ACCOUNTANCY EUROPE.

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Subject: Exposure Draft – *Risk Mitigation Accounting—Proposed amendments to IFRS 9 and IFRS 7*

Dear Mr. Woods, Dear Mr. Klinz,

We are pleased to respond to the International Accounting Standards Board (IASB or the Board) Exposure Draft (ED) *Risk Mitigation Accounting—Proposed amendments to IFRS 9 and IFRS 7. Our* comments also serve as our response to EFRAG's Draft Comment Letter (DCL).

OVERALL OBJECTIVE AND REFLECTION OF ACTUAL RISK MANAGEMENT

We generally agree with the overall objective of the proposed Risk Mitigation Accounting model (RMA), namely, to represent in the financial statements the economic effects of an entity's repricing risk management activities when such risk is managed on a net basis. However, the concept of "reflecting actual risk management" itself warrants further clarification in several areas where it creates tension with the accounting Conceptual Framework.

LEVEL OF APPLICATION AND INTRAGROUP TRANSACTIONS

One example of such tension relates to the Board's proposal to apply RMA at the level at which risk is actually managed, which we welcome. In practice, this may often result in RMA being applied at the

subsidiary level. However, this raises the question of how to treat intragroup cash transactions that are included in a subsidiary's risk management strategy but eliminated at the consolidated level.

We encourage the Board to clarify whether the model should i) include such internal cash transactions even though failing to fully eliminate their effects at the consolidated level would distort general consolidation principles, or ii) disregard these transactions thereby creating a major departure from the initial objective of depicting actual risk management practices.

SCOPE OF ELIGIBLE INSTRUMENTS

We believe that reflecting actual risk management should lead to some scope adjustments to the range of instruments considered to be eligible for inclusion in the model. For example, in the banking industry, we consider that items such as lease receivables held in the banking book should be included as eligible in the model regardless of their accounting classification, to depict more faithfully the risk management of the entity.

TREATMENT OF OVER-HEDGING

We agree with and support the Board's proposal to recognise in profit or loss (P&L) any remeasurement of a designated derivative that would cumulatively exceed the cumulative change in present value of the benchmark derivative. For that purpose, we agree with the proposal that the Risk Mitigation Objective used to determine the characteristics of the Benchmark Derivative, shall not exceed the amount of Net Repricing Risk Exposure (NRRE). This mechanism ensures that any "over-hedging" situation will trigger a P&L impact.

UNEXPECTED CHANGES AND SUBSEQUENT ASSESSMENT

The concept of unexpected changes is a pillar of the RMA model as it triggers adjustments of the benchmark derivatives and the excess test and deserves to be further clarified by the Board to avoid misinterpretation or diversity in practice.

Once appropriately defined, this concept triggers the need for the Board to choose between two alternatives:

- either requiring a kind of tracking mechanism to accurately monitor the behaviour of the RMA adjustment over time, and/or
- implementing a kind of impairment test to check that what it represents still has sufficient economic substance to be recognized as an asset or a liability on the balance sheet.

The former raises a cost benefit challenge and may be complex to implement, while the latter raises two challenges: clearly defining what is meant by present value of the NRRE, and defining an alternative test since the ED proposed excess test has proved to be too flawed to be maintained in its current format (please refer to our answer to question 6).

OTHER AREAS REQUIRING CLARIFICATION

We have also identified other areas of concern that warrant amendments to the proposed guidance such as the treatment of option-based strategies and non-zero fair value derivatives (please refer to our answers to questions 4 and 9).

We encourage the Board to pursue its investigation of RMA's interaction with insurance activities, considering notably the resulting effect of RMA adjustments on the balance sheet when a large portion of the NRRE consists of Fair Value through Other Comprehensive Income (FVOCI) instruments.

FURTHER WORK AND RE-EXPOSURE

Although in our opinion several issues will need to be addressed, triggering the need to re-expose the model given the significance of the changes required, we encourage the Board to pursue this important project and to build on the time and efforts already invested in this topic to support the Board's initiative. We consider that this momentum should be maintained to seize this opportunity to address the issue and ensure consistent application across all geographies in a timely manner.

We kindly refer to the Annex to this letter for our detailed responses.

Please do not hesitate to contact Nael Braham (nael@accountancyeurope.eu) in case of any questions or remarks.

Sincerely,



Eelco van der Enden

Chief Executive Officer

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Annex: IASB ED – Questions for respondents

We are pleased to provide below our detailed responses to the questions.

Question 1—Objective and scope of risk mitigation accounting (Section 7.1)

The IASB proposes that:

(a) the objective of risk mitigation accounting be for financial statements to represent the economic effect of an entity's risk management activities if the entity manages repricing risk on a net basis.

(b) risk mitigation accounting be applied on a voluntary basis. However, an entity would be permitted to apply risk mitigation accounting if, and only if, the entity mitigates repricing risk on a net basis and the entity's business and risk management activities have the characteristics specified in paragraph 7.1.4.

(c) an entity be required to document formally how it will apply risk mitigation accounting.

Paragraphs BC11–BC37 of the Basis for Conclusions explain the IASB's rationale for these proposals.

Do you agree with these proposals? Why or why not? If you disagree with any of these proposals, please explain what you would suggest instead and why.

Objective:

(1) We generally agree with the overall objective of the proposed Risk Mitigation Accounting model, namely, to represent in the financial statements the economic effect of an entity's repricing risk management activities when that risk is managed on a net basis. But the concept of "reflecting actual risk management" itself deserves clarification in several areas where it creates tension with accounting conceptual framework. One of the best examples of such tension is the following: We welcome the Board's proposal to apply RMA at the level at which the risk is actually managed. This often results in applying RMA at a subsidiary level. But this raises the question of how to deal with intragroup cash transactions that are included in the risk management strategy of the subsidiary but are eliminated at the consolidated level. We encourage the Board to clarify whether the model shall i) include such internal cash transactions despite the fact that not eliminating fully their effects at consolidated level would create a distortion to general principle of consolidation process, or ii) disregard these transactions creating a major departure from the initial objective to depict actual risk management practices.

(2) We also consider that "reflecting actual risk management" should allow an entity to consider an asset such as lease receivable as an eligible item regardless of its accounting classification.

(3) We consider that the term "repricing risk" is not sufficiently clear in the ED for all stakeholders. We do not object to retaining the term, provided that the final Standard includes a clearer explanation of its intended meaning to reduce the risk of misinterpretation.

(4) We also question whether the final model should remain limited to exposures managed on a "net basis" for repricing risk as there seems to be no conceptual basis for this requirement. It would nevertheless exclude commonly applied risk management practices such as dynamic portfolio risk management used for example by insurance companies or banks managing their core deposits on a gross basis only.

Voluntary basis:

(5) Agree with the ED proposal.

Documentation:

(6) We broadly agree with the ED's documentation proposals.

(7) That being said, we would welcome clarification of the required level of granularity. For example, a net position managed using several benchmark rates to address basis risk may require several accounting documentation packages even though management monitors it as one position. Similar issues may arise for currencies for example. The final requirements should therefore strike an appropriate balance between discipline, operational feasibility and auditability.

(8) More generally, the closer the accounting documentation is to existing risk management documentation, the less onerous the model will be for preparers. This would have merits in the auditability of the model as well from an auditor's point of view. Conversely, if the accounting model requires a separate construct that departs materially from the way management monitors those risks, the documentation burden would become disproportionate. The IASB should therefore clarify the documentation expected in consolidated financial statements when repricing risk is managed and documented at individual legal-entity or business-unit level.

Question 2—Underlying portfolios (paragraphs 7.2.1–7.2.4)

The IASB proposes that risk mitigation accounting be applied based on underlying portfolios—that is, portfolios of financial instruments that expose an entity to repricing risk. The IASB proposes that financial instruments be eligible for inclusion in underlying portfolios only if they are:

> *(a) financial assets classified as subsequently measured at amortised cost or fair value through other comprehensive income (in accordance with paragraphs 4.1.2 or 4.1.2A of IFRS 9 Financial Instruments);*
>
> *(b) financial liabilities classified as subsequently measured at amortised cost (in accordance with paragraph 4.2.1 of IFRS 9); or*
>
> *(c) future transactions that could result in the recognition or derecognition of financial instruments specified in (a) or (b).*

The IASB is also proposing that an entity apply risk mitigation accounting only to its exposure to repricing risk that is not otherwise mitigated. However, if a financial instrument is designated as a hedged item for a risk other than repricing risk, the hedged exposure would be eligible for inclusion in underlying portfolios.

Paragraphs BC38–BC63 of the Basis for Conclusions explain the IASB's rationale for these proposals.

Do you agree with these proposals? Why or why not? If you disagree with any of these proposals, please explain what you would suggest instead and why.

Amortised cost and future transactions

(9) We agree that financial assets and financial liabilities measured at amortised cost should fall within the scope of the model.

(10) We also agree, in principle, with the inclusion of future transactions, including firm commitments, highly probable forecast transactions and renewals, to the extent that those transactions genuinely contribute to repricing risk.

Fair value through profit or loss (FVTPL) and Fair value through other comprehensive income (FVOCI)

(11) We support the eligibility of instruments measured at FVOCI and FVPL when they form part of the managed net position to limit departure from actual risk management and, simplify reconciliation between risk management and RMA accounting. However, the IASB should analyse and explain the profit or loss, OCI and balance sheet consequences of the proposed mechanics. This analysis should ensure that the RMA adjustment does not obscure the economic meaning of either the FVOCI reserve or the statement of financial position (and limit the risk of unintended consequences on regulatory ratios even if we acknowledge that this is not within the IASB's realm). We do not prescribe a particular solution, but we strongly recommend that the IASB resolve these accounting consequences before finalising the model. Alternatives based on separate sub-portfolios or allocation by measurement category may improve accounting coherence but could introduce operational complexity and depart from the way the net position is managed. Any substantive redesign should therefore be exposed and field-tested.

Equity:

(12) The discussions confirmed that many European banks incorporate equity, directly or indirectly, into their interest rate risk management frameworks. This is therefore not a theoretical issue but a matter of existing market practice.

(13) More specifically, in certain cases we noted that, from a risk management perspective, a floating-rate gap approach and a fixed-rate gap approach are mathematically capable of describing the same economic exposure. In practice, however, accounting can only reflect that equivalence if the Standard provides an operable solution to the equity question.

(14) We agree that equity should not be directly eligible for inclusion in the NRRE because equity does not itself create repricing differences that affect profit or loss. Nevertheless, equity funding can affect the economic repricing profile of assets. We therefore support a proxy solution that reflects the economic effect of equity without treating equity itself as an eligible underlying item. For NII management, a fixed-rate gap approach that treats the stable portion of equity as a funding resource and a floating-rate gap approach that reflects the related refinancing, or reinvestment exposures can represent the same economic exposure. The final Standard should therefore clarify that the proxy operates consistently irrespective of whether an entity starts from fixed-rate or floating-rate gaps.

(15) Another issue arises for Additional Tier 1 instruments classified as equity but managed economically as debt instruments when the entity is managing EVE metrics. We therefore

encourage the IASB either to clarify that the practical solution developed for Equity can also be applied in a manner that captures the economic effect of such instruments, or to provide more specific guidance for AT1 instruments where they are part of repricing risk management for regulatory purposes.

(16) More generally, we encourage the IASB to expand and clarify its illustrative guidance, especially because the existing examples appear to be more relevant for certain NII-style fact patterns than for EVE approaches. In our view, additional guidance would materially improve consistency in application.

Lease receivables and lease liabilities:

(17) We recommend including lease receivables and lease liabilities within the scope of the model where they contribute to repricing risk and are managed accordingly. Although these items may in some cases be less significant in amount than traditional banking book instruments, the underlying principle appears consistent.

Internal cash transactions (linked to the broader question of the level at which risk management should be assessed):

(18) Internal cash transactions are intragroup cash transactions such as loans and borrowings that are included in the risk managed position when the group is managing interest rate risk at an entity or Business Unit level. For the purpose of applying Risk Mitigation Accounting at group level, these transactions, if not eligible in the underlying portfolios, would create potential significant misalignment between the Risk Mitigation Objective and the designated derivatives.

(19) The Board will have to make a clear choice between two alternatives: either i) allowing internal cash transactions to be reflected where this is necessary to represent the level at which repricing risk is actually managed. Such an approach considers that where risk management is performed at subsidiary or business-unit level, excluding internal cash transactions altogether may result in an accounting depiction that departs from the economic reality of the managed position. Or ii) maintaining the general accounting principle that internal cash transactions shall be eliminated in the consolidated accounts.

(20) We recommend that the IASB confirm the relevant level of application and the treatment of intragroup cash transactions. The analysis should address the risk that a derivative reduces risk at the managed entity level but creates or increases risk after elimination of intragroup positions at consolidated level, as well as the operational consequences of reconstructing the NRRE for consolidation purposes only. The IASB could also consider whether an externalisation condition could provide an appropriate safeguard.

Question 3— Determining the net repricing risk exposure (paragraphs 7.2.5–7.2.10)

The IASB proposes that an entity determine the net repricing risk exposure by aggregating the repricing risk arising from underlying portfolios by repricing time bands based on expected repricing dates. The expected repricing date is the earlier of the dates on which financial instruments in the underlying portfolios are expected to be settled or to reprice.

The IASB also proposes that the entity determine the net repricing risk exposure in a manner that is consistent with how it makes risk management decisions, including with regard to:

> *(a) the basis on which the entity aggregates the repricing risk arising from underlying portfolios and determines the repricing time bands (based on expected repricing dates); and*
>
> *(b) the measure the entity uses to quantify the repricing risk exposure in each repricing time band.*

Paragraphs BC64–BC69 of the Basis for Conclusions explain the IASB's rationale for these proposals.

Do you agree with these proposals? Why or why not? If you disagree with any of these proposals, please explain what you would suggest instead and why.

(21) Some entities assess the repricing risk arising from underlying portfolios before considering derivatives already in place, while others manage the combined net open position, including derivatives already in place for risk management purposes. For those using a combined net open position, as the Exposure Draft starts from the repricing risk arising from the underlying portfolios alone, this difference in starting point may produce results that appear inconsistent with the economic substance of the new hedging action. For that reason, we suggest that, solely for the purpose of assessing whether designated derivatives reduce risk, the model should permit existing designated derivatives to be considered as part of the NRRE and focus the prospective assessment only on new designated derivatives traded during the period if this represents the way repricing risk is managed by the entity. Some believe this suggestion merits further consideration because it may improve the alignment between the accounting model and the way risk is actually monitored and mitigated.

(22) We also recommend that the IASB clarifies whether potential over-hedging position shall be assessed on a time-bucket-by-time-bucket basis or whether offsetting with positions in adjacent time buckets should be permitted.

(23) Lastly, we think that the determination of the NRRE may require clearer application guidance where non-linear derivatives are used to mitigate one-sided or optional risks.

Question 4— Designated derivatives (Section 7.3)

The IASB proposes that only interest rate derivatives with a party external to the reporting entity that are used to mitigate the entity's repricing risk in accordance with its risk management strategy be eligible to be included as designated derivatives.

Paragraphs BC70–BC77 of the Basis for Conclusions explain the IASB's rationale for these proposals.

Do you agree with these proposals? Why or why not? If you disagree with any of these proposals, please explain what you would suggest instead and why.

(24) In principle, we agree with the proposals in this area.

(25) However, we recommend that the IASB clarifies how options can be incorporated into the RMA model. The interaction between designated options and the requirement that benchmark derivatives should have a zero fair value at inception remains difficult to understand in practice.

(26) In this regard, we would expect clarification on how to deal with the time value of options used to risk mitigate non-linear exposures. We encourage the Board to provide clarification as well on how non-linear risk is incorporated in the NRRE, how it interacts with risk measures, and how benchmark derivatives are constructed accordingly.

Question 5— Risk mitigation objective and benchmark derivatives (paragraphs 7.4.1–7.4.7)

The IASB proposes that an entity:

> *(a) specify a risk mitigation objective that is consistent with the amount of repricing risk the entity mitigates using designated derivatives, but does not exceed the amount of net repricing risk exposure in each repricing time band;*
>
> *(b) construct benchmark derivatives to replicate the timing and amount of repricing risk as specified in the risk mitigation objective; and*
>
> *(c) adjust the amount of repricing risk represented by the benchmark derivatives if unexpected changes in financial instruments included in underlying portfolios reduce the net repricing risk exposure to an amount below the risk mitigation objective specified at the beginning of the period.*

Paragraphs BC78–BC87 of the Basis for Conclusions explain the IASB's rationale for these proposals.

Do you agree with these proposals? Why or why not? If you disagree with any of these proposals, please explain what you would suggest instead and why.

(27) We agree with the proposals in paragraphs (a) and (b).

(28) We agree with the overall principle in the Exposure Draft that the specified risk mitigation objective should not exceed the net repricing risk exposure. We largely consider that gains or losses on derivatives creating an over-hedging situation should be recognised in the income statement.

(29) Some members suggested a refinement to the way benchmark derivatives are constructed by reference to the mitigated rate. In practice, risk managers may use derivatives referencing different benchmark rates, together with basis swaps, to manage basis risk arising from the underlying portfolios. Those instruments are often monitored as part of one overall repricing risk management strategy.

(30) Alternatively, some members support the IASB proposal to create one NRRE for each benchmark rate curve, but the risk is that it could result in an arbitrary split of NRRE and a deviation from risk management view. Indeed, for entities measuring the risk based on floating rate gaps measures, the proposition would be aligned with the risk management practices. However, for entities measuring the risk based on fixed rate gaps measures, the proposition would create a difference with the risk management practices because these entities aggregate portfolios without considering the underlying benchmark rate.

(31) Therefore, we emphasise that the accounting model should not impose a structure that differs from the way risk is actually managed. In particular, the number of NRREs required for accounting purposes should be aligned with the number of risk positions that are effectively monitored and managed by the entity.

(32) We generally agree with the principle of constructing a benchmark derivative with a zero initial fair value. However, there are situations where this principle deserves some adjustments, for example upon initial transition to RMA or when an entity is acquiring a business that includes existing derivatives eligible for RMA or starts documenting a new RMA involving existing derivatives. These situations may justify specific accounting requirements.

(33) Lastly, about paragraph (c), we recommend clarifying the concept of "unexpected changes" and the related methodology for adjusting benchmark derivatives. The definition of unexpected changes is a fundamental concept in the RMA mechanics but is missing in the Exposure Draft. A diversity in the interpretation of what is considered as being an unexpected change would result in very different outcomes. We have understood from entities performing the field test that the application of this concept in practice is not straight forward. We therefore recommend that the Board should provide additional guidance around this concept to limit the risk of significant diversity in interpretation. Given the importance, such additional guidance should be re-exposed before being included in a final standard.

Question 6— Recognising and measuring the risk mitigation adjustment (paragraphs 7.4.8–7.4.14)

The IASB proposes that an entity:

> *(a) recognise the risk mitigation adjustment in the statement of financial position based on the lower of: (i) the cumulative gains or losses on the designated derivatives; and (ii) the cumulative change in the fair value (present value) of the benchmark derivatives;*
>
> *(b) recognise in profit or loss the amount accumulated as the risk mitigation adjustment in the same periods during which the repricing differences arising from the financial instruments in the underlying portfolios affect profit or loss;*
>
> *(c) assess, at each reporting date, whether there is an indication that the risk mitigation adjustment might not be realised in full over the mitigated time horizon; and*
>
> *(d) recognise immediately in profit or loss a reduction in the amount accumulated as the risk mitigation adjustment if it exceeds the present value of the net repricing risk exposure as at the reporting date.*

Paragraphs BC88–BC116 of the Basis for Conclusions explain the IASB's rationale for these proposals.

Do you agree with these proposals? Why or why not? If you disagree with any of these proposals, please explain what you would suggest instead and why.

(34) We broadly agree with the proposals in paragraphs (a) and (b). However, we highlighted in paragraph 11 of the letter that the IASB should consider alternative recognition principles for underlying portfolios measured at fair value through OCI or P&L.

(35) Regarding paragraph (c), we agree in principle but recommend clarifying the circumstances in which the accumulated RMA may no longer be expected to be realised in full. In particular, we encourage the IASB to define carefully "unexpected changes" and provide additional guidance on how to assess whether unexpected changes have not been fully reflected in the adjustments made to benchmark derivatives.

(36) Regarding paragraph (d), we reflected on the need for an alternative or refined approach to the excess test to mitigate its conceptual flaws. One recurring concern was that the current test can

produce counterintuitive results in situations where the NRRE is underhedged or late hedged or changes without adjusting the derivatives used for risk management purpose, even where there has been no unexpected change that calls into question the economic effect of the risk mitigation strategy. More specifically, when an entity hedges only part of a net repricing risk exposure, the present value of the total NRRE may be affected by the unhedged portion in a way that causes the excess test to fail, notwithstanding that the designated derivatives continue to mitigate the intended risk in accordance with the entity's risk management objective. Our conclusion is therefore that the excess test embeds too significant flaws to be maintained as drafted in the ED.

(37) One alternative that we have considered would consist in refining the adjustment of benchmark derivatives by linking that adjustment more closely to the characteristics of the items affected by the unexpected change, for example by using the rates applicable to the derecognised or prepaid items rather than a simplified rate carried forward from the date when the risk mitigation objective was last specified. This approach seeks to avoid outcomes driven by the unhedged portion of the NRRE rather than by a failure of the risk mitigation strategy itself. As a more general comment, we are convinced that the so-called vintage / tracking approach would provide the most relevant information. We nevertheless understand the concerns expressed by preparers on the complexity to implement such a model that would trigger the need to store and use a large amount of data.

(38) To summarise, we consider that the Board is facing two alternatives: either requiring a kind of tracking mechanism to be able to monitor the behaviour of the RMA adjustment over time, or implementing a kind of impairment test to check that what it represents still has sufficient economic substance to be recognized on the balance sheet. The former raises a cost benefit challenge, while the latter raises two challenges: clearly defining what is meant by present value of the NRRE, and defining an alternative test as the currently proposed excess test proved to be too flawed to be maintained as drafted.

Question 7— Discontinuation of risk mitigation accounting (Section 7.5)

The IASB proposes that an entity discontinue risk mitigation accounting prospectively from the date on which the entity's risk management strategy changes—that is, when the entity changes how it manages repricing risk, including a change to the mitigated rate.

The IASB also proposes that an entity that discontinues risk mitigation accounting recognise the amount accumulated as the risk mitigation adjustment in profit or loss:

> *(a) on a systematic and rational basis over the mitigated time horizon, if the repricing differences arising from the financial instruments in underlying portfolios are still expected to affect profit or loss; or*
>
> *(b) immediately, if the repricing differences arising from the financial instruments in underlying portfolios are no longer expected to affect profit or loss.*

Paragraphs BC117–BC126 of the Basis for Conclusions explain the IASB's rationale for these proposals.

Do you agree with these proposals? Why or why not? If you disagree with any of these proposals, please explain what you would suggest instead and why.

(39) We broadly agree with the proposed principles regarding discontinuation of the model.

(40) We recommend that the IASB reconsider the cases triggering a discontinuation. Indeed, some examples in the Exposure Draft appear difficult to reconcile with the principle that a change in risk management strategy should be infrequent and should not occur in isolation. For example, extending the risk management horizon or adding new time buckets may simply reflect the decision to start hedging previously unhedged periods, rather than a fundamental change in the existing risk management strategy. We therefore recommend either removing examples that could be read as rule-based discontinuation triggers or redrafting them to explain why they meet the stated principle.

(41) In addition, we encourage the Board to clarify that an entity shall monitor RMA Adjustment following a discontinuation (i.e. that the alternatives considered in paragraph 38 would have to be applied to RMA adjustment on an on-going basis as well as after discontinuation).

Question 8—Effective date and withdrawal of IAS 39 (Section C1 of Appendix C to IFRS 9)

The IASB proposes that an entity be permitted to apply the requirements for risk mitigation accounting from the beginning of the annual reporting period starting on or after [the date the requirements are issued].

The IASB also proposes that an entity discontinue applying the hedge accounting requirements in IAS 39 Financial Instruments: Recognition and Measurement at the earlier of:

> *(a) the date on which the entity first applies the requirements for risk mitigation accounting; and*
>
> *(b) annual reporting periods beginning on or after [the date on which IAS 39 is withdrawn].*

Paragraphs BC127–BC128 of the Basis for Conclusions explain the IASB's rationale for these proposals.

Do you agree with the proposal to withdraw IAS 39? Why or why not? If you disagree, please explain what you would suggest instead and why. If the IASB decides to withdraw IAS 39, do you have any information for the IASB to consider in determining the withdrawal date, for example the time that is likely to be needed to transition from IAS 39?

(42) We agree with the proposed principles regarding the effective date and the withdrawal of IAS 39. However, we recommend at first that the IASB provide sufficient clarity on the final RMA requirements and on the transition mechanics before withdrawing the existing portfolio fair value hedge accounting requirements (please refer to our answer to question 9).

(43) We also encourage the Board to consider whether any existing IAS 39 implementation guidance remains necessary to support the accounting for amounts arising from discontinued portfolio fair value hedge accounting relationships. If such guidance is not transferred to IFRS 9, it would be helpful for the IASB to clarify its status and whether entities may continue to refer to it when accounting for legacy balances.

(44) Lastly, we draw the Board's attention to the significant implementation period that would be needed. The model may require new data, new controls, revised hedge documentation, additional disclosures and, in some cases, new interactions between accounting and ALM systems. Moreover, for a significant number of preparers (mainly banks) a simultaneous transition of the general hedge accounting models from IAS 39 to IFRS 9 is required.

(45) We therefore encourage the Board to leave preparers and stakeholders sufficient time between the issue of the final amendments and its effective date.

Question 9—Transition (Section C2 of Appendix C to IFRS 9)

The IASB proposes that:

> *(a) an entity apply the proposed requirements for risk mitigation accounting prospectively;*
>
> *(b) an entity be permitted to revoke its previous designation of financial assets or financial liabilities as measured at fair value through profit or loss, if those financial instruments will be included in underlying portfolios that the entity uses to determine the net repricing risk exposure;*
>
> *(c) an entity making the transition from IAS 39 discontinue hedge accounting for all hedging relationships and apply paragraphs 6.5.10 and 6.5.12 of IFRS 9 to the related hedge adjustments;*
>
> *(d) an entity making the transition from the hedge accounting requirements in Chapter 6 of IFRS 9 be permitted to discontinue hedge accounting for hedging relationships in which the hedged items are financial instruments that will be included in the underlying portfolios in accordance with paragraph 7.2.1; and*
>
> *(e) an entity be exempt from disclosing the quantitative information required by paragraph 28(f) of IAS 8 Basis of Preparation of Financial Statements in the reporting period in which the entity first applies the amendments.*

Paragraphs BC129–BC147 of the Basis for Conclusions explain the IASB's rationale for these proposals.

Do you agree with these proposals? Why or why not? If you disagree with any of these proposals, please explain what you would suggest instead and why.

(46) We agree with the proposed principles regarding transition. However, as explained in our response on benchmark derivatives, we recommend developing specific guidance (i.e., a waiver on this requirement) on how an entity should designate an RMA relationship on transition when the designated derivatives already have a non-zero fair value. The same issue may also arise in business combinations, when an entity acquires a portfolio that already includes derivatives.

(47) We encourage the Board to clarify the level at which the option to apply the RMA model is exercised. In our view, this option should be assessed at the level at which repricing risk is managed and documented. Accordingly, a financial conglomerate should be able to apply RMA to banking activities without automatically being required to apply it to insurance activities, provided those activities are managed separately. Similarly, a banking group should be able to apply RMA in those subsidiaries or jurisdictions where the relevant risk management practices and systems support the model, without being required to apply it to all entities in the consolidated group.

(48) This clarification is particularly important for groups that include both banking and insurance activities, or subsidiaries with different levels of sophistication in their ALM systems. The accounting requirements should be the same where the model is applied, but the decision to apply RMA should not be triggered merely because another part of the group manages repricing risk on a net basis.

(49) Considering that the RMA model is optional, we reflected on whether the ability to revoke previous fair value through profit or loss designations, and to discontinue existing IFRS 9 hedge accounting relationships, should be available only on first-time application of the amendments or also at a later date when an entity elects to apply RMA. We noted as well that different entities within a single group could decide to voluntarily apply RMA accounting at different dates. We concluded that such relief should be limited as proposed by the ED, to the first-time application date. Allowing entities to revisit fair value option designations at any later date would undermine the irrevocability principle in IFRS 9 and could create opportunities for accounting arbitrage.

Question 10—Disclosure requirements (proposed amendments to IFRS 7)

The IASB is proposing new presentation and disclosure requirements to be included in IFRS 7 Financial Instruments: Disclosures.

Paragraph 30E would require an entity to present separately from other line items:

> *(a) the risk mitigation adjustment, either as part of the entity's assets (when it has a debit balance) or as part of its liabilities (when it has a credit balance) in the statement of financial position; and*
>
> *(b) the amount of the risk mitigation adjustment recognised in profit or loss during the period in the statement of comprehensive income.*

Paragraphs 30F–30P would require an entity that applies risk mitigation accounting to disclose information that enables users of financial statements to understand:

> *(a) how the entity manages repricing risk according to its risk management strategy;*
>
> *(b) how the entity's risk management activities could affect the amount, timing and uncertainty of its future cash flows; and*
>
> *(c) how risk mitigation accounting has affected the entity's statement of financial position and its statement of comprehensive income.*

Paragraph 33A would apply to entities whose business and risk management activities have the characteristics specified in the proposed paragraph 7.1.4 of IFRS 9 but that choose not to apply risk mitigation accounting. Such entities would be required to provide a qualitative explanation of how they manage repricing risk.

Paragraphs BC148–BC171 of the Basis for Conclusions explain the IASB's rationale for these proposals.

Do you agree with these proposals? Why or why not? If you disagree with any of these proposals, please explain what you would suggest instead and why.

(50) We broadly agree with the presentation requirements described in paragraph 30E and the disclosure requirements described in paragraphs 30F to 30P. We support the objective of providing users with information about how RMA affects the statement of financial position and profit or loss, and about how the entity manages repricing risk on a net basis.

(51) However, we do not support a separate disclosure requirement for entities that are eligible for RMA but elect not to apply it. Existing IFRS 7 requirements already require qualitative information about market risk management and quantitative sensitivity information. Extending RMA-specific disclosures to non-applying entities could capture a broad population, including corporate treasury and insurance activities, without demonstrating that the incremental information would be decision-useful.

(52) In addition, we question whether the information required will always be relevant and understandable when a group manages a large number of NRREs at granular levels. This issue will arise especially when NRREs are defined at the level at which risk management decisions are actually made. We therefore recommend that the IASB consider whether aggregation principles, similar in spirit to those used for regulatory reporting, should be permitted so that disclosures remain useful without overwhelming users with excessive detail.

QUESTION RELATING TO ENTITIES THAT ISSUE INSURANCE CONTRACTS

Question 11—Risk management strategy

The questions below relate specifically to entities that issue insurance contracts as defined in IFRS 17 Insurance Contracts. When answering these questions, respondents should assume that insurance contract assets and liabilities are eligible to be included in underlying portfolios in accordance with paragraph 7.2.1.

Based on the proposals in this Exposure Draft:

(a) please describe the extent to which your risk management strategy and activities align with, or differ from, the descriptions in paragraphs 7.1.1–7.1.2; and

(b) please describe the extent to which your business and risk management activities align with, or differ from, the characteristics described in paragraph 7.1.4.

Would the proposals for risk mitigation accounting in this Exposure Draft achieve the IASB's objective of better representing in the financial statements the economic effects of your activities for managing repricing risk compared with the currently available accounting options? Please explain why or why not, and what you would suggest instead.

(53) For insurance entities, we recommend that the IASB clarify explicitly whether insurance contract liabilities and reinsurance assets can be included in the underlying portfolios when the entity is managing interest rate risk on a net basis. We also questioned the current terminology of repricing risk that is primarily used by banks and is not immediately transposable to insurance contracts.

(54) We agree with preparers who highlighted that the Risk Mitigation Accounting model is needed when IFRS 9 hedge accounting and the risk mitigation option in IFRS 17 are currently not sufficient to reflect all the interest rate risk management activities of insurance entities.

(55) Our discussions also highlighted that the main issue for insurers may be an accounting mismatch arising from the fact that financial assets and insurance liabilities are remeasured at each reporting date with a corresponding entry either in profit or loss or in OCI and the derivatives used to mitigate the risk are recognised at FVTPL. If the IASB intends the RMA model to be useful for insurers, the final Standard should explain how the RMA adjustment interacts with the IFRS 17 OCI option and whether the adjustment is intended to address this mismatch.

(56) We also recommend that the IASB consider FVTPL assets to be eligible for insurance entities where those assets are managed together with insurance liabilities within one net interest rate risk management framework. For the same reasons and with the same conditions as for banks (refer to paragraph 11) we consider that this scope adjustment will allow insurance entities to

better reflect their actual risk management and save significant costs and reconciliation effort between risk management and RMA documentation.

(57) The use of options in insurance risk management also requires clarification. Indeed, insurance entities use more frequently non-linear derivatives compared to banks because policyholder behaviour, surrender risk and mass lapse assumptions can affect the timing and amount of insurance cash flows with non-linear effects. The final Standard should therefore explain how such behavioural assumptions are incorporated into repricing dates and how designated options or other non-linear derivatives can be reflected in benchmark derivatives.

(58) Finally, if insurance liabilities are scoped in the model, the transition provisions should address whether entities should be permitted to revoke fair value option designations for insurance-related items on first-time application, consistently with the relief proposed for financial instruments (see our comment in paragraph 49).