

NZ IAS 39 has been replaced by NZ IFRS 9 Financial Instruments, except entities that continue to apply relevant hedge accounting guidance

Also refer: NZ IFRIC 16: *Hedges of a Net Investment in a Foreign Operation*

HEDGE ACCOUNTING

Hedge accounting may be applied if, and only if, all the following criteria are met:

- ▶ At the inception of the hedge there is formal designation and documentation of the hedging relationship and the entity's risk management objective and strategy for undertaking the hedge
- ▶ The hedge is expected to be highly effective (80 - 125 % effective) in achieving offsetting changes in fair value or cash flows attributable to the hedged risk, consistently with the originally documented risk management strategy for that particular hedging relationship
- ▶ For cash flow hedges, a forecast transaction that is the subject of the hedge must be highly probable and must present an exposure to variations in cash flows that could ultimately affect profit or loss
- ▶ The effectiveness of the hedge can be reliably measured, i.e., the fair value or cash flows of the hedged item that are attributable to the hedged risk and the fair value of the hedging instrument can be reliably measured
- ▶ The hedge is assessed on an ongoing basis and determined actually to have been highly effective throughout the financial reporting periods for which the hedge was designated.

CASH FLOW HEDGE

- ▶ Definition - a hedge of the exposure to variability in cash flows that (i) is attributable to a particular risk associated with a recognised asset or liability (such as all or some future interest payments on variable rate debt) or a highly probable forecast transaction and (ii) could affect profit or loss.
- ▶ The portion of the gain or loss on the hedging instrument that is determined to be an effective hedge is recognised in OCI; and the ineffective portion of the gain or loss on the hedging instrument is recognised in profit or loss.
- ▶ If the hedge results in the recognition of a financial asset or a financial liability, the associated gains or losses that were recognised in equity are reclassified from OCI to profit or loss as a reclassification adjustment in the same period(s) during which the asset acquired or liability assumed affects profit or loss.
- ▶ If the hedge results in the recognition of a non-financial asset or a non-financial liability, then the entity has an accounting policy election of either:
 - Reclassifying the associated gains and losses that were recognised in OCI to profit or loss as a reclassification adjustment in the same period or periods during which the asset acquired or liability assumed affects profit or loss (such as in the periods that depreciation expense or cost of sales is recognised); or
 - Removing the associated gains and losses that were recognised in OCI and includes them in the initial cost or other carrying amount of the asset or liability.
- ▶ Cash flow hedge accounting is discontinued prospectively if:
 - The hedging instrument expires or is sold, terminated or exercised (net amount recognised in OCI remains in equity until forecast transaction occurs and is then treated as described above).
 - The hedge no longer meets the criteria set out in the above block (net amount recognised in OCI remains in equity until forecast transaction occurs and is then treated as described above).
 - The forecast transaction is no longer expected to occur (net amount recognised in OCI is transferred immediately to profit or loss as a reclassification adjustment).
 - The entity revokes the designation (net amount recognised in OCI remains in equity until forecast transaction occurs and is then treated as described above).

FAIR VALUE HEDGE

- ▶ Definition - a hedge of the exposure to changes in fair value of a recognised asset or liability or an unrecognised firm commitment, or an identified portion of such an asset, liability or firm commitment, that is attributable to a particular risk and could affect profit or loss.
- ▶ Gain/loss from remeasuring the hedging instrument at fair value or the foreign currency component of its carrying amount is recognised in profit or loss.
- ▶ The gain/loss on the hedged item attributable to the hedged risk adjusts the carrying amount of the hedged item and is recognised in profit or loss.
- ▶ Fair value hedge accounting is discontinued prospectively if:
 - The hedging instrument expires or is sold, terminated or exercised.
 - The hedge no longer meets the criteria set out in the above block.
 - The entity revokes the designation.
- ▶ Adjustments to the carrying amount of a hedged financial asset for which the effective interest rate is used are amortised to profit or loss. The adjustment is based on a recalculated effective interest rate at the date amortisation begins.

HEDGE OF A NET INVESTMENT IN A FOREIGN OPERATION

Hedges of a net investment in a foreign operation, including a hedge of a monetary item that is accounted for as part of the net investment, are accounted for similarly to cash flow hedges:

- ▶ The portion of the gain or loss on the hedging instrument that is determined to be an effective hedge is recognised in equity; and
- ▶ The ineffective portion is recognised in profit or loss.

The gain or loss on the hedging instrument relating to the effective portion of the hedge that has been recognised in OCI is reclassified from equity to profit or loss as a reclassification adjustment on the disposal of the foreign operation.

NOVATION OF DERIVATIVES

Hedge accounting continues for novated derivatives so long as:

- ▶ The novation is a consequence of laws or regulations (or the introduction of laws or regulations)
- ▶ The parties to the hedging instrument agree that one or more clearing counterparties replace their original counterparty to become the new counterparty of each party.
- ▶ Any changes to the hedging instrument are limited only to those that are necessary to effect such a replacement of the counterparty (including changes in the collateral requirements, rights to offset receivable and payable balances, charges levied).

DESIGNATION OF NON-FINANCIAL ITEMS AS HEDGED ITEMS

If the hedged item is a non-financial asset or non-financial liability, it is designated as a hedged item, either:

- ▶ For foreign currency risks, or
- ▶ In its entirety for all risks, because of the difficulty of isolating and measuring the appropriate portion of the cash flows or fair value changes attributable to specific risks other than foreign currency risks.