft of such proposed amendments should be. The IASB decided:

a. to publish a proposal for a limited-scope amendment to IAS 39 *Financial Instruments: Recognition and Measurement* and IFRS 9 *Financial Instruments* that would require a continuation of the existing hedging relationship in the circumstances raised in this issue; and
b. to limit the scope of proposed amendments to circumstances in which:

    i. a novation is required as a result of legislation, regulation or similar statutory requirements;
    ii. all parties to the original OTC derivative contract are affected in the same way by the novation; and
    iii. there are no changes to the terms of the original OTC derivative contract other than the change of counterparty to a CCP.

c. The IASB also decided that the comment period for the Exposure Draft should be 30 days because of the urgency of this issue.

All IASB members agreed.

Next steps

The IASB directed the staff to prepare an Exposure Draft for proposed amendments, which will be published in February 2013.

Reports for the following sessions were not available for inclusion in today's daily *Update* and will be included in tomorrow's daily *Update*, if available:

- **Revenue Recognition**
- **Insurance Contracts**
- **Leases**