Risk advisory services
MBAF
CERTIFIED PUBLIC ACCOUNTANTS AND ADVISORS

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FASB Issues Guidance to Improve Accounting for Hedging Activities

Background

On 28 August 2017, the FASB issued ASU No. 2017-12, *Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities.* The FASB issued this ASU to simplify current hedge accounting requirements in U.S. GAAP, which currently does not always permit an entity to properly recognize the economic results of its hedging strategies in its financial statements.

What's new?

The amendments in this ASU are categorized into multiple facets:

1. *Alignment of Risk Management Activities and Financial Reporting*: This change aligns an entity's risk management activities and financial reporting for hedging relationships. To meet that objective, the amendments expand and refine hedge accounting for both nonfinancial and financial risk components and align the recognition and presentation of the effects of the hedging instrument and the hedged item in the financial statements.

2. *Risk Component Hedging:* Permitting hedge accounting for risk components in hedging relationships involving nonfinancial risk and interest rate risk.

3. *Accounting for the Hedged Item in Fair Value Hedges of Interest Rate Risk:* Changing the guidance for designating fair value hedges of interest rate risk and for measuring the change in fair value of the hedged item in fair value hedges of interest rate risk.

4. *Recognition and Presentation of the Effects of Hedging Instruments:* Aligning the recognition and presentation of the effects of the hedging instrument and the hedged item in the financial statements to increase the understandability of the results of an entity's intended hedging strategies.

5. *Amounts Excluded from the Assessment of Hedge Effectiveness:* Continuing to allow an entity to exclude those components of a hedging instrument's change in fair value from the assessment of hedge effectiveness. Additionally, the amendments permit an entity to exclude the portion of the change in fair value of a currency swap that is attributable to a cross-currency basis spread from the assessment of hedge effectiveness.

6. *Other Simplifications of the Hedge Accounting Guidance:* Certain targeted improvements will ease the application of current guidance related to the assessment of hedge effectiveness.

Effective dates and transition requirements

For public business entities, the amendments in this ASU are effective for fiscal years beginning after 15 December 2018, and interim periods within those fiscal years. For all other entities, the amendments are effective for fiscal years beginning after 15 December 2019, and interim periods beginning after 15 December 2020. Early application is permitted in any interim period after issuance of the ASU. All transition requirements and elections should be applied to hedging relationships existing (that is, hedging relationships in which the hedging instrument has not expired, been sold, terminated, or exercised or the entity has not removed the designation of the hedging relationship) on the date of adoption. The effect of adoption should be reflected as of the beginning of the fiscal year of adoption (that is, the initial application date).

For cash flow and net investment hedges existing at the date of adoption, an entity should apply a cumulative-effect adjustment related to eliminating the separate measurement of ineffectiveness to accumulated other comprehensive income with a corresponding adjustment to the opening balance of retained earnings as of the beginning of the fiscal year that an entity adopts the amendments in this ASU. The amended presentation and disclosure guidance is required only prospectively.

About us

MBAF's Risk & Transaction Advisory Services practice strives to help manage risks and improve operations within your business. We work with all organizations to help realize business opportunities in complex issues, respond to key market and financial reporting developments and deliver distinctive results.

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