



Mr Hans Hoogervorst
Chairman of the
International Accounting Standards Board
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Dear Hans,

IASB Exposure Draft ED/2019/1 *Interest Rate Benchmark Reform – Proposed amendments to IFRS 9 and IAS 39*

On behalf of the Accounting Standards Committee of Germany (ASCG) I am writing to comment on the Exposure Draft ED/2019/1 *Interest Rate Benchmark Reform – Proposed amendments to IFRS 9 and IAS 39* issued by the IASB on 3 May 2019 (herein referred to as 'ED'). We appreciate the opportunity to comment on the ED.

The IASB proposes to amend IFRS 9 *Financial Instruments* and IAS 39 *Financial Instruments: Recognition and Measurement* to provide relief from particular hedge accounting requirements in the run-up to the IBOR reform. We welcome IASB's efforts to address these pre-replacement issues in a timely manner and support the proposed amendments.

When the interest rate benchmark reform was first raised as a potential issue for financial reporting last year, we observed market uncertainty regarding the continuation of hedge accounting in view of future changes in reference interest rates. In the meantime, the parameters of the interest rate benchmark reform have become more apparent in several jurisdictions. Against this background, and from the facts we have seen so far, we consider that the upcoming changes in reference interest rates should not lead to discontinuation of hedge accounting at this point in time. We concur with the view of those that see the proposed amendments are of clarifying nature.

Where we suggest the Board takes a closer look, though, is at the specific differences in the cash flow hedge accounting provisions of IFRS 9, and IAS 39, respectively. For example, IFRS 9 does not have the rigid retrospective hedge effectiveness assessment (the 80-125% corridor) whereas IAS 39 does; IAS 39 allows for voluntary de-designation of hedges, IFRS 9 does not; etc. When reading the text of the proposed amendments to the two standards, it appears to us that the differences in approach may not have been thought in each and every case.

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Lastly, while we can understand the need for supporting additional disclosure requirements once the effects of the reform come into play, we have doubts whether the specificity is indeed needed at this stage. Similarly, we question whether all of the proposed additions are indeed proportionate and significant to every entity and suggest making clear that these requirements follow the general proportionality approach of IFRS 7. In our view, the disclosure requirements should focus on the information as to what extent an entity is affected by the interest rate benchmark reform.

As the specific conditions and details of the replacement of existing interest rate benchmarks with alternatives have yet to be finalised, the ED cannot and does not address replacement issues. The IASB intends to assess these issues separately in a second project phase, which in our view is the appropriate approach. That said, we encourage the IASB to consider issues that might affect financial reporting when interest rate benchmarks are replaced with alternative interest rates as soon as possible. Given the dynamic developments in individual jurisdictions relating to particular interest rate benchmarks, a timely deliberation of replacement issues seems warranted in order to provide clarity to constituents.

Our detailed comments in response to the ED questions are laid out in the appendix to this letter. If you would like to discuss our comments further, please do not hesitate to contact Kristina Schwedler (schwedler@drsc.de) or me.

Yours sincerely,

Andreas Barckow

President

Appendix – Answers to the questions in the DP

Question 1 [paragraphs 6.8.4–6.8.6 of IFRS 9 and paragraphs 102D–102F of IAS 39]

Highly probable requirement and prospective assessments

For hedges of interest rate risk that are affected by interest rate benchmark reform, the Board proposes amendments to IFRS 9 and IAS 39 as described below.

(a) For the reasons set out in paragraphs BC8–BC15, the Board proposes exceptions for determining whether a forecast transaction is highly probable or whether it is no longer expected to occur. Specifically, the Exposure Draft proposes that an entity would apply those requirements assuming that the interest rate benchmark on which the hedged cash flows are based is not altered as a result of interest rate benchmark reform.

(b) For the reasons set out in paragraphs BC16–BC23, the Board proposes exceptions to the hedge accounting requirements in IFRS 9 and IAS 39 so that an entity would assume that the interest rate benchmark on which the hedged cash flows are based, and/or the interest rate benchmark on which the cash flows of the hedging instrument are based, are not altered as a result of interest rate benchmark reform when the entity determines whether:

(i) there is an economic relationship between the hedged item and the hedging instrument applying IFRS 9; or

(ii) the hedge is expected to be highly effective in achieving offsetting applying IAS 39.

Do you agree with these proposals? Why or why not? If you agree with only parts of the proposals, please specify what you agree and disagree with. If you disagree with the proposals, please explain what you propose instead and why.

We welcome the IASB's intention to provide relief and exempt entities from specific hedge accounting requirements in IAS 39 and IFRS 9. As stated in our cover letter, we observed market uncertainty regarding the compliance with those requirements in light of the upcoming IBOR reform. The relief clarifies that uncertainty regarding the timing and the amount of future cash flows of the hedged item and the hedging instrument do not lead to discontinuation of hedge accounting. We agree with the IASB that the volatility resulting from the discontinuation of these hedging relationships would not provide decision-useful information.

Hence, we support the proposed exception from the highly probable requirement as this exemption appropriately presents the relief intended.



We also support the proposed exception from prospective assessments and agree with the reasoning in BC16-BC23. BC22 clarifies that the relief is not intended to change the measurement of hedge effectiveness or to change how hedges are reflected in the financial statements. We consider this clarification to be helpful and appropriate.

Question 2 [paragraph 6.8.7 of IFRS 9 and paragraph 102G of IAS 39]

Designating a component of an item as the hedged item

For the reasons set out in paragraphs BC24–BC27, the Board proposes amendments to the hedge accounting requirements in IFRS 9 and IAS 39 for hedges of the benchmark component of interest rate risk that is not contractually specified and that is affected by interest rate benchmark reform. Specifically, for such hedges, the Exposure Draft proposes that an entity applies the requirement—that the designated risk component or designated portion is separately identifiable—only at the inception of the hedging relationship.

Do you agree with this proposal? Why or why not? If you disagree with the proposal, please explain what you propose instead and why.

We agree with the proposal for the same reasons discussed in our answer to question 1. The proposed relief rightly allows continued designation and avoids unnecessary volatility in financial reporting.

Question 3 [paragraphs 6.8.8–6.8.10 of IFRS 9 and paragraphs 102H–102J of IAS 39]

Mandatory application and end of application

(a) For the reasons set out in paragraphs BC28–BC31, the Board proposes that the exceptions are mandatory. As a result, entities would be required to apply the proposed exceptions to all hedging relationships that are affected by interest rate benchmark reform.

(b) For the reasons set out in paragraphs BC32–BC42, the Board proposes that the exceptions would apply for a limited period. Specifically, an entity would prospectively cease applying the proposed amendments at the earlier of:

(i) when the uncertainty arising from interest rate benchmark reform is no longer present with respect to the timing and the amount of the interest rate benchmark-based cash flows; and

(ii) when the hedging relationship is discontinued, or if paragraph 6.8.9 of IFRS 9 or paragraph 102I of IAS 39 applies, when the entire amount accumulated in the cash flow hedge reserve with respect to that hedging relationship is reclassified to profit or loss.

(c) For the reasons set out in paragraph BC43, the Board is not proposing an end of application in relation to the separate identification requirement.

Do you agree with these proposals? Why or why not? If you agree with only parts of the proposals, please specify what you agree and disagree with. If you disagree with the proposals, please explain what you propose instead and why.

We agree with the proposed mandatory application of the exceptions to all hedging relationships that are affected by the interest rate benchmark reform as we share the view expressed in BC28-BC29. Voluntary application of the proposed amendments could give rise to selective discontinuation of hedge accounting and corresponding reclassification of amounts recorded in other comprehensive income to profit or loss.

Further, we agree with the proposed provisions regarding the end of application which focus on the end of uncertainty arising from the interest rate benchmark reform.

In addition, we support not proposing an end of the application for the exemption from the separate identification requirement as we agree with the IASB's reasoning in BC43 that an end of application would contradict the objective of the relief.

Question 4 [paragraph 6.8.11 of IFRS 9 and paragraph 102K of IAS 39]

Disclosures

For the reasons set out in paragraph BC44, the Board proposes that entities provide specific disclosures about the extent to which their hedging relationships are affected by the proposed amendments.

Do you agree with these proposed disclosures? Why or why not? If not, what disclosures would you propose instead and why?

We support the general objective of the additional disclosure requirements. However, we question whether all of the proposed additions are indeed proportionate and significant to every entity and suggest making clear that these requirements follow the general proportionality approach of IFRS 7. Otherwise, we fear that the costs could outweigh the benefits for some entities.

In our view, the disclosure requirements should focus on the information as to what extent an entity is affected by the interest benchmark reform. As we believe that this will already be achieved by the requirements in paragraphs 24A(a) and 24B(a)(i) of IFRS 7, we fail to see why the other disclosure requirements (with reference to 24A(c)-(d), 24B(a)(ii), 24B(a)(iv) und 24(B)(b) of IFRS 7) would be necessary.



Additionally, we emphasise that – because of the suggested effective date – the disclosures will already be required for the comparative periods, i.e. the year 2019 or even 2018 should an entity wish to adopt the new provisions early.

Against this background, we suggest the Board reconsider the specific disclosures proposed against the objective of the disclosure requirements as a whole.

Question 5 [paragraphs 7.1.9 and 7.2.26(d) of IFRS 9 and paragraph 108G of IAS 39]

Effective date and transition

For the reasons set out in paragraphs BC45–BC47, the Board proposes that the amendments would have an effective date of annual periods beginning on or after 1 January 2020. Earlier application would be permitted. The Board proposes that the amendments would be applied retrospectively. No specific transition provisions are proposed.

Do you agree with these proposals? Why or why not? If you disagree with the proposals, please explain what you propose instead and why.

We agree with the proposed effective date and the permission of earlier application taking into account the demand for a fast solution of issues affecting financial reporting in the run-up to the IBOR-Reform. We also agree with the proposal to apply the amendments retrospectively. As regards the disclosure requirements, our agreement should be read in the context of our answer to question 4.

Additional comments / Further remarks

We note that IAS 39 and IFRS 9 place different demands on hedge accounting. These differences should be given more attention and should be addressed in the Exposure Draft. As examples we refer to

- the effectiveness test in context with the retrospective assessment required by IAS 39 and
- the optional termination of a hedging relationship under IAS 39 which should be discussed in connection with the mandatory application of the proposed amendments.