ASC
ACCOUNTING STANDARDS COUNCIL
SINGAPORE

18 June 2019

Mr Hans Hoogervorst
Chairman
International Accounting Standards Board
Columbus Building
7 Westferry Circus
Canary Wharf
London E14 4HD
United Kingdom

(By online submission)

Dear Hans

RESPONSE TO EXPOSURE DRAFT ON INTEREST RATE BENCHMARK REFORM (PROPOSED AMENDMENTS TO IFRS 9 AND IAS 39)

The Singapore Accounting Standards Council appreciates the opportunity to comment on the Exposure Draft on *Interest Rate Benchmark Reform* (Proposed amendments to IFRS 9 and IAS 39) (the ED) issued by the International Accounting Standards Board (the IASB) in May 2019.

We welcome the IASB's approach to address the financial reporting issues that could arise from the interest rate benchmark reform (the reform).

Subject to our comments below, we are generally supportive of the IASB's proposals to provide relief from specific forward-looking hedge accounting requirements in response to the uncertainties of the reform during the pre-replacement period. We agree that useful information does not result from discontinuation of hedge accounting solely due to such uncertainties before the reform's economic effects are known, or preclusion of new hedge designations that would have otherwise qualified if such uncertainties are not present.

We are also supportive of the IASB's decision to not provide relief from all consequences of the reform, particularly changes in the economics of hedged items and hedging instruments that should be reflected in the financial statements.

Our specific comments on the ED proposals are as follows:

Scope of proposed amendments: Other risks affected by the reform

We note that the ED does not address hedges of other types of risk that may be affected by the uncertainties of the reform.

Address: The Secretariat, Singapore Accounting Standards Council,
10 Anson Road, #05-18, International Plaza, Singapore 079903.
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Specifically, the uncertainties affect all hedged items and hedging instruments of which cash flows are based on an existing interest rate benchmark, which may include hedging relationships of non-interest rate risk. An example is hedges of foreign currency risk using floating-for-floating cross currency interest rate swaps that reference existing interest rate benchmarks. Similar to hedges of interest rate risk, there may be uncertainties in terms of the timing and the amount of future cash flows because the hedging instrument is expected to be amended at some point to reference alternative interest rates.

Therefore, the IASB should consider refining the scope of the proposed amendments to avoid consequences similar to those addressed by the ED. For example, the scope may be defined based on hedging relationships that involve financial instruments containing interest rate benchmark-based cash flows, rather than simply hedging relationships of interest rate risk.

Separate identification: Wider implications for hedges of other risks

We note that the proposed amendment may have wider implications for hedging relationships that are outside the scope of the ED.

According to the February 2019 IASB staff paper, it could be argued that separate identification of a risk component is required only at initial designation of a hedging relationship. This alternative interpretation implies that it is possible for entities to have re-assessed separate identification with different degree of robustness, as part of the ongoing process to determine that hedged items remain eligible in order to continue with hedge accounting. For example, an entity may have implicitly determined that a hedged risk component remains separately identifiable, in the absence of significant changes to the particular market structure or as a conclusion drawn from continuing hedge effectiveness.

While the proposed amendment adds clarity to the requirement for continuous assessment of separate identification, it may change how entities perform the assessment to demonstrate separate identification. As the scope of the proposed amendments is limited to hedging relationships of interest rate risk, entities that have hedging relationships of other types of risks may not have considered potential implications for the existing practice.

Without delaying the finalisation of the proposed amendments, the IASB could consider separate work to determine whether there would be significant implications to practice with respect to hedging relationships of other types of risk, and if so, how those implications should be addressed.

Prospective assessments: Premature discontinuation from end of application

We note that premature discontinuation of hedge accounting may still occur because of the proposed end to an application of the proposed amendment for prospective assessments.

Specifically, an entity is required to discontinue hedge accounting during the period in which *either* the hedged item or the hedging instrument is amended, if it fails the prospective assessments using the pre-replacement cash flows of one instrument and the post-replacement cash flows of the other instrument. Such discontinuation may be premature, particularly if the

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subsequent contractual amendment to the first-mentioned instrument would have allowed the entity to meet the prospective assessments. In practice, it can be challenging to manage contractual amendments, such that both hedged items and hedging instruments would transition to alternative interest rates at the same time, because of the different mechanisms and counterparties that may be involved for derivative and cash instruments.

To avoid premature discontinuation, the IASB may consider an alternative relief that requires an entity to cease applying the proposed amendment for prospective assessments only when the uncertainty is no longer present for *both* the hedged item and the hedging instrument (subject to the condition of discontinued hedging relationship).

One of the consequences of the alterative relief is that the financial statements would not reflect the impact of temporarily failing the prospective assessments. Nevertheless, paragraph BC40 of the Basis for Conclusions on the ED states that the IASB 'expects a scenario in which there is significant divergence between hedged items and hedging instruments for an extended time period to be unlikely'. It follows that the relief should not apply, if the contractual divergence persists for such an extended time period that the hedging relationship fails to achieve its risk management objective. Moreover, any hedge ineffectiveness that may arise from temporary contractual divergence will continue to be recognised in the financial statements. On the whole, the alternative relief is likely to achieve a better balance of costs and benefits.

Retrospective application: Reinstatement of discontinued hedging relationships

We note that the proposed retrospective application does not result in a particular transition outcome described in the Basis for Conclusions on the ED.

Specifically, paragraph BC46 states that 'retrospective application of the amendments would not allow reinstating hedge accounting that has already been discontinued'. However, retrospective application means that an entity applies the proposed amendments as if they had always been applied, which would require the entity to reinstate hedge accounting for previously designated hedging relationships that have been discontinued solely due to the uncertainties of the reform.

Therefore, the IASB should refine its articulation of the intended transition outcomes in paragraph BC46. This would avoid confusion about how retrospective application of the proposed amendments would interact with prospective application of the hedge accounting requirements.

Replacement issues: Need for timely solutions

We expect many of the replacement issues to be broader in scope and to be significantly more challenging than the pre-replacement issues. Since some jurisdictions have already made clear progress in their reform, we encourage the IASB to expedite work on the replacement issues, with the aim of developing timely guidance to ease transition to alternative interest rates.

We hope that our comments will contribute to the IASB's deliberation on the ED. Should you require any further clarification, please contact our project manager Yat Hwa Guan at Guan_Yat_Hwa@asc.gov.sg.

Yours faithfully

Suat Cheng Goh
Technical Director
Singapore Accounting Standards Council