

FASB Considers Feedback on Targeted Improvements to Hedge Accounting and Sets Agenda for Redeliberations

At its January 25, 2017, [meeting](#), the FASB discussed comments received on its 2016 [proposed Accounting Standards Update \(ASU\), Targeted Improvements to Accounting for Hedging Activities](#), made a number of tentative decisions about the proposed amendments, and agreed on a plan for future redeliberations.

The Board affirmed the following amendments reflected in the proposed ASU; therefore, no redeliberations are anticipated for these areas:

- Permitting an entity to designate as the hedged risk the variability in cash flows attributable to changes in (1) a contractually specified component in a cash flow hedge of a forecasted purchase or sale of a nonfinancial asset or (2) the contractually specified interest rate in a cash flow hedge of a variable-rate financial instrument's interest rate risk.
- Changing the current hedge accounting presentation requirements by requiring that the change in the fair value of a hedging instrument, including amounts excluded from the assessment of effectiveness for fair value and cash flow hedges, be presented in the same income statement line item as the earnings effect of the hedged item. (However, see the discussion below related to excluded components and missed forecasts.)
- Simplifying the accounting for certain fair value hedges of interest rate risk involving (1) partial term hedges and (2) prepayable financial instruments, and allowing an entity to measure the change in the fair value of the hedged item in a fair value hedge of interest rate risk either on the basis of the benchmark interest rate component of the contractual coupon cash flows determined at hedge inception or the full contractual coupon cash flows as required by current GAAP. (See the discussion below related to the market yield test, i.e., the "sub-benchmark" issue.)
- Retaining the existing benchmark interest rate guidance for fair value hedges and designating the SIFMA¹ rate as another acceptable benchmark interest rate in the United States.
- Permitting a public business entity to perform the initial prospective quantitative assessment of hedge effectiveness up until the time of the initial quarterly effectiveness assessment date, using data as of hedge inception.
- Permitting an entity performing its assessment of whether the qualifying criteria for the critical terms match method are met for a group of forecasted transactions to assume that the hedging derivative matures at the same time as the forecasted transactions occur if both the derivative maturity and the forecasted transactions occur within the same 31-day period.
- Allowing an entity that initially applies the shortcut method to apply a long-haul method if it (1) determines that use of the shortcut method was not or is no longer appropriate, (2) determines that the hedge would still be highly effective under the long-haul method, and (3) had appropriately documented at hedge inception what the alternative long-haul method would be.
- Modifying the disclosure requirements to require an entity to provide (1) information about cumulative basis adjustments for fair value hedges and (2) revised tabular disclosures. (However, see the discussion below related to disclosure of quantitative hedging goals.)
- Permitting an entity to perform subsequent qualitative tests of hedge effectiveness in instances in which an initial quantitative test of hedge effectiveness is required. (However, see the discussion below related to returning to qualitative testing after having been required to perform a quantitative hedge effectiveness test.)

¹ Securities Industry and Financial Markets Association.

The Board also rescinded and decided not to redeliberate the proposed amendments that would have required:

- The change in the hedging instrument's fair value to be presented in the same income statement line as the earnings effect of the hedged forecasted transaction, had it occurred, for a hedged forecasted transaction that is probable of not occurring. (This decision would retain current GAAP for missed forecasts, which does not prescribe presentation guidance for such transactions.)
- Qualitative disclosure about quantitative hedge accounting goals.

Editor's Note: Various Board members expressed concern about the operability of allowing a more principles-based approach for (1) designating hedgeable components of nonfinancial items and (2) identifying benchmark interest rates. Although the Board does not intend to redeliberate these issues, it will (1) monitor implementation of IFRS 9, *Financial Instruments*, which allows designation of components that are separately identifiable and reliably measurable, and (2) assess whether to revisit the issues in the future. The Board also indicated that it would stand ready to assess adding additional interest rate indices to the list of acceptable benchmark interest rates in the United States, if such a need is warranted by marketplace developments.

Next Steps

The Board decided to address the following issues in its redeliberations:

- The need for a market yield test for fair value hedges of interest rate risk (i.e., the "sub-benchmark" issue).
- The recognition model for components excluded from an entity's assessment of effectiveness.
- Whether an entity should be permitted to return to performing qualitative assessments of hedge effectiveness after having been forced by facts and circumstances to perform a quantitative assessment.
- The timing of hedge documentation preparation for private companies.
- Whether an entity should be able to exclude the cross-currency basis spread in a cross-currency swap from the assessment of hedge effectiveness.

Refer to the summary of [tentative Board decisions](#) for additional information.

Editor's Note: The Board also agreed not to deliberate the issue originally raised in FASB Statement 133 Implementation Issue H17² because the issue was unrelated to any of the targeted improvements within the scope of this project.

Further, the Board agreed to allow its staff to perform further research "to determine whether to include in redeliberations potential amendments to the fair value portfolio hedging model of interest rate risk related to prepayable assets"; however, it noted that the timeline for finalizing the other targeted improvements should not be delayed by this research.

In addition, the Board tentatively decided that, in a cash flow hedge of a forecasted transaction, an entity would not be required to dedesignate a hedging relationship if the hedged risk changes from the risk originally designated (e.g., from LIBOR to Prime) if (1) the hedged forecasted transaction remains probable of occurring and (2) the hedging derivative remains highly effective at offsetting the cash flows associated with the hedged item. The Board also agreed that "a change in the hedged risk . . . would not affect an entity's conclusion of whether the forecasted transaction remains probable of occurring. This decision would apply to hedges of both financial instruments and nonfinancial items."

² In April 2007, the FASB voted not to finalize proposed Statement 133 Implementation Issue No. H17, "Hedging Functional-Currency-Equivalent Proceeds to Be Received From a Forecasted Foreign-Currency-Denominated Debt Issuance," and removed the project from its agenda.

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