FASB EXPOSURE DRAFT

Proposed Accounting Standards Update

Issued: October 29, 2020
Comments Due: November 13, 2020

Reference Rate Reform (Topic 848)

Scope Refinement

The Board issued this Exposure Draft to solicit public comment on proposed changes to Topic 848 of the *FASB Accounting Standards Codification*®. Individuals can submit comments in one of three ways: using the electronic feedback form on the FASB website, emailing comments to director@fasb.org, or sending a letter to "Technical Director, File Reference No. 2020-900, FASB, 401 Merritt 7, PO Box 5116, Norwalk, CT 06856-5116."

Financial Accounting Standards Board

Notice to Recipients of This Exposure Draft of a Proposed Accounting Standards Update

The Board invites comments on all matters in this Exposure Draft until November 13, 2020. Interested parties may submit comments in one of three ways:

- Using the electronic feedback form available on the FASB website at Exposure Documents Open for Comment
- Emailing comments to director@fasb.org, File Reference No. 2020-900
- Sending a letter to "Technical Director, File Reference No. 2020-900, FASB, 401 Merritt 7, PO Box 5116, Norwalk, CT 06856-5116."

All comments received are part of the FASB's public file and are available at www.fasb.org.

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. A copy of this Exposure Draft is available at www.fasb.org.

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FASB FINANCIAL ACCOUNTING STANDARDS BOARD®

Proposed Accounting Standards Update

Reference Rate Reform (Topic 848)

Scope Refinement

October 29, 2020

Comment Deadline: November 13, 2020

CONTENTS

Page
Numbers

Summary and Questions for Respondents

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

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.

The derivatives market is currently undergoing various transitions due to reference rate reform initiatives. Across jurisdictions, derivative instruments that use certain interest rate indexes for determining variable cash flows and for valuation and other purposes are transitioning to alternative rates. For example, for interest rate swaps, certain rates used to compute the cash flows for the swap's variable leg are transitioning to alternative rates. In addition, certain interest rate indexes used to discount the future cash flows of a derivative instrument to determine its fair value are transitioning to alternative rates. If an entity is required to exchange margin payments on the basis of changes in the derivative instrument's fair value, those margin payments are affected by a change to the interest rate used for discounting. Lastly, the compensation or interest amount earned on margin payments, referred to as contract price alignment, typically fluctuates with changes in an interest rate index and, therefore, is also affected by a change to the interest rate used for that purpose.

Stakeholders have indicated that changes in the interest rate used for margining, discounting, or contract price alignment for a derivative instrument that are being implemented as part of the market-wide transition to new reference rates (commonly referred to as the "discounting transition") create particular accounting implications.

Because of the broad population of derivatives affected by the discounting transition, stakeholders have been analyzing the accounting implications of the discounting transition against the available exceptions and expedients within Topic 848, Reference Rate Reform, which has led them to raise questions about the scope of that Topic. The discounting transition affects derivative instruments indexed to a wide variety of reference rates, including rates that will not be discontinued as a result of reference rate reform. Furthermore, the discounting transition is not limited to derivative trades cleared with a central counterparty; bilateral counterparties to non-cleared cash-collateralized derivatives may undergo the discounting transition as well.

As a result, stakeholders have raised questions about whether the guidance in Topic 848 can be applied to contracts that do not reference a rate that is expected to be discontinued (as required by the scope of Topic 848) but that are affected by reference rate reform as a result of the discounting transition. Stakeholders have raised concerns about the need to reassess previous accounting determinations related to those contracts and about the hedge accounting consequences of the discounting transition.

In response to stakeholder concerns, the Board is proposing to refine the scope of Topic 848 such that contracts affected by the discounting transition would be eligible for certain optional expedients and exceptions in Topic 848.

What Are the Main Provisions?

The amendments in this proposed Update would clarify that certain optional expedients and exceptions in Topic 848 for contract modifications and hedge accounting apply to contracts that are affected by the discounting transition.

Specifically, certain provisions in Topic 848, if elected by an entity, would apply to derivative instruments that use an interest rate for margining, discounting, or contract price alignment that is modified as a result of reference rate reform. Amendments in this proposed Update to the expedients and exceptions in Topic 848 are included to capture the incremental consequences of the proposed scope refinement and to tailor the existing guidance to derivative instruments affected by the discounting transition. The table below provides a summary of the proposed amendments to the Codification.

Codification Subtopic	**Description of Changes**
Reference Rate Reform—Overall (848-10)	• Refined the scope of Topic 848 to capture derivative instruments that will have changes in the interest rate used for margining, discounting, or contract price alignment because of the discounting transition that do not also reference LIBOR or another reference rate that is expected to be discontinued as a result of reference rate reform (paragraph 848-10-15-3A).
Contract Modifications (848-20)	• Added derivative instruments that meet the scope of paragraph 848-10-15-3A to the scope of derivative instruments eligible for contract modification relief in paragraph 848-20-35-4 (paragraph 848-20-15-2A).

Codification Subtopic	Description of Changes
	• Clarified that an entity may apply contract modification relief to derivative instruments affected by the discounting transition at a different date than it applies the contract modification relief to other derivative contract modifications (paragraphs 848-20-35-1 and 848-20-35-5).
Hedging—General (848-30)	• Clarified that derivative instruments that meet the scope of paragraph 848-10-15-3A that are designated as hedging instruments are eligible for certain optional expedients and exceptions to the requirements in Subtopic 815-20 (paragraph 848-30-15-1). • Extended the option to add one or more basis swaps to a derivative that meets the scope of paragraph 848-10-15-3A that is designated as a hedging instrument in a cash flow hedge or a fair value hedge without hedge dedesignation (paragraph 848-30-25-9A). • Added the option to subsequently remove one or more basis swaps that were added to the hedging instrument that is affected by either the discontinuance of a reference rate or the discounting transition without hedge dedesignation (paragraphs 848-30-25-9(b) and 848-30-25-9A). • Added the option to continue to apply the shortcut method to a fair value hedge in which an entity elects to jointly designate two or more derivative instruments, or proportions of those instruments, as the hedging instrument by extending the ability to elect the corresponding optional expedient for application of the fair value hedge shortcut method (paragraph 848-30-25-10). • Clarified that in a cash flow hedging relationship in which a derivative designated as the hedging instrument meets the scope of paragraph 848-10-15-3A (including when an entity elects to add one or more basis swaps or proportions of those basis swaps), an entity

Codification Subtopic	Description of Changes
	may continue to apply a perfectly effective assessment method by electing the corresponding optional expedient for subsequent assessments under that method (paragraph 848-30-25-11A). • Clarified that if a derivative affected by the discounting transition is designated as a hedging instrument in a fair value hedge accounted for under the shortcut method, an entity may adjust the cumulative fair value hedge basis adjustment and may continue to apply the shortcut method by electing the corresponding optional expedient for application of the fair value hedge shortcut method (paragraph 848-30-25-11B). • Clarified that if a derivative affected by a payment or receipt of a cash settlement (or equivalent) intended to compensate for a modification of the interest rate used for margining, discounting, or contract price alignment is designated as a hedging instrument in a cash flow hedge, an entity may adjust the recorded amount in accumulated other comprehensive income and apply certain effectiveness assessment expedients (paragraph 848-30-25-11C).
Fair Value Hedges (848-40)	• Extended the option to change the designated benchmark interest rate in a fair value hedge to a fair value hedging relationship in which the derivative designated as the hedging instrument meets the scope of paragraph 848-10-15-3A (paragraph 848-40-25-2). • Clarified that the optional expedient for the shortcut effectiveness assessment method expires as of December 31, 2022, for fair value hedges that jointly designate two or more derivative instruments, or proportions of those instruments, as the hedging instrument (paragraph 848-40-25-8).

Codification Subtopic	Description of Changes
Cash Flow Hedges (848-50)	• Clarified that relief provided for the application of subsequent assessment methods for assuming perfect effectiveness for cash flow hedges in which the hedging instrument meets the scope of paragraph 848-10-15-3A expires as of December 31, 2022 (paragraph 848-50-35-1). • Updated to reflect consequential amendments related to application to hedging instruments that meet the scope of paragraph 848-10-15-3A (paragraphs 848-50-35-19 through 35-20 and 848-50-35-24).

The Topic 848 optional expedients and exceptions that were not directly amended in this proposed Update but that may be applied to derivatives affected by the discounting transition are in the table below. The paragraphs referenced in the table below are not included in this proposed Update for readability purposes.

Codification Subtopic	Provisions That Apply to Derivatives Affected by the Discounting Transition That Were Not Directly Amended
Reference Rate Reform—Contract Modifications (848-20)	• Option to not reassess a previous accounting determination (paragraph 848-20-35-4). • Flowchart that summarizes how to navigate Topic 848 (paragraph 848-20-55-1). • Implementation guidance that illustrates relief in paragraph 848-20-35-4, including relief from reassessing whether a modified derivative is a hybrid instrument and includes a financing element (paragraph 848-20-55-2).
Hedging—General (848-30)	• Option to apply the hedging relief on an individual hedge basis (paragraph 848-30-25-2). • Option to not dedesignate a hedging relationship due to a change in a critical term (paragraph 848-30-25-3).

Codification Subtopic	Provisions That Apply to Derivatives Affected by the Discounting Transition That Were Not Directly Amended
	• Requirement to update hedge documentation for a change in a critical term (paragraph 848-30-25-4). • Option to change the contractual term of a hedging instrument, hedged item, or forecasted transaction and to not dedesignate a hedging relationship (paragraph 848-30-25-5). • Guidance that a change in the interest rate used for margining, discounting, or contract price alignment of a derivative hedging instrument should not be considered a change to the critical terms of the hedging relationship (paragraph 848-30-25-7). • Option to change the systematic and rational amortization method for excluded components (paragraphs 848-30-25-12 through 25-13).
Fair Value Hedges (848-40)	• Requirement for an entity that elects to apply the optional expedients in this Subtopic to continue to apply all other requirements applicable to fair value hedges in Subtopics 815-20 and 815-25 (paragraph 848-40-15-1). • Option to apply the fair value hedging relief on an individual hedge basis (paragraph 848-40-25-1). • Requirement to update hedge documentation upon a change in the designated benchmark rate (paragraph 848-40-25-3). • Requirements and expedients related to continuing fair value hedge accounting without dedesignation if an entity elects to change the designated benchmark interest rate (paragraphs 848-40-25-4 through 25-7 and 848-40-25-9).

Codification Subtopic	Provisions That Apply to Derivatives Affected by the Discounting Transition That Were Not Directly Amended
Cash Flow Hedges (848-50)	• Requirement for an entity that elects to apply the optional expedients in this Subtopic to continue to apply all other requirements applicable to cash value hedges in Subtopics 815-20 and 815-30 (paragraph 848-50-15-1). • Option to apply the cash flow hedging relief on an individual hedge basis (paragraph 848-50-25-1). • Option to apply the optional expedients in this Subtopic prospectively and the requirement to update hedge documentation if electing an optional expedient in this Subtopic (paragraphs 848-50-35-2 through 35-3). • Option to apply a subsequent effectiveness assessment method that assumes perfect effectiveness if an entity was applying the corresponding perfectly effective method under Subtopics 815-20 and 815-30 before the discounting transition (paragraphs 848-50-35-4 through 35-9). • Guidance on assessing hedge effectiveness when optional expedient methods are discontinued (paragraphs 848-50-35-21 and 848-50-35-23).

The amendments in this proposed Update would apply to all entities that elect to apply the optional guidance in Topic 848.

When Would the Amendments Be Effective?

The amendments in this proposed Update would be effective for all entities upon issuance of a final Accounting Standards Update.

An entity may elect to apply the amendments in this proposed Update retrospectively as of any date from the beginning of an interim period that includes or is subsequent to March 12, 2020, or prospectively to new modifications from any date within an interim period that includes or is subsequent to the date of the issuance of a final Update, up to the date that financial statements are available to be issued.

If an entity elects to apply any of the amendments in this proposed Update for an eligible hedging relationship, any adjustments as a result of those elections must be reflected as of the date the entity applies the election.

The amendments in this proposed Update do not apply to contract modifications made after December 31, 2022, new hedging relationships entered into after December 31, 2022, and existing hedging relationships evaluated for effectiveness in periods after December 31, 2022, except for hedging relationships existing as of December 31, 2022, that apply certain optional expedients in which the accounting effects are recorded through the end of the hedging relationship (including periods after December 31, 2022).

Questions for Respondents

The Board invites individuals and organizations to comment on all matters in this proposed Update, particularly on the issues and questions below. Comments are requested from those who agree with the proposed guidance as well as from those who do not agree. Comments are most helpful if they identify and clearly explain the issue or question to which they relate. Those who disagree with the proposed guidance are asked to describe their suggested alternatives, supported by specific reasoning.

Question 1—Scope Refinement: Do you agree that the scope of Topic 848 should be refined to include contracts that do not reference a rate expected to be discontinued as a result of reference rate reform but that are affected by the discounting transition? Why or why not?

Question 2—Operability: The Board is proposing amendments in this Update to the expedients and exceptions in Topic 848 to capture the incremental consequences of the proposed scope refinement and tailor the existing guidance to derivative instruments affected by the discounting transition. Are those proposed amendments complete and operable? If not, what suggestions do you have and why?

Question 3—Effective Date and Transition: Do you agree with the proposed effective date and transition guidance? Why or why not?

Question 4—Ongoing Monitoring: Are there other accounting consequences related to reference rate reform that the Board should consider?

Amendments to the *FASB Accounting Standards Codification*®

Introduction

1. The Accounting Standards Codification is amended as described in paragraphs 2–8. In some cases, to put the change in context, not only are the amended paragraphs shown but also the preceding and following paragraphs. Terms from the Master Glossary are in **bold** type. Added text is <u>underlined</u>, and deleted text is ~~struck out~~.

[Editor's Note: The superseded pending content paragraphs of the amended paragraphs of Topic 848 are not shown here.]

Amendments to Subtopic 848-10

2. Add paragraph 848-10-15-3A, with a link to transition paragraph 848-10-65-2, as follows:

Reference Rate Reform—Overall

Scope and Scope Exceptions

> 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.

<u>**848-10-15-3A** Certain provisions of the guidance in this Topic, if elected by an entity, shall apply to derivative instruments that do not meet the scope of paragraph 848-10-15-3 that use an interest rate for margining, discounting, or contract price alignment that is modified as a result of reference rate reform.</u>

3. Add paragraph 848-10-65-2 and its related heading as follows:

Transition and Open Effective Date Information

<u>**> Transition Related to Accounting Standards Update No. 2020-XX, *Reference Rate Reform (Topic 848): Scope Refinement***</u>

848-10-65-2 The following represents the transition, end of application, and effective date information related to Accounting Standards Update No. 2020-XX, *Reference Rate Reform (Topic 848): Scope Refinement:*

a. The pending content that links to this paragraph shall be effective for all entities as of [date of issuance of final Update] through December 31, 2022, as follows:
   1. An entity may elect to apply the pending content that links to this paragraph on contract modifications for derivative instruments that change the interest rate used for margining, discounting, or contract price alignment retrospectively as of any date from the beginning of an interim period that includes March 12, 2020, or prospectively to new modifications from any date within an interim period that includes or is subsequent to [date of issuance of final Update], up to the date that financial statements are available to be issued. On the date that an entity elects to apply the pending content that links to this paragraph on contract modifications for derivative instruments that change the interest rate used for margining, discounting, or contract price alignment, that pending content shall be applied to all eligible derivative contract modifications for derivative contracts modified in that manner 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. If an entity elects to apply any of the pending content that links to this paragraph to an eligible hedging relationship, any adjustments as a result of those elections shall be reflected as of the application date of the election and recognized in accordance with Subtopics 848-30, 848-40, and 848-50 (as applicable).
      i. For any private company that is not a financial institution as described in paragraph 942-320-50-1 and any not-for-profit entity (except for a not-for-profit entity that has issued, or is a conduit bond obligor for, securities that are traded, listed, or quoted on an exchange or an over-the-counter market) applying the pending content that links to this paragraph in a period before interim (if applicable) or annual financial statements are available to be issued, the 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. An entity that retrospectively applies the pending content that links to this paragraph to a prior interim (if applicable) or annual period shall update its hedge documentation (as applicable) noting the changes made for the

prior periods in which the entity is retrospectively applying the guidance upon adoption.

ii. For any other entity applying the pending content that links to this paragraph before its first quarterly assessment of effectiveness after the election, the 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. An entity that retrospectively applies the pending content that links to this paragraph to a prior interim or annual period shall update its hedge documentation (as applicable) noting the changes made for the prior periods in which the entity is retrospectively applying the pending content that links to this paragraph upon adoption.

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 that apply the following optional expedients in Subtopics 848-30, 848-40, and 848-50 that shall be retained through the end of the hedging relationship (including for periods evaluated after December 31, 2022):
      01. An optional expedient to adjust the fair value hedge basis adjustment in a fair value hedge accounted for under the shortcut method using a reasonable approach in paragraph 848-30-25-11B.
      02. 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 if the entity elected the practical expedient in paragraph 848-30-25-11B. (If an entity elects to apply the optional expedient in paragraph 848-40-25-8 in accordance with paragraph 848-30-25-10, it shall cease applying that expedient on December 31, 2022.)
      03. An optional expedient to adjust the amount recorded in accumulated other comprehensive income using a reasonable approach in paragraph 848-30-25-11C.
      04. An optional expedient to continue using a subsequent assessment method that assumes perfect effectiveness in paragraphs 848-50-35-4 through 35-9 for a cash flow hedge if the entity elected the practical expedient in paragraph 848-30-25-11C.

b. An entity may elect the optional expedients in Subtopics 848-30, 848-40, and 848-50 if it has adopted the amendments in Update 2017-12.

c. An entity that has not adopted the amendments in Update 2017-12 may elect the optional expedient allowing a change to the method designated for use in assessing hedge effectiveness in a cash flow hedge in paragraph 848-30-25-11A(b) if the optional expedient method being elected is the simplified hedge accounting approach for eligible private companies or for subsequent hedge effectiveness in paragraph 848-50-35-7.
d. 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 (d)(1) in each interim (if applicable) and annual financial statement period in the fiscal year of application.

Amendments to Subtopic 848-20

4. Add paragraph 848-20-15-2A and amend paragraphs 848-20-35-1 and 848-20-35-5, with a link to transition paragraph 848-10-65-2, as follows:

Reference Rate Reform—Contract Modifications

Scope and Scope Exceptions

> Modifications of Terms

848-20-15-2A Certain optional expedients in this Subtopic, if elected, shall apply to derivative instruments that meet the scope of paragraph 848-10-15-3A.

Subsequent Measurement

> 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 with the exception of derivative instruments that change the interest rate used for margining, discounting, or contract price alignment. An entity may elect to apply the guidance in this Subtopic to account for those derivative contract modifications separately from when it elects to apply the guidance in this Subtopic to account for other derivative contract modifications. 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.

> Optional Expedient: Contract Modifications Due to Reference Rate Reform

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 with the exception of derivative instruments that change the interest rate used for margining, discounting, or contract price alignment, as described in paragraph 848-20-35-1.

Amendments to Subtopic 848-30

5. Amend paragraphs 848-30-15-1 and 848-30-25-9 through 25-11 and add paragraphs 848-30-25-9A and 848-30-25-11A through 25-11C and their related headings, with a link to transition paragraph 848-10-65-2, as follows:

Reference Rate Reform—Hedging—General

Scope and Scope Exceptions

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. Certain optional expedients in this Subtopic may be applied if the hedging instrument meets the scope of paragraph 848-10-15-3A.

Recognition

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

> > 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. An entity may subsequently remove one or more derivative instruments, or proportions of those instruments, added in accordance with this paragraph without dedesignating the hedging relationship in accordance with paragraph 848-30-25-3.

848-30-25-9A If the hedging instrument meets the scope of paragraph 848-10-15-3A, an entity may change the designated hedging instrument to add one or more basis swaps or proportions of those basis swaps to be jointly designated as the hedging instrument in a hedging relationship if that basis swap addition is related to the modification of the interest rate used for margining, discounting, or contract price alignment for the hedging instrument. An entity may subsequently remove one or more basis swaps, or proportions of those basis swaps, added in accordance with this paragraph without dedesignating the hedging relationship in accordance with paragraph 848-30-25-3.

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) or paragraph 848-30-25-9A and is applying a quantitative subsequent effectiveness assessment method at the time of the change, 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. If an entity is applying the shortcut method in accordance with paragraphs 815-20-25-102 through 25-105, 815-20-25-107 through 25-109, and 815-20-25-111 through 25-117 at the time of the change, the entity may select the optional expedient to assess hedge effectiveness in accordance with paragraph 848-40-25-8 or a new method in accordance with Subtopics 815-20 and 815-25.

848-30-25-11 If an entity changes the ~~designated~~ hedging instrument that meets the scope of paragraph 848-10-15-3 that is designated 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.

848-30-25-11A For a cash flow hedge with a designated hedging instrument that meets the scope of paragraph 848-10-15-3A to which an entity is applying the relief in this Subtopic to continue hedge accounting without dedesignation (including a cash flow hedge in which an entity elects to change the hedging instrument in accordance with paragraph 848-30-25-9A), the entity shall assess the hedge effectiveness of the amended hedging relationship as follows:

a. An entity applying a subsequent quantitative or qualitative assessment method in accordance with Subtopics 815-20 and 815-30 at the time of the election shall continue to use the same method after the election.
b. An entity applying a subsequent assessment method that assumes perfect effectiveness in accordance with paragraph 815-20-25-3(b)(2)(iv)(01) at the time of the election may apply the corresponding optional expedient for the subsequent assessment method for assuming perfect effectiveness in accordance with paragraphs 848-50-35-4 through 35-9 or a quantitative method in accordance with Subtopics 815-20 and 815-30 after the election.

> > Optional Expedient: Adjustment to a Fair Value Hedge Basis Adjustment for a Fair Value Hedge Accounted for under the Shortcut Method and Affected by the Change in Interest Rate Used for Margining, Discounting, or Contract Price Alignment

848-30-25-11B For a fair value hedge in which the hedging instrument is a derivative that meets the scope of either paragraph 848-10-15-3 or paragraph 848-10-15-3A and the shortcut method is applied in accordance with paragraphs 815-20-25-102 through 25-105, 815-20-25-107 through 25-109, and 815-20-25-111 through 25-117, an entity may adjust the fair value hedge basis adjustment for the amount of the change in the fair value of the hedging instrument related to change in the interest rate used for margining, discounting, or contract price alignment using a reasonable approach. This Subtopic does not specify a single method for applying a reasonable approach. Ordinarily, an entity shall use a similar method for similar hedges. The entity shall justify the use of different methods for similar hedges. An entity applying the guidance in this paragraph may elect the optional expedient to continue to use the shortcut method to assess hedge effectiveness in accordance with paragraph 848-40-25-8 or a new method in accordance with Subtopics 815-20 and 815-25.

> > Optional Expedient: Adjustment to Accumulated Other Comprehensive Income for a Cash Flow Hedge Affected by a Cash Settlement (or Equivalent) Related to the Change in Interest Rate Used for Margining, Discounting, or Contract Price Alignment

848-30-25-11C For a cash flow hedge in which the hedging instrument is a derivative that meets the scope of either paragraph 848-10-15-3 or paragraph 848-10-15-3A that is affected by a payment or receipt of a cash settlement (or equivalent) intended to compensate for a modification of the interest rate used for margining, discounting, or contract price alignment for the derivative instrument related to reference rate reform, an entity may adjust the amount recorded in accumulated other comprehensive income for the amount of cash compensation (or equivalent) exchanged using a reasonable approach. This Subtopic does not specify a single method for applying a reasonable approach. Ordinarily, an entity shall use a similar method for similar hedges. The entity shall justify the use of different methods for similar hedges. If an entity elects the optional expedient in this paragraph for a cash flow hedge with a designating hedging instrument that meets the scope of paragraph 848-10-15-3A, the entity shall assess hedge effectiveness in accordance with paragraph 848-30-25-11A(a) through (b).

Amendments to Subtopic 848-40

6. Amend paragraphs 848-40-25-2 and 848-40-25-8, with a link to transition paragraph 810-10-65-2, as follows:

Reference Rate Reform—Fair Value Hedges

Recognition

> 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) or paragraph 848-30-25-9A (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 or paragraph 848-10-15-3A.
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.

> 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~~25-105, 815-20-25-107 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)). However, if an entity elects the practical expedient in accordance with paragraph 848-30-25-10, the entity is not permitted to continue to apply the shortcut method after December 31, 2022. In that case, if the hedging relationship continues after the entity is required to cease applying the optional expedient method because of the condition in paragraph 848-10-65-2(a)(3)(iii)(02) or because the entity elects to cease applying the optional expedient, the entity shall revert to applying the qualifying criteria and hedge assessment methods in Subtopics 815-20 and 815-25 to assess whether hedge accounting may continue for subsequent reporting periods. In that case, the change in the method of assessing hedge effectiveness upon discontinuing the application of the optional expedient method 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.

Amendments to Subtopic 848-50

7. Amend paragraphs 848-50-25-3, 848-50-35-1, 848-50-35-19 through 35-20, and 848-50-35-24 and add paragraph 848-50-35-19A, with a link to transition paragraph 810-10-65-2, as follows:

Reference Rate Reform—Cash Flow Hedges

Recognition

> Eligibility of Cash Flow Hedges Affected by Reference Rate Reform

> > 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 in accordance with paragraph 848-10-15-3, 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.

Subsequent Measurement

> 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. An entity may elect certain optional expedient methods if the hedging instrument meets the scope of paragraph 848-10-15-3A.

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

848-50-35-19 For an entity that elects an optional expedient for assessing cash flow hedge effectiveness in paragraphs 848-50-35-1 through 35-18 because either the hedged item or the hedging instrument references a rate that meets the scope of paragraph 848-10-15-3, the~~An~~ entity shall discontinue the use of that~~the~~ optional expedient~~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.

848-50-35-19A For an entity that elects an optional expedient for assessing cash flow hedge effectiveness in paragraphs 848-50-35-4 through 35-9 because the entity is applying the guidance in paragraph 848-30-25-11A(b), the entity shall discontinue the use of that optional expedient if any of the following occurs:

a. The guidance in this Topic is superseded (see paragraph 848-10-65-2(a)(3)).
b. 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 or paragraph 848-50-35-19A, 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.

848-50-35-24 If an entity discontinues an optional expedient method because of a condition in paragraph 848-50-35-19 or paragraph 848-50-35-19A 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

8. Supersede the paragraphs listed below, with a link to transition paragraph 848-10-65-2, as follows:

[Note: See table of superseded paragraphs below.]

Pending Content:

Transition Date: *(P) January 1, 2023; (N) January 1, 2023* | **Transition Guidance:** 848-10-65-2

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

Superseded Paragraphs
848-10-15-3A
848-20-15-2A
848-30-25-9A
848-30-25-11A through 25-11C
848-50-35-19A

The amendments in this proposed Update were approved for publication by the unanimous vote of the seven members of the Financial Accounting Standards Board:

Richard R. Jones, *Chairman*
James L. Kroeker, *Vice Chairman*
Christine A. Botosan
Gary R. Buesser
Susan M. Cosper
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 proposed 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. Since 2014, the Board has been actively monitoring the reference rate reform initiative undertaken globally to identify suitable alternatives to unsecured market benchmarks based on interbank offered rates. In March 2020, the Board issued Accounting Standards Update No. 2020-04, *Reference Rate Reform (Topic 848): Facilitation of the Effects of Reference Rate Reform on Financial Reporting*. The amendments in that Update provide optional guidance for a limited period of time to ease the potential burden on financial reporting in accounting for (or recognizing the effects of) reference rate reform.

BC3. Since the issuance of Topic 848, the Board has continued to monitor global reference rate reform developments to identify whether further improvements to the guidance in Topic 848 are needed to assist stakeholders. One such recent development relates to market-wide changes in the interest rate used for margining, discounting, or contract price alignment of a derivative instrument related to reference rate reform (commonly referred to as the "discounting transition"). The discounting transition is not limited to derivative trades cleared through a central counterparty; bilateral counterparties to non-cleared cash-collateralized derivatives may undergo the discounting transition as well.

BC4. The discounting transition may result in an immediate increase or decrease in a derivative instrument's fair value upon the change in the discount rate used by a market participant to value the affected derivative instrument, which may trigger a corresponding change in the related margining requirement. A cash compensation payment (or equivalent) may be exchanged to neutralize the effect of the change in the fair value of the derivative instrument, and the neutralizing adjustment may offset the receipt of or the requirement to post additional margin. Also, because the discounting transition may result in a change in a counterparty's risk profile, a central counterparty may require an affected participant to enter into one or more basis swaps to compensate for that risk profile change.

BC5. The specific mechanics of the discounting transition and the effect it will have on individual market participants has been evolving over the past several months. Recently, market participants began deciding how they would utilize basis swaps in existing hedging strategies and analyzing the accounting implications of those decisions against the available exceptions and expedients within Topic 848.

BC6. Stakeholders have raised questions about whether the guidance in Topic 848 can be applied to contracts that do not reference a rate that is expected to be discontinued but that are affected by reference rate reform as a result of the discounting transition. Stakeholders have raised concerns about the need to reassess previous accounting determinations related to those contracts. Stakeholders also have raised concerns about the hedge accounting consequences of the discounting transition. Because of the potential diversity in practice under current GAAP, timely standard setting was needed to ensure consistent application of available exceptions and optional expedients in Topic 848 for all derivative instruments and hedging relationships affected by the discounting transition.

Benefits and Costs

BC7. 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.

BC8. The Board concluded that the amendments in this proposed Update would reduce or mitigate the costs and complexity of accounting for contract modifications and hedging relationships affected by reference rate reform by providing optional expedients and exceptions to existing accounting requirements. Given the pervasiveness of contracts affected by reference rate reform, and the discounting transition in particular, the Board notes that the proposed scope clarification would provide cost savings to a wide array of financial statement preparers. Furthermore, the proposed amendments would result in financial reporting that reflects the intended continuation of contracts and hedging relationships. The Board determined that reassessing prior derivative accounting conclusions and discontinuing hedge accounting because of the discounting transition would not provide decision-useful information to users of financial statements. Overall, the Board concluded that the expected benefits, including cost savings for financial statement preparers, would justify any expected costs of adopting the proposed amendments.

Basis for Conclusions

Scope

BC9. The current scope of Topic 848 is limited to contracts and transactions that reference LIBOR or a reference rate that is expected to be discontinued as a result 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.

BC10. The Board recognizes that the current scope of Topic 848 precludes derivative instruments that are affected by the discounting transition from qualifying for relief if the derivative does not reference LIBOR or another rate expected to be discontinued due to reference rate reform. However, the Board observes that the changes being made to those derivative instruments because of the discounting transition also would stem from reference rate reform. Furthermore, the nature of the changes arising from the discounting transition are consistent, in a broad sense, with the notion of modifications "related to the replacement of a reference rate" under the criteria in paragraph 848-20-15-5. Specifically, paragraph 848-20-15-5(h), which indicates that changes that are necessary to comply with laws or regulations or to align with market conventions for the replacement rate, is an illustration of the type of event that the Board considered to be related to the replacement of a reference rate.

BC11. The Board acknowledges that the inability to qualify for accounting relief puts an operational burden on market participants with derivatives indexed to reference rates that are continuing after reference rate reform (for example, the Effective Federal Funds Rate [EFFR]) when those derivatives are undergoing the same discounting transition as derivatives that are indexed to reference rates that are expected to be discontinued because of reference rate reform (for example, LIBOR). The Board concluded that the financial reporting outcomes of reassessing accounting conclusions for such derivative contracts and for hedging relationships that include those derivatives as hedging instruments would not provide decision-useful information to users of financial statements.

BC12. For those reasons, the Board decided to refine the scope of Topic 848 to include derivatives affected by the discounting transition that do not reference LIBOR or another rate expected to be discontinued due to reference rate reform. As a result, certain provisions of the guidance in Topic 848, if elected by an entity, would apply to derivative instruments that use an interest rate for margining, discounting, or contract price alignment that is modified as a result of reference rate reform that do not reference a rate being discontinued due to reference rate reform.

BC13. The Board concluded that the proposed scope refinement would result in financial reporting that better reflects the economic substance of derivative instruments and transactions affected by the discounting transition. The Board observed that the discounting transition, in and of itself, should not cause entities to reassess previous accounting conclusions or result in the discontinuation of hedge accounting if those hedge relationships would otherwise continue to be highly effective.

BC14. As a consequence of refining the scope of Topic 848 to include derivative instruments affected by the discounting transition that do not reference LIBOR or another rate expected to be discontinued as a result of reference rate reform, those derivative instruments would be eligible for the contract modification relief in Topic 848. Specifically, modifications related to reference rate reform would not be considered an event that requires reassessment of previous accounting conclusions. An entity may elect to apply the contract modification relief in Subtopic 848-20 to derivative instruments that change the interest rate used for margining, discounting, or contract price alignment separately from when it elects to apply that guidance to account for other derivative contract modifications that meet the scope of Subtopic 848-20.

BC15. The scope refinement in this proposed Update also would provide for certain of the exceptions and optional expedients for applying hedge accounting guidance to be applied to derivative instruments that are subject to the discounting transition but that do not reference a rate that is expected to be discontinued as a result of reference rate reform. The proposed amendments would extend the following relief to address potential challenges for applying hedge accounting for such hedging relationships:

a. For a derivative designated as a hedging instrument in a fair value, cash flow, or net investment hedge, an entity would be permitted to continue hedge accounting rather than consider the discounting transition to cause a change in critical terms of the hedging relationship, which would otherwise require an entity to dedesignate the hedging relationship.
b. For a fair value or cash flow hedging relationship, including those accounted for using a method that assumes perfect hedge effectiveness, upon the discounting transition, an entity would be permitted to add one or more basis swaps, or proportions of those basis swaps, to be jointly designated as the hedging instrument, without dedesignation. The Board viewed this as consistent with the election in Topic 848 to add a basis swap to an existing hedge affected by a change to a derivative's reference rate. In that circumstance, because a central counterparty may require a participant to enter into one or more basis swaps in connection with the discounting transition, market participants may wish to incorporate those derivatives into existing hedging relationships. An entity

also would be allowed to subsequently remove those derivatives from the hedging relationship without dedesignation. If the affected hedge was previously applying an assessment method that assumes perfect effectiveness, an entity could continue to apply that method. However, if a basis swap is added to an existing hedging relationship accounted for under the shortcut method in connection with the discounting transition, the application of relief related to the continuation of the shortcut method would expire as of the sunset date in Topic 848. This is because changing the hedging instrument differs from the nature of a one-time adjustment to the hedging relationship that would run off in future periods (such as adjustments to the fair value hedge basis adjustment arising from the election to change the benchmark rate), as contemplated by the Board in allowing continued use of the shortcut method for the remainder of the fair value hedging relationship in Topic 848.

c. For a derivative designated as a hedging instrument in a fair value, cash flow, or net investment hedge, upon the discounting transition, an entity would be permitted 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.

BC16. Stakeholders also noted several unique accounting complexities that may arise for existing fair value and cash flow hedging relationships due to the discounting transition. Those complexities relate to the change in the discount rate and, in the case of cash flow hedges, may arise as a result of the accounting for the cash compensation payment (or equivalent) that may be exchanged to neutralize the effect of the change in the fair value of the derivative instrument as part of the discounting transition. Stakeholders indicated that those hedge accounting complexities may arise for both derivatives that reference a rate that is expected to be discontinued as a result of reference rate reform and those that reference a rate that is expected to continue thereafter.

BC17. Specifically, if the change in the fair value of the hedging instrument related to the discounting transition in a cash flow hedge is not reflected in accumulated other comprehensive income because of the neutralizing adjustment, there could be a mismatch between the fair value of the derivative and the amount deferred in accumulated other comprehensive income. Accordingly, as a consequence of refining the scope of Topic 848 to include derivative instruments affected by the discounting transition, the amendments in this proposed Update would address the following circumstances:

a. In a fair value hedging relationship accounted for under the shortcut method, as a result of the discounting transition, a difference would exist between the fair value of the derivative designated as the hedging instrument and the basis adjustment of the hedged item. A consequence of the proposed scope refinement would provide an entity the option to apply an approach that adjusts the hedged item's cumulative fair value hedge basis adjustment for the amount of that difference using a reasonable method. In that circumstance, an entity could continue to account for the fair value hedge under the shortcut method if the affected hedge was previously applying that method. In the Board's view, this is consistent with the relief provisions related to a change in the benchmark rate in a fair value hedge under the shortcut method as a result of reference rate reform.

b. In a cash flow hedging relationship, upon the discounting transition, a difference may arise between the amount deferred in accumulated other comprehensive income and the fair value of the derivative. Specifically, because of the recognition of the neutralizing adjustment as part of the discounting transition, there could be mismatch between the fair value of the derivative and the amount deferred in accumulated other comprehensive income. A consequence of the proposed scope refinement would allow an entity flexibility in adjusting the amount recorded in accumulated other comprehensive income for the amount of that difference using a reasonable method. In that circumstance, an entity could continue to apply an assessment method that assumes perfect effectiveness if the affected hedge was previously applying that method. In the Board's view, the neutralizing adjustment is similar to the spread adjustment that is expected to be reflected in derivative contracts as a result of the transition from LIBOR (or another rate that is expected to be discontinued) to a replacement rate, which is considered to be related to reference rate reform in paragraph 848-20-15-5(b). The inclusion of that spread adjustment was not intended to disrupt the application of hedge accounting.

The optional expedients in (a) and (b) would apply to hedges with designated hedging instruments that meet the scope of either paragraph 848-10-15-3 or 848-10-15-3A.

Effective Date and Transition

BC18. The Board decided that the amendments in this proposed Update would be effective for all entities upon issuance of a final Accounting Standards Update. Consistent with all exceptions and expedients within Topic 848, the proposed amendments related to the discounting transition would be optional.

BC19. An entity, regardless of whether it has adopted the amendments in Accounting Standards Update No. 2017-12, *Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities*, may elect to apply the amendments in this proposed Update for contract modifications to derivative instruments that change the interest rate used for margining, discounting, or contract price alignment retrospectively as of any date from the beginning of an interim period that includes March 12, 2020, or prospectively to new modifications from any date within an interim period that includes or is after the date of issuance of a final Update, up to the date that financial statements are available to be issued.

BC20. An entity may elect to apply the amendments in this proposed Update to eligible hedging relationships existing as of the beginning of an 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 proposed amendments for an eligible hedging relationship, any adjustments as a result of those elections must be reflected as of the date that the entity applies the election. Consistent with the transition provisions in Update 2020-04, an entity that has not adopted the amendments in Update 2017-12 may apply only certain elements of the hedge accounting relief in this proposed Update before it adopts the amendments in Update 2017-12.

BC21. The Board notes that an entity would 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, with the exception of certain of the optional expedients. This is consistent with the existing sunset provisions within Topic 848 in which the accounting effects of certain optional expedients are recorded over the remaining life of the hedging relationship and that hedging relationship may extend beyond December 31, 2022. The Board also notes that reference rate reform is expected to be temporary in nature, and the objective of the amendments in this proposed Update is to facilitate the effects of reference rate reform on financial reporting for the market-wide transition period in which an entity replaces the use of reference rates with alternative reference rates, including for the purposes of determining discounting, margining, and price alignment adjustments. Therefore, after an entity stops applying the proposed amendments, the entity should apply existing accounting requirements for contract modifications and hedging relationships.

Amendments to the XBRL Taxonomy

The provisions of this Exposure Draft, if finalized as proposed, would require improvements to the U.S. GAAP Financial Reporting Taxonomy (Taxonomy). We welcome comments on these proposed improvements to the Taxonomy at xbrled@fasb.org. After the FASB has completed its deliberations and issued a final Accounting Standards Update, the proposed improvements to the Taxonomy will be finalized as part of the annual release process.