Deutsches Rechnungslegungs Standards Committee e.V.

Accounting Standards Committee of Germany

DRSC

ASCG • Joachimsthaler Str. 34 • 10719 Berlin

Sam Woods
Chair of the
International Accounting Standards Board
Columbus Building
7 Westferry Circus / Canary Wharf
London E14 4HD

Financial Reporting Technical Committee
Phone: +49 (0)30 206412-20
E-Mail: info@drsc.de

Berlin, 26 November 2026

Dear Sam,

ED/2025/1 *Risk Mitigation Accounting – Proposed amendments to IFRS 9 and IFRS 7*

On behalf of the Accounting Standards Committee of Germany, I am writing to comment on ED/2025/1 *Risk Mitigation Accounting – Proposed amendments to IFRS 9 and IFRS 7*, issued on 3 December 2025 (herein referred to as 'ED'). We appreciate the opportunity to comment.

Our approach to reaching views

We welcome the IASB's efforts to develop and propose an additional accounting model, which addresses the presentation of effects from risk management activities, and which shall be applicable in addition to hedge accounting.

The proposals have been deliberated by our main technical body, the Financial Reporting Technical Committee. In addition, we have established two working groups with representatives from the banking sector (and related auditors) and from the insurance industry (and related auditors). Further we conducted Joint Outreach Events, during which we have shared the IASB proposals with constituents in our jurisdiction. In this comment letter, we thus provide the sum of all views and findings from those activities. Yet, in acknowledging that the RMA model is designed from and for the banking sector, which obviously is the target audience of the proposals, our detailed comments primarily reflect views from that industry.

Within our following comments, we distinguish between proposals we support, those we consider inappropriate, and others which appear unclear.

General views on the proposals

Overall, we ***support*** the direction of the proposed risk mitigation accounting (herein referred to as 'the RMA model') being a model that aims at (i) presenting in financial statements effects from risk management activities for repricing risk by way of (ii) recognising a risk mitigation adjustment that temporarily defers recognition of gains and losses from derivatives, thereby reducing current accounting mismatches arising from the "mixed measurement model" under IFRS 9.

To be more precise, we ***basically concur*** with the stated objective of the RMA model, but we also believe that solving the asymmetrical accounting between hedged exposures and hedging derivatives arising from the mixed measurement model in IFRS 9 should be an equally important part of the stated objective. In addition, we concur with the mechanics of a new balance sheet item (appearing as an accrual) and its voluntary application. Further, we tentatively agree – in acknowledging the RMA as a new accounting approach – that the RMA model is (currently) restricted to interest repricing risk exposures. Though, a restriction on this single type of risk appears not principles-based.

However, we identified main elements of the RMA model which we consider conceptually ***inadequate***, as they are not aligned with current interest rate risk management practices in the banking industry, including the introduction of a number of concepts that are not consistent with interest rate risk management activities. The requirement of risk management on a *net* basis, the exclusion of *internal* derivatives from "designated derivatives", and the narrow set of items eligible for underlying portfolios do severely limit the circumstances under which RMA would be applicable. These constraints lack practical relevance and result in the RMA model not, or not fully, representing the economic effects of risk management activities. Ultimately, the RMA model as proposed appear to not reach, and even conflict with, its own objective.

At the same time, we identified some other proposals, or details of these, which we consider ***operationally burdensome***. First, determining the NRRE seem challenging from a conceptual and practical perspective. Second, quantifying this exposure for repricing time bands is not always in line with how risk is managed, and the interaction of risk limits appears difficult. Third, specifying an RM objective and replicating it through benchmark derivatives, along with the lower-of mechanics and determining unexpected changes, seem complex and artificial. In addition, the restriction for over-hedges is conceptually unclear and would lead to effects perceived as "artificial ineffectiveness".

While each of these elements raise problems on its own, the field tests undertaken by banks confirmed that many of the identified shortcomings are not isolated; instead, greater concerns result from the cumulative effect due to the interaction of the different elements in the RMA model. Taken together, these elements raise the fundamental question of whether RMA as a whole is an operable and robust model that properly reflects risk management.

Given the significant amendments that would be needed to address the fundamental concerns mentioned above, we believe that a re-exposure is needed, thereby allowing for further comments by stakeholders prior to finalising the model.

As regards the intended withdrawal of IAS 39, we take a clear ***view against***:

- IAS 39 should not be withdrawn until a robust and operationally viable model is available that can appropriately replace the existing IAS 39 portfolio fair value hedge accounting requirements as well as IAS 39 Micro Hedge Accounting reflecting both the European

carve out. Field testing of the proposed RMA model by the banking industry raises fundamental concerns as to whether this condition is currently met.

- As far as RMA will not be applicable, for all hedge relationships used to manage the banking book (including cross currency hedges), withdrawing IAS 39 would create a more significant gap than the gap in IFRS 9 that RMA is intended to address.
- For those still using IAS 39 hedge accounting, including particular portfolio fair value hedge accounting under IAS 39 and the associated "EU version", the proposed RMA model has not demonstrated yet to provide an appropriate replacement. Accordingly, withdrawal of IAS 39 should not be driven by the availability of RMA in itself, but by whether the final model is capable of replacing existing approaches without reducing the extent to which the accounting reflects actual risk management activities.

For more details on our findings on the proposals in the ED, we refer to our responses to the questions which are laid out in the appendix to this letter.

Industry-specific views on the proposals

The ***banking industry*** within our jurisdiction considers the proposed RMA model to be of significant importance given its interest rate risk exposures and the limitations of existing accounting requirements in reflecting the associated risk management activities directly in financial reporting. However, field testing indicates that the proposed Net Repricing Risk Exposure (NRRE) does not sufficiently align with the IRRBB exposures managed in practice and that the resulting accounting requirements can create significant complexity, accounting-driven volatility and outcomes that do not faithfully reflect risk management, raising fundamental doubts as to whether the proposed model can achieve its stated objective. The industry's field-test results further suggest that these challenges are not limited to individual requirements but arise from the architecture of the model itself. As a result, incremental amendments alone are not sufficient, rather a holistic redesign of the currently proposed RMA model is required to achieve a robust and operationally viable solution. Therefore, a more fundamental reconsideration, including a full re-exposure, is necessary before replacing the existing IAS 39 portfolio hedge accounting approaches.

For more details about the banking sector's view, we refer to our responses to Q1-Q10.

The ***insurance industry*** within our jurisdiction also takes a clear view on the current proposals (however, less distinct as regards specific aspects in the ED). It is, in summary: The RMA model is relevant in limited circumstances only, and it does not appear applicable at all for that industry. Making insurance contracts eligible for underlying portfolios would be necessary but not sufficient for the RMA model to become suitable for insurers.

For more details about the insurance sector's view, we refer to our response to Q11.

From ***any other industries*** within our jurisdiction, we did not receive distinct views. The overall perception is that the RMA model seems to be of limited interest and/or relevance for them.

Additional fieldwork and conclusion

We are aware that the IASB had published a request for fieldwork. As a standard-setter, we were not in a position to undertake fieldwork on our own. However, we have communicated to our stakeholders about that opportunity initiated by the IASB.

We have been informed that German entities in the banking sector were undertaking field tests, and the results from these tests are reflected in this comment letter. We are not aware whether entities from other industries were also undertaking field tests.

We encourage the IASB to consider field-test results carefully, since operational feasibility and alignment with risk management practice are essential to the RMA model's usefulness.

Given the fundamental concerns about the proposed model and, in particular, given the significant amendments that will be needed to address these concerns, we believe that a comprehensive reconsideration, including a re-exposure, is necessary before finalising the RMA model and embedding it in IFRS 9, and before retiring IAS 39. We feel it worth mentioning, that a more intense re-deliberation and, potentially, a re-exposure is preferable to a soon or timely finalisation (and availability) of the model.

If you would like to discuss our views and comments further, please do not hesitate to contact Jan-Velten Große (grosse@drsc.de) or me.

Yours sincerely,

Sven Morich

Vice President

Appendix – Answers to the questions in the ED

Question 1 – Objective and scope

The IASB proposes:

*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 7.1.4.*

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

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.

a) Objective and Scope

We generally ***agree*** with the RMA objective to "*represent in financial statements the economic effect of an entity's risk management activities*" (ED 7.1.3). Further, we support the idea of recognising a risk mitigation adjustment, as a new balance sheet item that temporarily defers recognition of gains and losses from derivatives, thereby effectively reducing current accounting mismatches. However, we believe that eliminating accounting mismatches arising from the mixed measurement model in IFRS 9 should play a more important role in setting the objective for RMA, including mismatches in OCI from financial assets at FVOCI.

Apart from this, we are aware that the insurance industry takes a more critical view as regards (i) the need for an RMA model and (ii) the recognition of a "risk mitigation adjustment", both addressing accounting mismatches related to external derivatives. We expose that sector's view in more detail, and holistically, further below (see our answer on Q11).

We consider the RMA model, applicable in addition to hedge accounting, being relevant and helpful for entities that consider hedge accounting not a sufficient solution. However, we acknowledge that the relevance of such a model varies across industries. We tentatively perceive that an RMA model is very relevant for the banking industry, but significantly less relevant for the insurance industry, and – presumably – almost irrelevant for other sectors.

In contrast, we ***do not agree*** with the RMA scope of *"… the entity mitigates repricing risk on a net basis and the entity's business and risk management activities have the characteristics specified in para. 7.1.4.*" (ED.Q1(b)), as it narrows down severely the circumstances under which RMA is applicable. Particularly, managing *repricing* risk from *underlying portfolios* (as defined in the ED) on a *net basis* by using *external* derivatives are elements, or characteristics, that do not always correspond with how risks are managed in practice. Therefore, the scope should be expanded at least to include circumstances when repricing risk is managed on a gross basis using derivatives in accordance with the respective risk management strategy.

As regards the restriction to repricing risk, we like to comment in more detail and in ***a torn way***: On the one hand, we tentatively agree with this restriction – in acknowledging that (i) for the time being RMA is a new accounting approach proposed to fill a current gap in IFRS 9, and (ii) in the future the IASB will decide "whether the RMA model be extended to other businesses" (ED.IN19), presumably meaning a scope extension to other types of risk and, hopefully, to further items eligible for underlying portfolios. On the other hand, from a conceptual perspective we consider limiting the RMA model to repricing risk an inadequate restriction. Besides, the current definition and understanding of „repricing risk" lack some clarity. In detail, it seems unclear whether currency basis risks are comprised, whether inflation is an eligible part of repricing risk, and how tenor basis risks, non-linear risks or optionalities be included.

This all said, we consider the RMA scope as proposed leading to a limited, and therefore distorted, representation of economic effects of risk management activities. Overall, the RMA model – with the scope and criteria as proposed – appear to effectively not reaching, and even conflicting with, its own objective.

For further details on scope limitations, we refer to our answers on the following questions.

b) Voluntary application

We ***fully agree*** with RMA being an option, ie. applied on a voluntary basis (ED 7.1.5). We also agree with applying *all* RMA requirements, as soon as an entity decides to apply RMA.

c) Documentation

Overall, we consider the condition of formally documenting that and how RMA is applied to be consequent and ***generally appropriate***. Yet, we have not deliberated in depth whether all details about documentation seem appropriate and feasible.

Question 2 – Underlying portfolios

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. 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**;*
*b) financial **liabilities** classified as subsequently measured at **amortised cost**; 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.*

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.

We ***agree*** with the general idea of RMA be applied based on underlying portfolios. We agree that the risk exposure effectively derives from a portfolio (or portfolios) which need(s) to be defined, for risk management purposes as well as for accounting purposes.

We ***also agree*** with all items currently proposed to be eligible, which are: financial assets, financial liabilities, future transactions (comprising expected reinvestments and refinancing, firm commitments, and highly probable forecast transactions), and hedged exposures (as described in ED 7.2.2).

Nevertheless, the restriction of financial instruments eligible only if measured at amortised cost (AC) or at FV through OCI (FVOCI) seem ***inadequate***. Moreover, we acknowledge that financial instruments measured at FV through PL (FVPL) would also deserve being eligible if those are included in management of net repricing risk. Certainly, from an accounting perspective the mechanism of RMA leading to recognition of a “risk mitigation adjustment” is nonsensical for FVPL instruments – as FVPL instruments do not contribute to those accounting mismatches relevant for RMA purposes. However, from a risk management perspective (and given the RMA objective) the measurement category of a financial instrument is less relevant. Since accounting measurement categories do not matter for risk management purposes, categories should not matter for RMA purposes (ie. eligibility for underlying portfolio). Besides, in practice it might be difficult to separate financial instruments and resulting (repricing) risk exposure after accounting measurement categories.

Even more so, we deem it ***inadequate*** that other items are not eligible at all. We deem the following items be worth reconsidering their eligibility:

- Lease receivables and liabilities;
- Pension liabilities;
- Insurance contract assets and liabilities;
- Equity model book;
- Additional Tier 1 (AT1) instruments.

Field tests conducted by the banking sector have proven that it is essentially necessary to include all items that are used in risk management activities to be eligible for inclusion in the application of RMA. This would avoid artificial volatility in P&L arising from the exclusion of such items from the scope of RMA, while also reducing complexity and costs.

Further, there is clear evidence that for the insurance sector eligibility of insurance contracts as well as FVPL instruments would be essentially necessary, although not sufficient. For more details on this, we refer to our answer on Q11.

Overall, eligibility of items should generally not depend on their prevalence but be considered from a conceptual perspective. This said, we deem that both the risk management and the accounting perspective would warrant those items be included in underlying portfolios for RMA.

In addition to our comments above, we have further comments that point to some details which appear ***unclear***.

First, including equity in underlying portfolios by way of internal modelling (ie. equity modelling) is essential. While we perceive that the proxy as described in B7.2.17 is intended to replace the direct designation of equity modelling in the underlying portfolios, we struggle to understand how this could, or should, be effectively implemented when applying the RMA model. In particular, the example in B7.2.17 could be interpreted as allowing only variable-rate financial assets to be designated in underlying portfolios as proxy for the equity modelling. Moreover, banks also use equity modelling to fund fixed-rate financial assets, and therefore the proxy should be expanded accordingly. As an alternative proposal to the proxy solution, the IASB could permit a fixed-rate payer position that replicates the modelled equity to be designated in the underlying portfolios, so as to achieve better alignment with risk management practices.

In this context, we note that feedback received during our outreach activities indicates that the RMA model could accommodate equity modelling, including eg, AT1 instruments, where this is common practice. Despite this, we continue to believe that AT1 instruments should by themselves be eligible for inclusion in underlying portfolios, as those instruments are essentially debts and have the economic characteristics of a debt instrument. As this is a wide ***area of uncertainty***, we suggest further explanation on a principle's level – without too many details.

Second, it is unclear whether or to what extent internal transactions are eligible for underlying portfolios. While the wording strictly excludes those transactions (ED 7.2.3), we feel that the idea of underlying portfolios, from which the repricing risk exposure be aggregated, allow for internal transactions to be included given a robust demonstration of externalisation. Further, risk management effectively does include internal transactions when identifying and mitigating risk exposures (e.g. where repricing risk is managed at a decentralised level). Consequently, an RMA model fully ignoring these transactions/items seems to contradict the RMA's stated objective. This given, we would appreciate ***more clarity***.

Question 3 – Net repricing risk exposure

*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 repricing risk exposure in each repricing time band.*

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.

We consider determining the NRRE as a crucial element of the RMA model. While it seems basically clear *why* the NRRE be determined, we are unclear about *how* it be determined, even more so since it shall be consistent with how risk management decisions are made (ED 7.2.7, 7.2.9). To be more precise, the following requirements lack clarity in detail:

- Disaggregation into repricing time bands: As far as risk management considers risk exposures across time bands, a breakdown into time bands for NRRE purposes would be difficult. Though, as the NRRE shall be determined in accordance with the risk management strategy, we feel that this requirement is open for interpretation and provides leeway.
- Disaggregation based on mitigated rates: While the ED refers to the mitigated rate (ED 7.2.8) for which a (separate) NRRE be determined, we are not fully clear about this requirement and its practical consequences. Depending on the risk management approach, an entity may manage its underlying portfolio based on *one* mitigated rate, independent of the currency of a single exposure. If NRREs are constrained to a single currency (i.e. multi-currency NRREs are not permitted), this would lead to a misalignment with risk management and may require the split of designated derivatives to different NRREs, which is economically inappropriate. Further uncertainties arise when disaggregating underlying portfolios based on *different* mitigation rates.
- Using cash flow- or fair value-based measure(s): Selecting appropriate FV- or CF-based measures is not sufficiently clear (which risk metrics to be used, how often/in which time bands they are available). In this context, it is also not clear whether tenor-based risks as well as optional/non-linear risks should be included, even though their inclusion is common practice in risk management.

Beyond that, determining the NRRE appear even more questionable for the insurance sector. Insurers typically assess and mitigate repricing risk by focussing on the economic interaction between assets and insurance liabilities (ALM) over time, ie. exposures are determined rather on the basis of duration than on time bands.

Despite the aforementioned lack of clarity in detail, we consider it important that the RMA model retains sufficient flexibility for determining the NRRE in a manner that is consistent with an entity's actual risk management.

Since determining the NRRE per time band is very much connected with the idea of specifying a risk mitigation objective (a concept that is not found in an entity’s risk management activities), we also refer to our answer on Q5.

Question 4 – Designated derivatives

*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.*

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.

We understand, and ***concur*** with, the idea that external derivatives used to mitigate the entity's repricing risk exposure in accordance with the risk management strategy are eligible as designated derivatives under the RMA model.

We further understand that external derivatives do evidence both the existence of a repricing risk exposure and the intention to mitigate this risk exposure. If so, we feel that, as a matter of principle, *any* derivate that is effectively used to mitigate that risk (in accordance with the risk management strategy) equally has the purpose of risk mitigation. Hence, derivatives both with external and with internal parties do fit that purpose.

This given, we are ***unsure*** whether, and why, internal derivatives are not eligible as designated derivatives. While the wording strictly excludes them (ED 7.3.4), we feel that the concept of designated derivatives, used to effectively mitigate the entity's repricing risk (in accordance with the risk management strategy), would allow for internal and external derivatives to be equally eligible. Even more so, we note that feedback received during our outreach activities indicates that the RMA model is not intended to misunderstand (or distort) risk management practices, which widely make use of internal derivatives and, therefore, would justify its eligibility. Obviously, making internal derivatives eligible as designated derivates would require a robust demonstration of externalisation, which is already the case under CRR / FRTB regulations for evidencing the externalisation of interest rate risk in the banking book.

This all said, we would appreciate explicit clarity about whether a proof of externalisation does (or does not) make internal derivatives eligible.

Further, we perceive a ***lack of clarity*** on how cross currency hedges can be reflected under the RMA model. Since, in practice, designating cross currency hedges under IFRS 9 hedge accounting is not always appropriate or possible, we deem those hedges a relevant use case for the RMA Model and suggest further clarification as regards cross currency derivatives.

Question 5 – Risk mitigation objective and benchmark derivatives

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.*

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.

a) Risk Mitigation Objective

We are ***not convinced*** of the idea to specify a "risk mitigation objective" (RMO), thereby determining and disaggregating an amount of repricing risk for each time band, which an entity effectively mitigates through designated derivatives.

We consider the RMO (along with benchmark derivatives) a theoretical concept for illustrating, but not really matching with, actual risk management. This is perceived to be a source of systematic deviations between risk management practice and the presentation of its effects in financial statements.

First, specifying an RMO is not aligned with risk management activities as risk management does not differentiate between the risk stemming from outright transactions and derivative transactions. Rather, risk is measured on a holistic basis and aims to achieve overall risk limits. The consequence of this is (depending on the business model) that over-hedging can occur in the application of the RMA model.

Second, an RMO seem to not really comply with how an exposure is disaggregated. Moreover, RMO artificially disaggregates an exposure into time bands, ie. one "sub-exposure" for each time band. Instead, risk management often considers, and mitigates, risk exposures across time bands. The proposed concept of RMO comprises an "over-hedge test", which we consider inadequate. This test would lead to unjustified volatility in profit or loss, whenever derivatives for risk management purposes do not exactly hedge one repricing time band but instead adjacent buckets, eg. for reasons of market liquidity or cost effectiveness. As a result, over-hedging will occur in the adjacent buckets leading to unjustified P&L volatility.

This could potentially be overcome by allowing the "over-hedge test" on a level higher than a time band, eg. portfolio level.

b) Benchmark Derivatives

Along with our findings above, some constituents are ***not convinced*** of the idea to construct "benchmark derivatives", thereby replicating timing and amount of repricing risk. Similarly, we consider benchmark derivatives (along with the RMO) as too much of a theoretical concept, not really complying with actual risk management. This is also perceived to cause systematic deviations, namely effects that are considered as ineffectiveness from an accounting view, but not from a risk management perspective.

Further challenges arise due to ***some uncertainties***. First, the condition of benchmark derivatives having an initial fair value of zero (ED 7.4.5) seems challenging and contradicting to (effective) risk management. This is particularly relevant when options are included (their time value is not zero) and in the case of transition to RMA and business combinations. Second, it appears unclear what discount rate (e.g. OIS discounting) should be used for constructing benchmark derivatives.

All this make benchmark derivatives appear a complex element in the RMA model.

c) Unexpected changes

It seems ***unclear*** how to identify "unexpected changes" leading to benchmark derivatives be adjusted (ED 7.4.6). As the ED does not define "unexpected changes", distinguishing unexpected from expected changes is conceptually difficult and complex. Applying this concept would require to identify "unexpected changes" affecting the underlying items and to track those items comprehensively. Overcoming this challenge requires practical mechanisms to be implemented and performed, and we advocate for sufficient flexibility and relief.

This given, from a conceptual as well as a practical perspective we suggest omitting this test (for unexpected changes) and providing clarification for above mentioned uncertainties.

Ultimately, the concept of RMO along with benchmark derivatives – and in particular the over-hedge test – appear to be designed to prevent abuse and are neither conceptually sound nor do they fully comply with risk management practice.

Question 6 – Recognising and measuring the risk mitigation adjustment

The IASB proposes that an entity:

*a) recognise **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.*

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.

Recognition of a "risk mitigation adjustment" in the statement of financial position appears to be a new, but ***useful conceptual idea***. A balance sheet item that temporarily defers recognition of gains and losses from derivatives, thereby effectively reducing current accounting mismatches, is preferable to other IASB solutions considered in the past (eg. recognition of derivative effects in OCI).

We also ***concur*** with the principle of recognising in profit or loss the risk mitigation adjustment amount when repricing differences from items in underlying portfolios affect profit or loss and immediately when repricing differences from underlying items are no longer expected to occur.

As a caveat, we like to note that the concept of risk mitigation adjustment would need to be reconsidered, or refined, if FVPL assets/liabilities were also eligible for underlying portfolios.

Nevertheless, we have ***significant concerns*** regarding some of the proposed mechanics for determining the risk mitigation adjustment and their interaction with other elements of the RMA model.

- First, some uncertainty relates to the comparison of benchmark derivatives with designated derivatives ("lower-of test"). Issues lacking clarity are (a) whether this test be based on clean or dirty fair value, and (b) whether this test be performed for each time band or only in aggregate, in other words, can deviations within individual time bands be ignored if there is no (or smaller) overall deviation, and some further details. More fundamentally, the lower-of test should be considered together with the other safeguards already incorporated into the model, including the restriction on over-hedging and the excess test. The cumulative effect of these requirements may result in accounting outcomes and P&L volatility that do not reflect the economic effects of the entity's risk management activities.
- Second, assessing and determining a risk mitigation adjustment excess ("*excess test*") raises more fundamental concerns than a lack of clarity in its detailed application. One is assessing whether there is an "*indication that the amount … might not be realised in full*"

(ED 7.4.11), ie. whether there are trigger events (and which). Another is distinguishing unexpected (from expected) NRRE changes. Field testing by the banking industry indicates that the operation of the excess test can result in reductions of the risk mitigation adjustment and resulting P&L effects that are driven by the mechanics of the RMA model rather than by changes in the underlying risk management activity.

- Thirdly, we deem an "excess" resulting from "unexpected changes" to be rare. Moreover, if adjusting benchmark derivatives to capture effects of such unexpected changes (cf. ED 7.4.6) would be done regularly, an excess test should not be necessary. This raises the broader question of whether a separate excess test is necessary in addition to other safeguards incorporated in the RMA model. Furthermore, while an excess test for RMA/accounting purposes is required at each reporting date, the frequency of assessments (and adjustments) within risk management differs from reporting dates.

Overall, the different safeguards incorporated into the model, when considered together, raise significant conceptual and operational concerns. In particular, the interaction between the over-hedging restriction, the lower-of test, the excess test, benchmark derivatives and the treatment of unexpected changes need to be considered holistically. These requirements should not be assessed individually but comprehensively, since their cumulative effect may result in accounting outcomes that are not aligned with the entity's risk management activities.

Question 7 – Discontinuation

*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 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.*

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.

We generally ***agree*** with the proposals for when, and why, RMA shall be discontinued.

We also ***concur*** with the principle that RMA must not be discontinued voluntarily.

The distinction made in the ED between a change in risk management *strategy* and a change in risk management *activities* (ie. how risk is managed) seems sound in principle. However, this principle requires ***clarification***. The ED suggests that a change in risk management strategy occurs infrequently (ED B7.5.2), meaning that the RMA be discontinued in rare circumstances. This is fully appropriate and desirable. In particular, the normal evolution of risk management activities – including changes in underlying portfolios, assumptions, or the

execution of hedging activities – should not in itself result in discontinuation, while the underlying risk management strategy remains unchanged.

Notwithstanding this, changes in how an existing risk management strategy is implemented should be distinguished from a fundamental change in that strategy. Changes to risk management activities may be planned or form part of the normal evolution of risk management and should not, in themselves, lead to discontinuation of RMA. Otherwise, discontinuation could create accounting outcomes that are driven by changes inherent in the nature of evolving risk management activities rather than by a genuine change in the entity's risk management strategy. Nevertheless, this distinction should remain principles-based.

Further, we ***agree*** with the principle of how to account for the risk mitigation adjustment given that RMA be discontinued. In particular, the details for how to release the amount accumulated as risk mitigation adjustment to profit or loss appear largely clear and appropriate.

Question 8 – Effective date and withdrawal of IAS 39

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

*The IASB also proposes that an entity **discontinue** applying the hedge accounting requirements in **IAS 39** at the **earlier** of:*
a) the date on which the entity first applies requirements for risk mitigation accounting; and
b) annual reporting periods beginning on or after [the date on which IAS 39 is withdrawn].

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

As regards effective date and permission to early apply, we ***agree*** with the suggestion to allow for applying RMA as soon as the respective IFRS 9 requirements are issued. For entities able and willing for transition to RMA, immediate application is advantageous.

We ***consequently agree*** with discontinuing IAS 39 hedge accounting by an entity that voluntarily applies RMA, provided the final RMA model is capable of replacing the relevant IAS 39 hedge accounting approach.

A real "effective date" for applying RMA is only relevant for those currently applying IAS 39 hedge accounting (and considering RMA as its surrogate) and assumed that IAS 39 is indeed withdrawn at the same time.

As regards the intended withdrawal of IAS 39, we take a clear ***view against***:

- IAS 39 should not be withdrawn until a robust and operationally viable model is available that can appropriately replace the existing IAS 39 portfolio fair value hedge accounting requirements as well as IAS 39 Micro Hedge Accounting reflecting both the European

carve out. Field testing of the proposed RMA model by the banking industry raises fundamental concerns as to whether this condition is currently met.

- As far as RMA will not be applicable, for all hedge relationships used to manage the banking book (including cross currency hedges), withdrawing IAS 39 would create a more significant gap than the gap in IFRS 9 that RMA is intended to address.
- For those still using IAS 39 hedge accounting, including particular portfolio fair value hedge accounting under IAS 39 and the associated "EU version", the proposed RMA model has not demonstrated yet to provide an appropriate replacement. Accordingly, withdrawal of IAS 39 should not be driven by the availability of RMA in itself, but by whether the final model is capable of replacing existing approaches without reducing the extent to which the accounting reflects actual risk management activities.

Apart from this, withdrawing IAS 39 (and potentially transitioning to RMA) should come along with sufficient lead time. Feedback from the banking industry indicates that a period of at least five years may be necessary. We acknowledge that entities expect high costs and efforts when initially applying RMA, even more so if transitioning from IAS 39 hedge accounting to RMA. The required implementation effort is expected to extend beyond accounting policy changes and involve significant changes to systems, data, processes, and controls. These costs tentatively appear so high, presumably not outweighing the benefits of applying RMA, thus maybe preventing entities from applying RMA.

Overall, we ***reject*** the withdrawal of IAS 39 until the RMA model has been fundamentally reconsidered and proven to be a robust and operationally viable replacement for the existing portfolio hedge accounting requirements.

Question 9 – Transition

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 IFRS 9.6.5.10 and 6.5.12 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 para. 7.2.1; and*

*e) an entity be **exempt** from disclosing the quantitative information required by **IAS 8.28(f)** in the reporting period in which the entity first applies the amendments.*

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.

Apart from our reservations (as explained above) against IAS 39 withdrawal, that could virtually *require* entities to transition to RMA, we ***acknowledge*** the rationale for the proposed transition requirements. More specifically, we think that

a) applying RMA prospectively, along with
b) a permission to revoke previous FVPL designation,
c) a requirement to discontinue IAS 39 hedge accounting,
d) a permission to discontinue IFRS 9 hedge accounting, as far as hedged items be included in RMA portfolios, and
e) an exemption from disclosures required by IAS 8.28 (f)

to be consequential in the context of a transition to RMA. However, this assessment is subject to the IASB first developing an RMA model that is sufficiently robust and operationally viable to provide an appropriate replacement for existing portfolio hedge accounting approaches.

We ***do not agree*** with the current transition requirements for constructing benchmark derivatives with an initial fair value of zero. At the date of transition from IAS 39 or IFRS 9 hedge accounting to RMA, existing designated derivatives may be off-market and therefore have a non-zero fair value, while still economically reflecting the entity's risk mitigation objective. Such derivatives may also have risk sensitivities that differ from those of equivalent at-market derivatives. Requiring benchmark derivatives to be constructed at market solely to achieve a zero initial fair value may result in artificial benchmark profiles across different repricing time bands that do not correspond to observable risk management actions, thereby creating artificial accounting volatility and causing operational complexity at transition and potentially thereafter. We therefore suggest that the final RMA requirements permit entities to use existing off-market benchmark derivatives at transition, together with an appropriate pull-to-par mechanism for the initial fair value, where this better reflects the economics of the existing hedging relationship and avoids unnecessary artificial benchmark construction.

Furthermore, some banks have suggested a type of retrospective application based on the fact that hedge adjustments accumulated under IAS 39 until transition to RMA correspond to the initial fair value of the designated derivatives, thus, they constitute a component of the initial present value of the benchmark derivatives. These banks consider it appropriate to recognise an initial RMA adjustment at the amount of the hedge adjustments under IAS 39. In this way, the banking sector would not only avoid parallel accounting processes for many years and significant implementation costs, but also inconsistencies between the RMA and a separate amortisation schedule for hedge adjustments under IAS 39, which would lead to significant P&L volatility.

Question 10 – Disclosure requirements

The IASB is proposing new presentation and disclosure requirements to be included in IFRS 7. Para. 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.*

*Paras. 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.

*Para. 33A would apply to entities whose business and risk management activities have the characteris-tics specified in the proposed IFRS 9.7.1.4 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.*

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.

The disclosures required when RMA *is* applied appear ***only partially appropriate***. For example, sensitivity disclosures (para. 30K) should not be required as they would conflict with disclosures made by risk management, thereby confusing users of financial statements if RMA does not fully reflect risk management activities. In particular, the proposed sensitivity disclosures would reflect only the subset of exposures captured by the RMA model and, therefore, may provide a partial (and incomplete) view of an entity's overall interest rate risk exposure that is not aligned with the measures used for risk management purposes.

Details that are "commercially sensitive" should generally not be required to be disclosed. Further, disclosure requirements should, to the maximum extent possible, leverage existing risk management and regulatory disclosures and avoid requiring the development of separate accounting-specific risk measures. Additional disclosures are only justified if they directly relate to the "new" risk mitigation adjustment and explain the financial reporting effects of applying the RMA model.

Yet, many disclosures as proposed in the ED appear to be driven by the apprehension that the RMA objective is not fully achievable, and this be remedied through numerous additional disclosures. We do not believe that additional disclosures can compensate for recognition and measurement requirements that do not appropriately reflect an entity's risk management activities.

The disclosures required when the RMA *is not* applied (para. 33A) seem ***not justified***. Mandatory disclosure of details about repricing risk exposures and its management when RMA is not applied appear as a penalty for not applying the RMA model. Further, any such

disclosures feel like applying RMA is the "default" accounting, while not applying RMA appears as an (acceptable) exception. This effectively undermines the optional nature of RMA. Entities that choose not to apply RMA should continue to be subject to the generally applicable IFRS 7 risk disclosure requirements without an additional RMA-specific disclosure obligation.

Overall, we consider existing IFRS 7 disclosure requirements regarding risks and its management as comprehensive and sufficient. (Any incremental disclosure requirements should therefore be limited to information necessary to explain the application of RMA and its effects on the financial statements and should avoid unnecessary duplication with existing risk management and regulatory reporting.)

Question 11 – Risk management strategy

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

Our following comments describe current views of the insurance industry holistically, but less detailed than our comments above. The comments below comprise, amongst other aspects, our answer on Q11.

Entities that issue insurance contracts ("insurers", for sake of simplicity) consider the RMA model to be relevant in limited circumstances only. This derives from the fact that insurers do not (or to a much lower extent) manage risk by external derivatives, thus do not (or to a much lower extent) face respective accounting mismatches from these derivatives.

The RMA model as proposed does not appear applicable at all for that industry. Making insurance contracts eligible for underlying portfolios would be necessary but not sufficient for the RMA model to become suitable for insurers. More precisely, the model is based on characteristics that are atypical for insurers – which are: (a) repricing risk exposure, ie. considerable open interest rate positions, that reprice regularly, (b) underlying portfolios mainly comprising AC and FVOCI assets/liabilities, (c) using external derivatives for managing risk from those portfolios (as mentioned), and (d) disaggregating repricing risk exposures into time bands. Instead, insurers consider and manage risk exposures mainly from comprehensive

asset/liability portfolios (ALM), which comprise FVOCI assets as well as FVPL assets (but AC assets are rather rare) and, obviously, considerable liability positions from insurance contracts.

Neither objective and scope, nor the accounting mechanics are suitable for insurers. Conceptually, the RMA model is (for known reasons) designed from and for the banking sector. In particular, a risk mitigation adjustment that temporarily defers recognition of gains and losses from derivatives does not lead to comprehensible, or even better, information in financial statements of insurers. Since presenting insurers' business in financial statements already requires sophisticated understanding, it is doubtful that presenting risk mitigation adjustments in the balance sheet make it more understandable. Instead, measurement fluctuations and related "mismatches" may arise from FVOCI and/or FVPL positions but are different, and a risk mitigation adjustment as proposed appear not suitable.

As regards other elements of the RMA model (esp. NRRE, RMO, benchmark derivatives) and enclosing requirements (esp. discontinuation, disclosures), we are not in a position to illustrate insurers' distinct views on all aspects and details. This, again, results from the fact that the model appears nearly irrelevant and, besides, nontrivial and complex.

Finally, we like to note that, to our knowledge, the insurance industry has largely transitioned to IFRS 9 hedge accounting. Hence, only few insurers still apply IAS 39 hedge accounting. This allows for two preliminary conclusions: One is that withdrawal of IAS 39 would be less crucial for insurers. The other, and more meaningful, is that for insurers there is not much of a gap in IFRS 9 to be filled. Hence, from insurers' perspective there is little need for an RMA model eventually be extended to other types of risk and to further items eligible for underlying portfolios.