

FINANCIAL ACCOUNTING SERIES



ACCOUNTING STANDARDS UPDATE

No. 2020-04
March 2020

Reference Rate Reform (Topic 848)

Facilitation of the Effects of Reference
Rate Reform on Financial Reporting

An Amendment of the *FASB Accounting Standards Codification*®

Financial Accounting Standards Board

The *FASB Accounting Standards Codification*[®] is the source of authoritative generally accepted accounting principles (GAAP) recognized by the FASB to be applied by nongovernmental entities. An Accounting Standards Update is not authoritative; rather, it is a document that communicates how the Accounting Standards Codification is being amended. It also provides other information to help a user of GAAP understand how and why GAAP is changing and when the changes will be effective.

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Summary

Why Is the FASB Issuing This Accounting Standards Update (Update)?

The amendments in this Update provide optional guidance for a limited period of time to ease the potential burden in accounting for (or recognizing the effects of) reference rate reform on financial reporting.

In response to concerns about structural risks of interbank offered rates (IBORs), and, particularly, the risk of cessation of the London Interbank Offered Rate (LIBOR), regulators in several jurisdictions around the world have undertaken reference rate reform initiatives to identify alternative reference rates that are more observable or transaction based and less susceptible to manipulation.

Stakeholders raised certain operational challenges likely to arise in accounting for contract modifications and hedge accounting because of reference rate reform. Some of those challenges relate to the significant volume of contracts and other arrangements, such as debt agreements, lease agreements, and derivative instruments, which will be modified to replace references to discontinued rates with references to replacement rates. For accounting purposes, such contract modifications are required to be evaluated in determining whether the modifications result in the establishment of new contracts or the continuation of existing contracts. Stakeholders indicated that due to the significant volume of affected contracts and other arrangements, together with a compressed time frame for making contract modifications, the application of existing accounting standards on assessing modifications versus extinguishments could be costly and burdensome. In addition, stakeholders indicated that financial reporting results should reflect the intended continuation of such contracts and arrangements during the period of the market-wide transition to alternative reference rates.

Stakeholders raised additional accounting issues specific to hedge accounting. In particular, changes in a reference rate could disallow the application of certain hedge accounting guidance, and certain hedging relationships may not qualify as highly effective during the period of the market-wide transition to a replacement rate. Stakeholders indicated that the inability to apply hedge accounting because of reference rate reform could result in financial reporting outcomes that do not reflect entities' intended hedging strategies.

Who Is Affected by the Amendments in This Update?

The amendments in this Update are elective and apply to all entities, subject to meeting certain criteria, that have contracts, hedging relationships, and other

transactions that reference LIBOR or another reference rate expected to be discontinued because of reference rate reform.

What Are the Main Provisions?

The amendments in this Update provide optional expedients and exceptions for applying generally accepted accounting principles (GAAP) to contracts, hedging relationships, and other transactions affected by reference rate reform if certain criteria are met.

The amendments in this Update apply only to contracts, hedging relationships, and other transactions that reference LIBOR or another reference rate expected to be discontinued because of reference rate reform. The expedients and exceptions provided by the amendments do not apply to contract modifications made and hedging relationships entered into or evaluated after December 31, 2022, except for hedging relationships existing as of December 31, 2022, that an entity has elected certain optional expedients for and that are retained through the end of the hedging relationship.

Optional Expedients for Contract Modifications

The amendments in this Update apply to contract modifications that replace a reference rate affected by reference rate reform (including rates referenced in fallback provisions) and contemporaneous modifications of other contract terms related to the replacement of the reference rate (including contract modifications to add or change fallback provisions).

The following optional expedients for applying the requirements of certain Topics or Industry Subtopics in the Codification are permitted for contracts that are modified because of reference rate reform and that meet certain scope guidance:

1. Modifications of contracts within the scope of Topics 310, Receivables, and 470, Debt, should be accounted for by prospectively adjusting the effective interest rate.
2. Modifications of contracts within the scope of Topics 840, Leases, and 842, Leases, should be accounted for as a continuation of the existing contracts with no reassessments of the lease classification and the discount rate (for example, the incremental borrowing rate) or remeasurements of lease payments that otherwise would be required under those Topics for modifications not accounted for as separate contracts.
3. Modifications of contracts do not require an entity to reassess its original conclusion about whether that contract contains an embedded derivative that is clearly and closely related to the economic characteristics and risks of the host contract under Subtopic 815-15, Derivatives and Hedging—Embedded Derivatives.

For other Topics or Industry Subtopics in the Codification, the amendments in this Update also include a general principle that permits an entity to consider contract modifications due to reference rate reform to be an event that does not require contract remeasurement at the modification date or reassessment of a previous accounting determination.

When elected, the optional expedients for contract modifications must be applied consistently for all eligible contracts or eligible transactions within the relevant Topic or Industry Subtopic within the Codification that contains the guidance that otherwise would be required to be applied.

Exceptions to Topic 815 Guidance Related to Changes in Critical Terms of a Hedging Relationship

The amendments in this Update provide exceptions to the guidance in Topic 815 related to changes to the critical terms of a hedging relationship due to reference rate reform. The following changes should not result in the dedesignation of the hedging relationship if certain criteria are met:

1. Certain changes in the critical terms of a designated hedging instrument, a hedged item, or a forecasted transaction in a fair value hedge, a cash flow hedge, or a net investment hedge.
2. A change to rebalance or adjust the hedging relationship as follows:
 - a. In a fair value hedge, a change in the proportion of the derivative designated as the hedging instrument or in the proportion of the designated hedged item or both.
 - b. In a fair value hedge or a cash flow hedge, a change in the designated hedging instrument to add one or more additional derivatives (or proportions of those derivatives).
3. For a cash flow hedge, a change in the method used to assess hedge effectiveness when initially applying an optional expedient method and when reverting to the requirements in Subtopics 815-20, Derivatives and Hedging—Hedging—General, and 815-30, Derivatives and Hedging—Cash Flow Hedges.

Optional Expedients for Excluded Components

The amendments in this Update provide the following optional expedients for fair value hedging relationships, cash flow hedging relationships, and net investment hedging relationships for which the component excluded from the assessment of hedge effectiveness is affected by reference rate reform:

1. An entity may change its systematic and rational method used to recognize in earnings the components excluded from the assessment of effectiveness.

2. If the changes to the hedging instrument's contractual terms cause a change in the fair value of the excluded component, an entity may elect to recognize the change in fair value of the excluded component in current earnings.

The optional expedients for excluded components may be elected on an individual hedging relationship basis.

Optional Expedients for Fair Value Hedges

The amendments in this Update provide the following optional expedients for fair value hedging relationships for which the derivative designated as the hedging instrument is affected by reference rate reform if certain criteria are met:

1. An entity may change the designated benchmark interest rate documented at hedge inception to a different eligible benchmark interest rate under Subtopic 815-20. The amendments permit an entity to apply a method to change the designated benchmark interest rate that either adjusts the hedged item's cumulative fair value hedge basis adjustment or maintains the hedged item's cumulative basis adjustment. The method applied to change the designated benchmark interest rate must be reasonable and must be applied consistently across similar fair value hedging relationships. If an entity elects an approach that would result in a change to the cumulative fair value hedge basis adjustment, that change should be recognized in current earnings in the same income statement line item used to present the earnings effect of the hedged item.
2. An entity may disregard certain qualifying conditions for the shortcut method that are not met because of reference rate reform and may continue to disregard those qualifying conditions for the remainder of the fair value hedging relationship (including for the remainder of hedging relationships that end after December 31, 2022).

The optional expedients for fair value hedging relationships may be elected on an individual hedging relationship basis. The method applied by an entity to change the designated benchmark interest rate should be applied consistently across similar fair value hedging relationships.

Optional Expedients for Cash Flow Hedges

The amendments in this Update provide the following optional expedients for cash flow hedging relationships affected by reference rate reform if certain criteria are met:

1. If the designated hedged interest rate risk is a rate that is affected by reference rate reform:

- a. An entity should disregard the potential change in the designated hedged interest rate risk that may occur because of reference rate reform when the entity assesses whether the hedged forecasted transaction is probable in accordance with the requirements of Topic 815.
 - b. An entity may continue hedge accounting for a cash flow hedge for which the hedged interest rate risk changes if either the hedge is highly effective under an assessment method in Subtopics 815-20 and 815-30 or an optional expedient method in this Update is elected.
2. For cash flow hedges for which the shortcut method or another method that assumes perfect hedge effectiveness has been applied in accordance with Subtopic 815-20, an entity may disregard certain qualifying conditions for those methods that are not met because of reference rate reform and continue to apply the shortcut method.
3. For cash flow hedges for which either the hedging instrument or hedged forecasted transactions reference a rate that is expected to be affected by reference rate reform, an entity may adjust how it applies the methods in Subtopics 815-20 and 815-30 used to initially and subsequently assess hedge effectiveness (including the shortcut method and other assessment methods that assume perfect hedge effectiveness) to disregard certain mismatches between the designated hedging instrument and the hedged item.
4. If an entity has performed an initial hedge effectiveness assessment for a cash flow hedge using a method in Subtopics 815-20 and 815-30, or has adjusted those methods using an optional expedient in this Update, the entity may elect to subsequently assess hedge effectiveness using a qualitative method. This qualitative method effectively suspends subsequent hedge effectiveness assessments that would otherwise be required by Subtopics 815-20 and 815-30.
5. For cash flow hedges of portfolios of forecasted transactions that reference a rate that is expected to be affected by reference rate reform, an entity may disregard the requirement in Subtopic 815-20 that the group of individual transactions must share the same risk exposure for which they are designated as being hedged.

The optional expedients for cash flow hedging relationships may be elected on an individual hedging relationship basis. After electing an optional expedient method, an entity may revert to hedge accounting requirements in Subtopics 815-20 and 815-30 without dedesignating the hedging relationship. Use of the optional expedients (including the optional expedient for application of the shortcut method and other methods that assume perfect hedge effectiveness) must be discontinued either as of the date that neither the hedging instrument nor the hedged forecasted transaction references a rate that is affected by reference rate reform or after December 31, 2022. An entity must revert to applying the qualifying criteria and hedge assessment methods in Subtopics 815-20 and 815-30 to assess whether a

cash flow hedging relationship may continue after the entity discontinues applying an optional expedient method.

One-Time Election to Sell or Transfer Debt Securities Classified as Held to Maturity

In accordance with the amendments in this Update, an entity may make a one-time election to sell, transfer, or both sell and transfer debt securities classified as held to maturity that reference a rate affected by reference rate reform and that are classified as held to maturity before January 1, 2020.

When Will the Amendments Be Effective and What Are the Transition Requirements?

The amendments in this Update are effective for all entities as of March 12, 2020 through December 31, 2022.

An entity may elect to apply the amendments for contract modifications by Topic or Industry Subtopic as of any date from the beginning of an interim period that includes or is subsequent to March 12, 2020, or prospectively from a date within an interim period that includes or is subsequent to March 12, 2020, up to the date that the financial statements are available to be issued. Once elected for a Topic or an Industry Subtopic, the amendments in this Update must be applied prospectively for all eligible contract modifications for that Topic or Industry Subtopic.

An entity may elect to apply the amendments in this Update to eligible hedging relationships existing as of the beginning of the interim period that includes March 12, 2020 and to new eligible hedging relationships entered into after the beginning of the interim period that includes March 12, 2020.

If an entity elects to apply any of the amendments for an eligible hedging relationship existing as of the beginning of the interim period that includes March 12, 2020, any adjustments as a result of those elections must be reflected as of the beginning of that interim period and recognized in accordance with the guidance in Reference Rate Reform Subtopics 848-30, 848-40, and 848-50 (as applicable). If an entity elects to apply any of the amendments for a new hedging relationship entered into between the beginning of the interim period that includes March 12, 2020 and March 12, 2020, any adjustments as a result of those elections must be reflected as of the beginning of the hedging relationship and recognized in accordance with the guidance in Reference Rate Reform Subtopics 848-30, 848-40, and 848-50 (as applicable).

For private companies that are not financial institutions as described in paragraph 942-320-50-1 and not-for-profit entities (except for not-for-profit entities that have issued, or are a conduit bond obligor for, securities that are traded, listed, or quoted

on an exchange or an over-the-counter market), an entity must update its hedge documentation noting the changes made before the next interim (if applicable) or annual financial statements are available to be issued. For all other entities, an entity must update its hedge documentation noting the changes made no later than when the entity performs its first quarterly assessment of effectiveness after the election.

The amendments in this Update do not apply to contract modifications made after December 31, 2022, new hedging relationships entered into after December 31, 2022, and hedging relationships evaluated for periods after December 31, 2022, except for hedging relationships existing as of December 31, 2022, that apply the following optional expedients that are retained through the end of the hedging relationship (including for periods evaluated after December 31, 2022):

1. An optional expedient to the systematic and rational method used to recognize in earnings the components excluded from the assessment of effectiveness
2. An optional expedient to the rate to discount cash flows associated with the hedged item and any adjustment to the cash flows for the designated term or the partial term of the designated hedged item in a fair value hedge
3. An optional expedient to not periodically evaluate certain conditions when using the shortcut method for a fair value hedge.

If an entity has not adopted the amendments in Accounting Standards Update No. 2017-12, *Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities*, the entity may elect only the following optional expedients for hedge accounting:

1. An optional expedient allowing changes in critical terms of a hedging relationship
2. An optional expedient allowing a change in the method designated for use in assessing hedge effectiveness in a cash flow hedge, if the optional expedient method being elected is the simplified hedge accounting approach for eligible private companies for initial hedge effectiveness or for subsequent hedge effectiveness
3. An optional expedient allowing the entity to assume that the hedged forecasted transaction in a cash flow hedge is probable of occurring
4. An optional expedient allowing the entity to assume that the reference rate will not be replaced for the remainder of the hedging relationships for initial and subsequent hedge effectiveness when the entity is using any of the methods for assessing and measuring hedge effectiveness in a cash flow hedge on a quantitative basis and if both the hedged forecasted transaction and the hedging instrument have an eligible reference rate
5. An optional expedient allowing the entity to disregard certain requirements of the simplified hedge accounting approach for eligible

private companies for initial hedge effectiveness or for subsequent hedge effectiveness in a cash flow hedge.

The one-time election to sell, transfer, or both sell and transfer debt securities classified as held to maturity may be made at any time after March 12, 2020 but no later than December 31, 2022.

Amendments to the *FASB Accounting Standards Codification*[®]

Introduction

1. The Accounting Standards Codification is amended as described in paragraphs 2–12.

Addition of Topic 848

2. Add Subtopic 848-10 as follows:

[For ease of readability, the new Subtopic is not underlined.]

Reference Rate Reform—Overall

Overview and Background

General

848-10-05-1 The Reference Rate Reform Topic includes the following Subtopics:

- a. Overall
- b. Contract Modifications
- c. Hedging—General
- d. Fair Value Hedges
- e. Cash Flow Hedges.

848-10-05-2 Reference rates such as the London Interbank Offered Rate (LIBOR) are widely used in a broad range of financial instruments and other agreements. Regulators and market participants in various jurisdictions have undertaken efforts, generally referred to as reference rate reform, to eliminate certain reference rates and introduce new reference rates that are based on a larger and more liquid population of observable transactions. As a result of the reference rate reform initiative, certain widely used reference rates such as LIBOR are expected to be discontinued.

848-10-05-3 This Topic provides optional expedients for applying the guidance in certain Topics or Industry Subtopics for contract modifications or other situations affected by reference rate reform. The guidance in this Topic is temporary in accordance with the guidance in paragraph 848-10-65-1(a).

Scope and Scope Exceptions

General

> Overall Guidance

848-10-15-1 The Scope and Scope Exceptions Section of the Overall Subtopic establishes the pervasive scope for the Reference Rate Reform Topic. Unless explicitly addressed within the specific Subtopics, the following guidance applies to all Subtopics of the Reference Rate Reform Topic.

> Entities

848-10-15-2 The guidance in this Topic applies to all entities.

> Scope

848-10-15-3 The guidance in this Topic, if elected by an entity, shall apply to contracts or other transactions that reference the London Interbank Offered Rate (LIBOR) or a reference rate that is expected to be discontinued as a result of reference rate reform.

>> Identifying an Eligible Reference Rate

848-10-15-4 The guidance in this Topic applies to all maturities of LIBOR in all jurisdictions and currencies. For other reference rates, an expectation of the discontinuance of the rate may result from any of the following:

- a. A public statement or publication of information by or on behalf of the administrator of the relevant reference rate or by the regulatory supervisor for the administrator
- b. Initiatives by a significant number of market participants or by market participants representing a significant number of transactions to move away from the reference rate
- c. The production method for the calculation of the published reference rate that is either:
 1. Fundamentally restructured
 2. Reliant on another rate that is expected to discontinue.

Glossary

Financial Statements Are Available to Be Issued

Financial statements are considered available to be issued when they are complete in a form and format that complies with GAAP and all approvals necessary for issuance have been obtained, for example, from management, the board of directors, and/or significant shareholders. The process involved in creating and distributing the financial statements will vary depending on an entity's

management and corporate governance structure as well as statutory and regulatory requirements.

Subsequent Measurement

General

> Sale or Transfer from Held-to-Maturity Classification

848-10-35-1 An entity may make a one-time election to sell or transfer certain debt securities classified as held to maturity or to both sell and transfer certain debt securities classified as held to maturity to available for sale or trading. At the time of applying the one-time election, the entity may sell, transfer, or both sell and transfer debt securities classified as held to maturity that meet both of the following criteria:

- a. The debt securities reference a rate that meets the scope of paragraph 848-10-15-3.
- b. The debt securities were classified as held to maturity before January 1, 2020.

At the time of applying the one-time election, an entity is not required to transfer all its remaining debt securities classified as held to maturity that meet criteria (a) and (b). The one-time election to sell, transfer, or both sell and transfer debt securities classified as held to maturity may be made at any time, but no later than the date in paragraph 848-10-65-1(d).

848-10-35-2 An entity shall recognize the transfer of debt securities classified as held to maturity to available for sale or trading as of the date in the reporting period in which the entity makes its one-time election. The entity shall apply the measurement guidance for transfers of debt securities between categories in paragraphs 320-10-35-10 through 35-16. The sale or transfer, in and of itself, would not call into question the entity's assertion at prior reporting dates that it had the intent and ability to hold to maturity those debt securities that continued to be classified as held to maturity in those prior periods.

Disclosure

General

848-10-50-1 An entity that has applied the one-time election to sell, transfer, or both sell and transfer debt securities classified as held to maturity in accordance with paragraphs 848-10-35-1 through 35-2 shall apply the disclosure requirements in paragraph 320-10-50-10 for the sale or transfer of debt securities classified as held to maturity.

Transition and Open Effective Date Information

General

> Transition Related to Accounting Standards Update No. 2020-04, *Reference Rate Reform (Topic 848): Facilitation of the Effects of Reference Rate Reform on Financial Reporting*

848-10-65-1 The following represents the transition, end of application, and effective date information related to Accounting Standards Update No. 2020-04, *Reference Rate Reform (Topic 848): Facilitation of the Effects of Reference Rate Reform on Financial Reporting*:

- a. The pending content that links to this paragraph shall be effective for all entities as of March 12, 2020 through December 31, 2022, as follows:
 1. An entity may elect to apply the pending content that links to this paragraph for contract modifications by Topic or Industry Subtopic as of any date from the beginning of an interim period that includes or is subsequent to March 12, 2020, or prospectively from a date within an interim period that includes or is subsequent to March 12, 2020, up to the date that the **financial statements are available to be issued**. Once elected for a Topic or an Industry Subtopic, the pending content that links to this paragraph shall be applied prospectively for all eligible contract modifications for that Topic or Industry Subtopic in accordance with paragraph 848-20-35-1.
 2. An entity may elect to apply the pending content that links to this paragraph to eligible hedging relationships existing as of the beginning of the interim period that includes March 12, 2020 and to new eligible hedging relationships entered into after the beginning of the interim period that includes March 12, 2020.
 - i. If an entity elects to apply any of the pending content that links to this paragraph for an eligible hedging relationship existing as of the beginning of the interim period that includes March 12, 2020, any adjustments as a result of those elections shall be reflected as of the beginning of that interim period and recognized in accordance with Subtopics 848-30, 848-40, and 848-50 (as applicable). If an entity elects to apply any of the pending content that links to this paragraph for a new hedging relationship entered into between the beginning of the interim period that includes March 12, 2020 and March 12, 2020, any adjustments as a result of those elections shall be reflected as of the beginning of the hedging relationship and recognized in accordance with Subtopics 848-30, 848-40, and 848-50 (as applicable).
 01. For private companies that are not financial institutions as described in paragraph 942-320-50-1 and not-for-profit

- entities (except for not-for-profit entities that have issued, or are a conduit bond obligor for, securities that are traded, listed, or quoted on an exchange or an over-the-counter market), an entity shall update its hedge documentation (as applicable) noting the changes made before the next interim (if applicable) or annual financial statements are available to be issued.
02. For all other entities, an entity shall update its hedge documentation (as applicable) noting the changes made no later than when the entity performs its first quarterly assessment of effectiveness after the election.
3. The pending content that links to this paragraph shall not be applied to all the following:
 - i. Contract modifications made after December 31, 2022.
 - ii. New hedging relationships entered into after December 31, 2022.
 - iii. Hedging relationships evaluated for periods after December 31, 2022, except for hedging relationships existing as of December 31, 2022, that apply the following optional expedients in Subtopics 848-30 and 848-40 that shall be retained through the end of the hedging relationship (including for periods evaluated after December 31, 2022):
 01. An optional expedient to the systematic and rational method used to recognize in earnings the components excluded from the assessment of effectiveness in paragraph 848-30-25-12.
 02. An optional expedient to the rate to discount cash flows associated with the hedged item and any adjustment to the cash flows for the designated term or the partial term of the designated hedged item in a fair value hedge in paragraph 848-40-25-6.
 03. An optional expedient to not periodically evaluate the conditions in paragraph 815-20-25-104(d) and (g) when using the shortcut method for a fair value hedge in paragraph 848-40-25-8.
 - b. An entity may elect the optional expedients in Subtopics 848-30, 848-40, and 848-50 if it has adopted the amendments in Accounting Standards Update No. 2017-12, *Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities*.
 - c. An entity that has not adopted the amendments in Update 2017-12 may elect the following optional expedients in Subtopics 848-30, 848-40, and 848-50:
 1. An optional expedient allowing changes in critical terms of a hedging relationship in paragraphs 848-30-25-3 through 25-7.
 2. An optional expedient allowing a change to the method designated for use in assessing hedge effectiveness in a cash flow hedge in

paragraph 848-30-25-8 if the optional expedient method being elected is the simplified hedge accounting approach for eligible private companies for initial hedge effectiveness in paragraph 848-50-25-8 or for subsequent hedge effectiveness in paragraph 848-50-35-7.

3. An optional expedient allowing an entity to assume that the hedged forecasted transaction in a cash flow hedge is probable of occurring in paragraph 848-50-25-2.
 4. An optional expedient allowing an entity to assume that the reference rate will not be replaced for the remainder of the hedging relationships in paragraph 848-50-25-11(a) for initial hedge effectiveness and paragraph 848-50-35-17(a) for subsequent hedge effectiveness when the entity is using any of the methods for assessing and measuring hedge effectiveness in a cash flow hedge on a quantitative basis and if both the hedged forecasted transaction and the hedging instrument have a reference rate that meets the scope of paragraph 848-10-15-3.
 5. An optional expedient allowing an entity to disregard certain requirements of the simplified hedge accounting approach for eligible private companies for initial hedge effectiveness in paragraph 848-50-25-8 or for subsequent hedge effectiveness in paragraph 848-50-35-7 in a cash flow hedge.
- d. The one-time election to sell, transfer, or both sell and transfer debt securities classified as held to maturity in accordance with paragraphs 848-10-35-1 through 35-2 may be made at any time after March 12, 2020, but no later than December 31, 2022.
 - e. An entity shall provide the following disclosures:
 1. The nature of and reason for electing to apply the pending content that links to this paragraph.
 2. The disclosures in (e)(1) in each interim and annual financial statement period in the fiscal year of application.

3. Add Subtopic 848-20 as follows:

[For ease of readability, the new Subtopic is not underlined.]

Reference Rate Reform—Contract Modifications

Overview and Background

General

848-20-05-1 This Subtopic provides optional expedients for contract modifications undertaken because of reference rate reform. It specifically addresses the accounting for modifications of contracts within the scope of Topics 310 on

receivables, 470 on debt, and 840 and 842 on leases and Subtopic 815-15 on derivatives and hedging—embedded derivatives. This Subtopic also provides a principle to account for modifications of contracts within the scope of other Topics or Industry Subtopics not specifically addressed within this Subtopic.

Scope and Scope Exceptions

General

848-20-15-1 This Subtopic provides guidance on optional expedients for accounting for contract modifications when one or more terms are modified because of reference rate reform.

> Modifications of Terms

848-20-15-2 The guidance in this Subtopic, if elected, shall apply to contract modifications if the terms that are modified directly replace, or have the potential to replace, a reference rate within the scope of paragraph 848-10-15-3 with another interest rate index. If other terms are contemporaneously modified in a manner that changes, or has the potential to change, the amount or timing of contractual cash flows, the guidance in this Subtopic shall apply only if those modifications are related to the replacement of a reference rate. For example, the addition of contractual fallback terms or the amendment of existing contractual fallback terms related to the replacement of a reference rate that are contingent on one or more events occurring has the potential to change the amount or timing of contractual cash flows and the entity potentially would be eligible to apply the guidance in this Subtopic.

848-20-15-3 The guidance in this Subtopic shall not apply if a contract modification is made to a term that changes, or has the potential to change, the amount or timing of contractual cash flows and is unrelated to the replacement of a reference rate. That is, this Subtopic shall not apply if contract modifications are made contemporaneously to terms that are unrelated to the replacement of a reference rate.

848-20-15-4 Contemporaneous modifications of contract terms that do not change, or do not have the potential to change, the amount or timing of contractual cash flows shall not preclude application of the guidance in this Subtopic, regardless of whether those contemporaneous contract modifications are related or unrelated to the replacement of a reference rate.

> > Identifying Changes to Terms Related and Unrelated to the Replacement of the Reference Rate

848-20-15-5 Changes to terms that are related to the replacement of the reference rate are those that are made to effect the transition for reference rate reform and

are not the result of a business decision that is separate from or in addition to changes to the terms of a contract to effect that transition. Examples of changes to terms that are related to the replacement of a reference rate in accordance with the guidance in paragraph 848-20-15-2 include the following:

- a. Changes to the referenced interest rate index (for example, a change from London Interbank Offered Rate [LIBOR] to another interest rate index)
- b. Addition of or changes to a spread adjustment (for example, adding or adjusting a spread to the interest rate index, amending the fixed rate for an interest rate swap, or paying or receiving a cash settlement for any difference intended to compensate for the difference in reference rates)
- c. Changes to the reset period, reset dates, day-count conventions, business-day conventions, payment dates, payment frequency, and repricing calculation (for example, a change from a forward-looking term rate to an overnight rate or a compounded overnight rate in arrears)
- d. Changes to the strike price of an existing interest rate option (including an embedded interest rate option)
- e. Addition of an interest rate floor or cap that is out of the money on the basis of the spot rate at the time of the amendment of the contract
- f. Addition of a prepayment option for which exercise is contingent upon the replacement reference interest rate index not being determinable in accordance with the terms of the agreement
- g. Addition of or changes to contractual fallback terms that are consistent with fallback terms developed by a regulator or by a private-sector working group convened by a regulator
- h. Changes to terms (including those in the examples in paragraph 848-20-15-6) that are necessary to comply with laws or regulations or to align with market conventions for the replacement rate.

848-20-15-6 Examples of changes to terms that are generally unrelated to the replacement of a reference rate in accordance with paragraph 848-20-15-3 include the following:

- a. Changes to the notional amount
- b. Changes to the maturity date
- c. Changes from a referenced interest rate index to a stated fixed rate
- d. Changes to the loan structure (for example, changing a term loan to a revolver loan)
- e. The addition of an underlying or variable unrelated to the referenced rate index (for example, addition of payments that are indexed to the price of gold)
- f. The addition of an interest rate floor or cap that is in the money on the basis of the spot rate at the time of the amendment of the contract
- g. A concession granted to a debtor experiencing financial difficulty

- h. The addition or removal of a prepayment or conversion option except for the addition of a prepayment option for which exercise is contingent upon the replacement reference interest rate index not being determinable in accordance with the terms of the agreement
- i. The addition or removal of a feature that is intended to provide leverage
- j. Changes to the counterparty except in accordance with paragraphs 815-20-55-56A, 815-25-40-1A, and 815-30-40-1A
- k. Changes to the priority or seniority of an obligation in the event of a default or a liquidation event
- l. The addition or termination of a right to use one or more underlying assets in a lease contract
- m. Changes to renewal, termination, or purchase option provisions in a lease contract.

>>> **Changes to Contractual Fallback Terms**

848-20-15-7 The addition of contractual fallback terms, or the amendment of existing contractual fallback terms, to be consistent with fallback terms developed by a regulator or by a private-sector working group convened by a regulator is presumed to be related to reference rate reform in accordance with paragraph 848-20-15-5(g). That includes a predefined method to replace the current reference rate upon the discontinuance (or an anticipated discontinuance) of the reference rate.

848-20-15-8 If an entity modifies a contract to add contractual fallback terms or to change contractual fallback terms in a manner that is not consistent with fallback terms developed by a regulator or by a private-sector working group convened by a regulator, the entity shall assess whether the fallback terms include, or have the potential to include, a term that is unrelated to reference rate reform in accordance with paragraph 848-20-15-6 (for example, whether it is possible that the replacement rate could be a stated fixed rate). However, the inclusion of fallback terms that include, or have the potential to include, a term that is unrelated to reference rate reform shall be disregarded by an entity if at the time that the contractual fallback terms are added or amended the entity determines that activation of the term unrelated to reference rate reform is not probable of occurring if the fallback terms are triggered.

>>> **Changes from a Referenced Interest Rate Index to a Stated Fixed Rate**

848-20-15-9 A contract modification that directly replaces a reference rate index with a stated fixed rate is unrelated to reference rate reform in accordance with paragraph 848-20-15-6(c). However, the selection of a rate that is the last published rate of an interest rate index that is discontinued is not considered a stated fixed rate for the purpose of paragraph 848-20-15-6(c) (for example, a reference to the last published LIBOR rate is not considered unrelated to reference rate reform).

848-20-15-10 If a contract has existing contractual fallback terms that replace the current reference rate with a stated fixed rate upon the discontinuance of that current reference rate, a modification to those contractual fallback terms to replace the stated fixed rate with a new interest rate index is a change that is related to the replacement of the reference rate in accordance with paragraph 848-20-15-5.

> Modifications before the Discontinuance of a Reference Rate

848-20-15-11 An entity may modify the terms of a contract in anticipation of the discontinuance of the reference rate (that is, before the actual discontinuance of the reference rate).

Subsequent Measurement

General

> Option to Apply Expedients

848-20-35-1 An entity may elect to apply the guidance in this Subtopic to account for contract modifications that meet the scope of paragraphs 848-20-15-2 through 15-3. If an entity elects to apply the guidance in this Subtopic, the entity shall apply it for all contract modifications that meet the scope of paragraphs 848-20-15-2 through 15-3 that otherwise would be accounted for in accordance with the same Topic or Industry Subtopic. For example:

- a. If an entity applies the guidance in this Subtopic to modifications of a lease for a lessee accounted for in accordance with Topic 842, it shall apply the guidance in this Subtopic to all modifications of leases accounted for in accordance with Topic 842 that meet the scope of paragraphs 848-20-15-2 through 15-3.
- b. If an insurance entity applies the guidance in this Subtopic to modifications of a contract accounted for in accordance with Topic 310 on receivables, it shall apply the guidance in this Subtopic to all modifications of contracts accounted for in accordance with Industry Subtopic 944-310 that meet the scope of paragraphs 848-20-15-2 through 15-3. The entity does not need to apply the guidance in this Subtopic to contracts within the scope of other Industry Subtopics of Topic 944 that meet the scope of paragraphs 848-20-15-2 through 15-3.

848-20-35-2 If a contract modification does not meet the guidance for applying the optional relief in this Subtopic and, therefore, an entity must apply the guidance in another Topic or Industry Subtopic to assess the contract modification, that result shall not preclude the entity from applying the optional expedients in this Subtopic if other contract modifications meet the guidance for applying this Subtopic.

> Optional Expedient: Contract Modifications Due to Reference Rate Reform

848-20-35-3 This Subtopic provides optional expedients for accounting for modifications of contracts accounted for in accordance with the following Topics that meet the scope of paragraphs 848-20-15-2 through 15-3:

- a. Topic 310 on receivables
- b. Topic 470 on debt
- c. Topic 840 or 842 on leases.

848-20-35-4 If a contract is not within the scope of the Topics referenced in paragraph 848-20-35-3, an entity shall have the option to account for and present a modification that meets the scope of paragraphs 848-20-15-2 through 15-3 as an event that does not require contract remeasurement at the modification date or reassessment of a previous accounting determination required under the relevant Topic or Industry Subtopic. Paragraph 848-20-55-2 includes examples that illustrate the application of that guidance.

848-20-35-5 If the optional expedient in paragraphs 848-20-35-3 through 35-4 is elected, it shall be applied to all contracts accounted for under the relevant Topic or Industry Subtopic as described in paragraph 848-20-35-1.

> > Contracts within the Scope of Topic 310

848-20-35-6 If an entity elects the optional expedient in this paragraph, the entity shall account for a modification of a contract within the scope of Topic 310 that meets the scope of paragraphs 848-20-15-2 through 15-3 as if the modification was only minor in accordance with paragraph 310-20-35-10.

848-20-35-7 If the optional expedient in paragraph 848-20-35-6 is elected, it shall be applied to all contracts subject to Topic 310 as described in paragraph 848-20-35-1.

> > Contracts within the Scope of Topic 470

848-20-35-8 If an entity elects the optional expedient in this paragraph, the entity shall account for a modification of a contract within the scope of Topic 470 that meets the scope of paragraphs 848-20-15-2 through 15-3 in accordance with paragraphs 470-50-40-14, 470-50-40-16, 470-50-40-17(b), and 470-50-40-18(b) as if the modification was not substantial. That is, the original contract and the new contract shall be accounted for as if they were not substantially different from one another, and the modification shall not be accounted for in the same manner as a debt extinguishment in accordance with paragraph 470-50-40-13.

848-20-35-9 If the optional expedient in paragraph 848-20-35-8 is elected, it shall be applied to all contracts under Topic 470 as described in paragraph 848-20-35-1.

> > > Debt Exchanges or Modifications within a Year of the Current Modification

848-20-35-10 If the optional expedient in paragraph 848-20-35-8 is elected, an entity that applies the 10 percent cash flow test described in paragraph 470-50-40-10 for any subsequent contract modification within a year shall consider only terms and provisions that were in effect immediately following the election of the optional expedient for the particular contract.

> > Contracts within the Scope of Topic 840 or 842

848-20-35-11 If an entity elects the optional expedient in this paragraph for a modification of a contract within the scope of Topic 840 or 842 that meets the scope of paragraphs 848-20-15-2 through 15-3, the entity shall not do any of the following:

- a. Reassess lease classification and the discount rate (for example, the incremental borrowing rate for a lessee)
- b. Remeasure lease payments
- c. Perform other reassessments or remeasurements that would otherwise be required under Topic 840 or 842 when a modification of a lease contract is not accounted for as a separate contract.

848-20-35-12 If the optional expedient in paragraph 848-20-35-11 is elected, it shall be applied to all contracts under Topic 840 or 842 as described in paragraph 848-20-35-1.

> > > Lessees

848-20-35-13 If the optional expedient in paragraph 848-20-35-11 is elected, the modification of the reference rate and other terms related to the replacement of the reference rate on which variable lease payments in the original contract depended shall not require an entity to remeasure the lease liability. The change in the reference rate shall be treated in the same manner as the variable lease payments that were dependent on the reference rate in the original lease. That change shall not be included in the calculation of the lease liability; that is, the change shall be recognized in profit or loss in the period in which the obligation for those payments is incurred.

> > Embedded Derivatives within the Scope of Subtopic 815-15

848-20-35-14 If the optional expedient in this paragraph is elected, modification of a contract that meets the scope of paragraphs 848-20-15-2 through 15-3 (including the addition of an interest rate floor or cap that is out of the money in paragraph 848-20-15-5(e)) shall not require an entity to reassess its original conclusion about whether that contract contains an embedded derivative that is clearly and closely

related to the economic characteristics and risks of the host contract for the purposes of paragraph 815-15-25-1(a).

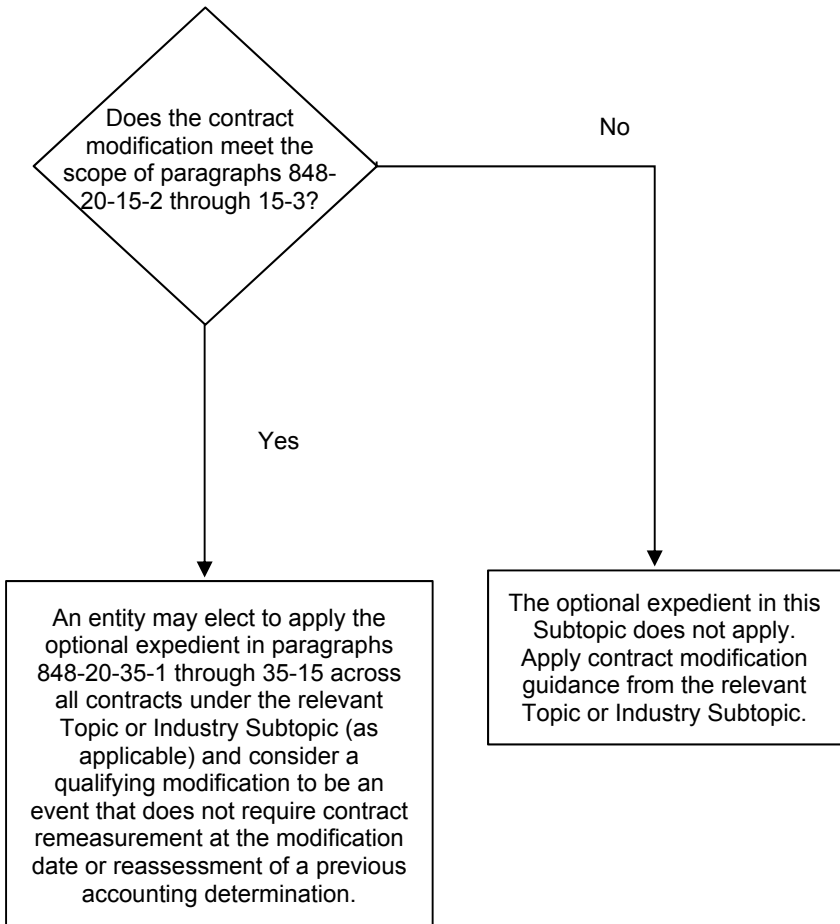
848-20-35-15 If the optional expedient in paragraph 848-20-35-14 is elected, it shall be applied to all contracts under Subtopic 815-15 as described in paragraph 848-20-35-1.

Implementation Guidance and Illustrations

General

> Implementation Guidance

848-20-55-1 The following flowchart summarizes the guidance in this Subtopic.



848-20-55-2 The following table illustrates the potential outcomes of applying the guidance in paragraph 848-20-35-4 to contract modifications that meet the scope of paragraphs 848-20-15-2 through 15-3 but are not within the scope of the Topics listed in paragraph 848-20-35-3. This table is not intended to be all-inclusive of the potential application of paragraph 848-20-35-4.

Contract or Instrument Modified as a Result of Reference Rate Reform	Potential Outcome of Applying Paragraph 848-20-35-4
An instrument accounted for as a derivative instrument in accordance with Subtopic 815-10	An entity should not reassess the modified instrument to determine whether it is a hybrid instrument and whether it includes a financing element in accordance with paragraphs 815-10-45-11 through 45-15. The modified instrument should be accounted for and presented in the same manner as the instrument existing before the modification.
A contract issued by an insurance entity and accounted for in accordance with Topic 944	An entity should not reassess the modified contract to determine whether it is substantially unchanged in accordance with Subtopic 944-30. The modified contract should be accounted for and presented as a continuation of the contract existing before the modification.
A contract accounted for in accordance with Topic 606 on revenue from contracts with customers	An entity should not reassess the modified contract in accordance with the contract modification guidance in paragraphs 606-10-25-10 through 25-13. Cash flow changes resulting from variability in the replacement reference rate should be accounted for and presented in the same manner as the cash flow changes that resulted from variability in the replaced reference rate before the modification for reference rate reform.

Contract or Instrument Modified as a Result of Reference Rate Reform	Potential Outcome of Applying Paragraph 848-20-35-4
A contract with a counterparty entity that is within the scope of the Variable Interest Entities (VIE) Subsections in accordance with Topic 810 on consolidation	An entity should not reconsider the determination of the counterparty entity's VIE status in accordance with paragraph 810-10-35-4. The counterparty entity's VIE status should remain unchanged from the VIE status determined before the modification.

4. Add Subtopic 848-30 as follows:

[For ease of readability, the new Subtopic is not underlined.]

Reference Rate Reform—Hedging—General

Overview and Background

General

848-30-05-1 This Subtopic provides guidance on optional expedients for allowing hedging relationships to continue when one or more of the critical terms of the hedging relationship change because of reference rate reform.

Scope and Scope Exceptions

General

848-30-15-1 The guidance in this Subtopic provides optional expedients for the requirements of Subtopic 815-20 related to changes in the critical terms of a hedging relationship that may be applied if the hedging instrument or the hedged item or the hedged forecasted transaction in the hedging relationship references a rate that meets the scope of paragraph 848-10-15-3.

Recognition

General

848-30-25-1 This Section sets forth the conditions that allow amendments to be made to the formal designation and documentation of hedging relationships upon a change due to reference rate reform.

> Option to Apply Expedients

848-30-25-2 An entity may elect to apply the guidance in this Subtopic for hedging relationships affected by reference rate reform on an individual hedging relationship basis. In addition, an entity may elect to apply the different optional expedients specified in paragraphs 848-30-25-3 through 25-13 on an individual hedging relationship basis. That is, each optional expedient may be elected for each individual hedging relationship and may not be elected for other similar hedging relationships. In addition, an entity may elect multiple optional expedients for the same individual hedging relationship and may elect those optional expedients in different reporting periods. For example, for a cash flow hedge, an entity may elect the optional expedient for the changes in the critical terms of the hedging instrument in accordance with paragraphs 848-30-25-5 through 25-7 when the fallback protocol of the hedging instrument is changed. In a different reporting period, the entity may elect to apply the optional expedient in paragraph 848-30-25-8 to change the method used in assessing hedge effectiveness and may elect to apply an optional expedient for subsequent assessments of effectiveness set forth in Subtopic 848-50.

> Optional Expedient: Change to the Formal Designation and Documentation for Change in Critical Terms

848-30-25-3 This paragraph provides an optional expedient for the guidance in paragraph 815-20-55-56. A change in the critical terms of the hedging relationship as documented at inception because of the election of an optional expedient in this Subtopic and Subtopics 848-40 and 848-50 shall not, in and of itself, be considered a dedesignation of the hedging relationship.

848-30-25-4 If an entity elects the optional expedient in paragraph 848-30-25-3, the entity shall update its hedge documentation (as applicable) noting the changes made no later than when the entity performs its first assessment of effectiveness after the change was identified in accordance with paragraphs 815-20-25-3(b)(2)(iv)(02) and 815-20-25-3A.

>> Optional Expedient: Changes in the Critical Terms of a Hedging Instrument, a Hedged Item, or a Forecasted Transaction Designated in a Fair Value Hedge, a Cash Flow Hedge, or a Net Investment Hedge

848-30-25-5 An entity may change the contractual terms of a hedging instrument, a hedged item, or a forecasted transaction designated in a fair value hedge, a cash flow hedge, or a net investment hedge that is affected or expected to be affected by reference rate reform and not be required to dedesignate the hedging relationship if the changes to the contractual terms meet the scope of paragraphs 848-20-15-2 through 15-3.

848-30-25-6 Some derivative instruments designated as hedging instruments may be modified through direct contract amendments to effectuate a change because of reference rate reform. Alternatively, a derivative designated as a hedging

instrument may be modified to effectuate the changes because of reference rate reform by both:

- a. Entering into a fully offsetting derivative contract to effectively cancel the original derivative contract
- b. Contemporaneously entering into a new derivative contract with the revised contractual terms.

Both methods of effectuating changes to contractual terms as a result of reference rate reform qualify for the optional expedient in paragraph 848-30-25-5.

848-30-25-7 A change to the interest rate used for margining, discounting, or contract price alignment for a derivative that is a hedging instrument in a fair value hedge, a cash flow hedge, or a net investment hedge shall not be considered a change to the critical terms of the hedging relationship that requires dedesignating the hedging relationship because of that change.

> > Optional Expedient: Changes to the Method Designated for Use in Assessing Hedge Effectiveness in a Cash Flow Hedge

848-30-25-8 An entity may change the method designated for use in assessing hedge effectiveness and documented at hedge inception in accordance with paragraph 815-20-25-3(b)(iv)(02) if both of the following criteria are met:

- a. Either the hedging instrument or the hedged forecasted transaction references a rate that meets the scope of paragraph 848-10-15-3.
- b. The new method designated for use in assessing hedge effectiveness is an optional expedient specified in Subtopic 848-50.

That expedient may be elected for a hedging relationship at the date an entity elects to apply any optional expedient method in accordance with this Subtopic. An entity also may change the method designated for use in assessing hedge effectiveness in Subtopics 815-20 and 815-30 upon the required discontinuance of an optional expedient as discussed in paragraph 848-50-35-19. An entity shall not be required to assess whether the replacement method is an improved method for assessing effectiveness or a preferable method of applying an accounting principle in accordance with Topic 250 on accounting changes and error corrections.

> > Optional Expedient: Changes to the Proportion of a Hedged Item or a Hedging Instrument in a Fair Value Hedge and to the Hedging Instruments That Are Designated in a Fair Value Hedge or a Cash Flow Hedge

848-30-25-9 If the hedging instrument or the hedged forecasted transaction or the designated benchmark interest rate in a fair value hedge references a rate that meets the scope of paragraph 848-10-15-3 and the hedging relationship is anticipated to be affected by reference rate reform, an entity may change:

- a. The proportion of a designated hedged item or a derivative instrument that is designated as a hedging instrument in a fair value hedge relationship. An entity may elect to rebalance the hedging relationship through any of the following approaches, including any combination of these approaches:
 - 1. Increasing the designated notional amount of the hedging instrument
 - 2. Decreasing the designated notional amount of the hedging instrument
 - 3. Increasing the designated portion of the hedged item
 - 4. Decreasing the designated portion of the hedged item.
 If an entity applies the optional expedient in (3) or (4), the cumulative effect of changing the designated proportion of the hedged item shall be recognized as an adjustment to the basis adjustment that shall be recognized in accordance with paragraph 848-40-25-7.
- b. The designated hedging instrument to combine two or more derivative instruments, or proportions of those instruments, to be jointly designated as the hedging instrument in a hedge relationship.

848-30-25-10 If an entity changes the designated hedging instrument in a fair value hedge to combine two or more derivative instruments, or proportions of those instruments, in accordance with paragraph 848-30-25-9(b), the entity shall assess the hedge effectiveness of the amended hedging relationship using a method in accordance with Subtopics 815-20 and 815-25. An entity also may select a new method in accordance with Subtopics 815-20 and 815-25 to assess the hedge effectiveness.

848-30-25-11 If an entity changes the designated hedging instrument in a cash flow hedge to combine two or more derivative instruments, or proportions of those instruments, in accordance with paragraph 848-30-25-9(b), the entity shall assess the hedge effectiveness of the amended hedging relationship using any of the following:

- a. A method in accordance with Subtopics 815-20 and 815-30
- b. An optional expedient for the subsequent assessment methods for assuming perfect effectiveness in accordance with paragraphs 848-50-35-4 through 35-9
- c. An optional expedient for the subsequent qualitative method after an initial assessment using a quantitative method in accordance with paragraphs 848-50-35-10 through 35-16
- d. An optional expedient for the subsequent quantitative methods in accordance with paragraphs 848-50-35-17 through 35-18.

> > Optional Expedient: Changes to the Systematic and Rational Method Used for Recognizing in Earnings the Excluded Components in a Fair Value Hedge, a Cash Flow Hedge, or a Net Investment Hedge

848-30-25-12 If the changes to a hedging instrument's contractual terms meet the scope of paragraphs 848-20-15-2 through 15-3, an entity may elect to change its systematic and rational method used to recognize in earnings the components excluded from the assessment of effectiveness in accordance with paragraph 815-20-25-83A. An entity shall apply the amended systematic and rational method prospectively and shall retain the amended systematic and rational method for the remaining life of the hedging relationship, including for periods after the date in paragraph 848-10-65-1(a)(3)(iii). The amended systematic and rational method may be subsequently amended for subsequent changes to a hedging instrument's contractual terms that meet the scope of paragraphs 848-20-15-2 through 15-3. If an entity does not apply this optional expedient, the entity's systematic and rational method documented at hedge inception may require an adjustment at the end of the hedging relationship so that no excluded components remain in accumulated other comprehensive income at the end of the hedging relationship.

848-30-25-13 In addition, if the changes to a hedging instrument's contractual terms meet the scope of paragraphs 848-20-15-2 through 15-3 and any change in those contractual terms causes a change in the fair value of the excluded component, an entity may elect to recognize the change in fair value of the excluded component in current earnings. An entity shall present the recognition of the adjustment in the same income statement line item that is used to present the earnings effect of the hedged item.

5. Add Subtopic 848-40 as follows:

[For ease of readability, the new Subtopic is not underlined.]

Reference Rate Reform—Fair Value Hedges

Overview and Background

General

848-40-05-1 This Subtopic provides guidance on optional expedients for the accounting for and financial reporting of fair value hedges under Topic 815 that are affected by reference rate reform.

Scope and Scope Exceptions

General

848-40-15-1 The guidance in this Subtopic provides optional expedients for certain requirements of Subtopics 815-20 and 815-25 related to fair value hedges. An entity shall continue to apply all other requirements applicable to fair value hedges in Subtopics 815-20 and 815-25.

Recognition

General

> Option to Apply Expedients

848-40-25-1 An entity may elect to apply the guidance in this Subtopic for fair value hedges affected by reference rate reform on an individual hedging relationship basis. In addition, an entity may elect to apply the different optional expedients specified in paragraphs 848-40-25-2 through 25-9 on an individual hedging relationship basis. For example, an entity may elect to apply the optional expedient in this Subtopic for the change in the designated benchmark interest rate and not elect to apply the optional expedient for the shortcut method for assessing hedge effectiveness. An entity may disregard the guidance in paragraph 815-20-25-81 when applying the guidance in this Subtopic and shall not be required to assess effectiveness for similar hedges in a similar manner.

> Optional Expedient: Change in the Designated Benchmark Interest Rate

848-40-25-2 If the hedged item is a financial asset or liability, a recognized loan servicing right, or a nonfinancial firm commitment with financial components, the designated risk being hedged may be the risk of changes in the hedged item's fair value attributable to changes in the designated benchmark interest rate in accordance with paragraph 815-20-25-12(f)(2). In a hedge of the changes in fair value attributable to the benchmark interest rate, if the referenced interest rate index of the hedging instrument changes or an entity changes the designated hedging instrument to combine two or more derivative instruments to be jointly designated as the hedging instrument in accordance with paragraph 848-30-25-9(b) (for example, adding a new interest rate basis swap to an existing interest rate swap), an entity may change the designated benchmark interest rate and the component of cash flows and continue to apply hedge accounting without dedesignation if all of the following criteria are met:

- a. The designated benchmark interest rate being changed is a rate within the scope of paragraph 848-10-15-3.
- b. The replacement designated benchmark interest rate is an eligible benchmark interest rate in accordance with paragraph 815-20-25-6A.
- c. The hedging instrument is expected to be prospectively highly effective at achieving offsetting changes in fair value attributable to the revised hedged risk on the basis of the amended terms of the hedging relationship.

848-40-25-3 An entity shall update its hedge documentation in accordance with paragraph 848-30-25-4 upon a change in the designated benchmark interest rate in accordance with paragraph 848-40-25-2.

> > Change in Fair Value of Hedged Item Due to a Change in the Designated Benchmark Interest Rate

848-40-25-4 If an entity elects the optional expedient in paragraphs 848-40-25-2 through 25-3 to change the designated benchmark interest rate, it shall, at a minimum, revise the rate used to discount the cash flows associated with the hedged item reflecting the change in the designated benchmark interest rate in accordance with paragraph 848-40-25-2. An entity may include a spread adjustment to the revised benchmark interest rate used to discount the cash flows associated with the hedged item in accordance with an approach in paragraph 848-40-25-5. In addition, an entity may adjust the cash flows for the designated term of the designated hedged item.

848-40-25-5 At the time of the change to the designated benchmark interest rate, an entity may either:

- a. Apply an approach that adjusts the hedged item's cumulative fair value hedge basis adjustment attributable to changing from the originally designated benchmark interest rate to the replacement designated benchmark interest rate
- b. Apply an approach that results in no adjustment to the hedged item's cumulative basis adjustment (that is, maintain the hedged item's cumulative basis adjustment immediately before the date of the change).

This Subtopic does not specify a single method for applying those approaches. The method an entity uses shall be reasonable, and an entity shall use a similar method for similar hedges and shall justify the use of different methods for similar hedges.

848-40-25-6 In calculating the subsequent changes in the hedged item's fair value attributable to changes in the replacement benchmark interest rate, an entity shall use the revised benchmark interest rate to discount the cash flows associated with the hedged item and shall use the remaining revised cash flows for the designated term of the designated hedged item. The revised benchmark interest rate (including the spread adjustment to the revised benchmark interest rate if applicable) to discount the cash flows associated with the hedged item and the remaining revised cash flows for the designated term shall be retained for periods after the date in paragraph 848-10-65-1(a)(3)(iii).

848-40-25-7 If an entity adjusts the cumulative basis adjustment because of the change in the designated benchmark interest rate in accordance with paragraph 848-40-25-5(a), the entity shall recognize the adjustment currently in earnings. An entity shall present the adjustment in the same income statement line item that is used to present the earnings effect of the hedged item.

> Optional Expedient: Assessment of Hedge Effectiveness When Assuming Perfect Hedge Effectiveness in a Hedge with an Interest Rate Swap (Shortcut Method)

848-40-25-8 For fair value hedges for which the shortcut method is applied in accordance with paragraphs 815-20-25-102 through 25-109 and 815-20-25-111 through 25-117, the following conditions from paragraph 815-20-25-104 that apply to fair value hedges may be disregarded in determining whether the hedging relationship continues to qualify for the shortcut method upon a change in the contractual terms of the hedging instrument in accordance with paragraphs 848-30-25-5 through 25-7:

- a. The formula for computing net settlements under the interest rate swap is the same for each net settlement in accordance with paragraph 815-20-25-104(d).
- b. The terms are typical of those instruments, and the terms do not invalidate the assumption of perfect effectiveness in accordance with paragraph 815-20-25-104(g).

If an entity elects the practical expedient in this paragraph for a fair value hedge for which the shortcut method is applied, the entity is not required to periodically evaluate the conditions in paragraph 815-20-25-104(d) and (g) for the remaining life of the hedging relationship, including for periods after December 31, 2022 (see paragraph 848-10-65-1(a)(3)(iii)).

848-40-25-9 If an entity elects to apply the optional expedient for the shortcut method in paragraph 848-40-25-8, the entity shall update its hedge documentation in accordance with paragraph 848-30-25-4.

6. Add Subtopic 848-50 as follows:

[For ease of readability, the new Subtopic is not underlined.]

Reference Rate Reform—Cash Flow Hedges

Overview and Background

General

848-50-05-1 This Subtopic provides guidance related to optional expedients for the accounting for and financial reporting of cash flow hedges under Topic 815 on derivatives and hedging that are affected by reference rate reform.

Scope and Scope Exceptions

General

848-50-15-1 The guidance in this Subtopic provides optional expedients for certain requirements of Subtopics 815-20 and 815-30 related to the assessment of hedge effectiveness and the designation of cash flow hedges. An entity shall continue to

apply all other cash flow hedge accounting requirements specified in Subtopics 815-20 and 815-30.

Recognition

General

> Option to Apply Expedients

848-50-25-1 An entity may elect to apply the optional expedients for the assessment of hedge effectiveness in this Subtopic to cash flow hedges affected by reference rate reform on an individual hedging relationship basis. In addition, an entity may elect to apply the different optional expedients for the assessment of hedge effectiveness in this Subtopic on an individual hedging relationship basis. An entity may disregard the guidance in paragraph 815-20-25-81 when applying the guidance in this Subtopic and shall not be required to assess effectiveness for similar hedges in a similar manner.

> Eligibility of Cash Flow Hedges Affected by Reference Rate Reform

> > Probability of the Hedged Forecasted Transaction

848-50-25-2 An entity shall continue to assess whether the underlying hedged forecasted transaction (for example, the future interest receipts of a financial asset or future interest payments of a financial liability or the forecasted issuance or purchase of a debt instrument) remains probable in accordance with paragraph 815-20-25-15(b). If the designated hedged interest rate risk in a cash flow hedge of a forecasted transaction is a reference rate that meets the scope of paragraph 848-10-15-3, an entity may assert that the hedged forecasted transaction (for example, the future interest receipts of a financial asset or future interest payments of a financial liability or the forecasted issuance or purchase of a debt instrument) remains probable in accordance with paragraph 815-20-25-15(b) regardless of the modification or expected modification of terms in accordance with paragraphs 848-20-15-2 through 15-3.

> > Change in the Designated Hedged Interest Rate Risk

848-50-25-3 Paragraph 815-30-35-37A specifies that the designated hedged risk for a cash flow hedge of a forecasted transaction may change during a hedging relationship and an entity may continue to apply hedge accounting if the hedge remains highly effective. For purposes of applying that guidance to a cash flow hedge affected by reference rate reform, a cash flow hedge may continue hedge accounting subject to either the hedging relationship remaining highly effective in accordance with Subtopics 815-20 and 815-30 or an entity electing an optional expedient method to subsequently assess hedge effectiveness in accordance with paragraphs 848-50-35-1 through 35-18. If an entity elects to change the

designated hedged interest rate risk for a cash flow hedge, the entity shall update its hedge documentation in accordance with paragraph 848-30-25-4.

> **Initial Assessment of Hedge Effectiveness**

> > **Optional Expedients for Initial Assessment of Hedge Effectiveness**

848-50-25-4 An entity may perform its initial hedge effectiveness assessment in a manner that adjusts how it applies certain guidance in Subtopics 815-20 and 815-30 as specified in paragraph 848-50-25-5 for cash flow hedges for which either the hedged forecasted transaction or the hedging instrument references a rate that meets the scope of paragraph 848-10-15-3. For subsequent hedge effectiveness assessments, an entity may use the eligible optional expedients for hedge effectiveness assessment in paragraphs 848-50-35-1 through 35-18.

848-50-25-5 In accordance with paragraph 815-20-25-3(b)(2)(iv)(01), an entity shall perform an initial prospective assessment of hedge effectiveness on a quantitative basis unless one of the methods listed in paragraph 815-20-25-3(b)(2)(iv)(01) applies. Paragraphs 848-50-25-6 through 25-12 describe certain modifications to the relevant methods for performing an initial assessment of hedge effectiveness for cash flow hedges within the scope of this Subtopic.

848-50-25-6 An entity may disregard the following conditions in determining whether it may apply the shortcut method for assuming perfect hedge effectiveness in a cash flow hedge with an interest rate swap in accordance with paragraphs 815-20-25-102 through 25-109 and 815-20-25-111 through 25-117:

- a. The formula for computing net settlements under the interest rate swap is the same for each net settlement in accordance with paragraph 815-20-25-104(d).
- b. The terms are typical of those derivative instruments and do not invalidate the assumption of perfect effectiveness in accordance with paragraph 815-20-25-104(g).
- c. The repricing dates of the variable-rate asset or variable-rate liability and the hedging instrument must occur on the same dates and be calculated the same way in accordance with paragraph 815-20-25-106(d).
- d. The index on which the variable leg of the interest rate swap is based matches the contractually specified interest rate designated as the interest rate being hedged for that hedging relationship in accordance with paragraph 815-20-25-106(g).

848-50-25-7 For cash flow hedges when an option's terminal value is used to assess hedge effectiveness, an entity may disregard the following conditions in determining whether a cash flow hedge of the option's terminal value may be considered perfectly effective in accordance with paragraphs 815-20-25-126 through 25-129A:

- a. The underlying of the hedging instrument needs to match the underlying of the hedged forecasted transaction in accordance with paragraph 815-20-25-129(a).
- b. The strike price (or prices) of the hedging option (or combination of options) matches the specified level (or levels) beyond (or within) which the entity's exposure is being hedged in accordance with paragraph 815-20-25-129(b).
- c. The hedging instrument's inflows (outflows) at its maturity date due to the underlying reference rate and strike price (or prices) of the hedging option (or combination of options) completely offset the change in the hedged transaction's cash flows for the risk being hedged in accordance with paragraph 815-20-25-129(c).

If all other conditions in paragraph 815-20-25-129 are met, the hedging relationship may be considered perfectly effective.

848-50-25-8 An eligible private company in accordance with paragraph 815-20-25-135 may disregard the following conditions in determining whether a cash flow hedge of a variable-rate borrowing with a receive-variable pay-fixed interest rate swap using the simplified hedge accounting approach may be considered perfectly effective in accordance with paragraphs 815-20-25-133 through 25-138:

- a. Both the variable rate on the swap and the borrowing are based on the same index and reset period in accordance with paragraph 815-20-25-137(a).
- b. The terms of the swap are typical in accordance with paragraph 815-20-25-137(b).
- c. The repricing and settlement dates for the swap and the borrowing match in accordance with paragraph 815-20-25-137(c).

If all other conditions of paragraph 815-20-25-137 are met, the hedging relationship may apply the simplified hedge accounting approach.

848-50-25-9 For the change-in-variable-cash-flows method in accordance with paragraphs 815-30-35-16 through 35-24, an entity may disregard the following conditions in assessing whether the method will result in a perfectly effective hedge in accordance with paragraph 815-30-35-22:

- a. The variable-rate leg of the interest rate swap and the hedged variable cash flows of the asset or liability are based on the same interest rate index in accordance with paragraph 815-30-35-22(a).
- b. The interest rate reset dates applicable to the variable-rate leg of the interest rate swap and to the hedged variable cash flows of the asset or liability are the same in accordance with paragraph 815-30-35-22(b).

In addition, an entity may disregard the condition in paragraph 815-30-35-22(c) if the basis differences are due to differences in a cap or floor between the variable-rate leg of the interest rate swap and the variable-rate asset or the variable-rate

liability. If all other conditions in paragraph 815-30-35-22 are met, the hedging relationship may be considered perfectly effective. If all other conditions in paragraph 815-30-35-22 are not met, an entity shall not consider that the method will result in a perfectly effective hedge.

848-50-25-10 For the hypothetical derivative method in accordance with paragraphs 815-30-35-25 through 35-29, an entity may disregard the following critical terms in assessing whether the method will result in a perfectly effective hedge:

- a. The same repricing dates in accordance with paragraph 815-30-35-25(b)(2)
- b. The same index in accordance with paragraph 815-30-35-25(b)(3)
- c. Mirror image caps and floors (including a cap or floor that exists in a variable-rate asset or a variable-rate liability and does not exist in a hedging instrument or vice versa) in accordance with paragraph 815-30-35-25(b)(4).

If all other conditions in paragraph 815-30-35-25 are met, the hedging relationship may be considered perfectly effective. If all other conditions in paragraph 815-30-35-25 are not met, an entity shall not consider that the method will result in a perfectly effective hedge.

> > > Optional Expedient: Initial Assessment Performed Using a Quantitative Method

848-50-25-11 An entity may adjust any of the three methods of assessing hedge effectiveness in paragraphs 815-30-35-10 through 35-32 when hedge effectiveness is assessed on a quantitative basis (using either a dollar-offset test or a statistical method such as regression analysis) as follows:

- a. If both the hedged forecasted transaction and the hedging instrument have a reference rate that meets the scope of paragraph 848-10-15-3 (or in a cash flow hedge of a forecasted purchase, sale, or issuance of a fixed-rate instrument in which the designated hedged interest rate risk is the benchmark interest rate if only the hedging instrument has a reference rate that meets the scope of paragraph 848-10-15-3), an entity may assume that the reference rate will not be replaced for the remainder of the hedging relationship. That is, the entity does not need to consider the likelihood of whether or when the reference rate will be discontinued or changed because of reference rate reform.
- b. If either the hedged forecasted transaction or the hedging instrument references a rate that meets the scope of paragraph 848-10-15-3, the terms of the hedged forecasted transaction may be altered to match the hedging instrument for the following:
 1. The referenced interest rate index

2. The reset period, reset dates, day-count conventions, business-day conventions, and repricing calculation (for example, forward-looking calculation or in-arrears calculation)
3. A spread adjustment for the difference between the existing reference rate and the replacement reference rate
4. A cap or floor (including a cap or floor that exists in a variable-rate asset or a variable-rate liability and does not exist in a hedging instrument or vice versa).

> > > Optional Expedient: Initial Assessment Based on an Option's Terminal Value

848-50-25-12 If an entity assesses hedge effectiveness on the basis of an option's terminal value in accordance with paragraph 815-20-25-126 and if either the hedged forecasted transaction or the hedging instrument references a rate that meets the scope of paragraph 848-10-15-3, an entity may adjust the critical terms of the perfectly effective hypothetical hedging instrument in accordance with paragraph 815-20-25-129 to match the hedging instrument for the following:

- a. The underlying reference rate
- b. The strike price (or prices) of the hedging option (or combination of options)
- c. The hedging instrument's inflows (outflows) at its maturity date due to the underlying reference rate and strike price (or prices) of the hedging option (or combination of options).

> > Hedging a Group of Forecasted Transactions

848-50-25-13 This paragraph provides an optional expedient for assessing a group of individual forecasted transactions in a cash flow hedge affected by reference rate reform. An entity may elect this optional expedient if a forecasted transaction in the hedged group of forecasted transactions references a rate that meets the scope of paragraph 848-10-15-3.

848-50-25-14 An entity may disregard the guidance in paragraph 815-20-25-15(a)(2) that states that a group of individual transactions shall share the same risk exposure for which they are designated as being hedged. However, other limitations in paragraph 815-20-25-15(a)(2) shall continue such that a forecasted purchase (including debt issuance) and a forecasted sale shall not both be included in the same group of individual transactions that constitute the hedged transaction.

Subsequent Measurement

General

> Subsequent Assessment of Hedge Effectiveness

848-50-35-1 This guidance provides optional expedients that may be elected for cash flow hedges affected by reference rate reform for the purposes of determining whether an entity shall be allowed to continue applying hedge accounting for the hedging relationship. An entity may elect these optional expedient methods if either the forecasted transaction or the hedging instrument references a rate that meets the scope of paragraph 848-10-15-3.

848-50-35-2 If an entity elects to apply an optional expedient method in this Subtopic for a cash flow hedging relationship, the entity need only apply the optional expedient method prospectively beginning on the date that the expedient method is first applied in determining whether the entity can continue to apply hedge accounting to that hedging relationship. After the date on which the optional expedient method is first applied (if the hedging relationship continues), the entity shall assess the hedging relationship using the optional expedient method both prospectively and retrospectively from the date on which the expedient method is first applied.

848-50-35-3 If an entity elects to change the method of assessing hedge effectiveness for a cash flow hedge to an optional expedient method in accordance with paragraphs 848-50-35-4 through 35-18, the entity shall update its hedge documentation in accordance with paragraph 848-30-25-4.

> > Optional Expedient: Subsequent Assessments Using a Method That Assumes Perfect Effectiveness

848-50-35-4 If an entity applies an initial assessment method in accordance with paragraph 815-20-25-3(b)(2)(iv)(01) or an initial assessment method in accordance with paragraphs 848-50-25-6 through 25-10 for the assessment of initial hedge effectiveness, paragraphs 848-50-35-5 through 35-9 describe certain modifications to the relevant methods for performing an ongoing assessment of hedge effectiveness for cash flow hedges.

848-50-35-5 An entity may disregard the following conditions from paragraphs 815-20-25-104 and 815-20-25-106 that apply to cash flow hedges in determining whether the hedging relationship continues to qualify for the shortcut method upon a change in the contractual terms of the hedging instrument in accordance with paragraphs 848-30-25-5 through 25-7:

- a. The formula for computing net settlements under the interest rate swap is the same for each net settlement in accordance with paragraph 815-20-25-104(d).
- b. The terms are typical of those derivative instruments and do not invalidate the assumption of perfect effectiveness in accordance with paragraph 815-20-25-104(g).

- c. The repricing dates of the variable-rate asset or variable-rate liability and the hedging instrument must occur on the same dates and be calculated the same way in accordance with paragraph 815-20-25-106(d).
- d. The index on which the variable leg of the interest rate swap is based matches the contractually specified interest rate designated as the interest rate being hedged for that hedging relationship in accordance with paragraph 815-20-25-106(g).

848-50-35-6 For cash flow hedges when an option's terminal value is used in assessing hedge effectiveness, an entity may disregard the following conditions in determining whether a cash flow hedge of the option's terminal value may continue to be considered perfectly effective in accordance with paragraphs 815-20-25-126 through 25-129A:

- a. The underlying of the hedging instrument needs to match the underlying of the hedged forecasted transaction in accordance with paragraph 815-20-25-129(a).
- b. The strike price (or prices) of the hedging option (or combination of options) matches the specified level (or levels) beyond (or within) which the entity's exposure is being hedged in accordance with paragraph 815-20-25-129(b).
- c. The hedging instrument's inflows (outflows) at its maturity date due to the underlying reference rate and strike price (or prices) of the hedging option (or combination of options) completely offset the change in the hedged transaction's cash flows for the risk being hedged in accordance with paragraph 815-20-25-129(c).

If all other conditions of paragraph 815-20-25-129 are met, the hedging relationship may continue to be considered perfectly effective.

848-50-35-7 An eligible private company in accordance with paragraph 815-20-25-135 may disregard the following conditions in determining whether a cash flow hedge of a variable-rate borrowing with a receive-variable pay-fixed interest rate swap using the simplified hedge accounting approach may continue to be considered perfectly effective in accordance with paragraphs 815-20-25-133 through 25-138:

- a. Both the variable rate on the swap and the borrowing are based on the same index and reset period in accordance with paragraph 815-20-25-137(a).
- b. The terms of the swap are typical in accordance with paragraph 815-20-25-137(b).
- c. The repricing and settlement dates for the swap and the borrowing match in accordance with paragraph 815-20-25-137(c).

If all other conditions of paragraph 815-20-25-137 continue to be met, the hedging relationship may continue to apply the simplified hedge accounting approach.

848-50-35-8 For the change-in-variable-cash-flows method in accordance with paragraphs 815-30-35-16 through 35-23, an entity may disregard the following conditions in assessing whether the method will result in a perfectly effective hedge in accordance with paragraph 815-30-35-22:

- a. The variable-rate leg of the interest rate swap and the hedged variable cash flows of the asset or liability are based on the same interest rate index in accordance with paragraph 815-30-35-22(a).
- b. The interest rate reset dates applicable to the variable-rate leg of the interest rate swap and to the hedged variable cash flows of the asset or liability are the same in accordance with paragraph 815-30-35-22(b).

In addition, an entity may disregard the condition in paragraph 815-30-35-22(c) if the basis differences are due to differences in a cap or floor between the variable-rate leg of the interest rate swap and the variable-rate asset or the variable-rate liability. If all other conditions of paragraph 815-30-35-22 continue to be met, the hedging relationship may continue to be considered perfectly effective. If all other conditions of paragraph 815-30-35-22 are not met, an entity shall not consider that the method will result in a perfectly effective hedge.

848-50-35-9 For the hypothetical-derivative method in accordance with paragraphs 815-30-35-25 through 35-29, an entity may disregard the following critical terms in assessing whether the method will result in a perfectly effective hedge:

- a. The same repricing dates in accordance with paragraph 815-30-35-25(b)(2)
- b. The same index in accordance with paragraph 815-30-35-25(b)(3)
- c. Mirror image caps and floors (including a cap or floor that exists in a variable-rate asset or a variable-rate liability and does not exist in a hedging instrument or vice versa) in accordance with paragraph 815-30-35-25(b)(4).

If all other conditions of paragraph 815-30-35-25 continue to be met, the hedging relationship may continue to be considered perfectly effective. If all other conditions of paragraph 815-30-35-25 are not met, an entity shall not consider that the method will result in a perfectly effective hedge.

> > Optional Expedient: Subsequent Assessments Performed Using a Qualitative Method

848-50-35-10 An entity may qualitatively assess cash flow hedges on an ongoing basis in accordance with paragraphs 848-50-35-11 through 35-16 after the entity has performed an initial assessment of hedge effectiveness using any of the following:

- a. A method in accordance with Subtopics 815-20 and 815-30

- b. An optional expedient method in accordance with paragraphs 848-50-25-6 through 25-12.

An entity that elects this optional expedient may disregard the guidance in paragraphs 815-20-35-2A through 35-2F for performing hedge effectiveness assessments on a qualitative basis.

848-50-35-11 The following criteria shall be met so that an entity may continue to assert qualitatively that it may continue to apply hedge accounting for a hedging relationship under this Subtopic:

- a. The hedged forecasted transaction or the hedging instrument references a rate that meets the scope of paragraph 848-10-15-3.
- b. There have been no changes to the terms of the hedging instrument or the forecasted transaction other than those specified in paragraphs 848-20-15-2 through 15-3.
- c. An entity shall consider the likelihood of the counterparty's compliance with the contractual terms of the hedging derivative that require the counterparty to make payments to the entity.

848-50-35-12 An entity shall verify and document whenever financial statements or earnings are reported and at least every three months that the facts and circumstances evaluated in accordance with paragraph 848-50-35-11 have not changed; therefore, the entity can assert qualitatively that the hedging relationship did qualify and continues to qualify for this optional expedient method. No other facts and circumstances related to paragraphs 815-20-35-2A through 35-2F need to be assessed as part of this evaluation.

848-50-35-13 If the facts and circumstances change in accordance with paragraph 848-50-35-12 such that an entity no longer can assert qualitatively that the hedging relationship may continue to qualify for hedge accounting under this Subtopic, the entity shall assess hedge effectiveness on a quantitative basis using the guidance in Subtopics 815-20 and 815-30 or using a quantitative optional expedient method in this Subtopic to the extent that the quantitative optional expedient method is eligible to be used.

848-50-35-14 If there is no identifiable event that led to the change in the facts and circumstances of the hedging relationship, the entity may begin performing quantitative assessments of effectiveness from the beginning of the current period. An entity may change its method of assessing hedge effectiveness and update its hedging documentation to reflect that change in accordance with paragraph 848-30-25-4.

848-50-35-15 After assessing the hedge effectiveness using a quantitative optional expedient method for one or more reporting periods, an entity may revert to a qualitative optional expedient method of hedge effectiveness under this Subtopic to the extent that the qualitative optional expedient method is eligible to be used.

848-50-35-16 An entity may perform a quantitative assessment of hedge effectiveness in any reporting period, and the results of that quantitative assessment shall not preclude an entity from using the qualitative optional expedient method in paragraphs 848-50-35-11 through 35-12 in a subsequent reporting period.

> > Optional Expedient: Subsequent Assessments Performed Using a Quantitative Method

848-50-35-17 After initially assessing the hedge effectiveness using a method in accordance with Subtopics 815-20 and 815-30 or using an optional expedient method in accordance with paragraphs 848-50-25-6 through 25-12, an entity may adjust any of the three methods of assessing subsequent hedge effectiveness in paragraphs 815-30-35-10 through 35-32 when hedge effectiveness is assessed on a quantitative basis (using either a dollar-offset test or a statistical method such as regression analysis) as follows:

- a. If both the hedged forecasted transaction and the hedging instrument have a reference rate that meets the scope of paragraph 848-10-15-3 (or in a cash flow hedge of a forecasted purchase, sale, or issuance of a fixed-rate instrument in which the designated hedged interest rate risk is the benchmark interest rate if only the hedging instrument has a reference rate that meets the scope of paragraph 848-10-15-3), an entity may assume that the reference rate will not be replaced for the remainder of the hedging relationship. That is, the entity does not need to consider the likelihood of whether the reference rate will be discontinued or changed because of reference rate reform.
- b. If either the hedged forecasted transaction or the hedging instrument references a rate that meets the scope of paragraph 848-10-15-3, the terms of the hedged forecasted transaction may be altered to match the hedging instrument for the following:
 1. The referenced interest rate index
 2. The reset period, reset dates, day-count conventions, business-day conventions, and repricing calculation (for example, forward-looking calculation or in-arrears calculation)
 3. A spread adjustment for the difference between the existing reference rate and the replacement reference rate
 4. A cap or floor (including a cap or floor that exists in a variable-rate asset or a variable-rate liability and does not exist in a hedging instrument or vice versa).

> > Optional Expedient: Subsequent Assessment Based on an Option's Terminal Value

848-50-35-18 If an entity assesses subsequent hedge effectiveness on the basis of an option's terminal value in accordance with paragraph 815-20-25-126 and if

either the forecasted transaction or the hedging instrument references a rate that meets the scope of paragraph 848-10-15-3, an entity may adjust the critical terms of the perfectly effective hypothetical hedging instrument in accordance with paragraph 815-20-25-129 to match the hedging instrument for the following:

- a. The underlying reference rate
- b. The strike price (or prices) of the hedging option (or combination of options)
- c. The hedging instrument's inflows (outflows) at its maturity date due to the underlying reference rate and strike price (or prices) of the hedging option (or combination of options).

> Conditions That Require Discontinuance of Optional Expedient for Assessing Hedge Effectiveness and Reversion to Subtopics 815-20 and 815-30

848-50-35-19 An entity shall discontinue the use of the optional expedients for assessing cash flow hedge effectiveness in paragraphs 848-50-35-1 through 35-18 if any of the following occurs:

- a. Neither the hedged item nor the hedging instrument references a rate that meets the scope of paragraph 848-10-15-3.
- b. The guidance in this Topic is superseded (see paragraph 848-10-65-1(a)(3)).
- c. The entity elects to cease to apply the optional expedients.

848-50-35-20 If an entity applies an optional expedient method for assessing hedge effectiveness in accordance with paragraphs 848-50-35-1 through 35-18 and the hedging relationship continues after the entity discontinues applying the optional expedient method because of a condition in paragraph 848-50-35-19, the entity shall revert to applying the qualifying criteria and hedge assessment methods in Subtopics 815-20 and 815-30 to assess whether hedge accounting may continue for subsequent reporting periods. The entity may elect any hedge assessment method in accordance with Subtopics 815-20 and 815-30, and the entity is not required to use a hedge assessment method that was used before the election of the optional expedient method in paragraphs 848-50-35-1 through 35-18. For example, an entity that is using the shortcut method optional expedient for the initial assessment of a cash flow hedging relationship in accordance with paragraph 848-50-25-6 and the subsequent assessment in accordance with paragraph 848-50-35-5 shall revert to a hedge assessment method in accordance with Subtopics 815-20 and 815-30 in assessing whether the hedging relationship continues to qualify for hedge accounting from the date that the replacement assessment method is first applied.

848-50-35-21 An entity shall perform the cash flow hedge effectiveness assessment in accordance with Subtopics 815-20 and 815-30 to assess whether hedge accounting may continue for subsequent reporting periods. An entity may

create the terms of the instrument used to estimate changes in the fair value of its hedged risk (in accordance with either the hypothetical derivative method or another acceptable method in Subtopics 815-20 and 815-30) on the basis of market data as of the inception of the hedging relationship. The entity shall not revise previous assessments of effectiveness that were performed in accordance with this Subtopic.

848-50-35-22 An entity shall continue to assess whether the underlying hedged forecasted transaction (for example, the future interest receipts of a financial asset or future interest payments of a financial liability or the forecasted issuance or purchase of a debt instrument) remains probable of occurring in accordance with paragraph 815-20-25-15(b). The assessments of whether the forecasted transactions remain probable are performed without regard to the replacement of the contractually specified interest rate.

848-50-35-23 A change in the method of assessing hedge effectiveness for a cash flow hedge upon discontinuing the application of an optional expedient method to a hedge assessment method in accordance with Subtopics 815-20 and 815-30 is not a change that results in dedesignation of the hedging relationship. An entity shall update its hedge documentation to reflect the change in the method of assessing hedge effectiveness in accordance with paragraph 848-30-25-4.

848-50-35-24 If an entity discontinues an optional expedient method because of a condition in paragraph 848-50-35-19 and the hedging relationship does not qualify for hedge accounting when applying a hedge assessment method in Subtopics 815-20 and 815-30, then the entity shall discontinue hedge accounting prospectively and apply the guidance in paragraphs 815-30-40-2 through 40-6A.

Amendments to Topic 848

7. Supersede all paragraphs in Topic 848, with a link to transition paragraph 848-10-65-1, as follows:

[Note: See table of superseded Subtopics and paragraphs below.]

Pending Content:

Transition Date: (P) *January 1, 2023*; (N) *January 1, 2023* | **Transition Guidance:** 848-10-65-1

Paragraph superseded by Accounting Standards Update No. 2020-04.

Superseded Subtopics	Superseded Paragraphs
848-10	848-10-05-1 through 05-3, 848-10-15-1 through 15-4, 848-10-35-1, 848-10-35-2, 848-10-50-1
848-20	848-20-05-1, 848-20-15-1 through 15-11, 848-20-35-1 through 35-15, 848-20-55-1, 848-20-55-2
848-30	848-30-05-1, 848-30-15-1, 848-30-25-1 through 25-13
848-40	848-40-05-1, 848-40-15-1, 848-40-25-1 through 25-9
848-50	848-50-05-1, 848-50-15-1, 848-50-25-1 through 25-14, 848-50-35-1 through 35-24

Amendments to Status Sections

8. Add paragraph 848-10-00-1 as follows:

848-10-00-1 The following table identifies the changes made to this Subtopic.

Paragraph	Action	Accounting Standards Update	Date
Financial Statements Are Available to Be Issued	Superseded	2020-04	03/12/2020
Financial Statements Are Available to Be Issued	Added	2020-04	03/12/2020
848-10-05-1 through 05-3	Superseded	2020-04	03/12/2020
848-10-05-1 through 05-3	Added	2020-04	03/12/2020
848-10-15-1 through 15-4	Superseded	2020-04	03/12/2020
848-10-15-1 through 15-4	Added	2020-04	03/12/2020
848-10-35-1	Superseded	2020-04	03/12/2020
848-10-35-1	Added	2020-04	03/12/2020
848-10-35-2	Superseded	2020-04	03/12/2020
848-10-35-2	Added	2020-04	03/12/2020
848-10-50-1	Superseded	2020-04	03/12/2020
848-10-50-1	Added	2020-04	03/12/2020

Paragraph	Action	Accounting Standards Update	Date
848-10-65-1	Superseded	2020-04	03/12/2020
848-10-65-1	Added	2020-04	03/12/2020

9. Add paragraph 848-20-00-1 as follows:

848-20-00-1 The following table identifies the changes made to this Subtopic.

Paragraph	Action	Accounting Standards Update	Date
848-20-05-1	Superseded	2020-04	03/12/2020
848-20-05-1	Added	2020-04	03/12/2020
848-20-15-1 through 15-11	Superseded	2020-04	03/12/2020
848-20-15-1 through 15-11	Added	2020-04	03/12/2020
848-20-35-1 through 35-15	Superseded	2020-04	03/12/2020
848-20-35-1 through 35-15	Added	2020-04	03/12/2020
848-20-55-1	Superseded	2020-04	03/12/2020
848-20-55-1	Added	2020-04	03/12/2020
848-20-55-2	Superseded	2020-04	03/12/2020
848-20-55-2	Added	2020-04	03/12/2020

10. Add paragraph 848-30-00-1 as follows:

848-30-00-1 The following table identifies the changes made to this Subtopic.

Paragraph	Action	Accounting Standards Update	Date
848-30-05-1	Superseded	2020-04	03/12/2020
848-30-05-1	Added	2020-04	03/12/2020
848-30-15-1	Superseded	2020-04	03/12/2020
848-30-15-1	Added	2020-04	03/12/2020
848-30-25-1 through 25-13	Superseded	2020-04	03/12/2020
848-30-25-1 through 25-13	Added	2020-04	03/12/2020

11. Add paragraph 848-40-00-1 as follows:

848-40-00-1 The following table identifies the changes made to this Subtopic.

Paragraph	Action	Accounting Standards Update	Date
848-40-05-1	Superseded	2020-04	03/12/2020
848-40-05-1	Added	2020-04	03/12/2020
848-40-15-1	Superseded	2020-04	03/12/2020
848-40-15-1	Added	2020-04	03/12/2020
848-40-25-1 through 25-9	Superseded	2020-04	03/12/2020
848-40-25-1 through 25-9	Added	2020-04	03/12/2020

12. Add paragraph 848-50-00-1 as follows:

848-50-00-1 The following table identifies the changes made to this Subtopic.

Paragraph	Action	Accounting Standards Update	Date
848-50-05-1	Superseded	2020-04	03/12/2020
848-50-05-1	Added	2020-04	03/12/2020
848-50-15-1	Superseded	2020-04	03/12/2020
848-50-15-1	Added	2020-04	03/12/2020
848-50-25-1 through 25-14	Superseded	2020-04	03/12/2020
848-50-25-1 through 25-14	Added	2020-04	03/12/2020
848-50-35-1 through 35-24	Superseded	2020-04	03/12/2020
848-50-35-1 through 35-24	Added	2020-04	03/12/2020

The amendments in this Update were adopted by the affirmative vote of four members of the Financial Accounting Standards Board. Ms. Botosan and Messrs. Buesser and Schroeder dissented.

Ms. Botosan and Messrs. Buesser and Schroeder support the objective of this Update to provide accounting relief—through a temporary option that permits an entity to bypass existing requirements—for assessing when a financial instrument subject to reference rate reform is modified. Given the large number and variety of

financial instruments affected, those requirements will likely prove burdensome for entities during an extended period of market-wide reference rate reform that necessitates a high volume of modifications to the underlying contracts. Nevertheless, Ms. Botosan and Messrs. Buesser and Schroeder dissent from the issuance of this Update because they believe it fails to achieve the objective of financial reporting, which is to provide decision-useful information to investors and other financial statement users.

Need for Quantitative Information

The basis for their dissent rests with the Board's decision to require only *qualitative* disclosures of the nature of and reason for electing the optional accounting relief. Ms. Botosan and Messrs. Buesser and Schroeder believe that those disclosures are unlikely to provide financial statement users with any decision-useful information. What is needed, but not required by the amendments in this Update, are *quantitative* disclosures about the portion of variable-rate financial instruments, by type, that are subject to modifications directly resulting from reference rate reform but that have not yet been modified. Such disclosures are needed regardless of whether the temporary accounting relief provided in this Update is elected.

Ms. Botosan and Messrs. Buesser and Schroeder acknowledge that the need for quantitative disclosures does not emanate from reference rate reform. In fact, they note that, well before the current reform efforts, investors have long voiced the need for better quantitative disclosures about interest rate risk exposures from financial instruments. U.S. entities alone hold, or are exposed to, trillions of dollars of financial instruments (including loans, debt securities, and derivatives) for which contractual payments are based on rates that fluctuate or vary over an instrument's life. Those variable-rate financial instruments are linked to a myriad of reference rates including the London Interbank Offered Rate (LIBOR). Quantification is needed because not all reference rates move in lockstep or are directly correlated with each other, and they fluctuate in different ways relative to the market. The decision usefulness of rate-exposure information is now even more important because investors will seek to understand the economic consequences of the modification of large volumes of variable-rate contracts as they transition to different reference rates.

The objective of quantitative disclosures would be to provide users with much-needed insights into an entity's exposure—at each period end during the transition period—to cash flow changes resulting from the market-driven replacement of certain reference rates. Entity-specific quantification of the exposure is needed because entities affected by reference rate reform are likely to experience a wide range of financial outcomes—both positive and negative—that could stretch over numerous quarters and years. Ms. Botosan and Messrs. Buesser and Schroeder are concerned that the lack of quantitative disclosure requirements in this Update will confound users' abilities to assess changing exposures and performance

during this uncertain transition period. For those reasons, they believe that quantification of an entity's exposure at each reporting period within the transition period is critical for users to understand.

Ideally, the quantitative disclosures envisioned by Ms. Botosan and Messrs. Buesser and Schroeder would be in the form of a period-to-period rollforward, quantifying the different sources of current-period changes in an entity's remaining contracts for which a new reference rate is needed. They also believe that an entity should provide the remaining expected durations of those financial instruments.

Terms of some contracts, commonly referred to as "fallback" protocols or provisions, specifically mandate when a change in reference rate is needed and what new rate should be used. Ms. Botosan and Messrs. Buesser and Schroeder would have required a further disaggregation between the portion of those variable-rate financial instruments with a contractually specified fallback rate and the portion for which no fallback rate is specified. Regardless of a contract's specific provisions, modifications resulting from reference rate reform will affect the amount or timing of real future cash flows, hence the need for quantitative disclosures during the transition period.

Additionally, Ms. Botosan objects to the Board's decision to limit the disclosure on the optional accounting relief afforded to hedge accounting transactions to the nature of the accounting relief elected and the reason for electing such relief. Financial statement users have expressed concern that such disclosure will be boilerplate in nature and have marginal informational value. Ms. Botosan agrees and is concerned that the limited disclosures required by the amendment, combined with the accounting flexibility afforded by this Update, will lessen users' ability to rely on financial reporting information during this period of market-wide transition. To help financial statement users gauge the extent to which an entity elects the accounting relief, Ms. Botosan would have required entities to augment existing quantitative disclosures about the volume of an entity's derivative activity to quantify the volume of activity effected by the application of optional accounting relief. Ms. Botosan also would have required disclosure of the amount of the noncash, nonrecurring change in a cumulative fair value hedge basis adjustment due to a change in the reference rate.

Cost-Benefit Assessment

A majority of the Board rejected the need to provide quantitative disclosures, in part, because of perceived costs. Ms. Botosan and Messrs. Buesser and Schroeder believe, however, that certain quantitative disclosures are justified on a cost-benefit basis. Their view is based on the fact that an entity is already required to provide quantitative disclosures about the volume of its derivatives activity, which could be augmented to quantify remaining contracts in need of a new reference rate. In addition, they understand that entities with material exposures

to reference-rate-based financial instruments are planning to track, or are already tracking, progress toward implementing any necessary modifications.

Ms. Botosan and Messrs. Buesser and Schroeder believe that any incremental costs of requiring the disclosure of data, already quantitatively tracked for purposes of operational decision making or communication with investors, would be minimal. However, instead of leveraging those already-incurred costs and efforts for the benefit of financial statement users, users will be forced to incur additional time and costs to search for alternative sources of information, which are limited at best.

Members of the Financial Accounting Standards Board:

Russell G. Golden, *Chairman*
James L. Kroeker, *Vice Chairman*
Christine A. Botosan
Gary R. Buesser
Susan M. Cospers
Marsha L. Hunt
R. Harold Schroeder

Background Information and Basis for Conclusions

Introduction

BC1. The following summarizes the Board's considerations in reaching the conclusions in this Update. It includes reasons for accepting certain approaches and rejecting others. Individual Board members gave greater weight to some factors than to others.

Background Information

BC2. In 2014, the Board began actively monitoring the reference rate reform initiative undertaken globally to identify suitable alternatives to unsecured market benchmarks based on interbank offered rates. At that time, the Federal Reserve Board and the Federal Reserve Bank of New York (Fed) convened the Alternative Reference Rates Committee (ARRC) to identify a suitable alternative to the U.S. Dollar London Interbank Offered Rate (LIBOR) and to create an adoption plan to facilitate the acceptance and use of one or more alternative reference rates. In 2017, the ARRC identified the Secured Overnight Financing Rate (SOFR) as its preferred alternative reference rate.

BC3. During the project that led to the issuance of Accounting Standards Update No. 2017-12, *Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities*, the Fed requested that the overnight index swap rate based on SOFR be considered eligible as a U.S. benchmark interest rate for purposes of applying hedge accounting under Topic 815. In December 2017, the Board added a project to its agenda to consider that request. The Fed began publishing the daily SOFR rate on April 3, 2018, and announced a transition plan for its integration into the financial markets.

BC4. In 2018, the Board issued Accounting Standards Update No. 2018-16, *Derivatives and Hedging (Topic 815): Inclusion of the Secured Overnight Financing Rate (SOFR) Overnight Index Swap (OIS) Rate as a Benchmark Interest Rate for Hedge Accounting Purposes*. The Board limited the scope of the amendments in Update 2018-16 to newly designated hedging relationships based on SOFR to expedite the issuance of that new guidance. However, during the course of that project, stakeholders communicated to the Board that the reference rate reform initiative was expected to affect the ability to retain hedge accounting under Topic 815 for hedging relationships and asked the Board to consider potential relief to allow hedge accounting to continue in that circumstance. In addition, stakeholders indicated that reference rate reform was expected to create potential operational challenges in applying other areas of GAAP related to

modifications of financial instruments. Because of those emerging issues, concurrently with the issuance of Update 2018-16, the Board added a project to its agenda to consider the need for potential accounting relief for hedging relationships and other areas of financial reporting beyond hedge accounting that may be affected by reference rate reform. The Board's objective for the project is to broadly consider changes to GAAP to facilitate the market-wide transition from LIBOR and other interbank offered rates (collectively referred to as IBORs).

BC5. The Board solicited feedback from preparers, auditors, and other stakeholders to identify the specific accounting issues in relation to the market-wide transition from IBORs. Stakeholder feedback indicated that one primary issue relates to the operational costs to preparers when assessing significant volumes of contract modifications under the guidance for accounting for contract modifications in accordance with various areas of GAAP. A second issue relates to the potential inability to retain hedge accounting for existing hedges due to anticipated changes to the critical terms of hedging relationships, which would require automatic dedesignation of a hedging relationship in accordance with current GAAP, as well as the potential inability to qualify for hedge accounting due to reference rate reform.

BC6. Addressing those issues presents several challenges from a standard-setting perspective, including determining the scope of contracts requiring relief, the nature of the appropriate relief from existing accounting requirements, and the timing of issuing guidance to coincide with the timing of contract amendments occurring in the marketplace.

BC7. Regarding the nature of contracts requiring relief from accounting requirements, a challenge of reference rate reform is the pervasiveness of expected modifications across various types of contracts, including derivatives, investments, debt instruments, and leases.

BC8. In terms of timing, the Board understands that both:

- a. The International Swaps and Derivatives Association (ISDA) is amending protocols for derivative financial instrument fallback language referencing certain rates.
- b. In the United States, that language is expected to be incorporated into ISDA protocols referencing LIBOR as soon as early 2020.

BC9. For cash instruments, the Board understands that the ARRC has developed fallback language for certain financial products. However, the Board also acknowledges that contract modifications (for cash instruments as well as over-the-counter derivatives) are a result of negotiation and agreement between the counterparties to the contract and, therefore, it is difficult to predict both the timing of certain contract modifications and the terms that may be amended as a result of reference rate reform. In undertaking this project, the Board determined that any relief related to applying existing accounting requirements would need to be effective at the earliest time that contract modifications are occurring in the

marketplace to achieve the cost-benefit objective of issuing any final guidance. Accordingly, the Board expedited the issuance of this Update with the objective of providing final guidance in time for use by market participants to apply the guidance as contracts are being modified.

BC10. Furthermore, after issuance of this guidance, the Board will continue to monitor developments in the marketplace about how contract modifications due to reference rate reform will be effectuated and is prepared to consider whether those future developments warrant changes to this guidance or additional guidance, as appropriate.

BC11. On September 5, 2019, the Board issued proposed Accounting Standards Update, *Reference Rate Reform (Topic 848): Facilitation of the Effects of Reference Rate Reform on Financial Reporting*, with comments due on October 7, 2019. The Board received 40 comment letters on that proposed Update. Overall, respondents supported the amendments in the proposed Update and said that the proposed amendments would ease the potential burden in accounting for reference rate reform. Some respondents made suggestions to clarify specific aspects of the proposed amendments, which are described below in the basis for conclusions section.

Benefits and Costs (or Cost Savings)

BC12. The objective of financial reporting is to provide information that is useful to present and potential investors, creditors, donors, and other capital market participants in making rational investment, credit, and similar resource allocation decisions. However, the benefits of providing information for that purpose should justify the related costs. Present and potential investors, creditors, donors, and other users of financial information benefit from improvements in financial reporting, while the costs to implement new guidance are borne primarily by present investors. The Board's assessment of the costs and benefits of issuing new guidance is unavoidably more qualitative than quantitative because there is no method to objectively measure the costs to implement new guidance or to quantify the value of improved information in financial statements.

BC13. The Board concluded that the amendments in this Update reduce or mitigate the costs and complexity of accounting for contract modifications and hedging relationships affected by reference rate reform by providing elective optional expedients and exceptions to existing accounting requirements. For contract modifications, hedging relationships, and other transactions affected by reference rate reform, the amendments provide temporary guidance that achieves the following:

- a. Simplifies accounting analyses under current GAAP for contract modifications
- b. Allows hedging relationships to continue without dedesignation upon a change in certain critical terms

- c. Allows a change in the designated benchmark interest rate to a different eligible benchmark interest rate in a fair value hedging relationship
- d. Suspends the assessment of certain qualifying conditions for fair value hedging relationships for which the shortcut method for assuming perfect hedge effectiveness is applied
- e. Simplifies or temporarily suspends the assessment of hedge effectiveness for cash flow hedging relationships.

BC14. Given the pervasiveness of IBOR-based contracts, the Board notes that those elective optional expedients and exceptions provide cost savings to a wide array of financial statement preparers. Furthermore, the amendments in this Update result in financial reporting that reflects the intended continuation of contracts and hedging relationships due to the replacement of a reference rate. Overall, the Board concluded that the expected benefits, including cost savings for financial statement preparers, justify any expected costs of adopting the amendments.

Basis for Conclusions

General Principles

BC15. The Board concluded that the amendments in this Update result in financial reporting that captures the economic substance of contract modifications occurring in the marketplace because of reference rate reform. That is, a qualifying modification should not be considered an event that requires contract remeasurement at the modification date or reassessment of a previous accounting determination. In contrast, the Board concluded that the application of existing guidance for changes to a hedging relationship and for assessing whether contract changes should be accounted for as a contract modification or as a contract extinguishment could be burdensome given the quantity of IBOR-based contracts and could result in financial reporting that is not reflective of an entity's business strategy or intent. Specifically, because reference rate changes relate to a market-wide reform initiative that is outside the control of an entity, thereby compelling an entity to make modifications to contracts or hedging strategies, the Board determined that the financial reporting outcomes of discontinuing such contracts (and treating the modified contract as an entirely new contract) and hedging relationships would not provide decision-useful information to users of financial statements. Therefore, the Board concluded that accounting relief should be broadly available to enable entities to continue accounting for affected contracts and hedging relationships through the period of market transition in a manner that would continue the previous accounting determinations for such arrangements before the effects of reference rate reform.

BC16. For contract modifications, current GAAP for loans and debt instruments broadly requires that an entity assess both qualitatively and quantitatively whether a modified contract substantially differs from the contract before the modification

to a degree that it is in substance a new contract rather than a continuation of an existing contract. The Board understands that loans and debt instruments that are modified solely to reflect the effects of reference rate reform may pass those tests if they are applied on an individual contract basis. However, stakeholders indicated that given the significant volume of contracts that are expected to be modified as a result of reference rate reform, applying those requirements on an individual contract basis would result in significant operational costs.

BC17. Other areas of GAAP, including Topic 840 or 842 on leases and Topic 815 on derivatives and hedging, require similar assessments of contract modifications or previous accounting determinations due to changes in terms. Given its view that financial reporting outcomes of discontinuing such contracts and hedging relationships would not necessarily provide decision-useful information to users of financial statements, the Board concluded that the expected benefit of applying existing accounting requirements for contract modifications on an individual contract basis likely will not justify the expected costs. Similarly, the Board determined that considering reference rate reform to be an event that requires reassessment of a previous accounting determination under GAAP on an individual contract or a transaction basis likely will not justify the expected costs. Therefore, the amendments in this Update provide various optional expedients and exceptions to applying certain accounting requirements to contracts, transactions, and hedging relationships affected by reference rate reform.

BC18. The Board concluded that because the amendments in this Update are intended to provide relief related to the accounting requirements in GAAP due to the effects of the market-wide transition away from IBORs, the relief provided by the amendments is temporary in its application in alignment with the expected market transition period.

Overall Scope of Reference Rate Reform Guidance

BC19. The amendments in this Update establish the overall scope of the guidance for contract modifications, hedging relationships, or other transactions that are eligible to apply optional expedients or exceptions to accounting requirements in GAAP.

BC20. The overall scope is that the contract must reference LIBOR or a reference rate that is expected to be discontinued as a result of reference rate reform. The Board decided to explicitly reference LIBOR in this criterion because it determined that the primary objective of the amendments in this Update is to facilitate the market-wide transition away from LIBOR as a consequence of the United Kingdom's Financial Conduct Authority announcing that it would no longer persuade, or compel, banks to submit to LIBOR as of the end of 2021. This applies to LIBOR in all jurisdictions and in all currencies.

BC21. However, the Board included within the scope guidance other reference rates that are expected to be discontinued because of reference rate reform and

observed that, in applying that provision, judgment may be required to identify those rates. The Board observed that certain reference rates (for example, the Singapore Dollar Swap Offer Rate) use an IBOR that is expected to be discontinued as an input into the calculation of the reference rate. The Board notes that contracts referencing interest rates that are computed using reference rates expected to be discontinued as an input also should be considered to meet the scope. In addition, the Board understands that for certain reference rates (for example, the Euro Interbank Offered Rate) there may be an effort to reform the production method of how the published reference rate is calculated, rather than discontinuing the publishing of the reference rate, which may be assessed by market participants to be a fundamental change in the reference rate such that in substance the previous reference rate is considered discontinued. The Board added that if such an assessment is made, those rates also should meet the scope guidance.

BC22. In developing the scope guidance, the Board considered providing a prescriptive list of reference rates that would qualify for optional expedients for contract modifications. The Board decided not to include such a list within the scope guidance on the basis that it would have required the Board to maintain and update that list on an ongoing basis as other reference rates undergo review. The Board understands that in addition to LIBOR, there are other rate reform initiatives that have recommended reducing reliance on certain other IBORs and other reference rates and that work is under way in multiple jurisdictions to transition away from those rates. The Board determined that it may be difficult to compile a complete list of all reference rates undergoing reform because some jurisdictions are still evaluating whether certain reference rates should be discontinued and that could affect its ability to provide relief in a timely manner.

BC23. The Board also considered restricting the replacement reference rate to one that is designated or endorsed by a regulator or private-public sector working group convened by the regulator. The Board received feedback from stakeholders that such a restriction may significantly limit the scope of the relief. There are various existing reference rates and potentially new reference rates that may replace the discontinued reference rates. The Board noted that it should be neutral on that matter and does not want to restrict the optional expedients in a manner that could influence the market-wide transition away from discontinued reference rates toward specific replacement rates. Therefore, the Board decided not to specify eligible replacement rates in the scope guidance.

Scope of Contract Modifications That Are Eligible for Accounting Relief

BC24. The amendments in this Update provide the scope of modifications to contracts that are eligible to apply optional expedients for the accounting requirements in GAAP to contract modifications. The scope is intended to distinguish those contract modifications occurring solely because of reference rate

reform from other contract modifications that occur in the ordinary course of business or for reasons unrelated to reference rate reform.

BC25. The Board decided that the scope of contract modifications that are eligible for the optional expedients should include only changes being made to the terms that include the direct replacement of a reference rate or the potential to replace a reference rate from one variable rate to another variable rate. For the purpose of the amendments in this Update, the Board determined that the terms that are permitted to be modified are those that affect or have the potential to affect the amount or timing of future cash flows of a financial instrument. The potential to affect the amount or timing of contractual cash flows includes terms such as fallback provisions in a contract that are triggered upon a contingent event (such as the discontinuance of the rate). In addition, contemporaneous changes to terms that do not affect or have the potential to affect the amount or timing of future cash flows are permitted by the amendments.

BC26. The Board observed that modifications of fallback protocols as a result of reference rate reform are captured within the scope of the amendments in this Update because they are modifications to the terms of a contract that have the potential to change the amount or timing of contractual cash flows. The Board recognizes that (a) changes to contract terms to change fallback protocols could occur before the discontinuance of the actual rate and (b) optional expedients could apply at that time. Given the varied types of contracts that could be affected by reference rate reform and the differing processes and timelines that may be followed to amend such contracts, the Board decided that the amendments should not provide restrictions on how far in advance of the anticipated reference rate discontinuance an entity may modify a contract to qualify for the optional expedients.

BC27. To qualify for the optional expedients for contract modifications, other terms being contemporaneously modified need to be *related* to the replacement of a reference rate because of reference rate reform. Modifications to terms that are considered *related* to the replacement of the reference rate are those made to effectuate the transition away from LIBOR or another reference rate expected to be discontinued and are not the result of a business decision that is separate from or in addition to changes to the terms of a contract to effect that transition. For example, the replacement of LIBOR with an overnight rate may require not only a change to the reference rate but also an additional spread adjustment and changes to the reset period. The amendments in this Update do not permit the optional expedients to be elected for contracts that are modified by changes to the terms of a contract that are *unrelated* to the replacement of the reference rate due to reference rate reform.

BC28. In deciding that entities should be required to consider whether modifications of terms *that affect or have the potential to affect the amount or timing of future cash flows are related to reference rate reform*, the Board was intentionally broad such that this criterion would capture any changes in terms that

could have a potential effect on future cash flows in certain circumstances. Such changes in terms that could affect the timing or amount of cash flows in future periods have economic consequences and that a business decision to change those terms that are driven by factors unrelated to reference rate reform should not be within the scope of this Update.

BC29. The amendments in this Update provide examples of changes to terms that are considered *related* to and *unrelated* to the replacement of the reference rate. The examples in paragraphs 848-20-15-5 through 15-6 are not an exhaustive list of all the changes to terms that may be considered *related* to and *unrelated* to the replacement of the reference rate. After considering stakeholder feedback, the Board decided to clarify that the list of examples of changes to terms that are related to reference rate reform include changes that are necessary to comply with laws or regulations or to align with market conventions for the replacement rate. The Board decided to make this change to acknowledge that there remains uncertainty about how the market-wide transition will be effectuated across different types of contracts affected by reference rate reform. Because market conventions will likely evolve over time, the Board wanted to provide flexibility in the guidance to accommodate those emerging market conventions.

BC30. A change from a variable rate to a stated fixed rate is not eligible for application of the optional expedients for contract modifications. The Board made that decision because the change from a variable-rate exposure to a negotiated stated fixed rate in a loan, debt instrument, or over-the-counter derivative could include components that reflect a business decision that is separate from or in addition to changes to the terms of a contract to effect the transition for reference rate reform. However, the Board does not intend to exclude modifications of the reference rate from applying the optional expedients if a fixed rate is predetermined on the basis of the most recent reset of a variable rate affected by reference rate reform.

BC31. Changes to fallback terms that are consistent with fallback terms developed by a regulator or a private-sector working group convened by a regulator (for example, the ARRC or ISDA) are presumed to be related to reference rate reform. This would include incorporating fallback terms that are qualitatively assessed to be substantially similar to the fallback terms developed by a regulator or a private-sector working group convened by a regulator. The fallback terms developed by those groups are generally developed after consulting with a wide range of market participants and considering stakeholder feedback. The fallback terms developed by those groups also contemplated industry-accepted rates in the related market or other market conventions.

BC32. If the revised terms are not consistent with fallback terms developed by a regulator or by a private-sector working group convened by a regulator, then an entity should assess whether those terms include, or have the potential to include, any changes unrelated to reference rate reform. If such revised fallback terms include, or have the potential to include, a change that is unrelated to reference

rate reform, the entity must disregard that change in the terms for the purposes of applying the relief if it is considered not probable of occurring. For example, if the replacement rate included a predefined sequence and the last step in that sequence is a rate to be negotiated and agreed upon at a future date, it is possible that a stated fixed rate could be selected at that future date (absent any terms or provisions to the contrary). The entity may apply the amendments in this Update if that last term in the predefined sequence of replacement methods is not probable of being the actual replacement rate method when the fallback terms are triggered and in effect.

BC33. In the case of a loan, some examples of changes in terms that generally would be considered *unrelated* to the replacement of a reference rate are changes in the maturity date and changes in the loan amount. The Board considers such changes in terms to be unrelated to reference rate reform because they would generally require a new business decision by a lender. For the same reason, the Board considers a concession granted by a lender to a borrower for the purposes of recovering its investment to be unrelated to reference rate reform, and, therefore, the amendments in this Update provide no optional expedient to the guidance in Subtopic 310-40, Receivables—Troubled Debt Restructurings by Creditors. Similarly, for a lease, the addition or removal of a right-of-use lease asset or change to the lease term involves a separate business decision, and, therefore, the Board considers those changes in terms to be unrelated to reference rate reform.

BC34. The Board chose to include an in-the-money cap or floor in the list of examples of changes in terms that are considered *unrelated* to a change in a reference rate because there could be some immediate transfer of value associated with that feature that is unrelated to reference rate reform. However, the Board notes that the addition of an out-of-the-money cap or floor should be considered *related* to a change in a reference rate because entities may be uncertain about the level of volatility associated with a new reference rate for which there is no history and may want protection from that exposure.

BC35. The Board also chose to include a change in the counterparty in the list of examples of changes in terms that are considered *unrelated* to a change in a reference rate because a change in the counterparty is a fundamental change to a contract and in some cases could change the risk profile of the contract (for example, changing the debtor specified in a borrowing agreement). After considering stakeholder feedback, the Board decided to clarify that it did not intend to change existing GAAP in relation to a change in the counterparty of a derivative designated in a hedging relationship and that such a change in the counterparty is not considered to be a change in the critical terms of the hedging relationship or a termination of the derivative contract.

BC36. The Board recognizes that there may be modifications to terms of a contract or an arrangement made concurrently with modifications due to reference rate reform that are administrative in nature and that do not affect or have the

potential to affect the amount or timing of future cash flows. The amendments in this Update allow changes to those terms to be made without having to assess whether such changes are related to reference rate reform.

BC37. In place of a principle with examples, the Board considered creating a prescriptive list of terms that would be eligible or ineligible for the optional practical expedients in this Update. The Board observed that a prescriptive list would be more straightforward to apply and would reduce implementation questions, thereby facilitating the market-wide transition by minimizing accounting analysis and judgments. However, on the basis of stakeholder feedback, the Board determined that because of uncertainty about how the market-wide transition would be effectuated across the various types of contracts affected by reference rate reform, it would be difficult to identify a sufficiently complete list of terms that may be changed in the time frame necessary for accounting relief to be available to entities as the market transition occurs. The Board therefore determined that a prescriptive list results in the optional expedients being more restrictive than otherwise intended.

Optional Expedients for Accounting for Contract Modifications

BC38. The amendments in this Update result in qualifying contract modifications being considered a continuation of the existing contract rather than an extinguishment of the existing contract and the establishment of a new contract. Similarly, the amendments result in a contract modification to which the optional expedient is being applied not being considered an event that requires reassessment of a previous accounting determination.

BC39. The Board determined that the qualitative criteria in the amendments in this Update are less operationally burdensome than the application of existing modification accounting guidance for a high volume of contract modifications. If a contract modification does not meet the criteria to apply the optional expedient, the contract modification should continue to be assessed using the guidance in the relevant Topic applicable to that contract.

BC40. The amendments in this Update provide specific optional expedients for accounting for contract modifications within the scope of Topic 310 on receivables, Topic 470 on debt, and Topic 840 or 842 on leases. On the basis of stakeholder feedback, the Board determined that the most significant number of contract modifications expected to be made for reference rate reform would otherwise be required to be evaluated in accordance with the accounting guidance in those Topics. Therefore, the Board decided to tailor the amendments to those areas to provide explicit guidance on practical expedients that are easily understandable in the context of the requirements of each of those Topics. The optional expedients for Topics 310 and 470 result in applying the provisions of those Topics related to the accounting for a continuation of the original contract rather than an extinguishment of the original contract and the issuance of a new contract.

BC41. The amendments in this Update allow for contract modifications that would otherwise be assessed under the contract modification guidance in Topic 840 or 842 to be accounted for as if no lease modification occurred. For lessees, this results in no reassessment of the lease classification and no remeasurement of the lease liability or the right-of-use asset. For lessors, this similarly results in no reassessment of the lease classification or remeasurement of any lease asset or liability.

BC42. In deciding to provide an optional expedient, the Board determined that the expected costs to preparers of following current GAAP for lease modifications outweigh the potential benefits to users. In addition, the expected benefits of what effectively would be a gross-up to the balance sheet (that is, because the change in the lease liability for changes in the reference rate would result in a corresponding change to the right-of-use asset) do not justify the expected costs to preparers of recording the gross-up. The Board noted that the total lease-related expenses recognized in profit or loss by a lessee would be the same for operating leases and substantially the same for finance leases, regardless of whether the lessee remeasures the lease liability for changes to the rate. The Board further concluded that users are able to reasonably assess the effect of future rent increases dependent upon the replacement rate on the basis of the disclosures provided by Topic 842 on (a) variable lease expense each period and (b) the terms and conditions of the variable lease payment arrangement.

BC43. Under the amendments in this Update, contract modifications that apply the optional expedient are not subject to an embedded derivative analysis under Subtopic 815-15. An embedded derivative in which the only underlying is an interest rate that alters net interest payments that otherwise would be paid or received on an interest-bearing host contract is generally considered to be clearly and closely related to the host contract unless it meets either of the conditions in paragraph 815-15-25-26(a) and (b). To determine the existence of those conditions, a reporting entity should perform an embedded derivative analysis at the date the hybrid instrument is acquired (or incurred) either at issuance of the hybrid instrument or upon acquisition in the secondary market. The Board concluded that an entity's conclusions before the modification of a hybrid instrument on whether to bifurcate the embedded derivative from the host contract are maintained if the hybrid instrument meets the criteria to apply the practical expedient. The Board concluded that clarifying that no embedded derivative reassessment is required for the purposes of this guidance reduces expected costs to preparers but does not reduce the usefulness of financial reporting.

BC44. The Board acknowledged that there may be contract modifications due to reference rate reform that would not be accounted for under Topics 310, 470, 840, and 842 and Subtopic 815-15. Therefore, the Board decided that the amendments in this Update should include a principle that may be applied to determine whether contract modifications accounted for in accordance with other relevant Topics or Industry Subtopics are eligible for an optional expedient to the accounting requirements of other relevant Topics or Industry Subtopics. The Board decided to

provide this principle because stakeholder feedback indicated that entities may encounter issues other than those for which explicit relief is provided when transitioning away from IBORs. The Board expected that these issues would be less pervasive than those for which explicit relief is provided and decided that a principle should provide flexible relief that generally guides entities to account for in-scope contract modifications as events that do not require contract remeasurement at the modification date or reassessment of a previous accounting determination. Such accounting is consistent with the intent of the optional expedients explicitly provided in the amendments.

BC45. The amendments in this Update allow an entity to elect the optional expedients for contract modifications on a Topic or Industry Subtopic basis. For example, if an entity elects the lease modification expedient, it must apply the optional expedient to all its lease contract modifications arising from reference rate reform that would otherwise be accounted for in accordance with Topic 840 or 842. The Board considered but rejected an alternative that would have mandatorily required an entity to apply the optional expedients for contract modifications arising from reference rate reform across all Topics because a mandatory requirement would preclude an entity from applying current GAAP, which in certain circumstances may be operationally less burdensome for entities. The Board also considered but rejected allowing an application on a contract-by-contract basis because the Board wanted to preclude an entity from selectively applying the optional expedients on the basis of the effect to earnings.

Hedge Accounting

BC46. The amendments in this Update provide several exceptions and optional expedients for applying hedge accounting guidance. Stakeholders requested the following relief to address potential challenges for applying hedge accounting for hedging relationships expected to be affected by reference rate reform:

- a. For any hedging relationship, upon a change to the critical terms of the hedging relationship, allow an entity to continue hedge accounting rather than dedesignate the hedging relationship.
- b. For any hedging relationship, upon a change to the terms of the designated hedging instrument, allow an entity to change its systematic and rational method used to recognize the excluded component into earnings and adjust the fair value of the excluded component through earnings.
- c. For fair value hedges, allow an entity to change the designated hedged benchmark interest rate and continue fair value hedge accounting.
- d. For cash flow hedges, adjust the guidance for assessment of hedge effectiveness to allow an entity to apply cash flow hedge accounting.

Exceptions to Accounting Requirements for a Change in Critical Terms of a Hedging Relationship

BC47. Generally, under current GAAP, hedge accounting must be discontinued if critical terms of a hedging relationship are modified. If an entity wishes to continue to apply hedge accounting, it may do so by designating a new hedging relationship. As a result of amendments to Topic 815 in Update 2017-12, current GAAP includes a narrow exception to this requirement that allows a change to the hedged risk in a cash flow hedge of a forecasted transaction without dedesignation of the hedging relationship if the hedging instrument continues to be highly effective at offsetting the revised hedged risk. That guidance has limited applicability and does not apply to a change to the terms of a hedging instrument or a change to any terms of fair value hedging relationships or net investment hedging relationships.

BC48. Stakeholders requested that entities be permitted to continue applying hedge accounting for hedging relationships for which a hedging instrument, a hedged item, or a forecasted transaction is modified because of reference rate reform. Stakeholders indicated that the following changes are expected to occur as a result of reference rate reform:

- a. The reference interest rate (for example, changing from LIBOR to another variable rate)
- b. The payment terms (for example, the addition of a spread adjustment)
- c. Reset period (for example, changing from a forward-looking term rate that resets quarterly to an overnight rate that resets daily).

BC49. In the ordinary course of business, modifications of contractual terms are initiated by two or more counterparties that are acting in their respective interests to make changes to the terms. As a result of reference rate reform, the counterparties are being compelled to amend the contractual terms, including those designated as hedging instruments, or hedged items, or forecasted transactions, because the reference rate is discontinued. The Board determined that the financial reporting outcome of forcing a discontinuance of hedge accounting does not provide decision-useful information to users of financial statements, particularly because entities will, in most circumstances, continue to use the modified derivative for the same risk management purposes as the contract before the modification. The Board concluded that a dedesignation of a hedging relationship due to a change in critical terms and potential designation of a new hedging relationship due to the discontinuation of a rate outside the entity's control without an accompanying change in a risk management objective will result in financial reporting that is not informative to users.

BC50. Therefore, the amendments in this Update provide an exception to the guidance on changes in the critical terms of a hedging relationship to allow the hedging relationship to continue without dedesignation if the changes to the contractual terms of the hedging instrument, the hedged item, or the forecasted

transaction meet the criteria for contractual modifications related to the replacement of the reference rate. The Board decided that the amendments on the optional expedient for changes in critical terms apply to fair value hedges, cash flow hedges, and net investment hedges because any type of hedging relationship could be affected by reference rate reform.

BC51. The amendments in this Update provide an exception to the guidance on changes in the critical terms of a hedging relationship to allow a change to the method of assessing hedge effectiveness documented at hedge inception without requiring dedesignation of the hedging relationship. The optional expedient is eligible if the critical terms of the hedging instrument or the hedged item or hedged transaction references LIBOR or another rate that is expected to be discontinued and the new method designated for assessing hedge effectiveness is an optional expedient in the amendments. The Board determined that this exception should be allowed to enable an entity to continue hedge accounting for hedging relationships using the optional expedients for fair value hedges and cash flow hedges without hedge dedesignation.

BC52. On the basis of stakeholder feedback, the Board understands that it may be necessary to rebalance the hedge ratio for duration-weighted fair value hedges that transition to a different eligible replacement benchmark interest rate to adjust for the changes in the hedged risk and instrument terms. Similarly, the Board understands that on the basis of stakeholder feedback there are a number of potential methods that an entity may use to manage its transition of a hedging relationship from a discontinued reference rate to a replacement rate, such as adding a new interest rate basis swap to an existing interest rate swap designated as the hedging instrument in a cash flow hedge. The Board agreed that it may be necessary for hedging relationships to be adjusted because of changes in the terms of hedging instruments and hedged items resulting from reference rate reform.

BC53. The amendments in this Update provide exceptions to the guidance on changes in critical terms that allows entities to rebalance hedging relationships as needed. The amendments allow an entity to change either the proportion of a designated hedging instrument or the proportion of the hedged item (or both) designated in a fair value hedge or a cash flow hedge to apply the optional expedients for hedge accounting. Similarly, the amendments allow an entity to change the designated hedging instrument to combine two or more derivative instruments in a hedging relationship eligible to apply the optional expedients for hedge accounting.

Optional Expedient for Excluded Components

BC54. In feedback on the proposed Update, some stakeholders asked that the Board consider providing optional relief to allow a change to the systematic and rational method used to recognize excluded components into earnings for hedging relationships affected by reference rate reform. When a hedging instrument's

contractual terms change because of reference rate reform, that change may affect the value of the component excluded from the assessment of hedge effectiveness. To allow the excluded component to continue to be recognized into earnings on a systematic and rational basis, the Board decided to provide optional relief to amend the method and continue hedge accounting. If an entity does not apply the optional relief, the entity's current systematic and rational method may result in a required cumulative catch-up at the end of the hedging relationship to ensure that no excluded components remain in accumulated other comprehensive income at the end of the hedging relationship.

BC55. The amendments in this Update provide an optional expedient to change the systematic and rational method used to recognize the components excluded from the assessment of hedge effectiveness into earnings if the derivative designated as the hedging instrument meets certain criteria. In addition, if the changes to the contractual terms of the designated derivative cause a change in the fair value of the excluded component, an entity may elect to recognize the change in fair value of the excluded component into earnings in the same income statement line item that is used to present the earnings effect of the hedged item.

Optional Expedient for Fair Value Hedges: Change in the Designated Benchmark Interest Rate

BC56. The amendments in this Update allow an optional expedient to change the designated benchmark interest rate in a fair value hedge if the derivative designated as the hedging instrument references LIBOR or another rate that is expected to be discontinued as a result of reference rate reform and if certain criteria are met. The Board decided to provide this optional expedient for circumstances in which a hedging instrument has a change to its reference rate that could affect the effectiveness of the hedging relationship for the remainder of its term. For example, if a LIBOR swap was designated as the hedging instrument in a fair value hedge and an entity selected the LIBOR swap rate as its designated hedged interest rate risk, the change in fair value of the swap and the change in fair value of the hedged item based on a LIBOR swap rate would diverge if the swap's variable rate changes to another rate, such as SOFR.

BC57. The Board decided that it is appropriate to allow an entity to bring such hedges into realignment by allowing a change to the benchmark interest rate to a different eligible benchmark interest rate, assuming that the hedging instrument is expected to be highly effective in offsetting changes in fair value attributable to the revised hedged risk. The Board determined that the financial reporting outcome of forcing an entity to discontinue fair value hedge accounting because of changes in the terms of the hedging instrument will not result in decision-useful information to users of financial statements. The Board also determined that dedesignation of a fair value hedge and potential designation of a new hedging relationship without an accompanying change in a risk management objective will result in financial reporting that could be uninformative to users.

BC58. There is no guidance on how to calculate the change in fair value attributable to a change from one benchmark interest rate to another eligible benchmark interest rate. Stakeholders provided feedback on multiple possible methods. Some of those methods would maintain the cumulative fair value hedge basis adjustment to be carried forward by adjusting the hedged benchmark cash flows or by adjusting the rate used to discount the original hedged benchmark cash flows to include a spread adjustment. Other methods would adjust the cumulative fair value hedge basis adjustment to be carried forward as a result of changing the hedged benchmark cash flows and the subsequent discount rate. The Board decided that the method selected needed to be reasonable and that an entity should be required to use a similar method for similar hedges. The Board considered but rejected prescribing a specific method because different methods may be reasonable for different entities depending on their facts and circumstances.

BC59. The amendments in this Update require that the change in fair value of a hedged item attributable to a change from one benchmark interest rate to another eligible benchmark interest rate be presented in the same line item that is used to present the earnings effect of the hedged item if the entity applies an approach that adjusts the hedged item's cumulative fair value hedge basis adjustment. The Board determined that this is consistent with its basis for conclusions in Update 2017-12 that if an entity designates a hedging instrument, all effects of that hedging instrument should be presented together with the earnings effect of the hedged item.

BC60. The amendments in this Update require that an entity recognize in current earnings any change in fair value attributable to a change in an eligible benchmark interest rate. The Board considered allowing an adjustment to opening retained earnings but rejected that alternative on the basis that allowing a retained earnings adjustment is inconsistent with accounting for the modified contract as a continuation of the original contract. In addition, changes to the critical terms of hedging instruments in fair value hedges that would drive a change in the designated benchmark interest rate may occur across different reporting periods, particularly if an entity has derivatives designated as fair value hedges with various reference rates that may be replaced at different times. The Board notes that allowing retained earnings adjustments across multiple reporting periods could be confusing to users.

BC61. The Board also considered allowing the adjustment of the cumulative fair value hedge basis adjustment (if the entity applies an approach that adjusts the hedged item's cumulative fair value hedge basis adjustment) to be recognized over time in the same manner as other components of the carrying amount of the hedged asset or liability. In feedback received on the proposed Update, some stakeholders indicated that applying an approach that adjusts the cumulative fair value hedge basis adjustment and recording an offsetting entry to the carrying amount of the hedged asset or liability essentially maintain the hedged asset's or the hedged liability's cumulative basis adjustment immediately before the change

in the designated benchmark interest rate, which is already provided for in a separate election. Some stakeholders also noted that recording an offsetting entry to the carrying amount of the hedged asset or liability is inconsistent with current GAAP recognition requirements for basis adjustments arising from fair value hedge accounting in Subtopic 815-25. On the basis of the feedback received, the Board decided to remove that option in this Update.

Optional Expedient for Fair Value Hedges: Shortcut Method

BC62. Current GAAP allows an entity to apply the shortcut method for assessing hedge effectiveness of fair value hedges if certain conditions are met. For fair value hedges applying the shortcut method, the amendments in this Update provide an optional expedient to allow an entity to continue to use the shortcut method if the reference rate in the hedging instrument is replaced by another eligible benchmark interest rate. For an entity that qualifies for and elects to use the optional expedient, the entity would continue to use the shortcut method and recognize the change in fair value of the hedging instrument as a fair value hedge basis adjustment of the hedged asset or hedged liability.

BC63. In the Board's view, an entity that applies the shortcut method should not be penalized because the entity is compelled to change the terms of a derivative because of reference rate reform. While a change in a derivative's reference rate does not meet the condition for the shortcut method of accounting because the settlements of the swap would not be computed in the same manner in all periods, the Board decided that the condition may be disregarded in this circumstance and that an entity could elect to continue to apply the shortcut method for the remainder of the hedging relationship.

Eligibility of Cash Flow Hedges: Probability of the Hedged Forecasted Transaction and Change in the Designated Hedged Interest Rate Risk

BC64. For a cash flow hedge to qualify for hedge accounting in accordance with GAAP, an entity must assert that the hedged forecasted transaction is probable of occurring. A change in the probability of the forecasted transaction may require that an entity discontinue hedge accounting and may affect the timing of recognizing in current earnings amounts deferred in accumulated other comprehensive income.

BC65. The amendments in this Update clarify that if the designated hedged risk in a hedged forecasted transaction references LIBOR or another rate that is expected to be discontinued because of reference rate reform, an entity may assert that the hedged forecasted transaction remains probable of occurring if the reference rate is expected to be replaced with another rate. However, the amendments require that an entity assess whether the underlying hedged

forecasted transaction (that is, the future interest receipts of a financial asset or the future interest payments of a financial liability or the forecasted issuance or purchase of a debt instrument) remains probable of occurring. For example, if the hedged forecasted transaction is the future interest payments on specific debt and the entity prepays that identified debt and does not replace the debt, the hedged forecasted transaction would be probable of not occurring.

BC66. In addition, the amendments in this Update clarify that a change to the designated hedged interest rate risk (for example, a change from LIBOR to another variable rate) does not require a dedesignation of a cash flow hedge of a forecasted transaction if the hedge is expected to be highly effective, which may be asserted if an entity applies an optional expedient for cash flow hedges that is in the amendments. The Board adds that it is important to clarify that in applying the amendments, an entity is not required to dedesignate a cash flow hedge for a technical reason related to the designation and documentation of the hedge. That is, the Board wanted to clarify that both:

- a. The guidance in Topic 815 on a permissible change in the hedged risk in a cash flow hedge of a forecasted transaction applies in the circumstance of reference rate reform.
- b. An entity is not required to discontinue hedge accounting if it can assert that the underlying cash flows remain probable of occurring regardless of how the hedged risk and the hedged forecasted transaction are documented.

Optional Expedients for Cash Flow Hedges: Application of Cash Flow Hedge Accounting

BC67. For a cash flow hedge to qualify for hedge accounting in accordance with current GAAP, an entity must assess that the hedging instrument is expected and is actually shown to be highly effective in offsetting the changes in cash flows due to changes in the hedged risk during the period that the hedge is designated. An entity is required to perform hedge effectiveness assessments at hedge inception and on an ongoing basis to continue to qualify for hedge accounting. Current GAAP describes various methods for assessing hedge effectiveness for the initial assessment and subsequent assessments. Certain methods permit an entity to assume that the hedge is perfectly effective if certain qualifying conditions are met.

BC68. Similar to its reasoning for fair value hedges, the Board concluded that existing cash flow hedges that are affected by reference rate reform should be permitted to continue without dedesignation because those hedging relationships continue to reflect an entity's intended risk management strategy. The Board also concluded that new cash flow hedges that are affected by reference rate reform because either the hedging instrument or the hedged item references LIBOR or another rate expected to be discontinued should be permitted to qualify for hedge

accounting because those hedging strategies also would reflect an entity's intended risk management strategy.

BC69. The Board concluded that without the optional expedients in the amendments in this Update, there would be an increased level of complexity in performing hedge effectiveness assessments for cash flow hedges that are expected to be affected by reference rate reform. For example, in a cash flow hedge that qualifies for hedge accounting, the reference rate in the hedging instrument and the reference rate in the hedged forecasted transaction may be replaced at different times during the hedging relationship. An entity would need to estimate the expected timing of when the hedging instrument and the hedged forecasted transaction will transition to the replacement rates—including for hedges of groups of forecasted transactions in which individual forecasted transactions in the group may have different transition timing—and incorporate those timing estimates into the hedge effectiveness assessment.

BC70. In addition, without the amendments in this Update, there may be periods of time during the transition to replacement rates in which a cash flow hedge would not be considered highly effective for the purposes of Subtopic 815-20 because of the basis differences between the reference rates in the hedging instrument and the reference rates in the hedged forecasted transaction. The Board determined that the discontinuance of hedge accounting in those cases will not provide decision-useful information to users of financial statements.

BC71. In providing the optional expedients for cash flow hedges affected by reference rate reform, the Board placed importance on several other provisions in hedge accounting guidance as a counterbalance to the flexibility that is provided by those optional expedient methods. First, the amendments in this Update rely on the guidance in Subtopic 815-20 that was added in Update 2017-12 to remove the concept of separately measuring and recognizing hedge ineffectiveness. Accordingly, if a hedging relationship qualifies for cash flow hedge accounting, all changes in the fair value of the derivative designated as the hedging instrument are deferred into accumulated other comprehensive income and recognized in earnings when the hedged forecasted transaction affects earnings.

BC72. Second, the amendments in Update 2017-12 added presentation guidance for hedging relationships such that the effects of the hedging instrument are required to be recorded in the same line item as the earnings effect of the hedged item. The Board considers that presentation guidance to be a safeguard for the application of the optional expedients for cash flow hedges. That is, the Board acknowledges that cash flow hedges for which an entity elects the optional expedients may not satisfy the requirement in which the hedging instrument is expected and actually shown to be highly effective in offsetting changes in cash flows due to changes in the hedged risk during the period that the hedge is designated. The Board understands that hedging relationships that are not highly effective may qualify for hedge accounting as an outcome of providing relief provisions that enable an entity to continue to reflect its intended risk management

strategies in the financial statements for the period that reference rates are expected to transition to replacement rates.

BC73. Third, the Board observes that the guidance can be applied for a limited time, and it does not apply to hedging relationships entered into or evaluated after December 31, 2022. An entity is required to revert to the cash flow hedge accounting requirements in Subtopics 815-20 and 815-30 for any cash flow hedging relationships that would remain in place.

Subsequent Hedge Effectiveness Assessments for Cash Flow Hedges

BC74. For cash flow hedges, if either the hedged forecasted transaction or the hedging instrument references LIBOR or another rate expected to be discontinued because of reference rate reform, the amendments in this Update allow an entity to effectively suspend subsequent hedge effectiveness assessments as long as the entity determines qualitatively that the following conditions continue to be met each period:

- a. The hedged forecasted transaction or the hedging instrument references an eligible rate.
- b. There have been no changes to the terms of the hedging instrument or the forecasted transaction other than those related to reference rate reform.
- c. An entity considers the likelihood of the counterparty's compliance with the contractual terms of the hedging derivative that require the counterparty to make payments to the entity.

BC75. The Board decided that an entity may switch to the shortcut method to assess subsequent hedge effectiveness if it elects to apply that optional expedient for the cash flow hedge. However, the Board decided not to provide similar relief for fair value hedges. The Board reasoned that under the fair value shortcut method, a change in fair value of a swap designated as the hedging instrument would be used as a proxy for the change in fair value of the hedged item, and if the variable rate on the swap did not match the designated benchmark interest rate, there would be a true fair value difference. However, because all changes in a swap designated as a hedging instrument in a cash flow hedge are recorded in other comprehensive income, there is no difference between the reporting effect of a cash flow shortcut method and the reporting effect of a quantitative method if the hedge is highly effective.

BC76. An entity also may elect optional expedients that allow it to adjust the methods for assessing subsequent hedge effectiveness in current GAAP so that the entity could remove from its assessment the differences between the hedged forecasted transaction and the hedging instrument that are due to the changes in the reference rates and the timing of when the rates reset. The Board determined that an entity should have the option to adjust existing quantitative methods of

assessing subsequent hedge effectiveness rather than assuming perfect hedge effectiveness or qualitatively assessing certain conditions each period, which introduces a new process for hedging relationships affected by reference rate reform. The Board anticipates that some entities may want to adjust existing quantitative methods and processes for subsequently assessing hedge effectiveness for hedging relationships that extend beyond the December 31, 2022 expiration of the optional expedients and are required to revert to existing GAAP.

BC77. The Board observes that cash flow hedges that have already qualified for hedge accounting by (at a minimum) satisfying an initial hedge effectiveness assessment in accordance with the requirements of Subtopics 815-20 and 815-30 have already passed a high hurdle to apply hedge accounting. Therefore, in the Board's view, it is unlikely that the hedging relationship will significantly deviate from the results of those previous hedge effectiveness assessments and that a change in the terms as a result of reference rate reform will not be expected to introduce excessive levels of hedge ineffectiveness. The Board adds that for the periods of an expected or actual mismatch in reference rates between the hedging instrument and the hedged item, an entity should be able to continue to portray in its financial statements the continuation of its original risk management strategy, especially considering that any mismatch will be reflected in earnings.

BC78. For similar reasons, the Board decided that an entity may disregard the shared risk exposure guidance in Subtopic 815-20 for a group of individual forecasted transactions in a cash flow hedge if a single forecasted transaction in the hedged group of forecasted transactions references LIBOR or another rate that is expected to be discontinued. However, an entity is not allowed to group interest receipts with interest expenses or forecasted purchases (including debt issuances) with forecasted sales.

BC79. The amendments in this Update require that an entity discontinue its use of the optional expedients for assessing hedge effectiveness at the earlier of any of the following events:

- a. Neither the hedged item nor the hedging instrument references LIBOR or another rate that is expected to be discontinued.
- b. The guidance in Topic 848 is superseded.
- c. The entity elects to cease to apply the guidance in Topic 848.

BC80. On the basis of stakeholder feedback, the Board notes that those provisions for discontinuing the application of optional expedients are sufficient to allow hedging relationships to continue until the effects of reference rate reform are resolved. Upon one of those events occurring, an entity may change the method of assessing subsequent hedge effectiveness. The Board decided that an entity should be allowed to continue hedge accounting without disruption by changing from an optional expedient method to a method of assessing hedge effectiveness in accordance with Subtopics 815-20 and 815-30 without dedesignation of the hedge.

Initial Hedge Effectiveness Assessments for Cash Flow Hedges

BC81. The amendments in this Update allow an entity to apply optional expedients for the purpose of assessing initial hedge effectiveness for cash flow hedges if either the hedged forecasted transaction or the hedging instrument references LIBOR or another rate that is expected to be discontinued as a result of reference rate reform. The amendments allow cash flow hedges to apply the same optional expedient methods for the initial assessment of hedge effectiveness as for subsequent assessments of hedge effectiveness, with the exception of the optional expedient for a qualitative method that may only be applied for subsequent assessments of hedge effectiveness.

BC82. The Board decided that extending relief to new cash flow hedges affected by reference rate reform is appropriate during the period of transition to replacement reference rates because an entity may enter into cash flow hedging relationships during that period that could have an immediate mismatch in rates. Because of the uncertainty on how reference rate reform will be effectuated in the respective markets, including across different derivatives and other financial instrument products, the immediate mismatch may be because of market-wide developments outside the control of an entity's risk management activities, such as the lack of liquidity of certain derivatives to match the underlying reference rate index of a replacement reference rate. The Board determined that the lack of hedge accounting should not hinder the development of those new markets. The Board also notes that given the uncertainty about the timing of the transition of different instruments and products, it is unclear whether an entity would be able to obtain derivatives referencing desired rates.

BC83. The amendments in this Update do not include incremental criteria for determining whether an optional expedient for new cash flow hedges may be elected. The Board notes that it is challenging to create criteria that do not diminish the objective of providing relief for application of the hedge accounting requirements during the period of market transition to replacement reference rates. The Board considered an approach that would limit the reference rates that could be incorporated into a hedging relationship that qualifies for optional expedients. However, as noted in paragraph BC23, in the Board's view, the amendments should remain neutral on eligible replacement rates, which creates a challenge for introducing such a limitation.

BC84. As an alternative, the Board considered requiring an initial assessment of hedge effectiveness using an existing method in Subtopics 815-20 and 815-30. However, the Board recognizes that when the reference rate of the hedging instrument and the hedged item differ at the inception of the hedging relationship, the requirement of an expectation that the hedge will be highly effective may not be satisfied. The Board observed that this is no different in the case of an initial assessment for a new hedge as compared with a subsequent assessment for an existing hedge.

BC85. As noted in paragraph BC70, the Board acknowledges that cash flow hedges for which an entity elects the optional expedients for initial assessment of hedge effectiveness may not be highly effective during the period that the hedge is designated. The Board accepts that as an outcome of providing temporary relief provisions enabling an entity to continue to reflect its intended risk management strategies in the financial statements during the transition period.

BC86. The Board noted that it was important to provide entities with the option to apply the expedients for initial assessment of hedge effectiveness to new cash flow hedges using either a method that assumes perfect effectiveness or quantitative methods to enable entities of all levels of sophistication to take advantage of the relief. The Board observed that without this option, an entity that applies only the simplified method would be required to use a “long haul” method to apply the relief when it potentially would have not applied that method in practice before.

BC87. The Board also considered developing criteria for cash flow hedges similar to the criteria for contract modifications that would have required an assessment of the terms of hedging instruments and hedged items that would qualify for the optional expedients. That would be similar to the requirement to apply the qualifying criteria for contract modifications to derivatives designated as hedging instruments in cash flow hedges when electing the optional expedient related to a change in critical terms. The Board ultimately decided against that approach for several reasons.

BC88. First, the Board expects that an entity employs derivatives as hedging instruments to execute a particular risk management strategy, and there are natural limitations, including internal risk management guidelines, to incorporating speculative features into hedging relationships. Second, the results of an entity's hedging relationships are reflected in an income statement line item that is typically an important metric for entities that have significant interest rate risk hedging programs. Therefore, in the Board's view, the results of systematically entering into drastically ineffective hedges would raise questions on the part of users of financial statements.

BC89. Third, the Board designed the initial assessment of hedge effectiveness to qualify for the optional practical expedient to be constrained in that it allows only a mismatch in the base rate, but not the introduction of unrelated risks or other features (such as a leverage factor) to avoid introducing elements into a hedging relationship that may be speculative in nature. For example, if the hedged forecasted transaction references three-month LIBOR but the derivative hedging instrument references a non-LIBOR rate and a leverage factor, an entity that elected to apply the optional expedient in paragraph 848-50-25-11(b) should model the hedged forecasted cash flows using the non-LIBOR interest rate index; however, the derivative instrument's leverage factor should not be used to model the hedged forecasted cash flows. As noted in paragraph BC72, the Board considers the income statement presentation requirements in Topic 815 to be an

important safeguard. The Board also notes that detailed scope requirements may impose costs to an entity to qualify for the relief that outweigh the expected benefits of the relief.

Option to Apply Exceptions and Expedients for Hedge Accounting

BC90. The amendments in this Update allow an entity to elect each of the optional expedients for hedge accounting on an individual hedging relationship basis. If an entity elects the optional expedients, it may apply them for each individual hedging relationship and is not required to apply the elections to the hedging programs or other hedging relationships. The Board determined that an entity may want to continue to use its existing hedge assessment processes for certain hedging relationships if the optional expedients are not needed to maintain hedge accounting. The Board decided that an entity should be free to determine whether the hedging relationship continues to qualify for hedge accounting using either current GAAP in Topic 815 or one or more optional expedients in the amendments. Furthermore, the Board concluded that if an entity did not elect an optional expedient to maintain hedge accounting and that resulted in a discontinuance of hedge accounting in Topic 815, the same outcome as if the entity had voluntarily discontinued hedge accounting under current GAAP would occur.

One-Time Election to Sell or Transfer Debt Securities Classified as Held to Maturity

BC91. In feedback on the proposed Update, some stakeholders asked the Board to consider providing optional relief to allow a one-time election to sell or transfer debt securities classified as held to maturity that reference a rate that is expected to be discontinued. The anticipated discontinuance of a reference rate is not explicitly included in the events or other circumstances that may justify the sale or transfer of a security classified as held to maturity without calling into question an entity's intent to hold other debt securities to maturity in the future. In addition, some stakeholders were uncertain on whether reference rate reform would meet the conditions in paragraph 320-10-25-9.

BC92. In the Board's view, accounting constraints should not be an impediment to an entity's strategy for managing certain risks associated with reference rate reform. Such strategies may include selling debt securities affected by reference rate reform or hedging the interest rate risk of those debt securities, and the Board recognizes that Topic 320, Investments—Debt and Equity Securities, includes constraints for employing such strategies for debt securities classified as held to maturity. Therefore, the amendments in this Update allow an entity to make a one-time election to sell, transfer, or both sell and transfer debt securities that meet certain eligibility criteria from held to maturity to available for sale and/or trading. An entity may sell, transfer, or both sell and transfer any of those held-to-maturity

debt securities that meet the eligibility criteria on the date of application of the one-time election.

BC93. The one-time election applies to debt securities that refer to a rate affected by reference rate reform and that were classified as held to maturity before January 1, 2020. The Board considered alternative dates that were earlier than January 1, 2020, such as securities classified as held to maturity as of the announcement by the United Kingdom's Financial Conduct Authority in 2017. However, the Board considered that there have been several subsequent significant milestones made toward the discontinuation of LIBOR since that announcement and for other IBORs.

BC94. The one-time election may be made at any time but no later than December 31, 2022. The Board determined that a one-time election should result in fewer reporting periods being affected by sales from held to maturity or transfers from held to maturity than an alternative that allowed for an election on a security-by-security basis at any time.

Sunset Provision

BC95. The Board decided that an entity will no longer be permitted to apply the provided exceptions and optional expedients for contract modifications and hedging relationships for reporting periods after December 31, 2022. The Board notes that reference rate reform is expected to be temporary in nature, and the objective of the amendments in this Update is to facilitate the effects of the reform on financial reporting for the market-wide transition period in which an entity replaces the use of reference rates with alternative reference rates. Therefore, after it stops applying the amendments, an entity should apply existing accounting requirements for contract modifications and hedging relationships.

BC96. As noted in paragraph BC20, while LIBOR is expected to be discontinued by the end of 2021, there are still uncertainties about when LIBOR and other reference rates will cease being published. Therefore, the Board decided to provide an extra year beyond the expected discontinuation date of LIBOR. The Board will monitor the market-wide IBOR transitions. As noted in paragraph BC10, the Board will consider whether future developments warrant any changes, including changes to the end date of the application of the amendments in this Update.

Transition and Disclosures

BC97. The Board decided that the amendments in this Update are effective for all entities upon issuance of this final Update on March 12, 2020. An entity may elect to apply the amendments for contract modifications by Topic or Industry Subtopic as of any date from the beginning of an interim period that includes or is subsequent to March 12, 2020 (that is, the date of issuance of this Update), or

prospectively from a date within an interim period that includes or is subsequent to March 12, 2020, up to the date that the financial statements are available to be issued. Once elected for a Topic or Industry Subtopic, the amendments must be applied prospectively for all eligible contract modifications for that Topic or Industry Subtopic.

BC98. An entity may elect to apply the amendments in this Update to eligible hedging relationships existing as of the beginning of the interim period that includes March 12, 2020 and to new eligible hedging relationships entered into after the beginning of the interim period that includes March 12, 2020. If an entity elects to apply any of the amendments for an eligible hedging relationship existing as of the beginning of an interim period that includes March 12, 2020, any adjustments as a result of those elections must be reflected as of the beginning of that interim period. If an entity elects to apply any of the amendments for a new eligible hedging relationship entered into between the beginning of the interim period that includes March 12, 2020 and March 12, 2020, any adjustments as a result of those elections must be reflected as of the beginning of the hedging relationship.

BC99. For private companies that are not financial institutions as described in paragraph 942-320-50-1 and not-for-profit entities (except for not-for-profit entities that have issued, or are a conduit bond obligor for, securities that are traded, listed, or quoted on an exchange or an over-the-counter market), an entity must update its hedge documentation noting the changes made before the next interim (if applicable) or annual financial statements are available to be issued. For all other entities, an entity must update its hedge documentation noting the changes made no later than when the entity performs its first quarterly assessment of effectiveness after the election.

BC100. The amendments do not apply to:

- a. Contract modifications made after December 31, 2022
- b. New hedging relationships entered into after December 31, 2022
- c. Hedging relationships evaluated for periods after December 31, 2022, except for hedging relationships existing as of December 31, 2022, that apply the following optional expedients that are retained through the end of the hedging relationship (including for periods evaluated after December 31, 2022):
 1. An optional expedient to the systematic and rational method used to recognize in earnings the components excluded from the assessment of effectiveness
 2. An optional expedient to the rate to discount cash flows associated with the hedged item and any adjustment to the cash flows for the designated term or the partial term of the designated hedged item in a fair value hedge
 3. An optional expedient to not periodically evaluate certain conditions when using the shortcut method for a fair value hedge.

BC101. As a practical matter, the Board anticipates that the amendments in this Update will be issued contemporaneously with the time frame in which an entity may begin modifying contracts for reference rate reform. Therefore, the Board notes that prospective application from the beginning of the interim period of issuance provides an entity with the ability to temporarily simplify or suspend application of certain areas of current GAAP for contracts and hedging relationships affected by reference rate reform.

BC102. The Board decided that the optional expedients for hedge accounting should be allowed if an entity has adopted the amendments in Update 2017-12. As noted in paragraph BC72, the Board considers the income statement presentation requirements in Topic 815 to be an important safeguard. Furthermore, the amendments in Update 2017-12 removed the requirement to separately measure and report the amount by which a hedging instrument does not offset a hedged item, generally referred to as the “ineffective” amount. The amendments on hedge accounting in this Update are in contemplation of those significant changes in Update 2017-12.

BC103. In feedback on the proposed Update, some stakeholders asked the Board to consider providing certain optional expedients for hedge accounting to nonpublic business entities that have not adopted the amendments in Update 2017-12. The Board decided that there are certain optional expedients for hedge accounting that are not dependent on the changes made in Update 2017-12 and therefore decided to allow an entity to elect the following optional expedients for hedge accounting if it has not yet adopted the amendments in Update 2017-12:

- a. Changes in critical terms of a hedging relationship.
- b. Changes to the method designated for use in assessing hedge effectiveness in a cash flow hedge if the optional expedient method being elected is the simplified hedge accounting approach for private companies for initial hedge effectiveness or for subsequent hedge effectiveness.
- c. Probability of the hedged forecasted transaction for cash flow hedges.
- d. Adjustment of any of the three methods of assessing and measuring hedge effectiveness in a cash flow hedge when hedge effectiveness is assessed on a quantitative basis, if both the hedged forecasted transaction and the hedging instrument have a reference rate that meets the scope of paragraph 848-10-15-3. The entity may assume that the reference rate will not be replaced for the remainder of the hedging relationship.
- e. The use of the simplified hedge accounting approach for eligible private companies for initial hedge effectiveness or for subsequent hedge effectiveness.

BC104. The Board decided that an entity should disclose the nature of and reason for electing the optional expedients in each interim and annual financial statement

period in the fiscal year of application. A majority of the Board indicated that this disclosure (a) highlights for users of financial statements that an entity is encountering the effects of reference rate reform and (b) helps users understand an entity's decision to apply relief to specific types of contracts and hedging relationships.

BC105. The Board considered whether private entities and not-for-profit entities should have a delayed effective date compared with that of public entities. The Board decided not to have a delayed effective date for private entities and not-for-profit entities because the guidance is optional and is aimed at providing expedients and exceptions to reduce accounting analyses and related costs that are triggered when the contracts or hedging relationships are modified. The Board determined that reference rate reform is a market-wide initiative that affects all entities that have contract modifications and hedging relationships that reference the discontinued reference rates and that the optional expedients should be available to all entities during the same effective period.

BC106. The Board considered including additional disclosures for entities that elect to apply the optional expedient for a change in the designated benchmark interest rate for fair value hedges. The amendments in this Update allow an entity to use a method to change the designated benchmark interest rate that results in a change to the hedged item's cumulative fair value basis adjustment and recognize that amount in current earnings. Although some Board members favored an approach that would require that the amount recognized in current earnings be reported separately because the amount may be viewed as additional information related to the effect of reference rate reform, the Board decided not to require that this amount be reported separately because the disclosures for hedge accounting in current GAAP include the amounts that would be recognized because an entity used the optional expedients for hedge accounting.

BC107. Given that the objective of this project was limited to providing accounting relief to ease the operational burden of reference rate reform, the Board considered whether additional required disclosures would be beneficial to financial statement users to understand the effects of reference rate reform on a reporting entity's current contracts (as of a reporting date) that are affected by reference rate reform and, if so, whether those disclosures would be considered part of a separate project. Additional disclosures related to existing contracts that are currently in the financial statements may be particularly useful to a user because reference rate reform could alter future cash flows related to those contracts. An improved understanding of those future cash flow changes could be helpful to users' analyses. However, the expectation that cash flows would be altered in a significant and predictable way is inconsistent with the basis for providing a practical expedient. That is, if cash flows are expected to change significantly, the Board should not have provided an alternative to assessing contracts for modifications.

BC108. An example of qualitative disclosures could include a description of

management's approach and its progress on addressing an entity's exposure to anticipated discontinued reference rates. An example of quantitative disclosures could include identifying (a) the broad categories of existing financial instruments that reference those rates as of the reporting date and (b) the percentage or dollar amounts of those existing financial instruments (based on the notional amounts or the carrying amounts of the financial instruments) that contain contract provisions that adequately contemplate the discontinuance of the reference rate and the percentage or dollar amounts of those existing financial instruments that do not contain contract provisions that adequately contemplate the discontinuance of the reference rate and would require some degree of additional negotiation. Over time, a reporting entity could quantitatively disclose those contracts that have replaced the reference rate with an alternative rate. Those disclosures would be required only during the period of the market-wide transition and could have an expiration date that is aligned with the sunset provision in the amendments in this Update or another date.

BC109. A reporting entity's exposure to specific variable interest rates, such as IBORs, is not required under current GAAP; therefore, in the absence of requiring such a disclosure, it may be difficult and costly for a user to understand a reporting entity's exposure to reference rate reform. Using a management approach to provide these types of quantitative and qualitative disclosures should minimize the expected costs of providing the information for preparers of financial statements.

BC110. In providing feedback on the amendments in the proposed Update, financial statement preparers were generally not supportive of the Board requiring additional disclosures for the application of the optional expedients (beyond those in the proposed Update) or entity exposures to interest rates affected by reference rate reform. Those stakeholders responded that other regulatory disclosure requirements (for example, disclosures required by the U.S. Securities and Exchange Commission for public entities) would meet the objectives and that the additional cost to require such disclosures in the financial statements does not provide sufficient additional benefits to users of financial statements. Feedback from users of financial statements indicated that those disclosures would be used to adjust GAAP net income as nonrecurring items. An entity's exposure to reference rates anticipated to be discontinued would provide an indication of the entity's progress in addressing the business risks related to the transition. Some stakeholders provided feedback that pervasive business risks for reference rate reform are concentrated to a limited number of entities in certain industries, and a disclosure requirement would add additional costs across all entities to demonstrate that reference rate reform is not expected to be material to the financial statements.

BC111. Although some Board members favored adding disclosure requirements, ultimately the Board concluded that the expected benefits of additional disclosures would not outweigh the expected costs, particularly when other regulatory disclosure requirements already exist to address risks presented by reference rate reform when material to a public entity, and, therefore, did not support adding a

separate disclosure project to its agenda. For private companies not subject to other regulatory disclosure requirements, the Board considered the *Private Company Decision-Making Framework: A Guide for Evaluating Financial Accounting and Reporting for Private Companies*, which indicates that users of private company financial statements have continuous access to management and the ability to obtain financial information throughout the year. Therefore, in the Board's view, the expected benefits for the users of those private company financial statements did not outweigh the expected costs to preparers of private company financial statements to provide additional disclosures on the application of the optional expedients or exposures to certain interest rates.

International Financial Reporting Standards (IFRS Standards)

BC112. In September 2019, the International Accounting Standards Board (IASB) published *Interest Rate Benchmark Reform: Amendments to IFRS 9, IAS 39 and IFRS 7*. The IASB amendments provide exceptions to specific hedge accounting requirements in IFRS 9, *Financial Instruments*, IAS 39, *Financial Instruments: Recognition and Measurement*, and IFRS 7, *Financial Instruments: Disclosures*.

BC113. In its outreach with stakeholders, the IASB identified the following two groups of accounting issues that could have financial reporting implications:

- a. Prereplacement issues—issues affecting financial reporting in the period before the reform and/or replacement of an existing interest rate benchmark with an alternative interest rate
- b. Replacement issues—issues that might affect financial reporting when an existing interest rate benchmark is reformed and/or replaced with an alternative interest rate.

BC114. The IASB decided to prioritize the prereplacement issues because they are more urgent. The IASB amendments provide exceptions to the following hedge accounting requirements that are based on forward-looking analyses:

- a. Highly probable requirements
- b. Prospective assessments
- c. Separately identifiable risk components
- d. IAS 39 retrospective assessments.

BC115. Other than the specific amendments listed, no other changes were made to IFRS Standards hedge accounting requirements as part of this phase of the project. The IASB is currently considering potential replacement issues on the basis of input gathered from research activities as well as the feedback received in comment letters on the IASB's May 2019 Exposure Draft, *Interest Rate Benchmark Reform*, addressing the prereplacement issues. The IASB has started its analysis and deliberations of potential replacement issues as part of its second phase of the project.

Amendments to the XBRL Taxonomy

The amendments to the *FASB Accounting Standards Codification*[®] in this Accounting Standards Update require improvements to the U.S. GAAP Financial Reporting Taxonomy (Taxonomy). Those improvements, which will be incorporated into the proposed 2021 Taxonomy, are available through Taxonomy Improvements provided at www.fasb.org, and finalized as part of the annual release process.