

IFRS Briefing Sheet

Exposure Draft of *Proposed Amendments to IAS 39 Financial Instruments: Recognition and Measurement – Exposures Qualifying for Hedge Accounting*

September 2007, **Issue 75**

This IFRS Briefing Sheet summarises the International Accounting Standards Board's (IASB) Exposure Draft (ED) of *Proposed Amendments to IAS 39 Financial Instruments: Recognition and Measurement – Exposures Qualifying for Hedge Accounting*, which was published on 6 September 2007.

The proposals would apply to financial assets and financial liabilities only.

Proposed Amendments

Qualifying Risks

If an entity does not hedge all the risks in a financial instrument, then the ED proposes limiting the risks that are eligible for designation as a hedged risk to the following:

- interest rate risk
- foreign currency risk
- credit risk
- prepayment risk
- risks associated with the contractually specified cash flows of a recognised financial instrument.

Therefore, for example, inflation risk could not be identified as the hedged risk.

The ED proposes to continue allowing the designation of a financial instrument in its entirety as a hedged item with respect to all of its risks.

The ED also proposes that risks designated as hedged risks must not in aggregate exceed the total risk of the financial instrument.

Qualifying Portions

The ED proposes limiting the portions of cash flows of a financial instrument that may be designated as the hedged item to the following:

Background and Issue

Paragraph 81 of IAS 39 *Financial Instruments: Recognition and Measurement* states that a hedged item may be hedged "with respect to the risks associated with only a portion of the cash flows or fair value ... provided that effectiveness can be measured".

The ED proposes to clarify the IASB's original intentions on eligible portions under IAS 39 by specifying those risks and portions that are eligible for designation as the hedged risk and the hedged portion.

The ED also is intended to outline those risks and portions that would be eligible for designation under IAS 39; therefore, no other risks or portions would be eligible for hedge accounting.

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- the cash flows of a financial instrument for part of its time period to maturity (i.e., a partial term hedge)
- a percentage of the cash flows of a financial instrument (i.e., a proportion)
- the cash flows of a financial instrument associated with a one-sided risk of that instrument
- any contractually specified cash flows that are independent of the other cash flows of that instrument
- the portion of the cash flows of an interest-bearing financial instrument that is equivalent to a financial instrument with a risk-free rate
- the portion of the cash flows of an interest-bearing financial instrument that is equivalent to a financial instrument with a quoted fixed or variable inter-bank rate.

The IASB has invited comments on whether there are any other situations in which an entity should be permitted to designate a portion of the cash flows of a financial instrument as the hedged item.

The ED proposes application guidance to clarify that in identifying a portion of a financial instrument as the hedged item, it is not possible to specify a cash flow that does not exist in the financial instrument, e.g., an entity cannot infer or impute the cash flows arising from the time value of a hypothetical written option in a non-derivative financial asset.

Effective Date

The ED does not propose an effective date but does propose to permit early adoption of the final amendments

to the standard. The ED proposes retrospective application of the requirements.

Response to the IASB

The IASB has invited comments on the ED by 11 January 2008.

If you would like further information on any of the matters discussed in this issue of *IFRS Briefing Sheet*, please talk to your usual local KPMG contact or call any of KPMG firms' offices.

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