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IASB consultation on IBOR changes to IFRS 9 and IAS 39 – impact on corporates

The replacement of IBORs as one of the most widely used interest rate benchmarks is work-in-progress with markets expected to transition over the next few years. However, the potential impact of transition on hedge accounting is a more immediate problem and, to address this, the International Accounting Standards Board (IASB) published in May 2019 an Exposure Draft: *Interest Rate Benchmark Reform.*

Any company that has adopted hedge accounting for IBOR-related hedges, such as hedges of loans with derivative instruments including interest rate swaps, interest rate options, and cross-currency swaps will be affected. The transition in the financial markets from IBORs to Risk Free Rate (RFR) benchmarks could inadvertently result in the discontinuation of hedge relationships under IFRS 9 and IAS 39 with a potential material impact on profit and loss. The Exposure Draft proposes to provide relief from specific hedge accounting requirements as detailed below. It is proposed that that the application of such relief would be mandatory for all hedging relationships that are affected by interest rate benchmark reform in order to avoid "cherry-picking" of hedges to be discontinued.

Specifically, the IASB proposes:

- **Cashflow hedges and forecast transactions:** An amendment such that IBOR transition is ignored when determining whether a forecast transaction is highly probable or is no longer expected to occur (i.e. the current interest rate benchmark (e.g. LIBOR) that forms the basis of the hedged cash flow is not changed as a result of benchmark reform).
- **Fair value hedge accounting:** An amendment whereby an entity would continue hedge accounting where a non-contractually specified IBOR risk component (e.g. a change in fair value of debt due to changes in LIBOR) met the separately identifiable requirement when the hedge was designated at inception, even if it does not meet that requirement at a later date.
- **Prospective hedge effectiveness:** An exception to IFRS 9 and IAS 39 that assumes that the currently used interest rate benchmark (e.g. LIBOR) will not be affected when determining whether there is an economic relationship between the hedged item and the hedging instrument (IFRS 9) or whether the hedge is expected to be highly effective in offsetting (IAS 39).
- **Retrospective hedge effectiveness:** No relief is proposed for measuring and accounting for retrospective hedge ineffectiveness. This includes no relief for having to discontinue a hedge if retrospective hedge effectiveness is outside the 80-125% threshold under IAS 39.

The IASB is considering the accounting implications arising from the interest rate benchmark reform in two stages. Initially, the proposed amendments in this Exposure Draft will address the effects of uncertainty in the period leading up to the replacement of interest rate benchmarks (i.e. before the replacement of LIBOR). As more information becomes available about the replacements, the IASB will assess whether there are any further potential accounting implications of the transition and determine whether to take further action.

The Exposure Draft is open for comments until 17 June 2019 with the IASB aiming to issue final amendments in late 2019. The IASB proposes that the amendments are applicable for financial years beginning on or after 1 January 2020, with earlier application permitted.

The ACT intends to submit a response to the Exposure Draft and encourages corporate treasurers to either submit a response directly to the IASB or send comments through to the ACT's policy & technical team by Wednesday 12 June to *technical@treasurers.org*