

(Tentative translation)

**[VII] "The Exposure Draft of Practical Solution on the Treatment of Hedge Accounting
for Financial Instruments that Reference LIBOR" released by the ASBJ**

- At the 405th Accounting Standards Board of Japan (ASBJ) meeting held in March 2019, the Standards Advisory Council, the advisory body to the ASBJ, proposed that the ASBJ should comprehensively address the accounting issues arising from the benchmark reform, including the necessity of developing standards, in a timely manner. In response to the proposal, the ASBJ decided to undertake the development of accounting standards in November 2019. After due consideration, the ASBJ has released the Exposure Draft of Practical Solution on the Treatment of Hedge Accounting for Financial Instruments that Reference LIBOR (Exposure Draft of the Practical Issue Task Force [PITF], No. 59, hereinafter referred to as the "Exposure Draft") on June 3, 2020.¹

Outline of the PITF

- With regard to financial instruments referencing LIBOR, the PITF aims to provide accounting relief for contract modifications and renewal that are to be carried out to keep the economic effect of the contracts essentially equivalent before and after the benchmark replacement.
- Before the benchmark replacement, the PITF mainly provides the following optional expedients.
 - With regard to the quantitative effectiveness test of the principle-based hedge accounting, an entity may conduct preliminary testing on the assumption that reference rates of the hedging instrument and the hedged item remain unchanged. In addition, even in a case where the hedge relationship is not deemed highly effective, as a result of the post-testing, the hedge accounting may be continued.
 - An entity may assume that reference rates of the hedging instrument and the hedged item remain unchanged when judging whether the hedging relationship meets the requirements for the exceptional accounting of interest rate swaps.
- After the benchmark replacement, an entity may apply the optional expedients for the post-testing of the hedge accounting and the exceptional accounting of interest rate swaps until the business year ending on and before March 31, 2023.²

¹ For details, see the ASBJ's website (https://www.asb.or.jp/en/jp-gaap/exposure_drafts/y2020/2020-0603.html). The deadline for comments is August 3, 2020.

² The deadline has been set approximately a year after the scheduled discontinuation of LIBOR.

Schedule for application

- The accounting and disclosure treatments proposed in the Exposure Draft may be adopted on or after the publication date of the PITF.
- An entity may elect the optional expedients for hedging relationships on an individual hedging relationship basis.
- Meanwhile, due to a number of uncertainties regarding the practice of selecting replacement benchmarks and the hedging behavior of entities, the expedients after the benchmark replacement will be reviewed approximately one year after the finalization of the Exposure Draft.
- The Cross-Industry Committee on Japanese Yen Interest Rate Benchmarks welcomes the release of the Exposure Draft by the ASBJ and expects each entity to make progress on necessary deliberations and preparations, as they reference the Exposure Draft and take advice from auditing firms.