Hong Kong Institute of
Certified Public Accountants
香港會計師公會

Our Ref.: C/FRSC

Sent electronically through the IASB Website (www.ifrs.org)

11 November 2014

International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

Dear Sirs,

IASB Discussion Paper of Accounting for Dynamic Risk Management: a Portfolio Revaluation Approach to Macro Hedging

The Hong Kong Institute of Certified Public Accountants is the only body authorised by law to promulgate financial reporting, auditing and ethical standards for professional accountants in Hong Kong. We welcome the opportunity to provide you with our comments on this Discussion Paper (DP). Our responses to the questions raised in your Invitation to Comment are set out in the Appendix for your consideration.

We support the Board's effort to address the accounting for risk management of open portfolios. We also support the objective of providing more useful information about an entity's risk management activities. However, we have concerns about the scope and the approach of the project. The project started as a review of existing macro hedge accounting requirements, primarily of interest to banks that hedge interest rate risk, with a view to reducing profit or loss volatility arising from recognition and measurement mismatches between hedged items and hedging instruments in the case of open portfolios, to which current hedge accounting requirements are difficult to apply. However, the project has now moved well beyond macro hedging and has expanded the scope of the project to a wider accounting for dynamic risk management.

In accordance with our due process, the Institute had issued our local invitation to comment on this IASB DP. We also held an IASB Outreach roundtable meeting on 29 May 2014 in Hong Kong with attendees from major banks in Hong Kong and large accountancy firms. We note that we received only a limited number of comment letters from our constituents (mainly from financial institutions). Based on the comments, there does not appear to be significant demand for fundamental change to macro hedging. Constituents are more interested in targeted improvements to the existing macro hedging requirements than a fundamental change.

The DP indicates that the proposed dynamic risk management approach is not limited to banks and not limited to interest rate risk, yet the DP is heavily focused on banks and interest rate risk. This focus makes it difficult to assess the implications of the approach for other types of entities and other types of risk.

We do not support an accounting model with a scope focused on dynamic risk management as explored in the DP. We believe that approach would result in the revaluation of all net open risk positions which goes far beyond the objective of the project which is to eliminate the misrepresentation resulting from the accounting mismatch between the fair value measurement of the hedging instruments and the amortised cost measurement of the hedged items. Revaluing all open net risk positions would not assist

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in understanding the performance of the entity and would introduce irrelevant and potentially significant volatility in net income which would not be decision-useful. In addition, applying the Portfolio Revaluation Approach (PRA) would mean that unhedged exposures that are classified and measured in accordance with IFRS 9 would be remeasured for changes in the managed risk. This could have the effect of over-riding the classification and measurement principles in IFRS 9.

We believe that the objective of the PRA should be consistent with the objective of IFRS 9 hedge accounting, that is, to better represent in the financial statements the effect of an entity's risk management activities and that a combination of the current accounting guidance in IFRS 9 and the new accounting for hedges of open portfolios would provide an entity with the necessary accounting alternatives to reflect its risk management strategies and objectives. We believe it is worthwhile for the IASB to explore further in this area and make clear in the standard that how the PRA interacts with the general hedging model in IFRS 9 and when an entity can choose to use to apply the PRA.

If you have any questions regarding the matters raised in our comment letter, please contact Winnie Chan, our Associate Director of Standard Setting at winniechan@hkicpa.org.hk.

Yours faithfully,

Chris Joy
Executive Director

CJ/WC

Encl.

Hong Kong Institute of CPAs

Question 1—Need for an accounting approach for dynamic risk Management

Do you think that there is a need for a specific accounting approach to represent dynamic risk management in entities' financial statements? Why or why not?

Based on the comments received, constituents generally agreed that there is a need to address macro hedge accounting as the current accounting requirements do not allow entities to reflect the effect of their risk management of open portfolios in accounting. The current absence of an accounting solution results in a situation whereby entities need to use a patchwork of accounting techniques which may not always faithfully reflect the effects of dynamic risk management.

However, we do not support an accounting model with a scope focused on dynamic risk management as explored in the Discussion Paper, but should instead be focused on risk mitigation for the reasons further explained in our response to question 15. It is also worthwhile for the IASB to explore further the approach of improving the existing macro hedging requirements than having a fundamental change.

Question 2—Current difficulties in representing dynamic risk management in entities' financial statements

(a) Do you think that this DP has correctly identified the main issues that entities currently face when applying the current hedge accounting requirements to dynamic risk management? Why or why not? If not, what additional issues would the IASB need to consider when developing an accounting approach for dynamic risk management?

(b) Do you think that the PRA would address the issues identified? Why or why not?

(a) – (b)

We agree that the DP has identified and discussed many of the main issues common to financial institutions. We believe that the PRA addresses most of the issues arising from risk managing the net exposure to interest rate risk of the fair value of their assets and liabilities. However, it is not clear how the dynamic cash flow hedges may apply the PRA approach. Some companies may manage their interest rate risk profiles on a cash flow basis rather than on a revaluation basis. It is debatable whether the PRA would provide a faithful representation of dynamic risk management for those companies, particularly for their hedges of floating interest rate exposures.

It would also be helpful for the IASB to clarify the principle of hedging behaviouralised cash flow, rather than purely contractual cash flow, would be applicable to both macro and micro hedges – e.g. hedges of specifically identified callable bonds.

Question 3—Dynamic risk management

Do you think that the description of dynamic risk management in paragraphs 2.1.1–2.1.2 is accurate and complete? Why or why not? If not, what changes do you suggest, and why?

Based on the comments received from financial institutions, they generally agree that many of the characteristics describing dynamic interest rate risk management in the DP reflect dynamic interest rate risk management within banks. However, there are concerns that some of these characteristics do not reflect dynamic risk management strategies in all banks as well as in other sectors. For example, insurance companies have exposure to and manage interest rate, equity price and inflation risks. They may want to explore whether the PRA would provide a faithful representation of their risk management activities.

Question 4—Pipeline transactions, EMB and behaviouralisation

Pipeline transactions

(a) Do you think that pipeline transactions should be included in the PRA if they are considered by an entity as part of its dynamic risk management? Why or why not? Please explain your reasons, taking into consideration operational feasibility, usefulness of the information provided in the financial statements and consistency with the *Conceptual Framework for Financial Reporting* (the *Conceptual Framework*).

We agree that pipeline transactions should be included in the scope of accounting for hedges of open portfolios if that is consistent with the entity's risk management strategy. Pipeline transactions are forecast volumes by banks of draw-downs on fixed rate products at advertised rates and are common in the banking sector. We believe that the Board should consider developing a principle on the use of behaviouralisation which would address when pipeline transactions can be included.

EMB

(b) Do you think that EMB should be included in the PRA if it is considered by an entity as part of its dynamic risk management? Why or why not? Please explain your reasons, taking into consideration operational feasibility, usefulness of the information provided in the financial statements and consistency with the *Conceptual Framework.*

We do not consider that EMB should be included in the PRA as the inclusion of exposures from equity are notional exposure rather than a reflection of a real economic exposure of the reporting entity which may lead to an inconsistency with the Conceptual Framework for financial reporting.

Behaviouralisation

(c) **For the purposes of applying the PRA, should the cash flows be based on a behaviouralised rather than on a contractual basis (for example, after considering prepayment expectations), when the risk is managed on a behaviouralised basis? Please explain your reasons, taking into consideration operational feasibility, usefulness of the information provided in the financial statements and consistency with the *Conceptual Framework.***

We consider that the PRA should be applied to behaviouralised (rather than contractual) cash flows. These provide a better representation of an entity's risk exposures. We believe the use of behaviouralisation is consistent with existing guidance in IAS 39 on fair value hedge accounting for portfolio hedges of interest rate risk and also with the guidance in IFRS 9 on impairment of revolving credit facilities.

However, we acknowledge that the consideration of behavioral factors is subjective and practices differ from entity to entity. We suggest that a principle on the use of behaviouralisation should be developed. We also believe that disclosures on the use of behaviouralisation will be important to enable users of financial statements to understand the entity's risk exposures and to enhance comparability amongst entities.

Question 5—Prepayment risk

When risk management instruments with optionality are used to manage prepayment risk as part of dynamic risk management, how do you think the PRA should consider this dynamic risk management activity? Please explain your reasons.

Generally, the interest rate risk on items that are prepayable is normally managed based on behaviouralised cash flows. If companies are entering into options to manage the prepayment risk, an issue arises as to how to treat the time value component of the option. However, we believe that either accounting approach by using behaviouralised cash flows or by building the optionality within the underlying managed portfolio should be allowed if it is consistent with the entity's risk management strategy.

Question 6—Recognition of changes in customer behavior

Do you think that the impact of changes in past assumptions of customer behaviour captured in the cash flow profile of behaviouralised portfolios should be recognised in profit or loss through the application of the PRA when and to the extent they occur? Why or why not?

We support the approach that the impact of changes in past assumptions of customer behavior should be recognized in the statement of comprehensive income when the change in expectation arise, but only to the extent that such changes affect the layer or proportion designated in accordance with the risk management strategy and objectives. It would be consistent with the way changes in estimates are generally recognized under IFRS.

We believe that it is important that changes in past assumptions should be clearly disclosed in the notes of the financial statements, so users can understand the changes, the basis for those changes, and their impact in the entity's financial statements.

Question 7—Bottom layers and proportions of managed exposures

If a bottom layer or a proportion approach is taken for dynamic risk management purposes, do you think that it should be permitted or required within the PRA? Why or why not? If yes, how would you suggest overcoming the conceptual and operational difficulties identified? Please explain your reasons.

We believe that the designation of bottom layers and proportions within the PRA model should be permitted if that is consistent with the entity's risk management strategy and objectives.

We acknowledge that the application of both bottom layers and proportions will require tracking mechanisms. It is more common for banks to use a bottom layer approach in managing the interest rate risk, therefore we believe that bottom layers should be accommodated in the accounting for hedges of open portfolio in order to better represent interest rate risk management.

Question 8—Risk limits

Do you think that risk limits should be reflected in the application of the PRA? Why or why not?

We do not support the introduction of risk limits in the PRA. We consider that internal risk limits should have already been included in the entities' hedging strategy and therefore we see no reason why accounting should impose additional risk limits on the risk management activity.

Question 9—Core demand deposits

(a) Do you think that core demand deposits should be included in the managed portfolio on a behaviouralised basis when applying the PRA if that is how an entity would consider them for dynamic risk management purposes? Why or why not?

(b) Do you think that guidance would be necessary for entities to determine the behaviouralised profile of core demand deposits? Why or why not?

(a) – (b)

We believe that core demand deposits should be eligible for inclusion in the managed portfolio under PRA on a behaviouralised basis. We believe this would reflect more faithfully the economic reality of an entity's exposure to interest rate risk and provide more relevant information for the users of the financial statements.

As noted in our response to question 4(c), it could be helpful if an accounting principle on the use of behaviouralisation is developed.

Question 10—Sub-benchmark rate managed risk instruments

(a) Do you think that sub-benchmark instruments should be included within the managed portfolio as benchmark instruments if it is consistent with an entity's dynamic risk management approach (ie Approach 3 in Section 3.10)? Why or why not? If not, do you think that the alternatives presented in the DP (ie Approaches 1 and 2 in Section 3.10) for calculating the revaluation adjustment for sub-benchmark instruments provide an appropriate reflection of the risk attached to sub-benchmark instruments? Why or why not?

We believe that sub-benchmark instruments should be included within the managed portfolio as benchmark instruments only if such benchmark rate is contractually specified and if that designation is consistent with the entity's risk management strategy. For such instruments we support 'Approach 3' of the DP since this approach would only revalue the benchmark cash flows and consistent with the dynamic risk management approach.

(b) If sub-benchmark variable interest rate financial instruments have an embedded floor that is not included in dynamic risk management because it remains with the business unit, do you think that it is appropriate not to reflect the floor within the managed portfolio? Why or why not?

We believe that embedded floors in variable rate exposures should be included in the managed portfolio as generally the embedded floors included within sub-benchmark instruments are not separately transferred to ALM, even though those embedded floors may have an impact on the actual cash flows when benchmark yield falls below the floor.

Question 11—Revaluation of the managed exposures

(a) Do you think that the revaluation calculations outlined in this Section provide a faithful representation of dynamic risk management? Why or why not?

We believe that the calculation of the revaluation adjustment is an appropriate way to overcome the accounting mismatch between hedged items at amortised cost and the fair value of the hedging derivatives. However, the revaluation calculations may not provide a faithful representation of dynamic risk management for those companies that manage their interest rate risk profiles on a cash flow basis rather than on a revaluation basis.

(b) When the dynamic risk management objective is to manage net interest income with respect to the funding curve of a bank, do you think that it is appropriate for the managed risk to be the funding rate? Why or why not? If not, what changes do you suggest, and why?

We believe that it is appropriate to include the funding rate in the PRA to the extent that it is being used to estimate future cash flows which are to be hedge accounted for.

Question 12—Transfer pricing transactions

(a) Do you think that transfer pricing transactions would provide a good representation of the managed risk in the managed portfolio for the purposes of applying the PRA? To what extent do you think that the risk transferred to ALM via transfer pricing is representative of the risk that exists in the managed portfolio (see paragraphs 4.2.23–4.2.24)?

(b) If the managed risk is a funding rate and is represented via transfer pricing transactions, which of the approaches discussed in paragraph 4.2.21 do you think provides the most faithful representation of dynamic risk management? If you consider none of the approaches to be appropriate, what alternatives do you suggest? In your answer please consider both representational faithfulness and operational feasibility.

(c) Do you think restrictions are required on the eligibility of the indexes and spreads that can be used in transfer pricing as a basis for applying the PRA? Why or why not? If not, what changes do you recommend, and why?

(d) If transfer pricing were to be used as a practical expedient, how would you resolve the issues identified in paragraphs 4.3.1–4.3.4 concerning ongoing linkage?

(a) – (d)

We do not support the use of transfer pricing transactions for the purpose of determining the revaluation adjustment for accounting for hedges of open portfolios. Transfer pricing transactions are entity specific and may include additional effects on the managed interest rate risk (e.g. profit margins charged within business units). As a result, they will not necessarily be a faithful representation of the managed interest rate risk.

Question 13—Selection of funding index

(a) Do you think that it is acceptable to identify a single funding index for all managed portfolios if funding is based on more than one funding index? Why or why not? If yes, please explain the circumstances under which this would be appropriate.

An entity may have different types of portfolios or sub-portfolios and each of these may be subject to different funding indexes or benchmark interest rates. We support the use of more than one benchmark rate or funding index if they represent the interest rate risk to which an entity is exposed in the managed portfolio.

(b) Do you think that criteria for selecting a suitable funding index or indexes are necessary?

We believe that the chosen index should represent the actual interest rate risk that exists in the managed portfolio.

Question 14—Pricing index

(a) Please provide one or more example(s) of dynamic risk management undertaken for portfolios with respect to a pricing index.

(b) How is the pricing index determined for these portfolios? Do you think that this pricing index would be an appropriate basis for applying the PRA if used in dynamic risk management? Why or why not? If not, what criteria should be required? Please explain your reasons.

(c) Do you think that the application of the PRA would provide useful information about these dynamic risk management activities when the pricing index is used in dynamic risk management? Why or why not?

(a) – (c)

Based on the comments received from our constituents, we have currently no information about situations whereby net positions are identified and subsequently hedged based upon a pricing index. However, we do not support the use of pricing index for calculating the revaluation adjustments for the purpose of accounting for hedges of open portfolios since the interest rate risk is only one of the component of a pricing index, therefore we believe that pricing indexes would not be a faithful representation of the managed interest rate risk.

Question 15—Scope

(a) Do you think that the PRA should be applied to all managed portfolios included in an entity's dynamic risk management (ie a scope focused on dynamic risk management) or should it be restricted to circumstances in which an entity has undertaken risk mitigation through hedging (ie a scope focused on risk mitigation)? Why or why not? If you do not agree with either of these alternatives, what do you suggest, and why?

(b) Please provide comments on the usefulness of the information that would result from the application of the PRA under each scope alternative. Do you think that a combination of the PRA limited to risk mitigation and the hedge accounting requirements in IFRS [3] would provide a faithful representation of dynamic risk management? Why or why not?

(c) Please provide comments on the operational feasibility of applying the PRA for each of the scope alternatives. In the case of a scope focused on risk mitigation, how could the need for frequent changes to the identified hedged sub-portfolio and/or proportion be accommodated?

(d) **Would the answers provided in questions (a)–(c) change when considering risks other than interest rate risk (for example, commodity price risk, FX risk)? If yes, how would those answers change, and why? If not, why not?**

(a) – (d)

As noted in our covering letter, we do not support an accounting model with a scope focused on dynamic risk management as explored in the Discussion Paper. We believe that approach would result in the revaluation of all net open risk positions which goes far beyond the objective of the project which is to eliminate the misrepresentation resulting from the accounting mismatch between the fair value measurement of the hedging instruments and the amortised cost measurement of the hedged items. Revaluing all open net risk positions would not assist in understanding the performance of the entity and would introduce irrelevant and potentially significant volatility in net income which would not be decision-useful. In addition, applying the PRA would mean that unhedged exposures that are classified and measured in accordance with IFRS 9 would be remeasured for changes in the managed risk. This could have the effect of over-riding the classification and measurement principles in IFRS 9.

We believe that the objective of the PRA should be consistent with the objective of IFRS 9 hedge accounting, that is, to better represent in the financial statements the effect of an entity's risk management activities. We support an accounting model with a scope based on a Risk Mitigation Approach. Under this approach, the PRA is applied to the designated managed risk exposures to the extent they are hedged. This accounting model would better represent the results of an entity's risk management activities, including any ineffectiveness, and therefore, provide relevant information for users of financial statements. We acknowledge that once an entity designates, for example a sub-portfolio and/or a proportion of an open portfolio for risk management purposes, some tracking mechanisms will be necessary. We encourage the Board to continue to investigate how such tracking mechanism might operate in practice.

Question 16—Mandatory or optional application of the PRA

(a) **Do you think that the application of the PRA should be mandatory if the scope of application of the PRA were focused on dynamic risk management? Why or why not?**

(b) **Do you think that the application of the PRA should be mandatory if the scope of the application of the PRA were focused on risk mitigation? Why or why not?**

(a) – (b)

We do not support the mandatory application of PRA. This is consistent with the optional application of general hedge accounting under IAS 39 and IFRS 9. Moreover, mandatory application could create problems for entities who seek to combine interactively both the macro hedge accounting approach and the general hedge accounting provisions of IFRS 9.

Question 17—Other eligibility criteria

(a) Do you think that if the scope of the application of the PRA were focused on dynamic risk management, then no additional criterion would be required to qualify for applying the PRA? Why or why not?

(i) Would your answer change depending on whether the application of the PRA was mandatory or not? Please explain your reasons.

(ii) If the application of the PRA were optional, but with a focus on dynamic risk management, what criteria regarding starting and stopping the application of the PRA would you propose? Please explain your reasons.

As noted in our response to Q15, we do not support the application of accounting for hedges of open portfolios with a scope focused on dynamic risk management.

(b) Do you think that if the scope of the application of the PRA were to be focused on risk mitigation, additional eligibility criteria would be needed regarding what is considered as risk mitigation through hedging under dynamic risk management? Why or why not? If your answer is yes, please explain what eligibility criteria you would suggest and, why.

**(i) Would your answer change depending on whether the application of the PRA was mandatory or not?
Please explain your reasons.**

**(ii) If the application of the PRA were optional, but with a focus on risk mitigation, what criteria regarding starting and stopping the application of the PRA would you propose?
Please explain your reasons.**

As noted in our response to Q16, we do not support a mandatory application of accounting for hedges of open portfolios.

We do not believe additional eligibility criteria should be required, other than requiring the accounting for hedges of open portfolios should be based on an entity's risk management strategy and objectives and the existence of an economic relationship.

Question 18—Presentation alternatives

(a) Which presentation alternative would you prefer in the statement of financial position, and why?

We support the approach of presenting the revaluation adjustment in a separate single net line item in the Statement of Financial Position. We believe that this approach provides information to enable users to more easily understand the accumulated net effect arising from the application of accounting for hedges of open portfolios. In addition, since the entity's risk management is performed on a net basis, any allocation of the revaluation effect to the different assets and liabilities would be arbitrary.

(b) Which presentation alternative would you prefer in the statement of comprehensive income, and why?

We support the actual net interest income presentation. Under this approach, net interest accruals from the hedging instruments would be reported as part of net interest income which provides relevant information to understand the financial information before and after the effect of accounting for hedges of open portfolios by presenting the actual interest revenue and expenses separately from the results of the risk mitigation activities.

(c) Please provide details of any alternative presentation in the statement of financial position and/or in the statement of comprehensive income that you think would result in a better representation of dynamic risk management activities. Please explain why you prefer this presentation taking into consideration the usefulness of the information and operational feasibility.

We have not identified any further alternative presentations.

Question 19—Presentation of internal derivatives

(a) If an entity uses internal derivatives as part of its dynamic risk management, the DP considers whether they should be eligible for inclusion in the application of the PRA. This would lead to a gross presentation of internal derivatives in the statement of comprehensive income. Do you think that a gross presentation enhances the usefulness of information provided on an entity's dynamic risk management and trading activities? Why or why not?

(b) Do you think that the described treatment of internal derivatives enhances the operational feasibility of the PRA? Why or why not?

(c) Do you think that additional conditions should be required in order for internal derivatives to be included in the application of the PRA?
If yes, which ones, and why?

(a) – (c)

We do not support the application of an accounting approach that leads to a gross presentation of internal derivatives in the statement of comprehensive income as this would contradict to the consolidation principles in IFRS.

Question 20—Disclosures

(a) Do you think that each of the four identified themes would provide useful information on dynamic risk management? For each theme, please explain the reasons for your views.

(b) If you think that an identified theme would not provide useful information, please identify that theme and explain why.

**(c) What additional disclosures, if any, do you think would result in useful information about an entity's dynamic risk management?
Please explain why you think these disclosures would be useful.**

(a) – (c)

We believe that the Board should develop accounting principles regarding disclosures, as opposed to detailed disclosure requirements. This could be consistent with the Board's current disclosure initiative. If the aim of the disclosures is to enable users to better understand companies' dynamic risk management activities, then the disclosure requirements should consider the key risks that arise from those activities and how the risks are monitored, measured and managed.

Question 21—Scope of disclosures

(a) Do you think that the scope of the disclosures should be the same as the scope of the application of the PRA? Why or why not?

(b) If you do not think that the scope of the disclosures should be the same as the scope of the application of the PRA, what do you think would be an appropriate scope for the disclosures, and why?

As noted in our response to Q15, we support an approach based on risk mitigation and believe that the disclosures should be aligned with this approach. It may be useful to provide additional disclosures on residual interest rate sensitivity for the dynamic risk management activity. However, we do not believe that it would be appropriate in terms of cost and benefit to require the introduction of the full PRA model just for disclosure purposes.

Question 22—Date of inclusion of exposures in a managed portfolio

Do you think that the PRA should allow for the inclusion of exposures in the managed portfolios after an entity first becomes a party to a contract? Why or why not?

(a) If yes, under which circumstances do you think it would be appropriate, and why?

We support the inclusion of exposures in the managed portfolios after an entity first becomes a party to a contract if that is consistent with the entity's risk management strategy and objectives. We believe that all exposures should be included in the scope of application of this accounting model at the time an entity decides to mitigate the managed risk in a net open position. This decision may be taken by an entity at points in time other than inception of the risk exposures.

(b) How would you propose to account for any non-zero Day 1 revaluations? Please explain your reasons and comment on any operational implications.

We believe this question should be addressed at a future stage of the process once the accounting model is further developed.

Question 23—Removal of exposures from a managed portfolio

(a) Do you agree with the criterion that once exposures are included within a managed portfolio they should remain there until derecognition? Why or why not?

(b) Are there any circumstances, other than those considered in this DP, under which you think it would be appropriate to remove exposures from a managed portfolio? If yes, what would those circumstances be and why would it be appropriate to remove them from the managed portfolio?

(c) If exposures are removed from a managed portfolio prior to maturity, how would you propose to account for the recognised revaluation adjustment, and why? Please explain your reasons, including commenting on the usefulness of information provided to users of financial statements.

(a) – (c)

The IFRS 9 general hedging model precludes a company voluntarily terminating a designated hedging relationship if the risk management objective has not changed. To consistent with IFRS 9, we believe that an entity should not de-designate, and thereby discontinue the application of accounting for hedges of open portfolios, if it still meets the entity's risk management objective.

Question 24—Dynamic risk management of foreign currency instruments

(a) Do you think that it is possible to apply the PRA to the dynamic risk management of FX risk in conjunction with interest rate risk that is being dynamically managed?

(b) Please provide an overview of such a dynamic risk management approach and how the PRA could be applied or the reasons why it could not.

(a) – (b)

In the context of the portfolio hedge accounting, we support that a model should be developed that permit the inclusion of foreign currency risk if both interest rate and foreign currency risk are hedged together (e.g. cross-currency interest rate swaps).

Question 25—Application of the PRA to other risks

(a) Should the PRA be available for dynamic risk management other than banks' dynamic interest rate risk management? Why or why not? If yes, for which additional fact patterns do you think it would be appropriate? Please explain your fact patterns.

(b) For each fact pattern in (a), please explain whether and how the PRA could be applied and whether it would provide useful information about dynamic risk management in entities' financial statements.

(a) – (b)

We believe that the accounting for hedges of open portfolio should be available for hedges of other than interest rate risk and for entities in industries other than the banking industry. As noted in our covering letter, the DP is heavily focused on banks and interest rate risk which makes it difficult to assess the implications of the approach for other types of entities and other types of risk.

Question 26—PRA through OCI

Do you think that an approach incorporating the use of OCI in the manner described in paragraphs 9.1–9.8 should be considered? Why or why not? If you think the use of OCI should be incorporated in the PRA, how could the conceptual and practical difficulties identified with this alternative approach be overcome?

We do not believe the PRA, which is based on a fair value approach, should be accounted for in OCI. We do believe, however, that there is merit in exploring a cash flow hedge accounting model that is very closely aligned with how risk is mitigated in practice, thereby the use of OCI would be appropriate.

~ End ~