

No. 2025-09  
November 2025

## Derivatives and Hedging (Topic 815)

### Hedge Accounting Improvements

An Amendment of the *FASB Accounting Standards Codification*®

The *FASB Accounting Standards Codification*<sup>®</sup> 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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Financial Accounting Standards Board  
801 Main Avenue • Norwalk, CT • 06851

# Accounting Standards Update 2025-09

## Derivatives and Hedging (Topic 815)

### Hedge Accounting Improvements

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## CONTENTS

	Page Numbers
Summary.....	1–5
Amendments to the <i>FASB Accounting Standards Codification</i> <sup>®</sup> .....	6–84
Background Information and Basis for Conclusions.....	85–126
Amendments to the GAAP Taxonomy .....	127

## Summary

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

The FASB is issuing this Update to clarify certain aspects of the guidance on hedge accounting and to address several incremental hedge accounting issues arising from the global reference rate reform initiative.

In 2017, the FASB issued Accounting Standards Update No. 2017-12, *Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities*, to better portray the economic results of an entity's risk management activities in its financial statements and to make certain targeted improvements to simplify the application of the hedge accounting guidance. After the issuance of Update 2017-12, stakeholders asked the Board to clarify certain aspects of the amendments of that Update. In 2019, the Board issued a proposed Accounting Standards Update, *Derivatives and Hedging (Topic 815): Codification Improvements to Hedge Accounting*, to clarify certain areas of the guidance to better align with the objective articulated in Update 2017-12. Stakeholders indicated that the amendments in the 2019 proposed Update would not sufficiently resolve certain issues. In addition, in response to the 2021 Invitation to Comment, *Agenda Consultation*, stakeholders identified several areas of the hedge accounting guidance requiring further updates to address the effects of reference rate reform on hedge accounting.

Consistent with the original objective of Update 2017-12, the objective of this Update is to more closely align hedge accounting with the economics of an entity's risk management activities. The amendments included in the five issues addressed in this Update are intended to better reflect those strategies in financial reporting by enabling entities to achieve and maintain hedge accounting for highly effective economic hedges of forecasted transactions.

### Who Is Affected by the Amendments in This Update?

The amendments in this Update apply to any entity that elects to apply hedge accounting in accordance with Topic 815.

# What Are the Main Provisions, How Do the Main Provisions Differ from Current Generally Accepted Accounting Principles (GAAP), and Why Are They an Improvement?

## Issue 1: Similar Risk Assessment for Cash Flow Hedges

The amendments in this Update expand the hedged risks permitted to be aggregated in a group of individual forecasted transactions in a cash flow hedge by changing the requirement to designate a group of individual forecasted transactions from having a *shared* risk exposure to having a *similar* risk exposure. Entities are required to assess risk similarity both at hedge inception and on an ongoing basis. The amendments also clarify that a group of individual forecasted transactions can be considered to have a similar risk exposure if the derivative used as the hedging instrument is highly effective against each hedged risk in the group. In addition, in some cases, entities are permitted to perform an ongoing qualitative assessment of whether a group of individual forecasted transactions has a similar risk exposure.

The amendments in this Update improve GAAP by expanding the hedged risks permitted to be aggregated in a group of individual forecasted transactions, thereby enabling entities to apply hedge accounting to potentially broader portfolios of forecasted transactions. Entities that aggregate larger groups of individual forecasted transactions in accordance with the amendments can achieve hedge accounting in a more efficient, cost-effective manner while reducing the risk of missed forecasts for highly effective economic hedges. Furthermore, the amendments improve operability and foster consistent application of the similar risk assessment. Therefore, an entity's financial statements can provide more relevant information to investors about the entity's risk management activities related to cash flow hedges of groups of forecasted transactions.

## Issue 2: Hedging Forecasted Interest Payments on Choose-Your-Rate Debt Instruments

The amendments in this Update provide a model to facilitate the application of cash flow hedge accounting to forecasted interest payments on variable-rate debt instruments with contractual terms that permit the borrower to change the interest rate index and interest rate tenor (that is, reset frequency) upon which interest is accrued (commonly referred to as “choose-your-rate” debt instruments). Under the choose-your-rate debt model, the contractual terms of the debt agreement specify the alternative interest rate indexes and interest rate tenors that an entity may select as being hedged during the hedging relationship without discontinuing hedge accounting. When applying this model, an entity may use simplified assumptions to assess both the probability of forecasted transactions occurring and hedge effectiveness. An entity may apply this model to existing, forecasted issuances of, and subsequent replacements of choose-your-rate debt. Entities are prohibited from applying this guidance by analogy to other circumstances.

The amendments in this Update improve GAAP by establishing an operable model that enables hedge accounting to be applied more broadly to choose-your-rate debt and address existing diversity in practice. Furthermore, the amendments mitigate the risk of hedge dedesignation events and missed forecasts for hedges of choose-your-rate debt. As a result, the amendments allow entities to more consistently reflect the economics of risk management strategies in their financial statements.

## Issue 3: Cash Flow Hedges of Nonfinancial Forecasted Transactions

The amendments in this Update expand hedge accounting for forecasted purchases and sales of nonfinancial assets. Subject to meeting specific criteria, entities are permitted to apply hedge accounting for eligible components of forecasted spot-market transactions, forward-market transactions, and subcomponents of explicitly referenced components in an agreement’s pricing formula. To qualify for hedge designation, the variable price component of the forecasted purchase or sale of a nonfinancial asset is required to meet the criteria to be considered clearly and closely related to the nonfinancial asset being purchased or sold, as provided in the current normal purchases and normal sales scope exception.

The amendments in this Update improve GAAP because the application of hedge accounting will not be limited by whether the execution of the nonfinancial purchase or sale transaction is in the spot or forward market. Relative to current GAAP, which limits designation of nonfinancial components to those that are contractually specified, a model based on the clearly-and-closely-related criteria permits hedge accounting for eligible components of forecasted spot-market transactions, forward-market transactions, and subcomponents of explicitly referenced components in an agreement's pricing formula. Furthermore, the amendments also may enable entities to reduce missed forecasts for highly effective economic hedges, more closely aligning hedge accounting with the economics of entities' risk management activities.

The amendments in this Update also clarify that entities may designate a variable price component in a contract that is accounted for as a derivative as the hedged risk if all other hedge criteria are satisfied. That clarification improves GAAP because it resolves diversity in practice about whether hedge accounting may be applied in those situations and allows hedge accounting to be applied to highly effective economic hedges.

#### Issue 4: Net Written Options as Hedging Instruments

The amendments in this Update on the use of net written options as hedging instruments improve GAAP by updating the hedge accounting guidance to accommodate differences in the loan and swap markets that developed after the cessation of the London Interbank Offered Rate. Specifically, the amendments in this Update eliminate the requirement to apply the net written option test to a compound derivative comprising a swap and a written option designated as the hedging instrument in a cash flow hedge or a fair value hedge of interest rate risk.

#### Issue 5: Foreign-Currency-Denominated Debt Instrument as Hedging Instrument and Hedged Item (Dual Hedge)

The amendments in this Update eliminate the recognition and presentation mismatch related to a dual hedge strategy (that is, a hedge for which a foreign-currency-denominated debt instrument is both designated as the hedging instrument in a net investment hedge and designated as the hedged item in a fair value hedge of interest rate risk). The amendments require that an entity exclude the debt instrument's fair value hedge basis adjustment from the net

investment hedge effectiveness assessment. As a result, an entity immediately recognizes in earnings the gains and losses from the remeasurement of the debt instrument's fair value hedge basis adjustment at the spot exchange rate. Entities are prohibited from applying this guidance by analogy to other circumstances.

The amendments in this Update improve GAAP by enabling entities that utilize dual hedging strategies to reflect the economic offset of changes attributable to both interest rate risk and foreign exchange risk.

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

For public business entities, the amendments in this Update are effective for annual reporting periods beginning after December 15, 2026, and interim periods within those annual reporting periods. For entities other than public business entities, the amendments are effective for annual reporting periods beginning after December 15, 2027, and interim periods within those annual reporting periods. Early adoption is permitted on any date on or after the issuance of this Update.

Entities should apply the amendments in this Update on a prospective basis for all hedging relationships. An entity may elect to adopt the amendments in this Update for hedging relationships that exist as of the date of adoption.

Upon adoption of the amendments in this Update, entities are permitted to modify certain critical terms of certain existing hedging relationships without dedesignating the hedge.

# Amendments to the *FASB Accounting Standards Codification*<sup>®</sup>

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## Summary of Amendments to the Accounting Standards Codification

1. The following table provides a summary of the amendments to the Accounting Standards Codification.

Codification Section	Description of Changes
Subtopic 815-20, Derivatives and Hedging—Hedging—General	<p><b>Issue 1: Similar Risk Assessment for Cash Flow Hedges</b></p> <ul style="list-style-type: none"> <li>• Amended paragraph 815-20-25-3(d)(2) to require formal documentation, at hedge inception, of the method that will be used to determine whether a group of individual forecasted transactions have a similar risk exposure.</li> <li>• Amended paragraph 815-20-25-15(a)(2) to clarify that a group of individual transactions must have a similar risk exposure to be designated as a hedged transaction in a cash flow hedge.</li> <li>• Amended paragraph 815-20-55-23 to require that individual forecasted transactions have a similar risk exposure both at hedge inception and on an ongoing basis.</li> <li>• Added implementation guidance in paragraphs 815-20-55-23A through 55-23D to clarify how an entity should assess whether a group of forecasted transactions in a cash flow hedge have a similar risk exposure.</li> </ul>

Codification Section	Description of Changes
	<ul style="list-style-type: none"> <li>• Amended paragraph 815-20-55-33A to cross-reference to paragraph 815-20-55-96A.</li> <li>• Amended paragraph 815-20-55-56 to clarify that changing the method designated to assess similar risk exposure requires the dedesignation of the original hedging relationship.</li> <li>• Amended the illustrative example beginning in paragraph 815-20-55-88 and added paragraphs 815-20-55-89B, 815-20-55-96A, and 815-20-55-99A through 55-99E to illustrate different approaches to designate variable interest payments on a group of variable-rate, interest-bearing loans as the hedged item.</li> </ul> <p><b>Issue 2: Hedging Forecasted Interest Payments on Choose-Your-Rate Debt Instruments</b></p> <ul style="list-style-type: none"> <li>• Amended paragraph 815-20-25-3 to refer to the guidance on changing the contractually specified interest rate for hedges of forecasted interest payments on choose-your-rate debt instruments.</li> <li>• Amended paragraphs 815-20-25-79 through 25-79A and added paragraph 815-20-25-79B to clarify the requirements of the quantitative prospective assessment of hedge effectiveness for cash flow hedges of forecasted interest payments on choose-your-rate debt instruments.</li> <li>• Amended paragraph 815-20-55-56 to clarify that changes in the contractually specified interest rate on choose-your-rate debt</li> </ul>

Codification Section	Description of Changes
	<p>instruments do not result in automatic dedesignation of the hedging relationship if certain conditions are met.</p> <p><b>Issue 3: Cash Flow Hedges of Nonfinancial Forecasted Transactions</b></p> <ul style="list-style-type: none"> <li>• Amended paragraph 815-20-25-3(d)(1)(vii) to require documentation of the component (or subcomponent) being designated as the hedged risk in a cash flow hedge of the forecasted purchase or sale of a nonfinancial asset.</li> <li>• Amended paragraph 815-20-25-15(e) to add an example illustrating that a variable price component or subcomponent can be designated as the hedged risk in a forecasted purchase or sale of a nonfinancial item under a contract that is accounted for as a derivative.</li> <li>• Amended paragraph 815-20-25-15(i)(3) to permit designation of the risk of changes in the cash flows relating to a component (or subcomponent) of the price of a nonfinancial asset that is clearly and closely related to the purchase price or sales price of the nonfinancial asset.</li> <li>• Superseded the guidance in paragraphs 815-20-25-22A through 25-22B for hedging contractually specified components in cash flow hedges of a forecasted purchase or sale of a nonfinancial asset.</li> <li>• Added paragraph 815-20-25-22C to provide additional criteria for designating the variability in cash flows attributable to changes in a</li> </ul>

Codification Section	Description of Changes
	<p>component (or subcomponent) of the price of a nonfinancial asset as the hedged risk.</p> <ul style="list-style-type: none"> <li>• Amended paragraphs 815-20-25-46B, 815-20-25-77, 815-20-25-84, and 815-20-55-79P to remove the references to contractually specified components.</li> <li>• Amended the navigation guidance included in paragraph 815-20-55-17 related to implementation guidance on hedged items in cash flow hedges.</li> <li>• Added implementation guidance in paragraphs 815-20-55-18A through 55-18D and amended paragraph 815-20-55-19 on designating a variable price component (or subcomponent) as the hedged risk in a cash flow hedge of a forecasted transaction to purchase or sell a nonfinancial asset.</li> <li>• Superseded the implementation guidance in paragraphs 815-20-55-26A through 55-26E on the contractually specified component model for hedging nonfinancial assets.</li> </ul> <p><b>Issue 4: Net Written Options as Hedging Instruments</b></p> <ul style="list-style-type: none"> <li>• Amended paragraph 815-20-25-88 to specify that in a cash flow hedge or a fair value hedge of interest rate risk a compound derivative instrument comprising a written option and a swap should not be considered a written option for purposes of the net written option test.</li> </ul>

Codification Section	Description of Changes
	<p data-bbox="630 325 1339 445"><b>Issue 5: Foreign-Currency-Denominated Debt Instrument as Hedging Instrument and Hedged Item (Dual Hedge)</b></p> <ul data-bbox="630 478 1339 1003" style="list-style-type: none"> <li data-bbox="630 478 1339 808">• Amended implementation guidance in paragraph 815-20-55-38 to require that an entity exclude from the assessment of effectiveness in the net investment hedging relationship the fair value hedge basis adjustment resulting from designating the foreign-currency-denominated debt instrument in the fair value hedge.</li> <li data-bbox="630 842 1339 1003">• Amended paragraph 815-20-55-129 of the illustrative example that demonstrates how an entity should perform the hedge effectiveness assessment for dual hedges.</li> </ul>
<p data-bbox="272 1045 581 1207">Subtopic 815-30, Derivatives and Hedging—Cash Flow Hedges</p>	<p data-bbox="630 1045 1274 1123"><b>Issue 1: Similar Risk Assessment for Cash Flow Hedges</b></p> <ul data-bbox="630 1157 1339 1360" style="list-style-type: none"> <li data-bbox="630 1157 1339 1360">• Amended paragraphs 815-30-55-147 through 55-148 of the illustrative example that demonstrates an entity utilizing the similar risk assessment for a forecasted purchase of inventory.</li> </ul> <p data-bbox="630 1394 1193 1507"><b>Issue 2: Hedging Forecasted Interest Payments on Choose-Your-Rate Debt Instruments</b></p> <ul data-bbox="630 1541 1339 1785" style="list-style-type: none"> <li data-bbox="630 1541 1339 1785">• Amended paragraph 815-30-35-8 to remove a change in the designated hedged risk from the list and replace it with a change in the contractually specified interest rate for forecasted interest payments on choose-your-rate debt instruments.</li> </ul>

Codification Section	Description of Changes
	<ul style="list-style-type: none"> <li>• Superseded paragraph 815-30-35-37A and added paragraphs 815-30-35-37B through 35-37M to provide guidance for changing the contractually specified interest rate for hedges of forecasted interest payments on choose-your-rate debt instruments.</li> <li>• Amended the illustrative example beginning in paragraph 815-30-55-60 to illustrate the application of the guidance to changes in a cash flow hedge of forecasted interest payments with an interest rate swap.</li> <li>• Added paragraphs 815-30-55-165 through 55-181 to provide an illustrative example of the guidance in paragraphs 815-30-35-37B through 35-37M.</li> </ul> <p><b>Issue 3: Cash Flow Hedges of Nonfinancial Forecasted Transactions</b></p> <ul style="list-style-type: none"> <li>• Amended paragraphs 815-30-55-2 through 55-4 to update the illustrative example to reflect the nonfinancial component hedging model.</li> <li>• Amended paragraphs 815-30-55-20 through 55-23 to update the illustrative example to reflect the nonfinancial component hedging model.</li> <li>• Amended paragraph 815-30-55-41 to update the illustrative example to remove the reference to contractually specified components.</li> <li>• Amended paragraphs 815-30-55-134 and 815-30-55-138 to update the illustrative example to</li> </ul>

Codification Section	Description of Changes
	<p>reflect the nonfinancial component hedging model.</p> <ul style="list-style-type: none"> <li>• Amended paragraphs 815-30-55-146 through 55-148 to update the illustrative example to reflect the nonfinancial component hedging model.</li> <li>• Added paragraphs 815-30-55-149 through 55-164 to provide illustrative examples of the nonfinancial component hedging model.</li> </ul>

## Introduction

2. The Accounting Standards Codification is amended as described in paragraphs 3–15. 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 underlined, and deleted text is ~~struck out~~.

## Amendments to Master Glossary

3. Supersede the Master Glossary term *Contractually Specified Component*, with a link to transition paragraph 815-20-65-7, as follows:

## **Contractually Specified Component**

An index or price explicitly referenced in an agreement to purchase or sell a nonfinancial asset other than an index or price calculated or measured solely by reference to an entity's own operations.

## **Issue 1: Similar Risk Assessment for Cash Flow Hedges**

### **Amendments to Subtopic 815-20**

4. Amend paragraphs 815-20-25-3(d)(2), 815-20-25-15(a)(2), 815-20-55-23, 815-20-55-33A, 815-20-55-56, 815-20-55-88 through 55-89, 815-20-55-91 through 55-92 and their related heading, 815-20-55-94 through 55-95, and 815-20-55-97 through 55-98 and add paragraphs 815-20-55-23A through 55-23D, 815-20-55-89A through 55-89B, 815-20-55-96A, and 815-20-55-99A through 55-99E and their related heading, with a link to transition paragraph 815-20-65-7, as follows:

## **Derivatives and Hedging—Hedging—General**

### **Recognition**

#### **> Formal Designation and Documentation at Hedge Inception**

**815-20-25-3** Concurrent designation and documentation of a hedge is critical; without it, an entity could retroactively identify a hedged item, a hedged **transaction**, or a method of assessing effectiveness to achieve a desired accounting result. To qualify for hedge accounting, there shall be, at inception of the hedge, formal documentation of all of the following:

- d. Documentation requirement applicable to cash flow hedges only:
  2. For a cash flow hedge of a group of forecasted transactions, the method that will be used to determine whether a group of individual forecasted transactions have a similar risk exposure in accordance with paragraph 815-20-55-23A.

#### **> Eligibility of Hedged Items and Transactions**

- **> Hedged Transaction Criteria Applicable to Cash Flow Hedges Only**

**815-20-25-15** A forecasted transaction is eligible for designation as a hedged transaction in a cash flow hedge if all of the following additional criteria are met:

- a. The forecasted transaction is specifically identified as either of the following:
  1. A single transaction
  2. A group of individual transactions that ~~share the same~~ have a similar risk exposure for which they are designated as being hedged. A forecasted purchase and a forecasted sale shall not both be included in the same group of individual transactions that constitute the hedged transaction.

## Implementation Guidance and Illustrations

### > Implementation Guidance

#### • > Eligibility of Hedged Items

#### • • > Hedged Items in Cash Flow Hedges Only

#### • • • > Grouping Individual Transactions

**815-20-55-20** It sometimes will be impractical (perhaps impossible) and not cost-effective for an entity to identify each individual transaction that is being hedged. An example is a group of sales or purchases over a period of time to or from one or more parties. This Subtopic permits an entity to aggregate individual forecasted transactions for hedging purposes in some circumstances. As it does for a hedge of a single forecasted transaction, paragraph 815-20-25-3(d)(1)(vi) requires that an entity identify the hedged transactions with sufficient specificity that it is possible to determine which transactions are hedged transactions when they occur.

**815-20-55-21** For example, an entity that expects to sell at least 300,000 units of a particular product in its next fiscal quarter might designate the sales of the first 300,000 units as the hedged transactions. Alternatively, it might designate the first 100,000 sales in each month as the hedged transactions. It could not, however, simply designate any sales of 300,000 units during the quarter as the hedged transaction because it then would be impossible to determine whether the first sales transaction of the quarter was a hedged transaction. Similarly, an entity could not designate the last 300,000 sales of the quarter as the

hedged transaction because it would not be possible to determine whether sales early in the quarter were hedged or not.

**815-20-55-22** Under the guidance in this Subtopic, a single derivative instrument of appropriate size could be designated as hedging a given amount of aggregated forecasted transactions, such as any of the following:

- a. Forecasted sales of a particular product to numerous customers within a specified time period, such as a month, a quarter, or a year
- b. Forecasted purchases of a particular product from the same or different vendors at different dates within a specified time period
- c. Forecasted interest payments on several variable-rate debt instruments within a specified time period.

**815-20-55-23** ~~At the time of hedge designation only, the~~ The transactions in each group must share the have a similar risk exposure for which they are being hedged. For example, the interest payments in the group in (c) in the preceding paragraph shall vary with the same index to qualify for hedging with a single derivative instrument. To satisfy that requirement, an entity should determine whether the forecasted transactions are expected to have a similar risk exposure prospectively at hedge inception and on an ongoing basis. In addition, an entity should determine whether the forecasted transactions had a similar risk exposure retrospectively on an ongoing basis during the hedge period. An entity should assess similarity each time it assesses hedge effectiveness for a group (for timing of hedge effectiveness assessments, see paragraphs 815-20-25-79 through 25-79A, and for certain private companies and certain not-for-profit entities, see paragraphs 815-20-25-139 through 25-143).

**815-20-55-23A** An entity should determine that the risk exposures being hedged in a group of forecasted transactions are similar by applying either of the following methods:

- a. The entity determines whether the designated hedging instrument is highly effective in achieving offsetting changes in cash flows attributable to each hedged risk in the group, assessed on an individual basis, by applying the guidance in paragraph 815-20-25-79 and paragraphs 815-30-35-10 through 35-32 for assessing hedge effectiveness.

- b. The entity determines whether each hedged risk related to a forecasted transaction hedged in a group is similar to each other hedged risk in the group. In that assessment, an entity should use the same threshold applied to determine whether a relationship is highly effective. When assessing whether hedged risks in a group of forecasted transactions are similar, an entity should consider the guidance in paragraph 815-20-25-79 as well as the guidance in paragraphs 815-30-35-10 through 35-32 for hedges of interest rate risk.

Ordinarily, an entity should apply the selected method consistently to similar hedges. Use of different methods for similar hedges should be justified.

**815-20-55-23B** If an entity applies one of the qualitative methods in paragraph 815-20-25-3(b)(2)(iv)(01) for purposes of assessing hedge effectiveness and it applies the similar risk assessment method described in paragraph 815-20-55-23A(a), it also may assume that the hedged risks related to a group of forecasted transactions are similar because the hedging instrument is considered highly effective qualitatively against each hedged risk in the group.

**815-20-55-23C** After performing an initial quantitative assessment at hedge inception (if required), an entity may elect on a hedge-by-hedge basis to qualitatively assess whether a group of individual forecasted transactions have a similar risk exposure in subsequent periods, if the entity can reasonably support an expectation of similar risk on a qualitative basis, in a manner similar to the guidance in paragraphs 815-20-35-2A through 35-2F. The qualitative assessment used to reasonably support an expectation of high effectiveness also may be used to support an expectation of similar risk exposure if an entity applies the similar risk assessment method described in paragraph 815-20-55-23A(a).

**815-20-55-23D** If an entity determines as part of its ongoing similar risk assessment that one or more hedged risks related to the group of individual forecasted transactions are no longer similar, it should dedesignate the hedging relationship as of the last date when all hedged risks in the group were assessed to have similar risk exposure, unless the entity can determine the specific date that all hedged risks in the group were no longer similar. Amounts previously recognized in accumulated other comprehensive income should remain until the forecasted transactions affect earnings or become probable of not occurring in accordance with paragraphs 815-30-40-4 through 40-6.

• • • > **First-Payments-Received Technique in Hedging Variable Interest Payments on a Group of Loans**

**815-20-55-33A** A first-payments-received technique for identifying the hedged forecasted transactions (that is, the hedged interest payments) may be used in a cash flow hedge of interest rate risk associated with interest payments for a rolling portfolio of prepayable interest-bearing loans (or other interest-bearing financial assets), ~~provided if~~ all other conditions for a cash flow hedge have been met. Such a technique involves identifying the hedged forecasted transactions in a cash flow hedge as the first interest payments based on the contractually specified interest rate received by an entity during each recurring period of a specified length and beginning date for the period covered by the hedging instrument. Example 4, Case A (see paragraphs 815-20-55-91 through 55-96A ~~55-96~~) illustrates this technique.

• > **Hedge Effectiveness**

• • > **Changes in Quantitative Assessment Methods**

**815-20-55-56** This Subtopic permits a hedging relationship to be dedesignated (that is, discontinued) at any time. (See paragraphs 815-25-40-1(c) and 815-30-40-1(c).) If an entity wishes to change any of the critical terms of the hedging relationship (including the method designated for use in assessing hedge effectiveness or the method of assessing similar risk exposure), as documented at inception, the mechanism provided in this Subtopic to accomplish that change is the dedesignation of the original hedging relationship and the designation of a new hedging relationship that incorporates the desired changes. However, as discussed in ~~paragraph 815-30-35-37A,~~ paragraphs 815-30-35-37B through 35-37M, for a cash flow hedge of forecasted interest payments on choose-your-rate debt (and related replacement debt), a change to the hedged risk in a cash flow hedge of a forecasted transaction in the contractually specified interest rate (and associated change in the number and timing of forecasted interest payments within the hedged period, if any) does not result in an automatic dedesignation of the hedging relationship if the conditions in those paragraphs are met ~~hedging instrument continues to be highly effective at achieving offsetting cash flows associated with the hedged item attributable to the revised hedged risk.~~ The dedesignation of an original hedging relationship and the designation of a new hedging relationship ~~represents~~ represent the application of this Subtopic and is not a change in accounting principle under Topic 250, even though the

new hedging relationship may differ from the original hedging relationship only with respect to the method designated for use in assessing the similar risk exposure or hedge effectiveness of that hedging relationship. Although paragraph 815-20-35-19 refers to discontinuing an existing hedging relationship and then designating and documenting a new hedging relationship using an improved method for assessing effectiveness, that reference was not meant to imply that the perceived improved method had to be justified as a preferable method of applying an accounting principle under Topic 250. **[For convenience, this paragraph also contains the amendments from Issue 2.]**

### > Illustrations

#### • > Example 4: Variable Interest Payments on a Group of Variable-Rate, Interest-Bearing Loans as Hedged Item

**815-20-55-88** The following Cases illustrate the implications of ~~two~~ different approaches to designation of variable interest payments on a group of variable-rate, interest-bearing loans:

- a. Designation based on ~~first payments received~~ a single interest rate index under the first-payments-received technique (Case A)
- b. Designation based on a specific group of individual loans (Case B) ~~(Case B)~~.
- c. Designation based on multiple interest rate indexes under the first-payments-received technique (Case C).

**815-20-55-89** For Cases A, B, and C ~~A and B~~, assume that Entities A, B, and C each ~~Entity A and Entity B~~ both make to their respective customers Secured Overnight Financing Rate (SOFR-) ~~London Interbank Offered Rate (LIBOR-)~~ indexed variable-rate loans for which monthly interest payments are based on 30-Day Average SOFR (in arrears) (that is, daily compounded average of SOFR during the past 30 days) ~~due at the end of each calendar quarter, and the LIBOR-based interest rate resets at the end of each quarter for the interest payment that is due at the end of the following quarter.~~ Entity C also originates SOFR-indexed variable-rate loans for which interest payments are based on both 1-Month Term SOFR (that is, 1-month forward-looking SOFR) and 30-Day Average Effective Federal Funds Rate (in arrears) (that is, daily compounded average Effective Federal Funds Rate during the past 30 days). All loans made by Entities A, B, and C have interest rate floors that range from 0 percent to 0.5

percent and reset and payment dates that occur over the course of a month. Both entities determine that they will each always have at least \$100 million of those LIBOR-indexed variable-rate loans outstanding throughout the next 3 years, even though the composition of those loans will likely change to some degree due to prepayments, loan sales, and potential defaults. [Content amended and moved to paragraph 815-20-55-89A]

**815-20-55-89A** Both entities—Entities A and B determine that they will each always have at least \$100 million of 30-Day Average SOFR-indexed (in arrears) those LIBOR-indexed variable-rate loans outstanding throughout the next 3 years, even though the composition of those loans will likely change to some degree due to prepayments, loan sales, and potential defaults. [Content amended as shown and moved from paragraph 815-20-55-89] Entity C determines that it will always have at least \$100 million of variable-rate loans outstanding indexed to any combination of 30-Day Average SOFR (in arrears), 1-Month Term SOFR, and 30-Day Average Effective Federal Funds Rate (in arrears) throughout the next 3 years.

**815-20-55-89B** Entities A, B, and C each execute a 3-year, receive-fixed, pay-variable (30-Day Average SOFR [in arrears]) interest rate swap with a \$100 million notional amount that settles at the end of each calendar month. Each interest rate swap does not include a floor and has a fair value of \$0 at inception.

**815-20-55-90** This Example does not address cash flow hedging relationships in which the hedged risk is the risk of overall changes in the hedged cash flows related to an asset or liability, as discussed in paragraph 815-20-25-15(j)(1).

**• • > Case A: Designation Based on a Single Interest Rate Index under the First-Payments-Received Technique ~~First Payments Received~~**

**815-20-55-91** In this Case, Entity A designates the 30-Day Average SOFR (in arrears) interest rate swap (described in paragraph 815-20-55-89B) as hedging the cash flow variability attributable to changes in the first interest payments received during each month for the next 3 years on \$100 million principal of 30-Day Average SOFR-indexed (in arrears) variable-rate loans. wishes to hedge its interest rate exposure to changes in the quarterly interest receipts on \$100 million principal of those LIBOR-indexed variable-rate loans by entering into a 3-year interest rate swap that provides for quarterly net settlements based on

~~Entity A receiving a fixed interest rate on a \$100 million notional amount and paying a variable LIBOR-based rate on a \$100 million notional amount.~~

~~**815-20-55-92** In a cash flow hedge of interest rate risk, Entity A may identify the hedged forecasted transactions as the first LIBOR-based interest payments received by Entity A during each 4-week period that begins 1 week before each quarterly due date for the next 3 years that, in the aggregate for each quarter, are payments on \$100 million principal of its then existing LIBOR-indexed variable-rate loans. The LIBOR-based Any 30-Day Average SOFR-indexed (in arrears) interest payments received by Entity A after it has received payments on \$100 million aggregate principal would be unhedged interest payments for that period quarter.~~

~~**815-20-55-93** The hedged forecasted transactions for Entity A in this Case are described with sufficient specificity so that when a transaction occurs, it is clear whether that transaction is or is not the hedged transaction.~~

~~**815-20-55-94** Because Entity A has designated the hedging relationship as hedging the risk of changes attributable to changes in the 30-Day Average SOFR (in arrears) LIBOR interest rate in Entity A's first LIBOR-based 30-Day Average SOFR (in arrears) interest payments received, any prepayment, sale, or credit difficulties related to an individual 30-Day Average SOFR-indexed (in arrears) LIBOR-indexed variable-rate loan would not necessarily affect the designated hedging relationship.~~

~~**815-20-55-95** Provided Entity A determines it is probable that it will continue to receive interest payments on at least \$100 million principal of its then existing LIBOR-indexed 30-Day Average SOFR-indexed (in arrears) variable-rate loans, Entity A can conclude that the hedged forecasted transactions in the documented cash flow hedging relationships are probable of occurring.~~

~~**815-20-55-96** An entity may not assume perfect effectiveness in such a hedging relationship as described in paragraph 815-20-25-102 because the hedging relationship does not involve hedging the interest payments related to the same recognized interest-bearing loan throughout the life of the hedging relationship. Consequently, at a minimum, Entity A must consider the timing of the hedged cash flows vis-à-vis the swap's cash flows when assessing effectiveness.~~

**815-20-55-96A** Entity A elects to assess similar risk exposure for the group of forecasted transactions by determining that the designated hedging instrument is highly effective against each hedged risk in the group in accordance with the method outlined in paragraph 815-20-55-23A(a) and determines that the similar risk exposure requirement is met. Entity A also utilizes that same assessment to satisfy the initial prospective effectiveness assessment. In performing that assessment, Entity A considers the differences between the individual forecasted transactions in the group and the contractual terms of the hedging instrument. Those differences include, for example, payment dates, reset dates, and interest rate floors.

**• • > Case B: Designation Based on a Specific Group of Individual Loans**

**815-20-55-97** In this Case, Entity B designates the 30-Day Average SOFR (in arrears) interest rate swap (described in paragraph 815-20-55-89B) as hedging the cash flow variability attributable to changes in the interest payments received during each month for the next 3 years ~~wishes to hedge its interest rate exposure to changes in the quarterly interest receipts on \$100 million principal of those LIBOR-indexed variable-rate loans by entering into a 3-year interest rate swap that provides for quarterly net settlements based on Entity B receiving a fixed interest rate on a \$100 million notional amount and paying a variable LIBOR-based rate on a \$100 million notional amount. Entity B initially designates cash flow hedging relationships of interest rate risk and identifies as the related hedged forecasted transactions each of the variable interest receipts on a specified group of individual 30-Day Average SOFR-indexed (in arrears) LIBOR-indexed variable-rate loans aggregating \$100 million principal but then some of those loans experience prepayments, are sold, or experience credit difficulties.~~ Entity B elects to assess similar risk exposure in accordance with the method outlined in paragraph 815-20-55-23A(a). Consistent with the differences considered by Entity A in paragraph 815-20-55-96A, Entity B should consider differences between the individual forecasted transactions in the group and the contractual terms of the hedging instrument, including, for example, payment dates, reset dates, and interest rate floors.

**815-20-55-98** After designation, some of the specifically identified loans experience prepayments, are sold, or experience credit difficulties. This Case addresses whether the original cash flow hedging relationships remain intact if the composition of the group of loans whose interest payments are the hedged forecasted transactions is changed by replacing the principal amount of the

specified loans that experience a prepayment, have been sold, or experience a change in **expected cash flows** due to credit difficulties with similar variable-rate interest-bearing loans. Entity B cannot conclude that the original cash flow hedging relationships have remained intact if the composition of the group of loans whose interest payments are the hedged forecasted transactions is changed by replacing the principal amount of the originally specified loans with similar variable-rate interest-bearing loans. Paragraph 815-20-25-15(a) requires that, for a cash flow hedge, the forecasted transaction be specifically identified as a single transaction or group of transactions. At inception, the entity designated cash flow hedging relationships for each of the variable interest receipts on a specified group of variable-rate loans. If a loan within the group experiences a prepayment, has been sold, or experiences an unexpected change in its **{remove glossary link}expected cash flows{remove glossary link}** due to credit difficulties, the remaining hedged interest payments to Entity B specifically related to that loan are now no longer probable of occurring. Pursuant to paragraphs 815-30-40-1 through 40-3, Entity B must discontinue the hedging relationships with respect to the hedged forecasted transactions that are now no longer probable of occurring. However, had the hedged forecasted transactions been designated in a manner similar to that described in Case A, the consequences of a loan's prepayment, a loan sale, or an unexpected change in a loan's expected cash flows due to credit difficulties would not have been the same. How the forecasted transaction in a cash flow hedge is designated can have a significant effect on the application of the Derivatives and Hedging Topic.

**815-20-55-99** Changing the composition of the specified individual loans within the group of variable-rate interest-bearing loans due to prepayment, a loan sale, or an unexpected change in a loan's expected cash flows due to credit difficulties reflects a change in the probability of the identified hedged forecasted transactions for the hedging relationships related to the individual loans removed from the group of variable-rate interest-bearing loans. Consequently, the hedging relationships for future interest payments that are no longer probable of occurring must be terminated. The provisions related to immediately reclassifying a derivative instrument's gain or loss out of accumulated other comprehensive income into earnings are based on the hedged forecasted transaction being probable that it will not occur—not no longer being probable of occurring—and includes consideration of an additional two-month period of time. After the discontinuation of the hedging relationships for interest payments related to the individual loans removed from

the group of variable-rate interest-bearing loans and the reclassification into earnings of the net gain or loss in accumulated other comprehensive income related to those hedging relationships, the derivative instrument (or a proportion thereof) specifically related to the hedging relationships that have been terminated is eligible to be redesignated as the hedging instrument in a new cash flow hedging relationship. However, paragraph 815-30-40-5 warns that a pattern of determining that hedged forecasted transactions are probable of not occurring would call into question both the entity's ability to accurately predict forecasted transactions and the propriety of using hedge accounting in the future for similar forecasted transactions.

**• • > Case C: Designation Based on Multiple Interest Rate Indexes under the First-Payments-Received Technique**

**815-20-55-99A** In this Case, Entity C designates the 30-Day Average SOFR (in arrears) interest rate swap (described in paragraph 815-20-55-89B) as hedging cash flow variability in the first interest payments received during each month for the next 3 years attributable to the contractually specified interest rates on \$100 million of variable rate loans indexed to any combination of 30-Day Average SOFR (in arrears), 1-Month Term SOFR, and 30-Day Average Effective Federal Funds Rate (in arrears).

**815-20-55-99B** By designating the hedged forecasted transactions as the first interest payments received on 30-Day Average SOFR-indexed (in arrears), 1-Month Term SOFR-indexed, and 30-Day Average Effective Federal Funds Rate-indexed (in arrears) variable-rate loans, Entity C considers the first interest payments on any of those loans as the hedged forecasted transactions when they occur. This method of designation allows Entity C to fulfill its forecasted transactions across a broader population of loans if any variable-rate loans experience a prepayment, are sold, or experience a change in its expected cash flows related to credit difficulties.

**815-20-55-99C** If Entity C elects to assess similar risk exposure for the group of forecasted transactions using the method outlined in paragraph 815-20-55-23A(a) and determines that the similar risk exposure requirement is met, then Entity C also may reasonably conclude that the hedging relationship is expected to be highly effective at hedge inception if it documents the method described in paragraph 815-20-55-23A(a) as its method for assessing hedge effectiveness. Entity C should consider the differences between the individual forecasted transactions in the group and the contractual terms of the hedging

instrument when performing those assessments. Those differences include, for example, interest rates, payment dates, reset dates, and interest rate floors.

**815-20-55-99D** Alternatively, if Entity C elects to assess similar risk exposure for the group of forecasted transactions using the method in paragraph 815-20-55-23A(b) and determines that the similar risk exposure requirement is met, then Entity C should perform a separate assessment to conclude that the hedging relationship is expected to be highly effective at hedge inception. Entity C should use the concepts underlying assessments of hedge effectiveness, such as the hypothetical derivative method and regression analysis, when assessing whether each hedged risk is similar to each other risk in the group. Entity C should consider the differences between the respective hedged risks of the individual forecasted transactions in the group when performing the similar risk exposure assessment. Those differences include attributes that affect the hedged indexes, for example, interest rates, reset dates, and interest rate floors.

**815-20-55-99E** If Entity C determines as part of its ongoing assessments that one or more hedged risks related to individual forecasted transactions in the group are no longer similar, Entity C should dedesignate the hedging relationship as of the last date when all hedged risks in the group were assessed to have similar risk exposure, unless Entity C can determine the specific date that all hedged risks in the group were no longer similar. However, the determination that one or more hedged risks in the group are no longer similar does not affect Entity C's probability assessment related to the hedged forecasted transactions performed in accordance with paragraphs 815-30-40-4 through 40-6.

## Amendments to Subtopic 815-30

5. Amend paragraphs 815-30-55-147 through 55-148, with a link to transition paragraph 815-20-65-7, as follows:

### **Derivatives and Hedging—Cash Flow Hedges**

#### **Implementation Guidance and Illustrations**

##### **> Illustrations**

• > **Example 23: Designation of a Cash Flow Hedge of a Forecasted Purchase of Inventory for Which Commodity Exposure Is Managed Centrally**

**815-30-55-147** Because Entity Q determined that it will purchase at least 80,000 pounds of plastic each month in the coming 12 months to fulfill its expected manufacturing requirements, it documents that the hedged item (that is, the **forecasted transaction** within each month) is probable of occurring. Entity Q designates each forward contract as a cash flow hedge of the variability in cash flows attributable to changes in the ~~contractually specified~~ explicitly referenced JP index on the first 80,000 pounds of plastic purchased (regardless of grade or plant location delivered to) for the appropriate month. ~~The individual purchases of differing grades of plastic by Plant A and Plant B during each month share the risk exposure to the variability in the purchase price of the plastic attributable to changes in the contractually specified JP index. Therefore, the individual transactions in the hedged portfolio of plastic purchases for each month share the same risk exposure for which they are designated as being hedged in accordance with paragraph 815-20-25-15(a)(2).~~ **[For convenience, this paragraph also contains the amendments from Issue 3.]**

**815-30-55-148** In accordance with paragraph 815-20-25-3(b)(2)(iv)(01)(B), if Entity Q has determined that the critical terms of the hedged item and hedging instrument match, it may elect to assess effectiveness qualitatively both at inception of the hedging relationship and on an ongoing basis on the basis of the following factors in accordance with paragraphs 815-20-25-84 through 25-85:

- a. The hedging instrument's underlying matches the index upon which plastic purchases will be determined (that is, the JP index~~Index~~).
- b. The notional of the hedging instrument matches the forecasted quantity designated as the hedged item.
- c. The date on which the derivatives mature matches the timing in which the forecasted purchases are expected to be made. That is, the quantity of the hedged item, ~~80,000 pounds,~~ (80,000 pounds) is an aggregate amount expected to be purchased over the course of the respective month (that is, the same 31-day period) in which the derivative matures.
- d. Each hedging instrument was traded with at-market terms (that is, it has an initial fair value of zero).

- e. Assessment of effectiveness will be performed on the basis of the total change in the fair value of the hedging instrument.
- f. Although the amount of plastic being hedged each period is a cumulative amount across multiple grades of plastic, the basis differentials between grades of plastic and location are not required to be included in assessments of effectiveness because Entity Q has designated the variability in cash flows attributable to changes in the JP index ~~(the contractually specified component)~~ (the explicitly referenced variable component of the forecasted purchase price) as the hedged risk ~~within its purchases of plastics.~~

In accordance with paragraph 815-20-55-23B, if Entity Q assesses hedge effectiveness in accordance with paragraphs 815-20-25-84 through 25-85 and applies the similar risk assessment method described in paragraph 815-20-55-23A(a), it also may assume that the hedged risks related to the group of forecasted transactions are similar. [For convenience, this paragraph also contains the amendments from Issue 3.]

## Issue 2: Hedging Forecasted Interest Payments on Choose-Your-Rate Debt Instruments

### Amendments to Subtopic 815-20

6. Amend paragraphs 815-20-25-3(b)(2)(iii) and (d)(1)(viii), 815-20-25-79 through 25-79A, and 815-20-55-56 and add paragraph 815-20-25-79B, with a link to transition paragraph 815-20-65-7, as follows:

### **Derivatives and Hedging—Hedging—General**

#### **Recognition**

##### **> Formal Designation and Documentation at Hedge Inception**

**815-20-25-3** Concurrent designation and documentation of a hedge is critical; without it, an entity could retroactively identify a hedged item, a hedged **transaction**, or a method of assessing effectiveness to achieve a desired accounting result. To qualify for hedge accounting, there shall be, at inception of the hedge, formal documentation of all of the following:

- b. Documentation requirement applicable to fair value hedges, cash flow hedges, and net investment hedges:
  - 2. The entity's risk management objective and strategy for undertaking the hedge, including identification of all of the following:
    - iii. The nature of the risk being hedged (also see the requirements in (d)(1)(viii)).
- d. Documentation requirement applicable to cash flow hedges only:
  - 1. For a cash flow hedge of a **forecasted transaction**, documentation shall include all relevant details, including all of the following:
    - viii. If the hedged risk is the variability in cash flows attributable to changes in a contractually specified interest rate for forecasted interest receipts or payments on a variable-rate financial asset or liability, identification of the contractually specified interest rate. See paragraphs 815-30-35-37B through 35-37M for guidance on changing the contractually specified interest rate for a hedge of forecasted interest payments on a variable-rate debt instrument that permits the borrower to select at each reset period the interest rate index from a list of contractual options (including the interest rate tenor) upon which interest is accrued (this debt instrument is referred to throughout Topic 815 as "choose-your-rate" debt).

## > Hedge Effectiveness

### • > Hedge Effectiveness Criteria Applicable to both Fair Value Hedges and Cash Flow Hedges

**815-20-25-79** An entity shall consider hedge effectiveness in two different ways—in prospective considerations and in retrospective evaluations:

- a. Prospective considerations. The entity's expectation that the relationship will be highly effective over future periods in achieving offsetting changes in fair value or cash flows, which is forward looking, must be assessed on a quantitative basis at hedge inception unless one of the exceptions in paragraph 815-20-25-3(b)(2)(iv)(01) is met. Prospective assessments shall be subsequently performed whenever financial statements or earnings are reported and at least every three months. The entity shall elect at hedge inception in accordance with paragraph 815-20-25-3(b)(2)(iv)(03) whether to perform subsequent assessments on a quantitative or qualitative basis. See paragraphs 815-

20-35-2A through 35-2F for additional guidance on qualitative assessments of hedge effectiveness. A quantitative assessment can be based on regression or other statistical analysis of past changes in fair values or cash flows as well as on other relevant information. Except as described in paragraph 815-20-25-79B, the The quantitative prospective assessment of hedge effectiveness shall consider all reasonably possible changes in fair value (if a fair value hedge) or in fair value or cash flows (if a cash flow hedge) of the derivative instrument and the hedged items for the period used to assess whether the requirement for expectation of highly effective offset is satisfied. The quantitative prospective assessment may not be limited only to the likely or expected changes in fair value (if a fair value hedge) or in fair value or cash flows (if a cash flow hedge) of the derivative instrument or the hedged items. Generally, the process of formulating an expectation regarding the effectiveness of a proposed hedging relationship involves a probability-weighted analysis of the possible changes in fair value (if a fair value hedge) or in fair value or cash flows (if a cash flow hedge) of the derivative instrument and the hedged items for the hedge period. Therefore, a probable future change in fair value will be more heavily weighted than a reasonably possible future change. That calculation technique is consistent with the definition of the term **expected cash flow**.

- b. Retrospective evaluations. An assessment of effectiveness may be performed on a quantitative or qualitative basis on the basis of the entity's election at hedge inception in accordance with paragraph 815-20-25-3(b)(2)(iv)(03). That assessment shall be performed whenever financial statements or earnings are reported, and at least every three months. See paragraphs 815-20-35-2 through 35-4 for further guidance. At inception of the hedge, an entity electing a dollar-offset approach to perform retrospective evaluations on a quantitative basis may choose either a period-by-period approach or a cumulative approach in designating how effectiveness of a fair value hedge or of a cash flow hedge will be assessed retrospectively under that approach, depending on the nature of the hedge documented in accordance with paragraph 815-20-25-3. For example, an entity may decide that the cumulative approach is generally preferred, yet may wish to use the period-by-period approach in certain circumstances. See paragraphs 815-20-35-5 through 35-6 for further guidance. See paragraphs 815-30-35-37F and 815-30-35-37L through 35-37M for guidance on the retrospective

effectiveness assessment for a cash flow hedge within the scope of paragraph 815-30-35-37B related to choose-your-rate debt.

**815-20-25-79A** See paragraphs 815-20-25-139 through 25-143 25-142 about the timing of hedge effectiveness assessments required by paragraph 815-20-25-79 for a private company that is not a financial institution or a 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).

**815-20-25-79B** For a cash flow hedge of forecasted interest payments on a choose-your-rate debt instrument for which an entity chooses to apply the guidance in paragraphs 815-30-35-37B through 35-37M, the quantitative prospective assessment of hedge effectiveness shall consider all reasonably possible changes in cash flows of the forecasted transaction attributable to only the then-designated contractually specified interest rate. An entity shall not consider possible changes in cash flows of the forecasted transaction attributable to a contractually specified interest rate that may be designated in the future. The quantitative prospective assessment of hedge effectiveness shall consider all reasonably possible changes in cash flows of the derivative instrument in accordance with paragraph 815-20-25-79(a).

## **Implementation Guidance and Illustrations**

### **> Implementation Guidance**

#### **• > Hedge Effectiveness**

#### **• • > Changes in Quantitative Assessment Methods**

**815-20-55-56** This Subtopic permits a hedging relationship to be dedesignated (that is, discontinued) at any time. (See paragraphs 815-25-40-1(c) and 815-30-40-1(c).) If an entity wishes to change any of the critical terms of the hedging relationship (including the method designated for use in assessing hedge effectiveness or the method of assessing similar risk exposure), as documented at inception, the mechanism provided in this Subtopic to accomplish that change is the dedesignation of the original hedging relationship and the designation of a new hedging relationship that incorporates the desired changes. However, as discussed in ~~paragraph 815-30-35-37A,~~ paragraphs 815-30-35-37B through 35-37M, for a cash flow hedge of

forecasted interest payments on choose-your-rate debt (and related replacement debt), a change to the hedged risk in a cash flow hedge of a forecasted transaction in the contractually specified interest rate (and associated change in the number and timing of forecasted interest payments within the hedged period, if any) does not result in an automatic dedesignation of the hedging relationship if the conditions in those paragraphs are met ~~hedging instrument continues to be highly effective at achieving offsetting cash flows associated with the hedged item attributable to the revised hedged risk.~~ The dedesignation of an original hedging relationship and the designation of a new hedging relationship ~~represents~~ represent the application of this Subtopic and is not a change in accounting principle under Topic 250, even though the new hedging relationship may differ from the original hedging relationship only with respect to the method designated for use in assessing the similar risk exposure or hedge effectiveness of that hedging relationship. Although paragraph 815-20-35-19 refers to discontinuing an existing hedging relationship and then designating and documenting a new hedging relationship using an improved method for assessing effectiveness, that reference was not meant to imply that the perceived improved method had to be justified as a preferable method of applying an accounting principle under Topic 250. **[For convenience, this paragraph also contains the amendments from Issue 1.]**

## Amendments to Subtopic 815-30

7. Amend paragraph 815-30-35-8, the heading preceding paragraph 815-30-35-37A, and paragraphs 815-30-55-60 through 55-61, supersede paragraph 815-30-35-37A, and add paragraphs 815-30-35-37B through 35-37M and 815-30-55-165 through 55-181 and their related headings, with a link to transition paragraph 815-20-65-7, as follows:

### **Derivatives and Hedging—Cash Flow Hedges**

#### **Subsequent Measurement**

##### **> Subsequent Recognition and Measurement of Gains and Losses on Hedging Instrument**

**815-30-35-8** The remainder of this guidance addresses the following matters:

- a. Application to single cash flow hedge of a forecasted sale or purchase on credit for foreign exchange risk
- b. Assessing hedge effectiveness in certain cash flow hedges involving **interest rate risk** when effectiveness is assessed on a quantitative basis
- c. Hedging relationship in which hedge effectiveness is based on an option's terminal value ~~value~~.
- d. Change in the contractually specified interest rate for forecasted interest payments on choose-your-rate debt ~~designated hedged risk~~.

• > **Change in the Contractually Specified Interest Rate for Forecasted Interest Payments on Choose-Your-Rate Debt** ~~Designated Hedged Risk~~

**815-30-35-37A** Paragraph superseded by Accounting Standards Update No. 2025-09. If the designated hedged risk changes during the life of a hedging relationship, an entity may continue to apply hedge accounting if the hedging instrument is highly effective at achieving offsetting cash flows attributable to the revised hedged risk. The guidance in paragraph 815-20-55-56 does not apply to changes in the hedged risk for a cash flow hedge of a forecasted transaction.

**815-30-35-37B** For a cash flow hedge of forecasted interest payments on choose-your-rate debt:

- a. With respect to the forecasted issuance of a choose-your-rate debt instrument, an entity may choose to apply the guidance in paragraphs 815-30-35-37C through 35-37H on a hedge-by-hedge basis if both of the following conditions are satisfied:
  - 1. The forecasted interest payments designated as being hedged relate to the forecasted issuance of a choose-your-rate debt instrument that will be classified as a liability.
  - 2. The entity designates the hedged risk as the variability in cash flows attributable to changes in a contractually specified interest rate in accordance with paragraph 815-20-25-19A(b).
- b. With respect to an existing choose-your-rate debt instrument or replacement debt, an entity may choose to apply the guidance in paragraphs 815-30-35-37I through 35-37M on a hedge-by-hedge basis if both of the following conditions are satisfied:

1. The forecasted interest payments designated as being hedged have begun to accrue and relate to an existing choose-your-rate debt or replacement debt (see paragraph 815-30-35-37K for additional guidance on replacement debt) instrument classified as a liability.
2. The entity designates the hedged risk as the variability in cash flows attributable to changes in a contractually specified interest rate.

The guidance in paragraphs 815-30-35-37C through 35-37M shall not be applied by analogy, including to hedges designated under the first-payments-received technique (Example 4, Case A [paragraphs 815-20-55-91 through 55-96A] illustrates this technique) or to hedges of a choose-your-rate debt instrument or group of choose-your-rate debt instruments classified as assets.

#### **• • > Hedging the Forecasted Issuance of Choose-Your-Rate Debt**

**815-30-35-37C** In a cash flow hedge of forecasted interest payments that meets the conditions described in paragraph 815-30-35-37B(a), an entity shall designate the contractually specified interest rate (and interest rate tenor) as the entity's best estimate of the interest rate index (and interest rate tenor) that it will initially select for the first interest period when the choose-your-rate debt instrument is issued. The currently designated best estimate of the interest rate index (and interest rate tenor) shall be considered the interest rate index (and interest rate tenor) upon which interest will accrue over the entire hedge period for purposes of assessing hedge effectiveness during the period before the debt is issued. The selection of an interest rate index (and interest rate tenor) in a subsequent period that alters the number and timing of the hedged forecasted interest payments within the hedge period shall not result in an automatic dedesignation of the hedging relationship.

**815-30-35-37D** When designating the hedged risk in a cash flow hedge of forecasted interest payments that meets the conditions described in paragraph 815-30-35-37B(a), an entity shall document the interest rate indexes (and interest rate tenors) that are included in choose-your-rate debt being offered in the market. If the entity determines that it is probable that it will issue choose-your-rate debt and initially select one of those documented interest rate indexes (and interest rate tenors) for the first interest period when the choose-your-rate debt instrument is issued, and if all of the other requirements of hedge accounting are met, hedge accounting may be applied.

**815-30-35-37E** If, during the forecast period, the entity's best estimate of the interest rate index (and interest rate tenor) that it will initially select for the first interest period when the choose-your-rate debt instrument is issued changes to another rate that was documented at hedge inception, the entity shall apply the guidance in paragraphs 815-30-35-37F through 35-37G to determine whether hedge accounting can continue. If the entity determines that it is probable that the interest rate index (and interest rate tenor) that it will initially select for the first interest period when the choose-your-rate debt instrument is issued will not be a rate that was documented at hedge inception or if the entity determines that it is probable that it will not issue choose-your-rate debt, the entity shall immediately reclassify the gain or loss on the hedging instrument reported in accumulated other comprehensive income into earnings in accordance with paragraph 815-30-40-5. The entity also shall consider whether it has demonstrated a pattern of determining that hedged forecasted transactions are probable of not occurring and the propriety of using hedge accounting in the future for similar forecasted transactions in accordance with paragraph 815-30-40-5.

**815-30-35-37F** If the best estimate of the interest rate index (and interest rate tenor) that the entity will select when the choose-your-rate debt instrument is issued changes to another rate that was documented in accordance with paragraph 815-30-35-37D during the forecast period, the entity shall perform a final retrospective assessment of hedge effectiveness on the basis of changes in cash flows attributable to the previous best estimate of the interest rate. If the entity concludes on the basis of that retrospective assessment that the hedging relationship was not highly effective in having achieved offsetting cash flows, hedge accounting may not be applied during that period (that is, the overall change in the fair value of the hedging instrument for that period shall be recognized in earnings). However, the hedging relationship may continue if there is an expectation that the relationship will be highly effective in achieving offsetting cash flows in future periods and all other hedge accounting requirements are met. In that circumstance, the entity shall begin prospectively assessing hedge effectiveness on the basis of changes in cash flows attributable to the new best estimate of the interest rate in the period in which the best estimate of the interest rate changes.

**815-30-35-37G** In performing a prospective assessment with the new best estimate of the interest rate index (and interest rate tenor), the entity shall create the terms of the instrument used to estimate changes in the cash flows

attributable to the new best estimate of the interest rate (under the originally designated method, for example, the hypothetical derivative method or another acceptable method in Subtopic 815-30) on the basis of market data as of the inception of the hedging relationship as if the new best estimate of the interest rate had been designated for the entire hedge period. If the best estimate of the interest rate does not change again, all subsequent retrospective and prospective assessments of hedge effectiveness shall be performed using the currently designated best estimate of the interest rate. With respect to the timing, an entity shall perform its assessments of effectiveness in a manner consistent with paragraph 815-20-25-3(b)(2)(iv)(02).

**815-30-35-37H** After the choose-your-rate debt instrument is issued and the entity chooses the first interest rate index (and interest rate tenor) upon which interest will accrue, the entity shall no longer apply the guidance in paragraphs 815-30-35-37C through 35-37G. Instead, if the entity continues to apply hedge accounting, it shall apply the guidance on existing choose-your-rate debt and related replacement debt (if applicable) in accordance with paragraphs 815-30-35-37I through 35-37M and update its hedge documentation without dedesignating the hedging relationship. Example 28 (paragraph 815-30-55-171) illustrates how an entity should transition from the guidance on the forecasted issuance of choose-your-rate debt to the guidance on choose-your-rate debt and related replacement debt.

#### **• • > Hedging Existing Choose-Your-Rate Debt and Replacement Debt**

**815-30-35-37I** In a cash flow hedge of forecasted interest payments that meets the conditions in paragraph 815-30-35-37B(b), an entity shall designate the contractually specified interest rate (and interest rate tenor) as the then-selected interest rate index (and interest rate tenor). The currently designated interest rate index (and interest rate tenor) shall be considered the interest rate index (and interest rate tenor) upon which interest will accrue over the entire hedge period for purposes of assessing hedge effectiveness. The selection of an interest rate index (and interest rate tenor) in a subsequent period that alters the number and timing of the hedged forecasted interest payments within the hedge period shall not result in an automatic dedesignation of the hedging relationship as long as the selected interest rate index (and interest rate tenor) is one of the options included in the original existing choose-your-rate debt instrument as documented in accordance with paragraph 815-30-35-37J.

**815-30-35-37J** When designating the hedged risk in a cash flow hedge of forecasted interest payments that meets the conditions described in paragraph 815-30-35-37B(b), an entity shall document the interest rate indexes (and interest rate tenors) that are included in the existing choose-your-rate debt instrument. If the entity determines that it is probable that the forecasted interest payments related to the existing choose-your-rate debt instrument or replacement debt will occur at one of the documented interest rate indexes (and interest rate tenors) during the hedge period and all of the other requirements of hedge accounting are met, hedge accounting may be applied.

**815-30-35-37K** An entity may designate the forecasted interest payments in a manner that includes debt that is expected to replace existing choose-your-rate debt. If the contractually specified interest rate at which interest is accruing on the replacement debt matches one of the interest rate index (and interest rate tenor) options included in the original choose-your-rate debt instrument that was outstanding when the first hedged interest payment began to accrue, the forecasted interest payments on the replacement debt shall be considered the hedged forecasted transactions without dedesignating the hedging relationship. If it becomes probable that the interest rate index (and interest rate tenor) at which interest will accrue on the replacement debt will not match one of the interest rate index (and interest rate tenor) options included in the original choose-your-rate debt instrument that was outstanding when the hedging relationship was initially designated, or that the replacement debt will be fixed-rate debt, the entity shall discontinue the application of hedge accounting and immediately reclassify the gain or loss on the hedging instrument recognized in accumulated other comprehensive income into earnings in accordance with paragraph 815-30-40-5. The entity also shall consider whether it has demonstrated a pattern of determining that hedged forecasted transactions are probable of not occurring and the propriety of using hedge accounting in the future for similar forecasted transactions in accordance with paragraph 815-30-40-5.

**815-30-35-37L** If the contractually specified interest rate in the hedging relationship is changed in accordance with paragraph 815-30-35-37I, the entity shall perform a final retrospective assessment of hedge effectiveness that is based on changes in cash flows attributable to the previously selected contractually specified interest rate for the last period in which interest was accruing at that interest rate. If the entity concludes on the basis of that retrospective assessment that the hedging relationship was not highly effective

in having achieved offsetting cash flows, hedge accounting may not be applied during that period (that is, the change in the fair value of the hedging instrument for that period is recognized in earnings). However, the hedging relationship may continue if there is an expectation that the relationship will be highly effective in achieving offsetting cash flows in future periods and all other hedge accounting requirements are met. The entity shall begin prospectively assessing hedge effectiveness on the basis of changes in cash flows attributable to the newly selected contractually specified interest rate in the period in which interest begins accruing at that newly selected interest rate.

**815-30-35-37M** In performing a prospective assessment with the newly selected contractually specified interest rate, the entity shall create the terms of the instrument used to estimate changes in the cash flows attributable to the newly selected contractually specified interest rate (under the originally designated method, for example, the hypothetical derivative method or another acceptable method in Subtopic 815-30) on the basis of market data as of the inception of the hedging relationship as if the newly selected contractually specified interest rate had been designated for the entire hedge period. All subsequent retrospective and prospective assessments of hedge effectiveness shall be performed using the currently designated interest rate. With respect to the timing, an entity shall perform its assessments of effectiveness in a manner consistent with paragraph 815-20-25-3(b)(2)(iv)(02).

## **Implementation Guidance and Illustrations**

### **> Illustrations**

#### **• > Example 9: Changes in a Cash Flow Hedge of Forecasted Interest Payments with an Interest Rate Swap**

#### **• • > Case B: Basis of Hedged Forecasted Transactions Is Changed**

**815-30-55-60** At the end of the second year of the 5-year hedging relationship, Entity MNO discontinues its practice of issuing 90-day notes and issues a 3-year, \$5 million note with a different contractually specified interest rate (that is, an interest rate that is not LIBOR) that adjusts every 90 days. As of this date, Entity MNO must begin performing assessments of effectiveness for the hedging relationship by comparing changes in fair value of the hedging instrument (indexed to LIBOR) with changes in the value of the hedged item based on the different ~~revised~~ contractually specified interest rate. Because the

hedged forecasted transactions (future interest payments) are still probable of occurring, Entity MNO may continue to apply hedge accounting in accordance with ~~paragraph 815-30-35-37A~~ if the hedging instrument (indexed to LIBOR) is highly effective at achieving offsetting cash flows attributable to the different revised contractually specified interest rate.

**815-30-55-61** If the ~~revised~~ hedging relationship is not determined to be highly effective, the hedging relationship must be discontinued. However, the net gain or loss on Swap 1 in accumulated other comprehensive income as of the date Entity MNO issues the three-year note is not reclassified into earnings immediately. Immediate reclassification would be required only if, as part of its normal process of assessing whether it remains probable that the hedged forecasted transaction will occur, Entity MNO determines that it is probable that the hedged transactions (future interest payments) will not occur. In this case, the expected amounts of those payments have changed (because they will be based on a different revised contractually specified interest rate instead of LIBOR, as originally expected), but it still is probable that the payments will occur. Thus, those gains or losses will continue to be reclassified to earnings as the interest payments affect earnings and presented in the same income statement line item as the earnings effect of the hedged item.

**• > Example 28: Hedges of Forecasted Interest Payments on Choose-Your-Rate Debt**

**815-30-55-165** This Example illustrates the application of the guidance in paragraphs 815-30-35-37B through 35-37M in which the designated hedged risk is the variability in cash flows attributable to changes in the contractually specified interest rate on a choose-your-rate debt instrument that is:

- a. Yet to be issued
- b. Issued and outstanding
- c. Replaced during the hedge period.

**815-30-55-166** On January 1, 20X1, Entity A determines that it is probable it will enter into a choose-your-rate debt arrangement with a bank for a 5-year, \$20 million variable-rate note payable to be issued on April 1, 20X1, with the principal due at maturity. On January 1, 20X1, Entity A determines that the interest rate indexes and interest rate tenors included in choose-your-rate debt being offered in the market are as follows:

- a. 1-Month Term SOFR (paid every 30 days)
- b. 3-Month Term SOFR (paid every 90 days)
- c. 6-Month Term SOFR (paid every 6 months)
- d. 1-Month U.S. Treasury Rate (paid every 30 days)
- e. Prime (paid every 30 days).

**815-30-55-167** Entity A seeks to hedge the cash flow variability attributable to changes in the contractually specified interest rate on this choose-your-rate debt instrument. Accordingly, on January 1, 20X1, Entity A enters into a forward-starting receive-variable, pay-fixed, 5-year, \$20 million notional interest rate swap that requires settlement and resets every 30 days beginning after April 1, 20X1. Under the terms of the swap, Entity A receives variable payments every 30 days beginning after April 1, 20X1, based on the average of Daily SOFR over the past 30 days (that is, the variable-rate interest payments are indexed to 30-Day Average SOFR, in arrears) and pays a fixed rate of 5 percent. On January 1, 20X1, the fair value of the interest rate swap is zero.

**815-30-55-168** On January 1, 20X1, Entity A designates the swap as hedging the variability in cash flows attributable to changes in the contractually specified interest rate on the 5-year, \$20 million notional choose-your-rate debt instrument forecasted to begin accruing interest on April 1, 20X1, and any related replacement debt, in accordance with paragraph 815-30-35-37B. On January 1, 20X1, Entity A documents the interest rate indexes and interest rate tenors included in choose-your-rate debt being offered in the market (that is, those interest rate indexes and interest rate tenors included in paragraph 815-30-55-166(a) through (e)) in accordance with paragraph 815-30-35-37D. Only interest rate indexes and interest rate tenors are required to be documented in accordance with paragraph 815-30-35-37D (that is, payment conventions included in paragraph 815-30-55-166(a) through (e) are included only for illustrative purposes and do not depict an incremental documentation requirement). Entity A determines that it is probable that it will issue choose-your-rate debt and initially select one of those interest rate indexes and interest rate tenors when the choose-your-rate debt is issued on April 1, 20X1.

**815-30-55-169** Entity A's best estimate of the interest rate index and interest rate tenor that it will initially select for the first interest period when the choose-your-rate debt is issued is 1-Month Term SOFR. In accordance with paragraph 815-30-35-37C, Entity A designates that interest rate index and interest rate

tenor as its contractually specified interest rate. Entity A performs an initial quantitative hedge effectiveness assessment on January 1, 20X1, based on this best estimate (that is, 60 monthly interest payments that begin to accrue on April 1, 20X1, based on 1-Month Term SOFR, with the rate resetting immediately following each payment due date) and concludes that the relationship is highly effective. In accordance with paragraph 815-20-25-79B, this effectiveness assessment does not consider the optionality expected to be embedded within the choose-your-rate debt instrument. That is, the terms used to estimate changes in the hedged forecasted cash flows for purposes of the hedge effectiveness assessment only consider Entity A's best estimate of the interest rate index and interest rate tenor that it will select for the first interest period when the choose-your-rate debt is issued, which is 1-Month Term SOFR.

**815-30-55-170** On April 1, 20X1, the note payable is issued. The note payable allows Entity A to pay interest at any of the following variable interest rates based on the rate that the entity selects at each reset date:

- a. 1-Month Term SOFR (paid every 30 days)
- b. 3-Month Term SOFR (paid every 90 days)
- c. 6-Month Term SOFR (paid every 6 months)
- d. 1-Month U.S. Treasury Rate (paid every 30 days)
- e. Prime (paid every 30 days)
- f. Effective Federal Funds Rate (paid every 30 days).

Entity A chooses to pay interest based on 1-Month Term SOFR with the rate resetting immediately following each payment due date. If Entity A had determined that it was probable that Entity A would issue fixed-rate or single variable-rate debt or choose to pay interest at the Effective Federal Funds Rate (an interest rate that was not documented at hedge inception) for the first interest period, the entity would have discontinued applying hedge accounting and immediately reclassified the gain or loss on the interest rate swap reported in accumulated other comprehensive income into earnings in accordance with paragraph 815-30-40-5. Entity A also would have considered whether it had demonstrated a pattern of determining that hedged forecasted transactions are probable of not occurring and the propriety of using hedge accounting in the future for similar forecasted transactions in accordance with paragraph 815-30-40-5.

**815-30-55-171** In accordance with paragraphs 815-30-35-37H through 35-37J, after the choose-your-rate debt is issued and Entity A chooses the first interest rate index and interest rate tenor upon which interest will accrue, the list of interest rates and interest rate tenors documented at hedge inception is replaced by the list of interest rates and interest rate tenors included in the issued choose-your-rate debt agreement for the purposes of determining whether hedge accounting can continue. After Entity A chooses the first interest rate index and interest rate tenor upon which interest will accrue, it updates its hedge documentation in accordance with paragraph 815-30-35-37J to indicate that it will choose to designate the contractually specified interest rate index and interest rate tenor as any interest rate index and interest rate tenor selected in the issued choose-your-rate debt, which would include the Effective Federal Funds Rate. In the future, if Entity A selects an alternative interest rate index or interest rate tenor on the choose-your-rate debt instrument, the designated contractually specified interest rate would be the interest rate index and interest rate tenor selected at that time. Similarly, if Entity A replaces the choose-your-rate debt instrument with a debt instrument for which the interest rate index and interest rate tenor match one of the interest rate index and interest rate tenor options included in the originally issued choose-your-rate debt instrument, interest payments on the replacement debt would continue to be considered the designated forecasted transactions.

**815-30-55-172** After the choose-your-rate debt is issued on April 1, 20X1, Entity A performs a prospective and retrospective hedge effectiveness assessment based on the then-selected interest rate index and interest rate tenor of the debt instrument. In accordance with paragraph 815-20-25-79B, this effectiveness assessment does not consider the optionality embedded within the choose-your-rate debt instrument. That is, the terms used to estimate changes in the hedged forecasted cash flows for purposes of the hedge effectiveness assessment only consider the currently selected interest rate index and interest rate tenor of 1-Month Term SOFR.

**815-30-55-173** Subsequent elections to change the interest rate index and interest rate tenor on the choose-your-rate debt instrument or replacement debt instrument may affect ongoing hedge accounting for this relationship. Consider the following scenarios, each occurring on April 1, 20X4:

- a. Entity A changes the variable interest rate on the choose-your-rate debt instrument to 3-Month Term SOFR, payable every 90 days, with the rate resetting immediately following each payment (Scenario A).
- b. Entity A changes the variable interest rate on the choose-your-rate debt instrument to Prime, payable every 30 days, with the rate resetting immediately following each payment (Scenario B).
- c. Entity A replaces the choose-your-rate debt instrument with a 1-year, \$30 million 3-Month Term SOFR note, payable every 90 days, with the rate resetting immediately following each payment, with the principal due at maturity (Scenario C).
- d. Entity A replaces the choose-your-rate debt instrument with a 2-year, \$20 million 12-Month Term SOFR note, payable annually, with the rate resetting immediately following each payment, with the principal due at maturity (Scenario D).

#### **• • > Scenario A**

**815-30-55-174** On April 1, 20X4, Entity A elects to make future interest payments on the existing choose-your-rate debt instrument based on 3-Month Term SOFR. Consistent with Entity A's hedge documentation, this election automatically changes the contractually specified interest rate in the hedging relationship from 1-Month Term SOFR to 3-Month Term SOFR. The resulting change in the number and frequency of hedged interest payments in the hedging relationship does not result in a mandatory hedge dedesignation or require that Entity A consider the guidance in paragraphs 815-30-40-4 through 40-6.

**815-30-55-175** Entity A performs a final retrospective assessment of hedge effectiveness on the basis of changes in cash flows on 1-Month Term SOFR interest payments (payable every 30 days), assuming that the contractually specified interest rate will not change, and determines that the hedging relationship was highly effective through April 1, 20X4. Entity A then performs a prospective assessment of hedge effectiveness on the basis of changes in cash flows on 3-Month Term SOFR interest payments (payable every 90 days). When assessing hedge effectiveness with the new risk, Entity A creates the terms of the instrument used to estimate the changes in the cash flows of the 3-Month Term SOFR interest payments on the basis of market data as of January 1, 20X1, as required by paragraphs 815-30-35-37L through 35-37M. In performing this assessment, Entity A assumes that 3-Month Term SOFR was and will continue to be the contractually specified interest rate designated

in the hedging relationship. Entity A determines that the revised hedging relationship is expected to continue to be highly effective at achieving offsetting cash flows attributable to 3-Month Term SOFR on a prospective basis and continues to apply hedge accounting.

**• • > Scenario B**

**815-30-55-176** On April 1, 20X4, Entity A elects to make future interest payments on the existing choose-your-rate debt instrument based on Prime, payable every 30 days, with the rate resetting immediately following each payment. Consistent with Entity A's hedge documentation, this election automatically changes the contractually specified interest rate in the hedging relationship from 1-Month Term SOFR to Prime (30-day reset).

**815-30-55-177** Entity A performs a final retrospective assessment of hedge effectiveness on the basis of changes in cash flows on 1-Month Term SOFR interest payments (payable every 30 days), assuming that the contractually specified interest rate will not change, and determines that the hedging relationship was highly effective through April 1, 20X4. Entity A then performs a prospective assessment of hedge effectiveness on the basis of changes in cash flows on Prime interest payments (payable every 30 days). When assessing hedge effectiveness with the new risk, Entity A creates the terms of the instrument used to estimate the changes in the cash flows of the Prime interest payments on the basis of market data as of January 1, 20X1, as required by paragraphs 815-30-35-37L through 35-37M. In performing this assessment, Entity A assumes that 30-day Prime was and will continue to be the contractually specified interest rate in the hedging relationship. Entity A determines that the revised hedging relationship is not expected to be highly effective at achieving offsetting cash flows attributable to 30-day Prime on a prospective basis. As a result, Entity A discontinues hedge accounting but continues to report the previously recognized derivative gain or loss on the hedging instrument in accumulated other comprehensive income until the forecasted interest payments affect earnings or it is probable that the forecasted interest payments will not occur.

## • • > Scenario C

**815-30-55-178** On April 1, 20X4, Entity A replaces the choose-your-rate debt instrument with a 1-year, \$30 million 3-Month Term SOFR note, payable every 90 days. The replacement debt instrument does not need to be choose-your-rate debt in order for interest payments on the replacement debt to continue to be considered the forecasted transactions designated at hedge inception. That is, the replacement debt may have a single contractual variable rate or a list of possible contractual interest rate indexes and interest rate tenors from which the borrower may select. In either circumstance, if the interest rate index and interest rate tenor at which the replacement debt instrument is accruing interest match one of the interest rate index and interest rate tenor options included in the original choose-your-rate debt instrument, interest payments on the replacement debt will continue to be considered the designated forecasted transactions. However, if the replacement debt is fixed-rate debt or includes interest rate indexes or interest rate tenors not included in the terms of the original debt instrument and Entity A selects one of those interest rate indexes or interest rate tenors, the interest payments should not be considered the designated forecasted transactions. Once that instance becomes probable, the entity should discontinue applying hedge accounting and immediately reclassify the gain or loss on the hedging instrument recognized in accumulated other comprehensive income into earnings in accordance with paragraph 815-30-40-5. The entity also should consider whether it has demonstrated a pattern of determining that hedged forecasted transactions are probable of not occurring and the propriety of using hedge accounting in the future for similar forecasted transactions in accordance with paragraph 815-30-40-5.

**815-30-55-179** Although the replacement debt matures before the end of the hedge period (that is, the replacement debt matures March 31, 20X5, while the hedge period ends March 31, 20X6), Entity A determines that it is probable that it will issue eligible replacement debt for the remaining hedge period. Accordingly, while the currently outstanding replacement debt matures before the end of the hedge period, Entity A may continue to apply hedge accounting because it is probable that replacement debt will accrue interest payments over the remainder of the hedge period at one of the interest rate indexes and interest rate tenors included in the terms of the original choose-your-rate debt instrument. In addition, the forecasted interest payments on the outstanding replacement debt instrument should be considered the forecasted transactions

in accordance with paragraph 815-30-35-37K because the interest rate specified in the outstanding replacement debt (3-Month Term SOFR) was an interest rate index and interest rate tenor option included in the original choose-your-rate debt instrument. The fact that the principal of the outstanding replacement debt exceeds the principal hedged does not result in interest payments on the replacement debt instrument being ineligible to be hedged. Consistent with Entity A's hedge documentation, replacing the hedged debt instrument automatically changes the contractually specified interest rate designated in the hedging relationship from 1-Month Term SOFR to 3-Month Term SOFR.

**815-30-55-180** Entity A performs a final retrospective assessment of hedge effectiveness on the basis of changes in cash flows on 1-Month Term SOFR interest payments (payable every 30 days), assuming that the contractually specified interest rate will not change, and determines that the hedging relationship was highly effective through April 1, 20X4. Entity A then performs a prospective assessment of hedge effectiveness on the basis of changes in cash flows on 3-Month Term SOFR interest payments (payable every 90 days). When assessing hedge effectiveness with the new risk, Entity A creates the terms of the instrument used to estimate the changes in the cash flows of the 3-Month Term SOFR interest payments on the basis of market data as of January 1, 20X1, as required by paragraphs 815-30-35-37L through 35-37M. In performing this assessment, Entity A assumes that 3-Month Term SOFR was and will continue to be the contractually specified interest rate designated in the hedging relationship. Entity A determines that the revised hedging relationship is expected to continue to be highly effective at achieving offsetting cash flows attributable to 3-Month Term SOFR on a prospective basis and continues to apply hedge accounting.

#### **• • > Scenario D**

**815-30-55-181** On April 1, 20X4, Entity A replaces the choose-your-rate debt instrument with a 2-year, \$20 million 12-Month Term SOFR note, payable every 360 days. Because 12-Month Term SOFR was not listed as one of the interest rate index and interest rate tenor options included in the original choose-your-rate debt instrument, interest payments on this 12-Month Term SOFR note are not eligible to be designated as hedged forecasted transactions. Once it becomes probable that the choose-your-rate debt instrument will be replaced with a 2-year, \$20 million 12-Month Term SOFR note that is payable every 360

days, Entity A must immediately reclassify amounts previously recognized in accumulated other comprehensive income into earnings in accordance with paragraph 815-30-40-5. Entity A also should consider whether it has demonstrated a pattern of determining that hedged forecasted transactions are probable of not occurring and the propriety of using hedge accounting in the future for similar forecasted transactions in accordance with paragraph 815-30-40-5.

## Issue 3: Cash Flow Hedges of Nonfinancial Forecasted Transactions

### Amendments to Subtopic 815-20

8. Amend paragraphs 815-20-25-3(d)(1)(vii), 815-20-25-15(e), 815-20-25-15(i)(3), the heading preceding paragraph 815-20-25-22A, 815-20-25-46B, 815-20-25-77, and 815-20-25-84, supersede paragraphs 815-20-25-22A through 25-22B, and add paragraph 815-20-25-22C, with a link to transition paragraph 815-20-65-7, as follows:

### **Derivatives and Hedging—Hedging—General**

#### **Recognition**

##### **> Formal Designation and Documentation at Hedge Inception**

**815-20-25-3** Concurrent designation and documentation of a hedge is critical; without it, an entity could retroactively identify a hedged item, a hedged **transaction**, or a method of assessing effectiveness to achieve a desired accounting result. To qualify for hedge accounting, there shall be, at inception of the hedge, formal documentation of all of the following:

- d. Documentation requirement applicable to cash flow hedges only:
  1. For a cash flow hedge of a **forecasted transaction**, documentation shall include all relevant details, including all of the following:
    - vii. If the hedged risk is the variability in cash flows attributable to changes in a **contractually specified component** component of the price of a nonfinancial asset (or a subcomponent as described in paragraph 815-20-25-22C(b)(2)) in a forecasted purchase or sale of a nonfinancial asset that meets the criterion

in paragraph 815-20-25-15(i)(3), identification of the contractually specified component (or subcomponent).

## > Eligibility of Hedged Items and Transactions

### • > Hedged Transaction Criteria Applicable to Cash Flow Hedges Only

**815-20-25-15** A forecasted transaction is eligible for designation as a hedged transaction in a cash flow hedge if all of the following additional criteria are met:

- e. If the forecasted transaction relates to a recognized asset or liability, the asset or liability is not remeasured with changes in fair value attributable to the hedged risk reported currently in earnings. For example, if the forecasted transaction relates to the purchase or sale of a nonfinancial item under a contract that is accounted for as a derivative under Topic 815 (that is, a recognized asset or liability), an entity may designate the variable price component (or subcomponent) in the contract as the hedged risk if all other hedge criteria are satisfied.
- i. If the hedged transaction is the forecasted purchase or sale of a nonfinancial asset, the designated risk being hedged is any of the following:
  3. ~~The risk of variability changes in cash flows relating to a variable component (or subcomponent) of the purchase or sales price of a nonfinancial asset that meets the criteria in paragraph 815-20-25-22C. attributable to changes in a contractually specified component. (See additional criteria in paragraphs 815-20-25-22A through 25-22B for designating the variability in cash flows attributable to changes in a contractually specified component as the hedged risk.)~~

### • • > Eligibility Criteria for Designating the Variability in Cash Flows Attributable to Changes in a Contractually Specified Component (or Subcomponent) of for the Purchase Price or Sale Sales Price of a Nonfinancial Asset as the Hedged Risk

**815-20-25-22A** Paragraph superseded by Accounting Standards Update No. 2025-09. ~~For existing contracts, determining whether the variability in cash flows attributable to changes in a contractually specified component may be designated as the hedged risk in a cash flow hedge is based on the following:~~

- a. ~~If the contract to purchase or sell a nonfinancial asset is a derivative in its entirety and an entity applies the normal purchases and normal sales scope exception in accordance with Subtopic 815-10, any contractually specified component in the contract is eligible to be designated as the hedged risk. If the entity does not apply the normal purchases and normal sales scope exception, no pricing component is eligible to be designated as the hedged risk.~~
- b. ~~If the contract to purchase or sell a nonfinancial asset is not a derivative in its entirety, any contractually specified component remaining in the host contract (that is, the contract to purchase or sell a nonfinancial asset after any embedded derivatives have been bifurcated in accordance with Subtopic 815-15) is eligible to be designated as the hedged risk.~~

**815-20-25-22B** Paragraph superseded by Accounting Standards Update No. 2025-09. ~~An entity may designate the variability in cash flows attributable to changes in a contractually specified component in accordance with paragraph 815-20-25-15(i)(3) to purchase or sell a nonfinancial asset for a period longer than the contractual term or for a not-yet-existing contract to purchase or sell a nonfinancial asset if the entity expects that the requirements in paragraph 815-20-25-22A will be met when the contract is executed. Once the contract is executed, the entity shall apply the guidance in paragraph 815-20-25-22A to determine whether the variability in cash flows attributable to changes in the contractually specified component can continue to be designated as the hedged risk. See paragraphs 815-20-55-26A through 55-26E for related implementation guidance.~~

**815-20-25-22C** An entity may designate the variability in cash flows attributable to changes in a component (or subcomponent) of the forecasted purchase price or sales price of a nonfinancial asset as the hedged risk in a cash flow hedge as follows:

- a. If the purchase price or sales price of the nonfinancial asset is not determined in accordance with a pricing formula in an agreement, the hedged variable component is clearly and closely related (as described in paragraph 815-10-15-32(a) through (b)) to the nonfinancial asset being purchased or sold.
- b. If the purchase price or sales price of the nonfinancial asset is determined in accordance with a pricing formula in an agreement, the hedged variable component is either of the following:

1. Explicitly referenced in the agreement's pricing formula and clearly and closely related (as described in paragraph 815-10-15-32(a) through (b)) to the nonfinancial asset being purchased or sold
2. Clearly and closely related (as described in paragraph 815-10-15-32(a) through (b)) to a variable component that meets the conditions in (b)(1) (that is, a "subcomponent"). (Throughout Subtopic 815-20, reference to a subcomponent refers only to the designation guidance in this subparagraph.)

## > Eligibility of Hedging Instruments

### • > Intra-entity Derivatives

**815-20-25-46A** There is no requirement in this Subtopic that the operating unit with the interest rate, market price, or credit risk exposure be a party to the hedging instrument. Thus, for example, a parent entity's central treasury function can enter into a derivative instrument with a third party and designate it as the hedging instrument in a hedge of a subsidiary's interest rate risk for purposes of the consolidated financial statements. However, if the subsidiary wishes to qualify for hedge accounting of the interest rate exposure in its separate-entity financial statements, the subsidiary (as the reporting entity) shall be a party to the hedging instrument, which can be an intra-entity derivative obtained from the central treasury function. Thus, an intra-entity derivative for interest rate risk can qualify for designation as the hedging instrument in separate-entity financial statements but not in consolidated financial statements. (As used in this guidance, the term *subsidiary* refers only to a consolidated subsidiary. This guidance shall not be applied directly or by analogy to an equity method investee.)

**815-20-25-46B** An intra-entity derivative shall not be designated as the hedging instrument if the hedged risk is any of the following:

- a. The risk of changes in the overall fair value or cash flows of the entire hedged item or transaction
- b. The risk of changes in hedged item's or transaction's fair value attributable to changes in the designated benchmark interest rate or cash flows attributable to changes in the contractually specified interest rate or designated benchmark interest rate
- c. The risk of changes in hedged item's or transaction's fair value or cash flows attributable to changes in credit risk.

- d. The risk of variability in cash flows attributable to changes in a ~~contractually specified component~~ (or subcomponent) of the price to purchase or sell a nonfinancial asset that meets the conditions in paragraph 815-20-25-22C.

Similarly, a derivative instrument contract between operating units within a single legal entity shall not be designated as the hedging instrument in a hedge of those risks. Only a derivative instrument with an unrelated third party can be designated as the hedging instrument in a hedge of those risks in consolidated financial statements.

### > Hedge Effectiveness

#### • > Hedge Effectiveness Criteria Applicable to both Fair Value Hedges and Cash Flow Hedges

**815-20-25-77** There would be a mismatch between the change in fair value or cash flows of the hedging instrument and the change in fair value or cash flows of the hedged item or hedged transaction in any of the following circumstances, among others:

- a. A difference between the basis of the hedging instrument and the hedged item or hedged transaction, to the extent that those bases do not move in tandem
- b. Differences in critical terms of the hedging instrument and hedged item or hedged transaction, such as differences in any of the following:
  1. Notional amounts
  2. Maturities
  3. Quantity
  4. Location (not applicable if the hedging instrument's underlying and the designated hedged risk are the same) ~~for hedging relationships in which the variability in cash flows attributable to changes in a contractually specified component is designated as the hedged risk~~)
  5. Delivery dates.
- c. A change in the counterparty's creditworthiness.

**815-20-25-84** If the critical terms of the hedging instrument and of the hedged item or hedged forecasted transaction are the same, the entity could conclude that changes in fair value or cash flows attributable to the risk being hedged

are expected to completely offset at inception and on an ongoing basis. For example, an entity may assume that a hedge of a forecasted purchase of a commodity with a forward contract will be perfectly effective if all of the following criteria are met:

- a. The forward contract is for purchase of the same quantity of the same commodity at the same time and location as the hedged forecasted purchase. Location differences do not need to be considered if the forward contract's underlying and the designated hedged risk are the same ~~an entity designates the variability in cash flows attributable to changes in a **contractually specified component** as the hedged risk and the requirements in paragraphs 815-20-25-22A through 25-22B are met.~~
- b. The fair value of the forward contract at inception is zero.
- c. Either of the following criteria is met:
  1. The change in the discount or premium on the forward contract is excluded from the assessment of effectiveness pursuant to paragraphs 815-20-25-81 through 25-83.
  2. The change in expected cash flows on the forecasted transaction is based on the forward price for the commodity.

9. Amend paragraphs 815-20-55-17, 815-20-55-19 and its related heading, 815-20-55-79P, and 815-20-55-79R, supersede paragraphs 815-20-55-26A through 55-26E and their related headings, and add paragraphs 815-20-55-18A through 55-18D, with a link to transition paragraph 815-20-65-7, as follows:

## **Implementation Guidance and Illustrations**

### **> Implementation Guidance**

#### **• > Eligibility of Hedged Items**

#### **• • > Hedged Items in Cash Flow Hedges Only**

**815-20-55-17** This guidance on hedged items in cash flow hedges only is organized as follows:

- a. Exposure to variability in cash flows
- b. Variable price component (or subcomponent) of a ~~purchase contract~~ forecasted transaction to purchase or sell a nonfinancial asset as hedged risk item

- c. Grouping individual transactions
- d. Probability of a **forecasted transaction**
- e. Specificity of timing of a forecasted transaction
- ee. Subparagraph superseded by Accounting Standards Update No. 2025-09. Determining if a **contractually specified component** exists
- eee. Subparagraph superseded by Accounting Standards Update No. 2025-09. Contractually specified component in a not-yet-existing contract
- f. Forecasted acquisition of a marketable debt security
- g. Stock-appreciation-right obligation as a hedged item
- h. First-payments-received technique in hedging variable-~~nonbenchmark~~ interest payments on a group of loans.

••• > **Exposure to Variability in Cash Flows**

**815-20-55-18** The future sale of an asset or settlement of a liability that exposes an entity (consistent with the criterion in paragraph 815-20-25-15(c)(2)) to the risk of a change in fair value may result in recognizing a gain or loss in earnings when the sale or settlement occurs. Changes in market price could change the amount for which the asset or liability could be sold or settled and, consequently, change the amount of gain or loss recognized. **Forecasted transactions** that expose an entity to cash flow risk have the potential to affect reported earnings because the amount of related revenue or expense may differ depending on the price eventually paid or received. Thus, an entity could designate the forecasted sale of a product at the market price at the date of sale as a hedged transaction because revenue will be recorded at that future sales price.

••• > **Variable Price Component (or Subcomponent) of a Purchase Contract-Forecasted Transaction to Purchase or Sell a Nonfinancial Asset as Hedged Risk Item**

**815-20-55-18A** This guidance discusses the implementation of paragraphs 815-20-25-15(i)(3) and 815-20-25-22C.

**815-20-55-18B** An entity may designate the variability in cash flows attributable to changes in a component (or subcomponent) of the forecasted purchase price or sales price of a nonfinancial asset as the hedged risk in a cash flow hedge if the conditions in paragraph 815-20-25-22C are satisfied. The scope of that paragraph includes forecasted transactions to purchase or sell nonfinancial assets consummated in spot markets and in accordance with

arrangements to purchase or sell nonfinancial assets in the future.

**815-20-55-18C** To be eligible to designate a hedge of a variable component of a forecasted purchase price or sales price of a nonfinancial asset in the spot market, paragraph 815-20-25-22C(a) requires that the component being designated as the hedged risk be clearly and closely related (as described in paragraph 815-10-15-32(a) through (b)) to the nonfinancial asset being purchased or sold. If an entity wants to designate a hedge of a variable component of a forecasted purchase or sales price of a nonfinancial asset to be consummated in accordance with a variable price contract, paragraph 815-20-25-22C(b)(1) requires that the component being hedged be both clearly and closely related (as described in paragraph 815-10-15-32(a) through (b)) to the nonfinancial asset being purchased or sold and explicitly referenced in the agreement's pricing formula used to determine that purchase or sales price. Alternatively, if an entity wants to hedge a subcomponent of an explicitly referenced component in an agreement's pricing formula, paragraph 815-20-25-22C(b)(2) requires that the subcomponent be clearly and closely related (as described in paragraph 815-10-15-32(a) through (b)) to that explicitly referenced component and that the explicitly referenced component is clearly and closely related (as described in paragraph 815-10-15-32(a) through (b)) to the nonfinancial asset being purchased or sold.

**815-20-55-18D** If an entity enters into an agreement to purchase or sell a nonfinancial asset that meets the definition of a derivative and the entity applies the normal purchases and normal sales scope exception in Subtopic 815-10, the condition in paragraph 815-20-25-22C(b)(1) is met for the variable pricing component that is explicitly referenced in the agreement. Entities that do not apply the normal purchases and normal sales scope exception in Subtopic 815-10 and account for an agreement to purchase or sell a nonfinancial asset as a derivative may, as permitted by paragraph 815-20-25-15(e), designate a variable component (or subcomponent) of the forecasted purchase price or sales price as the hedged risk as discussed in paragraph 815-20-55-18C if the conditions in paragraph 815-20-25-22C are met.

**815-20-55-19** This guidance discusses several hedge designation methods that an entity may use when hedging the purchase of a nonfinancial asset—the implementation of paragraph 815-20-25-15(i). An entity enters into a contract that requires it to pay a total contract price based on the VWX sugar index on the date of purchase plus a variable basis differential related to transportation costs. The entity may use a derivative instrument whose underlying is the price of sugar or any other underlying for which the derivative would be highly effective in achieving offsetting cash flows attributable to the hedged risk in a

cash flow hedge of its forecasted purchases under the contract. In accordance with paragraph ~~815-20-25-15(i)(2)~~ ~~815-20-25-15(i)~~, the entity may designate as the risk being hedged the risk of changes in the cash flows relating to all changes in the purchase price of the items being acquired under the contract. ~~The~~ ~~In accordance with paragraph 815-20-25-15(i)(3), the~~ entity also may designate the variability in cash flows attributable to changes in a the contractually specified component (or subcomponent) of the purchase price of the nonfinancial asset (VWX sugar index) as the hedged risk. ~~In that case, the entity not only must consider whether~~ In this Example, the entity could designate as the hedged risk the VWX sugar index or the variable basis differential related to transportation costs, both of which are variable components ~~is~~ explicitly referenced in the purchase agreement if the conditions in paragraph 815-20-25-22C(b)(1) are met. The entity also could designate a subcomponent of either the VWX sugar index or transportation costs as the hedged risk. If designating a subcomponent, the entity ~~but also~~ must ensure that the ~~requirements~~ conditions in paragraph ~~815-20-25-22C(b)(2)~~ ~~815-20-25-22A~~ are met. In ~~both~~ all scenarios, the entity must determine that all the criteria for cash flow hedges are satisfied, including that the hedging relationship is highly effective in achieving offsetting cash flows attributable to the hedged risk during the term of the hedge.

#### ~~••• > Determining Whether a Contractually Specified Component Exists~~

~~**815-20-55-26A** Paragraph superseded by Accounting Standards Update No. 2025-09.~~ The definition of a contractually specified component is considered to be met if the component is explicitly referenced in agreements that support the price at which a nonfinancial asset will be purchased or sold. For example, an entity intends to purchase a commodity in the commodity's spot market. If as part of the governing agreements of the transaction or commodities exchange it is noted that prices are based on a pre-defined formula that includes a specific index and a basis, those agreements may be utilized to identify a contractually specified component. After an entity determines that a contractually specified component exists, it must assess whether the variability in cash flows attributable to changes in the contractually specified component may be designated as the hedged risk in accordance with paragraphs 815-20-25-22A through 25-22B.

#### ~~••• > Contractually Specified Component in a Not-Yet-Existing Contract~~

~~**815-20-55-26B** Paragraph superseded by Accounting Standards Update No.~~

~~2025-09. This guidance discusses the implementation of paragraphs 815-20-25-22B and 815-30-35-37A. Entity A's objective is to hedge the variability in cash flows attributable to changes in a contractually specified component in forecasted purchases of a specified quantity of soybeans on various dates during June 20X1. Entity A has executed contracts to purchase soybeans only through the end of March 20X1. Entity A's contracts to purchase soybeans typically are based on the ABC soybean index price plus a variable basis differential representing transportation costs. Entity A expects that the forecasted purchases during June 20X1 will be based on the ABC soybean index price plus a variable basis differential.~~

**815-20-55-26C** Paragraph superseded by Accounting Standards Update No. 2025-09. ~~On January 1, 20X1, Entity A enters into a forward contract indexed to the ABC soybean index that matures on June 30, 20X1. The forward contract is designated as a hedging instrument in a cash flow hedge in which the hedged item is documented as the forecasted purchases of a specified quantity of soybeans during June 20X1. As of the date of hedge designation, Entity A expects the contractually specified component that will be in the contract once it is executed to be the ABC soybean index. Therefore, in accordance with paragraph 815-20-25-3(d)(1), Entity A documents as the hedged risk the variability in cash flows attributable to changes in the contractually specified ABC soybean index in the not yet existing contract. On January 1, 20X1, Entity A determines that all requirements for cash flow hedge accounting are met and that the requirements of paragraph 815-20-25-22A will be met in the contract once executed in accordance with paragraph 815-20-25-22B. Entity A also will assess whether the criteria in 815-20-25-22A are met when the contract is executed.~~

**815-20-55-26D** Paragraph superseded by Accounting Standards Update No. 2025-09. ~~As part of its normal process of assessing whether it remains probable that the hedged forecasted transactions will occur, on March 31, 20X1, Entity A determines that the forecasted purchases of soybeans in June 20X1 will occur but that the price of the soybeans to be purchased will be based on the XYZ soybean index rather than the ABC soybean index. As of March 31, 20X1, Entity A begins assessing the hedge effectiveness of the hedging relationship on the basis of the changes in cash flows associated with the forecasted purchases of soybeans attributable to variability in the XYZ soybean index. Because the hedged forecasted transactions (that is, purchases of soybeans) are still probable of occurring, Entity A may continue to apply hedge accounting~~

~~if the hedging instrument (indexed to the ABC soybean index) is highly effective at achieving offsetting cash flows attributable to the revised contractually specified component (the XYZ soybean index). On April 30, 20X1, Entity A enters into a contract to purchase soybeans throughout June 20X1 based on the XYZ soybean index price plus a variable basis differential representing transportation costs.~~

**815-20-55-26E** Paragraph superseded by Accounting Standards Update No. 2025-09.~~If the hedging instrument is not highly effective at achieving offsetting cash flows attributable to the revised contractually specified component, the hedging relationship must be discontinued. As long as the hedged forecasted transactions (that is, the forecasted purchases of the specified quantity of soybeans) are still probable of occurring, Entity A would reclassify amounts from accumulated other comprehensive income to earnings when the hedged forecasted transaction affects earnings in accordance with paragraphs 815-30-35-38 through 35-41. The reclassified amounts should be presented in the same income statement line item as the earnings effect of the hedged item. Immediate reclassification of amounts from accumulated other comprehensive income to earnings would be required only if it becomes probable that the hedged forecasted transaction (that is, the purchases of the specified quantity of soybeans in June 20X1) will not occur. As discussed in paragraph 815-30-40-5, a pattern of determining that hedged forecasted transactions are probable of not occurring would call into question both an entity's ability to accurately predict forecasted transactions and the propriety of applying cash flow hedge accounting in the future for similar forecasted transactions.~~

- > **Hedge Effectiveness**

- • > **Change in Facts and Circumstances in Qualitative Effectiveness Assessments**

**815-20-55-79O** The following scenarios illustrate the application of paragraphs 815-20-35-2A through 35-2F.

- • • > **Scenario A**

**815-20-55-79P** Entity B expects to purchase 10,000 metric tons of cottonseed meal throughout April 20X3 based on the spot price of the cottonseed meal index on the respective date of each purchase. Entity B wants to hedge the variability in cash flows attributable to changes in the cottonseed meal index

on the price that it will pay for the cottonseed meal. It enters into a forward contract on August 24, 20X1, with a notional of 10,000 metric tons, a maturity of April 1, 20X3, and an underlying of the soybean meal index because no market exists for derivatives indexed to the cottonseed meal index. Concurrent with the execution of the forward, Entity B designates the forward as the hedging instrument in a hedging relationship in which the hedged item is documented as the forecasted purchases of the first 10,000 metric tons of cottonseed meal expected to be purchased during April 20X3 and the hedged risk is documented as the variability in cash flows attributable to changes in the ~~contractually specified cottonseed meal index in the not yet existing contract~~. On August 24, 20X1, Entity B determines that all requirements for cash flow hedge accounting are ~~met and that~~ met, including the requirements of relevant conditions in paragraph 815-20-25-22C on designating the variability in cash flows attributable to changes in a component of the forecasted purchase price of a nonfinancial asset as the hedged risk 815-20-25-22A will be met in the contract once executed in accordance with paragraph 815-20-25-22B. Entity B ~~also will assess whether the criteria in 815-20-25-22A are met in the contract when it is executed.~~

**815-20-55-79Q** Because the hedged risk and forward contract are based on different indexes, the hedging relationship does not qualify for one of the exemptions in paragraph 815-20-25-3(b)(2)(iv)(01). Entity B performs an initial quantitative hedge effectiveness assessment and determines that the hedging instrument is highly effective at achieving offsetting cash flows associated with the hedged item attributable to the hedged risk. In Entity B's hedge documentation, it elects to perform subsequent assessments of hedge effectiveness on a qualitative basis. It makes this election based on the following factors:

- a. The results of the quantitative effectiveness assessment performed at hedge inception indicate that the hedging relationship is close to achieving perfect offset.
- b. Changes in the value of the cottonseed meal index have been consistently highly correlated with changes in value of the soybean meal index such that expected changes in market conditions are not anticipated to prevent the hedging relationship from achieving highly effective offset.
- c. Although the underlyings of the hedging instrument and hedged item do not match, the notional amount of the derivative and the expected

quantity to be purchased do match. Based on the quantitative effectiveness assessment, Entity B also determined that the difference in timing between the maturity date of the derivative and the dates on which the group of forecasted purchases is expected to occur is insignificant.

**815-20-55-79R** During the fourth quarter of 20X1, a storm damages the soybean harvest, which leads to a shortage in soybean meal supply and a sharp increase in the price of soybean meal based on the soybean meal index. The cottonseed meal index has not experienced a similar increase because cotton harvests were unaffected by the storm that damaged the soybean harvest. Because the increase in the soybean meal index is not reflected in the cottonseed meal index, Entity B concludes that a change in facts and ~~circumstance~~ circumstances has occurred that prevents a qualitative assertion in subsequent periods that the hedging relationship continues to be highly effective at achieving offsetting cash flows. Thus, on the next subsequent effectiveness assessment date (December 31, 20X1), the company begins performing quantitative assessments of hedge effectiveness based on the method used to perform the initial prospective assessment of effectiveness. In the effectiveness assessment performed on December 31, 20X1, Entity B determines that the hedging relationship remains highly effective but that it is not close to achieving perfect offset.

**815-20-55-79S** Entity B returns to assessing effectiveness qualitatively as of June 30, 20X2, because the evaluation of the following criteria leads to the conclusion that high effectiveness can be asserted prospectively on a qualitative basis:

- a. Entity B determines that the event that caused the soybean meal index and cottonseed meal index to experience a lack of correlation was temporary, that it was an isolated weather event, and the effect of the weather event has passed.
- b. The changes in value of the soybean meal index and cottonseed meal index reverted to levels of correlation that were consistent with those before the storm.
- c. The results of the June 30, 20X2 quantitative assessment of effectiveness are in line with the results of the quantitative assessment of effectiveness performed at hedge inception.
- d. No further disruptions in supply are expected.

## Amendments to Subtopic 815-30

10. Amend paragraphs 815-30-55-2 through 55-4, 815-30-55-20 through 55-23, 815-30-55-41, 815-30-55-134 and its related heading, 815-30-55-138, and 815-30-55-146 through 55-148 and add paragraphs 815-30-55-149 through 55-164 and their related headings, with a link to transition paragraph 815-20-65-7, as follows:

### Derivatives and Hedging—Cash Flow Hedges

#### Implementation Guidance and Illustrations

##### > Illustrations

##### • > Example 1: Effectiveness of Cash Flow Hedge of a Forecasted Purchase of Inventory with a Forward Contract

**815-30-55-1A** This Example illustrates the application of the guidance in Subtopic 815-20 and this Subtopic to assessing effectiveness for a **cash flow hedge** of a forecasted purchase of inventory with a forward contract in which the forward contract index differs from the index of the underlying hedged transaction. Assume that the entity elected to perform subsequent quarterly hedge effectiveness assessments on a quantitative basis and that all hedge documentation requirements were satisfied at inception.

**815-30-55-2** Entity G forecasts the purchase of 500,000 pounds of Brazilian coffee for U.S. dollars in 6 months. The agreement outlining purchase terms between Entity G and its supplier contains a ~~contractually specified component~~ referencing a pricing formula that explicitly references the Brazilian coffee index denominated in U.S. dollars. Thus, the purchase price will be based on that coffee index as of the delivery date (that is, in six months). Entity G designates the variability in cash flows related to its forecasted purchase of Brazilian coffee attributable to changes in the ~~contractually specified component (Brazilian Brazilian coffee index index)~~ as the hedged risk. Entity G determines that the Brazilian coffee index explicitly referenced in the agreement's pricing formula is clearly and closely related to the forecasted purchase of 500,000 pounds of Brazilian coffee and therefore meets the conditions in paragraph 815-20-25-22C(b)(1). Rather than acquire a **derivative instrument** based on Brazilian coffee, Entity G enters into a 6-month forward contract to purchase 500,000 pounds of Colombian coffee for U.S. dollars and

designates the forward contract as a hedging instrument in a cash flow hedge of the variability in cash flows attributable to changes in the ~~contractually specified~~ explicitly referenced Brazilian coffee index component of its forecasted purchase of Brazilian coffee.

**815-30-55-3** Entity G bases its assessment of hedge effectiveness on changes in forward prices, with the resulting gain or loss discounted to reflect the time value of money. Both at inception and on an ongoing basis, Entity G could assess the effectiveness of the hedge by comparing changes in the expected cash flows from the Colombian coffee forward contract with the expected net change in cash outflows attributable to changes in the ~~contractually specified component~~ price index explicitly referenced in the agreement for purchasing the Brazilian coffee for different market prices. (A simpler method that should produce the same results would consider the expected future correlation of the prices of Brazilian and Colombian coffee, based on the correlation of those prices over past six-month periods.)

**815-30-55-4** In assessing hedge effectiveness on an ongoing basis, Entity G also must consider the extent of offset between the change in expected cash flows on its Colombian coffee forward contract and the expected net change in expected cash flows for the forecasted purchase of Brazilian coffee attributable to changes in the ~~contractually specified~~ designated price component (Brazilian coffee index). Both changes would be measured on a cumulative basis for actual changes in the forward price of the respective coffees during the hedge period.

**815-30-55-5** See Topic 820 (including paragraph 820-10-55-13) for a discussion of expected cash flows.

**815-30-55-6** Because the only difference between the forward contract and forecasted purchase relates to the type of coffee (Colombian versus Brazilian), Entity G could consider the changes in the cash flows on a forward contract for Brazilian coffee to be a measure of perfectly offsetting changes in cash flows for its forecasted purchase of Brazilian coffee. For example, for given changes in the U.S. dollar prices of six-month and three-month Brazilian and Colombian contracts, Entity G could compute the effect of a change in the price of coffee on the expected cash flows of its forward contract on Colombian coffee and of a forward contract for Brazilian coffee as follows.

	<b>Estimate of Change in Cash Flows</b>	
	<b><i>Hedging Instrument: Forward Contract on Colombian Coffee</i></b>	<b><i>Estimate of Forecasted Transaction: Forward Contract on Brazilian Coffee</i></b>
Forward price of Colombian and Brazilian coffee:		
At hedge inception—6-month price	\$ 2.54	\$ 2.43
3 months later—3-month price	2.63	2.53
Cumulative change in price—gain	\$ 0.09	\$ 0.10
× 500,000 pounds of coffee	× 500,000	× 500,000
Estimate of change in cash flows	<u>\$ 45,000</u>	<u>\$ 50,000</u>

**815-30-55-7** See Topic 820 (including paragraph 820-10-55-13) for a discussion of expected cash flows.

**815-30-55-8** Using the amounts in paragraph 815-30-55-6, Entity G could evaluate effectiveness 3 months into the hedge on its first subsequent quarterly effectiveness assessment testing date by comparing the \$45,000 change on its Colombian coffee contract with what would have been a perfectly offsetting change in cash flow for its forecasted purchase—the \$50,000 change on an otherwise identical forward contract for Brazilian coffee. Entity G concludes that the hedging relationship would be highly effective, and it would record the \$45,000 change in the fair value of the forward contract on Colombian coffee in other comprehensive income.

- a. Subparagraph superseded by Accounting Standards Update No. 2017-12.
- b. Subparagraph superseded by Accounting Standards Update No. 2017-12.

• > **Example 5: Cash Flow Hedge of the Forecasted Sale of a Commodity When the Critical Terms Match**

**815-30-55-20** This Example illustrates the application of the guidance in paragraphs 815-20-25-84 through 25-85 and this Subtopic to the accounting for a cash flow hedge of a forecasted sale of a commodity. The terms of the hedging derivative have been negotiated to match the terms of the designated price component of the forecasted transaction. ~~Assume that there is no time value in the derivative instrument.~~ Entity ABC has chosen to hedge the variability of the cash flows from the forecasted sale of the commodity instead of the changes in its fair value. For simplicity, the time value in the derivative instrument and commissions and most other transaction costs, initial margin,

and income taxes are ignored unless otherwise stated. Assume that there are no changes in creditworthiness that would alter the effectiveness of the hedging relationship.

**815-30-55-21** Entity ABC seeks to hedge the variability of cash flows from the forecasted sale of Commodity A in the spot market at a future date. Accordingly ~~Because there is no contractually specified component~~, Entity ABC hedges the risk of changes in its cash flows relating to changes in the sales price of a forecasted sale of 100,000 bushels of Commodity A in the spot market by entering into a derivative instrument, Derivative DEF Z. Entity ABC expects to sell the 100,000 bushels of Commodity A on the last day of Period 1. On the first day of Period 1, Entity ABC enters into Derivative DEF Z and designates it as a cash flow hedge of changes in the DEF index component of the forecasted sales price sale. Entity ABC determines that the DEF index is clearly and closely related (as described in paragraph 815-10-15-32(a) through (b)) to Commodity A in the pertinent spot market and concludes that the conditions in paragraph 815-20-25-22C(a) are met. Entity ABC ~~neither pays nor receives a premium on Derivative Z (that is, its fair value is zero).~~ Entity ABC expects that there will be perfect offset between the hedging instrument and the hedged item because all of the following conditions exist:

- a. The notional amount of Derivative DEF Z is 100,000 bushels and the forecasted sale is for 100,000 bushels.
- b. The **underlying** of Derivative DEF Z is the price of the same as the designated price component variety and grade of Commodity A that Entity ABC expects to sell ~~(assuming delivery to Entity ABC's selling point).~~
- c. The settlement date of Derivative DEF Z is the last day of Period 1 and the forecasted sale is expected to occur on the last day of Period 1.
- d. Entity ABC neither pays nor receives a premium on Derivative DEF (that is, its fair value is zero).

The entity need not perform an initial quantitative assessment of hedge effectiveness in accordance with paragraph 815-20-25-3(b)(2)(iv)(01) because the conditions in paragraphs 815-20-25-84 through 25-85 are met.

**815-30-55-22** At inception of the hedge, the expected sales price of 100,000 bushels of Commodity A is \$1,100,000. On the last day of Period 1, the fair value of Derivative DEF Z has increased by \$25,000, and the expected sales price of 100,000 bushels of Commodity A has decreased by \$25,000 because

of changes attributable to the DEF index. Both the sale of 100,000 bushels of Commodity A and the settlement of Derivative DEF Z occur on the last day of Period 1. The following table illustrates the accounting, including the net effect on earnings and other comprehensive income, for the situation described.

	Debit (Credit)			
	Cash	Derivative	Other Comprehensive Income	Earnings <sup>(a)</sup>
Recognize change in fair value of derivative		\$ 25,000	\$ (25,000)	
Recognize revenue from sale	\$ 1,075,000			\$ (1,075,000)
Recognize settlement of derivative	25,000	(25,000)		
Reclassify change in fair value of derivative to earnings			25,000	(25,000)
Total	<u>\$ 1,100,000</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ (1,100,000)</u>

(a) The change in fair value of the hedging derivative is presented in the same income statement line item as the earnings effect of the hedged item.

**815-30-55-23** At the inception of the hedge, Entity ABC anticipated that it would receive \$1,100,000 from the sale of 100,000 bushels of Commodity A. This Example illustrates that by hedging the risk of changes in its cash flow variability attributable flows relating to changes in the DEF index component of the forecasted sale of 100,000 bushels of Commodity A, Entity ABC still received a total of \$1,100,000 in cash flows even though the sales price of Commodity A declined during the period.

• > **Example 8: Designation and Discontinuance of a Cash Flow Hedge of the Forecasted Purchase of Inventory**

**815-30-55-40** This Example illustrates the effect on earnings and other comprehensive income of discontinuing a cash flow hedge by dedesignating the hedging derivative under paragraph 815-30-40-1(c) before the variability of the cash flows from the hedged forecasted transaction has been eliminated. It also discusses the effect that the location of a physical asset has on the effectiveness of a hedging relationship. For simplicity, commissions and most other transaction costs, initial margin, and income taxes are ignored unless otherwise stated. Assume that there are no changes in creditworthiness that would alter the effectiveness of the hedging relationship.

**815-30-55-41** On February 3, 20X1, Entity JKL forecasts the purchase of 100,000 bushels of corn on May 20, 20X1. ~~The contract does not contain a~~ **contractually specified component**, and Entity JKL designates changes in cash flows related to the forecasted transaction attributable to all changes in the purchase price as the hedged risk. It expects to sell finished products

produced from the corn on May 31, 20X1. On February 3, 20X1, Entity JKL enters into 20 futures contracts, each for the purchase of 5,000 bushels of corn on May 20, 20X1 (100,000 in total), and designates those contracts as a hedging instrument in a cash flow hedge of the forecasted purchase of corn.

• > **Example 22: Assessing Effectiveness of a Cash Flow Hedge of a Forecasted Purchase of Inventory with a Forward Contract**  
**(Contractually Specified Component)**

**815-30-55-134** This Example illustrates the application of the guidance in Subtopic 815-20 and this Subtopic for assessing effectiveness for a cash flow hedge of a forecasted purchase of inventory with a forward contract for which the hedged risk is variability in cash flows attributable to changes in a—~~an~~ explicitly referenced variable component of the purchase price of the inventory contractually specified component. Assume the entity elects to perform subsequent assessments of hedge effectiveness on a quantitative basis using a cumulative-dollar-offset approach and all hedge documentation requirements were satisfied at inception.

**815-30-55-135** Entity J manufactures keys for door locks on buildings and cars. The keys are cut from sheets of metal called *key plates*. Entity J primarily purchases its key plates from Supplier 1 as needed. Supplier 1 and Entity J have an outstanding agreement specifying that the per-unit cost of each key plate will be determined by Supplier 1 on the first business day of each month on the basis of the following pricing formula:

- a. Spot price of COMEX Zinc per pound × 0.2 pounds, plus
- b. Spot price of COMEX Copper per pound × 0.1 pounds, plus
- c. The current cost of refining copper and zinc into key plates, plus
- d. The current cost of transporting the key plates to Entity J.

**815-30-55-136** In January 20X1, Entity J expects to purchase 100,000 key plates in July 20X1, which requires 10,000 pounds of copper for the manufacturing process. Entity J decides that it wishes to hedge only the change in value of the price of COMEX Copper used to create the key plates being purchased in July 20X1.

**815-30-55-137** On January 15, 20X1, Entity J enters into a forward contract maturing on July 1, 20X1 (that is, the date on which the price of copper used to manufacture the key plates is fixed) to purchase 10,000 pounds of COMEX Copper at \$2.10 per pound. Any settlement amount on the forward contract will be based on the difference between the contract price of \$2.10 per pound and the spot price of COMEX Copper on the maturity date (July 1, 20X1), multiplied by the notional amount of 10,000 pounds.

**815-30-55-138** Entity J designates a cash flow hedge in which the hedging instrument is the forward contract, the hedged item is the forecasted purchase of key plates in July 20X1, and the hedged risk is the variability in the purchase price of the key plates attributable to changes in the COMEX Copper price index. index, which is a contractually specified component within the frame agreement. Entity J documents in its hedge documentation that the requirements to designate variability in cash flows attributable to changes in a contractually specified component as the hedged risk in paragraph 815-20-25-22A are met. Entity J determines that the COMEX Copper price index explicitly referenced in the agreement's pricing formula is clearly and closely related (as described in paragraph 815-10-15-32(a) through (b)) to key plates and concludes that the conditions in paragraph 815-20-25-22C(b)(1) are met.

**815-30-55-139** Entity J bases its assessment of hedge effectiveness on cumulative changes in the fair value of the hedging instrument and the hedged item attributable to changes in the hedged risk.

**815-30-55-140** In assessing hedge effectiveness on an ongoing basis, Entity J must consider the extent of offset between the change in expected cash flows on the hedging instrument (the copper forward contract) and the hedged item attributable to changes in the hedged risk (change in expected cash flows associated with forecasted purchases of key plates attributable to changes in the COMEX Copper price index). The table below illustrates the cumulative changes in the hedging instrument and hedged item attributable to changes in the hedged risk as of the first subsequent quarterly effectiveness assessment date.

	Estimate of Change in Cash Flows	
	Hedging Instrument	Hedged Item Due to Fluctuation in Hedged Risk
Forward price of copper (dollars per pound)		
At hedge inception (Jan 15, 20X1)	\$ 2.10	\$ 2.10
At first subsequent assessment date (March 31, 20X1)	\$ 2.25	\$ 2.25
Change in forward price of copper	\$ 0.15	\$ 0.15
Cumulative change in copper (per pound) × 10,000 pounds of copper	\$ 1,500.00	\$ 1,500.00

**815-30-55-141** Entity J could assess effectiveness as of March 31, 20X1, by comparing the \$1,500 change in the hedging instrument with the \$1,500 change in the hedged item attributable to changes in the hedged risk because the hedging instrument's maturity date and the date on which the price of copper will be fixed match (that is, July 1, 20X1).

• > **Example 23: Designation of a Cash Flow Hedge of a Forecasted Purchase of Inventory for Which Commodity Exposure Is Managed Centrally**

**815-30-55-142** This Example illustrates the application of the guidance in Subtopic 815-20 and this Subtopic to the designation of a **cash flow hedge** of a forecasted purchase of inventory in which the commodity exposure is managed centrally at the aggregate level. Assume the entity elects to perform subsequent assessments of hedge effectiveness on a qualitative basis and all hedge documentation requirements were satisfied at inception.

**815-30-55-143** Entity Q is seeking to hedge the variability in cash flows associated with commodity price risk of its monthly plastic purchases for the next 12 months. It has two different manufacturing plant locations (Plant A and Plant B) that are purchasing five different grades of plastic from Supplier A. The plastic purchase price for each month is based on the month-end Joint Plastic (JP) index and a fixed basis differential component. The fixed basis differential offered by the supplier is determined by:

- a. The grade of the plastic purchased
- b. The distance between the plant location and supplier location.

**815-30-55-144** At January 1, 20X1, Entity Q enters into a supply agreement with Supplier A to purchase plastic over the next 12 months. The respective agreements allow Entity Q to purchase the various grades of plastic at both of its plant locations as the need arises over the following year. The following table

summarizes the pricing provisions contained in the supply agreement for each grade of plastic.

	<u>Grade 1</u>	<u>Grade 2</u>	<u>Grade 3</u>	<u>Grade 4</u>	<u>Grade 5</u>
Plant A	JP + \$0.14	JP + \$0.11	JP + \$0.09	JP + \$0.05	JP – \$0.02
Plant B	JP + \$0.16	JP + \$0.12	JP + \$0.07	JP + \$0.06	JP – \$0.03

**815-30-55-145** Entity Q’s risk management objective is to hedge the variability in the purchase price of plastic attributable to changes in the JP index of the first 80,000 pounds of plastic purchased in each month regardless of grade or plant location delivered to. To accomplish this objective, Entity Q executes 12 separate forward contracts at January 1, 20X1, to purchase plastic as follows.

	<u>Settlement Date</u>	<u>Notional Amount</u>	<u>Underlying Index</u>
Jan forward	January 30, 20X1	80,000 (lbs)	JP
Feb forward	February 28, 20X1	80,000 (lbs)	JP
Mar forward	March 30, 20X1	80,000 (lbs)	JP
April forward	April 30, 20X1	80,000 (lbs)	JP
May forward	May 30, 20X1	80,000 (lbs)	JP
June forward	June 30, 20X1	80,000 (lbs)	JP
July forward	July 30, 20X1	80,000 (lbs)	JP
Aug forward	August 30, 20X1	80,000 (lbs)	JP
Sep forward	September 30, 20X1	80,000 (lbs)	JP
Oct forward	October 30, 20X1	80,000 (lbs)	JP
Nov forward	November 30, 20X1	80,000 (lbs)	JP
Dec forward	December 30, 20X1	80,000 (lbs)	JP

**815-30-55-146** Entity Q ~~determines that the variable JP index referenced in the supply agreement constitutes a contractually specified component and that the requirements to designate designates the variability in the cash flows attributable to changes in a contractually specified the JP index component as the hedged risk in paragraph 815-20-25-22A are met. Entity Q determines that the JP index explicitly referenced in the supply agreement is clearly and closely related (as described in paragraph 815-10-15-32(a) through (b)) to plastic and concludes that the conditions in paragraph 815-20-25-22C(b)(1) are met.~~

**815-30-55-147** Because Entity Q determined that it will purchase at least 80,000 pounds of plastic each month in the coming 12 months to fulfill its expected manufacturing requirements, it documents that the hedged item (that is, the **forecasted transaction** within each month) is probable of occurring. Entity Q designates each forward contract as a cash flow hedge of the variability in cash flows attributable to changes in the contractually specified explicitly referenced JP index on the first 80,000 pounds of plastic purchased

(regardless of grade or plant location delivered to) for the appropriate month. ~~The individual purchases of differing grades of plastic by Plant A and Plant B during each month share the risk exposure to the variability in the purchase price of the plastic attributable to changes in the contractually specified JP index. Therefore, the individual transactions in the hedged portfolio of plastic purchases for each month share the same risk exposure for which they are designated as being hedged in accordance with paragraph 815-20-25-15(a)(2).~~ **[For convenience, this paragraph also contains the amendments from Issue 1.]**

**815-30-55-148** In accordance with paragraph 815-20-25-3(b)(2)(iv)(01)(B), if Entity Q has determined that the critical terms of the hedged item and hedging instrument match, it may elect to assess effectiveness qualitatively both at inception of the hedging relationship and on an ongoing basis on the basis of the following factors in accordance with paragraphs 815-20-25-84 through 25-85:

- a. The hedging instrument's underlying matches the index upon which plastic purchases will be determined (that is, the JP index ~~index~~).
- b. The notional of the hedging instrument matches the forecasted quantity designated as the hedged item.
- c. The date on which the derivatives mature matches the timing in which the forecasted purchases are expected to be made. That is, the quantity of the hedged item, ~~80,000 pounds,~~ (80,000 pounds) is an aggregate amount expected to be purchased over the course of the respective month (that is, the same 31-day period) in which the derivative matures.
- d. Each hedging instrument was traded with at-market terms (that is, it has an initial fair value of zero).
- e. Assessment of effectiveness will be performed on the basis of the total change in the fair value of the hedging instrument.
- f. Although the amount of plastic being hedged each period is a cumulative amount across multiple grades of plastic, the basis differentials between grades of plastic and location are not required to be included in assessments of effectiveness because Entity Q has designated the variability in cash flows attributable to changes in the JP index ~~(the contractually specified component)~~ (the explicitly referenced variable component of the forecasted purchase price) as the hedged risk ~~within its purchases of plastics.~~

In accordance with paragraph 815-20-55-23B, if Entity Q assesses hedge effectiveness in accordance with paragraphs 815-20-25-84 through 25-85 and applies the similar risk assessment method described in paragraph 815-20-55-23A(a), it also may assume that the hedged risks related to the group of forecasted transactions are similar. [For convenience, this paragraph also contains the amendments from Issue 1.]

**• > Example 24: Designation of a Price Component as the Hedged Risk in a Forecasted Purchase of Nonfinancial Assets in a Cash Flow Hedge for Which Any Contractual Shortfall Is Expected to Be Purchased in the Spot Market**

**815-30-55-149** This Example illustrates the application of the guidance in paragraphs 815-20-25-15(e) and 815-20-25-22C to determine whether a price component is eligible to be designated as the hedged risk in a forecasted purchase of nonfinancial assets in which the associated forward contracts are accounted for as derivatives because physical settlement is not probable of occurring but it is probable that any shortfall will be purchased in the spot market. On January 1, 20X1, Entity R enters into forward contracts with multiple suppliers to purchase an aggregate 1,000 bushels of soybeans for delivery in June 20X1 to use in its operations. Each contract stipulates that the purchase price per bushel is equal to the ABC soybean index price (June maturity) plus a variable basis differential representing transportation costs. Furthermore, each contract permits net settlement of the contract if the quality of the soybeans delivered does not meet Entity R's specifications. If that happens, Entity R will net settle the affected forward contracts and purchase soybeans of the appropriate specifications in the spot market to make up for any shortfall. Given a history of suppliers not delivering soybeans meeting the required specifications, Entity R cannot assert that any specific forward contract will be physically settled and, therefore, determines that the forward contracts do not qualify for the normal purchases and normal sales scope exception.

**815-30-55-150** On January 1, 20X1, Entity R enters into a futures contract to fix the price of 1,000 bushels of ABC soybeans in accordance with its risk management objective. Entity R designates this futures contract as a hedge of the variability in cash flows attributable to changes in the ABC soybean index (a component of the price of soybeans) related to the first 1,000 bushels of soybeans forecasted to be purchased in June 20X1. The forecasted purchases

include ABC soybeans purchased from suppliers in accordance with forward contracts and ABC soybeans purchased in the spot market.

**815-30-55-151** Entity R determines that the ABC soybean index is an eligible hedged risk for the forecasted purchase of 1,000 bushels of ABC soybeans for delivery in June 20X1 either in the spot market or in accordance with the supplier contracts. To reach that conclusion, Entity R performs two distinct assessments. In accordance with paragraph 815-20-25-22C(a), Entity R determines that the ABC soybean index (that is, the hedged variable component) is clearly and closely related to the nonfinancial asset being purchased (that is, ABC soybeans in the pertinent spot market). In accordance with paragraph 815-20-25-22C(b)(1), Entity R determines that the ABC soybean index (that is, the hedged variable component) is explicitly referenced in the pricing formula of the supplier contracts and that the ABC soybean index is clearly and closely related to ABC soybeans purchased in accordance with the supplier contracts. Although Entity R is unable to assert that forward contracts with suppliers are probable of physical settlement, Entity R can assert that the forecasted transactions are probable of occurring through a combination of physically settled forward contracts and spot market transactions.

**• > Example 25: Designation of a Price Subcomponent of an Explicitly Referenced Component in an Agreement as the Hedged Risk in a Cash Flow Hedge of a Forecasted Purchase of Nonfinancial Assets**

**815-30-55-152** This Example illustrates the application of the guidance in paragraph 815-20-25-22C to determine whether a subcomponent of a component that is explicitly referenced in an agreement can be designated as the hedged risk in a cash flow hedge of a forecasted purchase of a nonfinancial asset.

**815-30-55-153** Entity X is a manufacturing company that uses copper wire (that is, copper that has been drawn down to size and processed for manufacturing purposes) in the normal course of business. On January 1, 20X1, Entity X enters into a supply agreement to purchase 1,000 pounds of copper wire for its manufacturing operations in each of the next 12 months. The supply agreement stipulates that the monthly purchase price per pound is equal to the ABC Copper Wire index price (maturing in month of delivery), plus other basis differentials. Entity X determines that the supply agreement meets the definition of a derivative in Topic 815.

**815-30-55-154** Entity X is seeking to reduce its commodity price exposure to the forecasted purchase of 1,000 pounds of copper wire in each of the next 12 months. Derivatives referencing the ABC Copper Wire index are less liquid than derivatives referencing the core underlying ingredient in copper wire, which is raw copper. Entity X determines that the market for the ABC Copper Wire index is based on the price of raw copper plus processing costs, that it takes one pound of raw copper to produce one pound of copper wire, and that raw copper prices are based on COMEX Copper futures. Therefore, on January 1, 20X1, Entity X executes 12 futures contracts, each having a 1,000-pound notional amount tied to the COMEX Copper index futures price (maturing in successive months). Those derivatives are designated as hedging the risk of cash flow variability attributable to the COMEX Copper index (a subcomponent of the explicitly referenced ABC Copper Wire index) related to its forecasted purchase of the first 1,000 pounds of copper wire per month.

**815-30-55-155** Entity X applies the normal purchases and normal sales scope exception in accordance with Subtopic 815-10 to the contract to purchase copper wire. Therefore, Entity X determines that the condition in paragraph 815-20-25-22C(b)(1) is met and the ABC Copper Wire index (the explicitly referenced component in the forward contract) is clearly and closely related (as described in paragraph 815-10-15-32(a) through (b)) to the forecasted transaction in accordance with paragraph 815-20-55-18D. In addition, Entity X determines that the COMEX Copper index is clearly and closely related (as described in paragraph 815-10-15-32(a) through (b)) to the explicitly referenced ABC Copper Wire index. Thus, Entity X determines that the COMEX Copper index is an eligible risk subcomponent in accordance with paragraph 815-20-25-22C(b)(2).

**• > Example 26: Designation of a Price Component as the Hedged Risk in a Cash Flow Hedge of a Forecasted Purchase of Nonfinancial Assets in the Spot Market**

**815-30-55-156** This Example illustrates the application of the guidance in paragraph 815-20-25-22C to determine whether a price component in a forecasted purchase of a nonfinancial asset in the spot market is eligible to be designated as the hedged risk.

**815-30-55-157** On December 31, 20X0, Entity C forecasts that it will purchase at least 20,000 MMBtus of natural gas in the spot market for production purposes in June 20X1. On January 1, 20X1, Entity C enters into a futures

contract to fix the price of 20,000 MMBtus of natural gas that is tied to the XYZ National NatGas index (June 20X1 maturity) in accordance with its risk management objective. Entity C designates the futures contract as the hedging instrument in a cash flow hedge of the variability in cash flows attributable to the XYZ National NatGas index component related to its forecasted purchase of the first 20,000 MMBtus of natural gas in the spot market in June 20X1.

**815-30-55-158** Entity C concludes that agreements to purchase natural gas in this region are frequently priced using one of the following formulas:

- a. ABC Regional NatGas index price + Fixed Spread
- b. XYZ National NatGas index price + Cost to Transport + Fixed Spread.

Purchases of natural gas in this region are often tied to the ABC Regional NatGas index because it reflects the natural gas prices of the closest geographical proximity to an entity. Additionally, the XYZ National NatGas index is a nationally recognized index that is commonly used by market participants to price contracts throughout the country, adjusted for the cost to transport that natural gas to various hubs for sale. Entity C reasonably determines that the ABC Regional NatGas index and the XYZ National NatGas index are not extraneous to changes in the fair value of natural gas in the region of the transaction.

**815-30-55-159** Entity C determines that the XYZ National NatGas index component is clearly and closely related (as described in paragraph 815-10-15-32(a) through (b)) to the forecasted purchase of natural gas in the spot market in accordance with paragraph 815-20-25-22C(a). Because the price of natural gas being purchased by Entity C is not set forth in an agreement, the guidance in paragraph 815-20-25-22C(b) would not apply. If Entity C had chosen to designate the ABC Regional NatGas index as the hedged risk and determined that this index was clearly and closely related to the forecasted purchase of natural gas in the spot market, that also would be permissible under paragraph 815-20-25-22C(a).

**• > Example 27: Designation of Multiple Price Components as the Hedged Risks in a Group of Forecasted Purchases of Nonfinancial Assets in Not-Yet-Existing Contracts**

**815-30-55-160** This Example illustrates the application of the guidance in paragraph 815-20-25-22C to determine whether multiple price components are eligible to be designated as the hedged risks in a group of forecasted purchases of nonfinancial assets when uncertainty exists about which component or components will be explicitly referenced in the pricing formulas of not-yet-existing contracts.

**815-30-55-161** Entity Y's objective is to hedge the variability in cash flows attributable to changes in the explicitly referenced component or components in not-yet-existing agreements to purchase 1,000 bushels of soybeans. On January 1, 20X1, Entity Y begins negotiations with multiple vendors to purchase 1,000 bushels of soybeans on June 30, 20X2. As of April 1, 20X1, the counterparties have not agreed on whether the pricing formula of the agreements will price the soybeans on the basis of the ABC Soybean index or the DEF Soybean index. Entity Y concludes that it is probable that 1,000 bushels of soybeans will be purchased and that the pricing formula in the agreements will reference any combination of the ABC Soybean index and the DEF Soybean index.

**815-30-55-162** On April 1, 20X1, Entity Y enters into a futures contract for 1,000 bushels of ABC Soybeans maturing on June 30, 20X2. Entity Y designates that futures contract as a hedge of cash flow variability attributable to the designated hedged risk for the forecasted purchase of the first 1,000 bushels of soybeans purchased under agreements with a pricing formula that references any combination of the ABC Soybean index and the DEF Soybean index on June 30, 20X2. Because of the uncertainty of whether the not-yet-existing agreements' pricing formulas will reference the ABC Soybean index or the DEF Soybean index, Entity Y designates both indexes as the hedged risks in the cash flow hedge.

**815-30-55-163** At hedge inception, Entity Y expects that the forecasted transactions will have multiple risks occurring at the same time (that is, the purchase agreements will reference a combination of the ABC Soybean index and the DEF Soybean index), but Entity Y is uncertain what combination of the ABC Soybean index and the DEF Soybean index will be explicitly referenced in the pricing formulas in the agreements. Entity Y determines that both the ABC Soybean index and the DEF Soybean index will be eligible components for designation in accordance with paragraph 815-20-25-22C(b) upon execution of the purchase agreements. Entity Y elects to assess whether the

hedged risks in the group of individual forecasted transactions have similar risk exposure by assessing whether the designated hedging instrument is highly effective in achieving offsetting changes in cash flows attributable to each hedged risk in the group, on an individual basis, in accordance with paragraph 815-20-55-23A(a). That is, Entity Y assesses and determines that the hedging instrument is highly effective against both designated risks (ABC and DEF Soybean indexes) in the group. Entity Y uses that assessment as a “dual purpose” test to support that the forecasted transactions in the group are similar and that the hedging instrument is highly effective at achieving offsetting cash flows of the forecasted transactions, regardless of whether the ABC Soybean index or the DEF Soybean index is ultimately referenced in the not-yet-existing agreements’ pricing formulas.

**815-30-55-164** On June 30, 20X1, Entity Y enters into forward contracts with multiple vendors. Each agreement includes a pricing formula referencing either the ABC Soybean index or the DEF Soybean index, with a June 30, 20X2 delivery date. The hedging relationship continues to be eligible for hedge accounting in accordance with paragraph 815-20-25-22C(b). Entity Y determines that the designated hedged risks (ABC and DEF Soybean indexes) in the group are similar because the hedging instrument is highly effective against both risks in the group in accordance with paragraph 815-20-55-23A(a). Therefore, Entity Y concludes that the relationship continues to be eligible for hedge accounting.

## Issue 4: Net Written Options as Hedging Instruments

### Amendments to Subtopic 815-20

11. Amend paragraph 815-20-25-88 and its related headings, with a link to transition paragraph 815-20-65-7, as follows:

#### **Derivatives and Hedging—Hedging—General**

##### **Recognition**

###### **> Hedge Effectiveness**

- **> Hedge Effectiveness Criteria Applicable to both Fair Value Hedges and Cash Flow Hedges**

• • > **Hedge Effectiveness When the Hedging Instrument Is an Option or Combination of Options Instruments**

• • • > **Determining Whether a Combination of Options Instruments Is Net Written**

**815-20-25-88** This guidance addresses how an entity shall determine whether a combination of options is considered a net written option subject to the requirements of paragraph 815-20-25-94. A combination of options (for example, an interest rate collar) entered into contemporaneously shall be considered a written option if either at inception or over the life of the contracts a net premium is received in cash or as a favorable rate or other term. ~~Furthermore, a derivative instrument that results from combining a written option and any other non-option derivative instrument shall be considered a written option.~~ The determination of whether a combination of options is considered a net written option depends in part on whether strike prices and notional amounts of the options remain constant. Furthermore, a derivative instrument that results from combining a written option and any other non-option derivative instrument shall be considered a written option unless all of the following criteria are satisfied:

- a. The derivative is designated as the hedging instrument in a cash flow hedge or fair value hedge of interest rate risk (including the interest rate risk portion of a hedge of both interest rate risk and foreign exchange risk).
- b. The hedging instrument is a combination of a written option and a swap.
- c. The notional amount of the written option matches the notional amount of the swap.

For example, an entity designates a receive-fixed, pay-variable interest rate swap with a 1 percent floor and a variable leg that is indexed to Daily SOFR as the hedging instrument in a cash flow hedge of interest rate risk. The notional amounts of the interest rate swap and the interest rate floor match. The forecasted transactions are designated as the interest payments on a portfolio of variable-rate loans that are indexed to 1-Month Term SOFR with a 1 percent floor. The combination of the interest rate swap and the interest rate floor is not considered a net written option. Therefore, the entity would not apply the net written option test to that hedging relationship.

## Issue 5: Foreign-Currency-Denominated Debt Instrument as Hedging Instrument and Hedged Item (Dual Hedge)

### Amendments to Subtopic 815-20

12. Amend paragraphs 815-20-55-38 and 815-20-55-129, with a link to transition paragraph 815-20-65-7, as follows:

### **Derivatives and Hedging—Hedging—General**

#### **Implementation Guidance and Illustrations**

##### **> Implementation Guidance**

##### **• > Eligibility of Hedged Items**

##### **• • > Hedged Items Involving Foreign Exchange Risk**

##### **• • • > Foreign-Currency-Denominated Debt Instrument as both Hedging Instrument and Hedged Item**

**815-20-55-38** A foreign-currency-denominated debt instrument that is designated as the hedging instrument in a net investment hedge may also be designated as the hedged item in a fair value hedge of **interest rate risk**. The two hedging relationships address separate risk types that are permitted to be hedged individually under this Subtopic. When a foreign-currency-denominated debt instrument is designated as both a hedging instrument and a hedged item, an entity should exclude from the assessment of effectiveness in the net investment hedging relationship the fair value hedge basis adjustment resulting from designating the foreign-currency-denominated debt instrument in the fair value hedge. In those situations, an entity should recognize gains and losses from the remeasurement of the foreign-currency-denominated debt instrument's fair value basis adjustment at the spot exchange rate currently in earnings in accordance with Subtopic 830-20. If the fair value hedge of the foreign-currency-denominated debt instrument is subsequently discontinued in accordance with the guidance in Section 815-25-40, an entity should consider the foreign-currency-denominated debt instrument's fair value hedge basis adjustment when prospectively assessing the effectiveness of the net investment hedge after the date of discontinuing

the fair value hedge. Excluding the fair value hedge basis adjustment from the assessment of effectiveness in the designated net investment hedging relationship should not be applied by analogy to other circumstances. Example 10 (see paragraph 815-20-55-127) illustrates this circumstance—the circumstances in which a foreign-currency-denominated debt instrument that is designated as the hedging instrument in a net investment hedge also is designated as the hedged item in a fair value hedge of interest rate risk.

## > Illustrations

### • > Example 10: Foreign-Currency-Denominated Debt Instrument as both Hedging Instrument and Hedged Item

**815-20-55-127** This Example illustrates the application of paragraph 815-20-55-38.

**815-20-55-128** A U.S. parent entity (Parent A) with a U.S. dollar (USD) functional currency has a German subsidiary that has the Euro (EUR) as its functional currency. On January 1, 2001, Parent A issues a five-year, fixed-rate EUR-denominated debt instrument and designates that EUR-denominated debt instrument as a hedge of its net investment in the German subsidiary. On the same date, Parent A enters into a five-year EUR-denominated receive-fixed, pay-Euribor-interest rate swap. Parent A designates the interest rate swap as a hedge of the foreign-currency-denominated fair value of the fixed-rate EUR-denominated debt instrument attributable to changes in Euribor interest rates, which is considered the benchmark interest rate for a hedge of the EUR-denominated fair value of that instrument.

**815-20-55-129** As permitted by paragraph 815-20-55-38, Parent A may designate the EUR-denominated debt instrument as a hedge of its net investment in the German subsidiary and also as the hedged item in a fair value hedge of the debt instrument's foreign-currency-denominated fair value attributable to changes in the designated benchmark interest rate. As a result of applying fair value hedge accounting, the debt's carrying amount will be adjusted to reflect changes in its foreign-currency-denominated fair value attributable to interest rate risk. Parent A should exclude the fair value hedge basis adjustment from the assessment of effectiveness in the designated net investment hedging relationship. Accordingly, the ~~The~~ notional amount of the debt that is designated as the hedging instrument in the net investment hedge will not change over time as a result of applying fair value hedge accounting such that it may ~~not continue to match the notional amount portion of the net investment being hedged—net investment~~. The entity then applies the net investment hedge guidance in Subtopic 815-35 and the fair value hedge

guidance in Subtopic 815-25. Because the debt's fair value hedge basis adjustment is not included in the assessment of effectiveness of the net investment hedging relationship, the effect of changes in the spot rate on the fair value hedge basis adjustment is recognized currently in earnings in accordance with Subtopic 830-20. As discussed in paragraphs 815-35-35-13 through 35-14, because the notional amount of the nonderivative instrument designated as a hedge of the net investment does not match the portion of the net investment designated as being hedged, hedge effectiveness is assessed by comparing the following two values:

- a. The foreign currency transaction gain or loss based on the spot rate change (after tax effects, if appropriate) of that nonderivative hedging instrument
- b. The transaction gain or loss based on the spot rate change (after tax effects, if appropriate) that would result from the appropriate hypothetical nonderivative instrument that has a notional amount that matches the portion of the net investment being hedged. The hypothetical nonderivative instrument also would have a maturity that matches the maturity of the actual nonderivative instrument designated as the net investment hedge.

13. Add paragraph 815-20-65-7 and its related heading as follows:

## **Transition and Open Effective Date Information**

### **> Transition Related to Accounting Standards Update No. 2025-09, *Derivatives and Hedging (Topic 815): Hedge Accounting Improvements***

**815-20-65-7** The following represents the transition and effective date information related to Accounting Standards Update No. 2025-09, *Derivatives and Hedging (Topic 815): Hedge Accounting Improvements*:

#### **Effective date and early adoption**

- a. For public business entities, the pending content that links to this paragraph shall be effective for annual reporting periods beginning after December 15, 2026, and interim reporting periods within those annual reporting periods.
- b. For entities other than public business entities, the pending content that links to this paragraph shall be effective for annual reporting periods beginning after December 15, 2027, and interim reporting periods within those annual reporting periods.

- c. Early adoption of the pending content that links to this paragraph is permitted for all entities on any date on or after [date of issuance of Update 2025-09].

### **Transition method**

- d. An entity shall apply the pending content that links to this paragraph on a prospective basis, including the guidance described in (e) for existing hedging relationships (that is, the hedging instrument has not expired, been sold, terminated, or exercised, or the entity has not removed the designation of the hedging relationship) beginning on or after the date of adoption.
- e. For cash flow hedges existing as of the date of adoption, without dedesignating the hedging relationship, an entity may:
  - 1. For hedges of variability in cash flows attributable to a group of individual forecasted transactions, modify its method for assessing similar risk exposure to a method described in paragraph 815-20-55-23A. If an entity is applying one of the methods described in paragraph 815-20-55-23A, it may elect to change to the other method. If an entity modifies its method of assessing similar risk exposure to the method described in paragraph 815-20-55-23A(a), the entity also may change its method of assessing hedge effectiveness if the revised method leverages the similar risk assessment in determining that the hedging relationship is highly effective. An entity is not required to apply the guidance in paragraph 815-20-25-81 when comparing hedging relationships executed before and after the date of adoption in relation to the guidance in (e)(1).
  - 2. For hedges of variability in cash flows attributable to changes in the overall price or the contractually specified component of the price in a forecasted purchase or sale of a nonfinancial asset, modify the hedging relationship to designate the hedged risk as variability in cash flows attributable to changes in a component (or subcomponent) of the forecasted purchase price or sales price of a nonfinancial asset in accordance with paragraph 815-20-25-22C. The entity is not required to amend its hedge documentation for hedges of a contractually specified component to reflect amendments in accordance with paragraph 815-20-25-22C if the hedged risk is unchanged.

3. For hedges of variability in cash flows attributable to a group of individual forecasted transactions:
  - i. Modify the hedging relationship to add an additional hedged risk or risks to an existing portfolio if the hedging relationship continues to meet all other requirements to apply cash flow hedge accounting.
  - ii. Migrate some or all of the individual forecasted transactions from one existing pool or pools to a new pool or pools, an existing pool or pools, or a combination of new and existing pools.
  - iii. Reassign and reorder existing hedging instruments to a new or existing pool.
4. For hedges of forecasted interest payments on an existing choose-your-rate debt instrument:
  - i. Amend the hedging relationship to include interest payments on replacement debt.
  - ii. Specify the quantitative method that an entity will use in the event that it must assess hedge effectiveness on a quantitative basis in subsequent periods (for entities assessing hedge effectiveness on a qualitative basis).
5. For hedges of forecasted interest payments that may include interest payments on an existing choose-your-rate debt instrument designated as part of a group of forecasted transactions under the first-payments-received technique:
  - i. Amend the hedging relationship to include only interest payments on the individual existing choose-your-rate debt instrument and replacement debt.
  - ii. Specify the quantitative method that an entity will use in the event that it must assess hedge effectiveness on a quantitative basis in subsequent periods (for entities assessing hedge effectiveness on a qualitative basis).
- f. For hedges that were discontinued before the date of adoption for which amounts are still reported in accumulated other comprehensive income at the date of adoption, an entity may migrate the individual forecasted transactions to align with the pools of existing hedges considering the migration described in (e)(3)(ii).
- g. Gains or losses on hedging instruments that are reported in accumulated other comprehensive income at the date of adoption shall be reassigned using a systematic and rational manner to align with the pool or pools after the migrations described in (e)(3)(ii) and (f) and

reassignments and reorderings described in (e)(3)(iii). Amounts from accumulated other comprehensive income shall be reclassified to earnings when the hedged forecasted transaction affects earnings in accordance with paragraphs 815-30-35-38 through 35-41.

- h. If adoption of the pending content that links to this paragraph in (e) changes the designated hedged risk, an entity shall create the terms of the instrument used to estimate the change in value of the hedged risk (under the originally designated method, for example, the hypothetical derivative method, or another acceptable method in Subtopic 815-30) in the assessment of hedge effectiveness and the similar risk assessment, if applicable, on the basis of market data as of the inception of the hedging relationship. Furthermore, an entity shall amend hedge documentation upon adoption, including documentation of critical terms, the hedged forecasted transactions, hedge effectiveness assessments, and similar risk assessments, as needed to apply the pending content in (e) through (g) for all existing and discontinued hedging relationships.

### **Transition disclosures**

- i. An entity shall disclose the nature of and reason for the change in accounting principle, as well as the method of applying the change, in both the interim reporting period and the annual reporting period that the entity adopts the pending content that links to this paragraph.

## **Amendments to Status Sections**

14. Amend paragraph 815-20-00-1, by adding the following items to the table, as follows:

**815-20-00-1** The following table identifies the changes made to this Subtopic.

<b>Paragraph</b>	<b>Action</b>	<b>Accounting Standards Update</b>	<b>Date</b>
<b>Contractually Specified Component</b>	Superseded	2025-09	11/25/2025
815-20-25-3	Amended	2025-09	11/25/2025

<b>Paragraph</b>	<b>Action</b>	<b>Accounting Standards Update</b>	<b>Date</b>
815-20-25-15	Amended	2025-09	11/25/2025
815-20-25-22A	Superseded	2025-09	11/25/2025
815-20-25-22B	Superseded	2025-09	11/25/2025
815-20-25-22C	Added	2025-09	11/25/2025
815-20-25-46B	Amended	2025-09	11/25/2025
815-20-25-77	Amended	2025-09	11/25/2025
815-20-25-79	Amended	2025-09	11/25/2025
815-20-25-79A	Amended	2025-09	11/25/2025
815-20-25-79B	Added	2025-09	11/25/2025
815-20-25-84	Amended	2025-09	11/25/2025
815-20-25-88	Amended	2025-09	11/25/2025
815-20-55-17	Amended	2025-09	11/25/2025
815-20-55-18A through 55-18D	Added	2025-09	11/25/2025
815-20-55-19	Amended	2025-09	11/25/2025
815-20-55-23	Amended	2025-09	11/25/2025
815-20-55-23A through 55-23D	Added	2025-09	11/25/2025
815-20-55-26A through 55-26E	Superseded	2025-09	11/25/2025
815-20-55-33A	Amended	2025-09	11/25/2025
815-20-55-38	Amended	2025-09	11/25/2025

<b>Paragraph</b>	<b>Action</b>	<b>Accounting Standards Update</b>	<b>Date</b>
815-20-55-56	Amended	2025-09	11/25/2025
815-20-55-79P	Amended	2025-09	11/25/2025
815-20-55-79R	Amended	2025-09	11/25/2025
815-20-55-88	Amended	2025-09	11/25/2025
815-20-55-89	Amended	2025-09	11/25/2025
815-20-55-89A	Added	2025-09	11/25/2025
815-20-55-89B	Added	2025-09	11/25/2025
815-20-55-91	Amended	2025-09	11/25/2025
815-20-55-92	Amended	2025-09	11/25/2025
815-20-55-94	Amended	2025-09	11/25/2025
815-20-55-95	Amended	2025-09	11/25/2025
815-20-55-96A	Added	2025-09	11/25/2025
815-20-55-97	Amended	2025-09	11/25/2025
815-20-55-98	Amended	2025-09	11/25/2025
815-20-55-99A through 55-99E	Added	2025-09	11/25/2025
815-20-55-129	Amended	2025-09	11/25/2025
815-20-65-7	Added	2025-09	11/25/2025

15. Amend paragraph 815-30-00-1, by adding the following items to the table, as follows:

**815-30-00-1** The following table identifies the changes made to this Subtopic.

<b>Paragraph</b>	<b>Action</b>	<b>Accounting Standards Update</b>	<b>Date</b>
<b>Contractually Specified Component</b>	Superseded	2025-09	11/25/2025
815-30-35-8	Amended	2025-09	11/25/2025
815-30-35-37A	Superseded	2025-09	11/25/2025
815-30-35-37B through 35-37M	Added	2025-09	11/25/2025
815-30-55-2 through 55-4	Amended	2025-09	11/25/2025
815-30-55-20 through 55-23	Amended	2025-09	11/25/2025
815-30-55-41	Amended	2025-09	11/25/2025
815-30-55-60	Amended	2025-09	11/25/2025
815-30-55-61	Amended	2025-09	11/25/2025
815-30-55-134	Amended	2025-09	11/25/2025
815-30-55-138	Amended	2025-09	11/25/2025
815-30-55-146 through 55-148	Amended	2025-09	11/25/2025
815-30-55-149 through 55-181	Added	2025-09	11/25/2025

*The amendments in this Update were adopted by the unanimous vote of the seven members of the Financial Accounting Standards Board:*

Richard R. Jones, *Chair*  
Hillary H. Salo, *Vice Chair*  
Christine A. Botosan  
Frederick L. Cannon  
Susan M. Cospers  
Marsha L. Hunt  
Dr. Joyce T. Joseph

# Background Information and Basis for Conclusions

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## 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 2017, the Board issued Accounting Standards Update No. 2017-12, *Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities*, to more closely align hedge accounting with an entity's risk management activities and to make certain targeted improvements to simplify the application of the hedge accounting guidance on the basis of feedback received from preparers, auditors, users, and other stakeholders. After the issuance of Update 2017-12, stakeholders asked that the Board clarify certain aspects of the guidance in the amendments of that Update.

BC3. In 2019, the Board issued proposed Accounting Standards Update, *Derivatives and Hedging (Topic 815): Codification Improvements to Hedge Accounting*, to better reflect the Board's objectives related to the following four issues:

- a. Change in hedged risk in a cash flow hedge
- b. Contractually specified components in a cash flow hedge of nonfinancial forecasted transactions
- c. Foreign-currency-denominated debt instrument used as a hedging instrument and hedged item (dual hedge)
- d. Use of the term *prepayable* under the shortcut method.

BC4. Stakeholders indicated that the amendments in the 2019 proposed Update would not sufficiently resolve the issues identified related to the change in hedged risk in a cash flow hedge (Issue A) and contractually specified components in a cash flow hedge of nonfinancial forecasted transactions (Issue B). Stakeholders generally supported the proposed amendments related

to dual hedges (Issue C). Some feedback indicated that the amendments related to the use of the term *prepayable* under the shortcut method (Issue D) were not necessary given the absence of questions emerging from practice, the elimination of the term *prepayable* from the guidance supporting the portfolio layer method strategy, and concerns raised about the potential confusion and unintended consequences that could result from amending longstanding guidance for applying the shortcut method.

BC5. In response to the 2021 Invitation to Comment, *Agenda Consultation*, stakeholders continued to ask that the Board clarify certain aspects of Update 2017-12. Stakeholders also requested that the Board address a variety of additional issues related to hedge accounting and identified several issues resulting from the effect of the London Interbank Offered Rate (LIBOR) cessation on hedge accounting as the highest priority. After considering stakeholders' feedback, the Board decided to focus its efforts on continuing to clarify certain aspects of Update 2017-12 and addressing incremental issues arising from LIBOR cessation. In doing so, the Board decided to address two incremental issues resulting from the effects of LIBOR cessation (shared risk assessment in cash flow hedges and net written options as hedging instruments) and decided not to address one issue (use of the term *prepayable* in the shortcut method) for the reasons described in paragraph BC4.

BC6. In September 2024, the Board issued proposed Accounting Standards Update, *Derivatives and Hedging (Topic 815): Hedge Accounting Improvements*. The Board addressed the following issues in the proposed Update:

- a. Shared risk assessment in cash flow hedges
- b. Hedging forecasted interest payments on choose-your-rate debt instruments (referred to as "change in hedged risk in a cash flow hedge" in the 2019 proposed Update)
- c. Cash flow hedges of nonfinancial forecasted transactions (referred to as "contractually specified components in a cash flow hedge of nonfinancial forecasted transactions" in the 2019 proposed Update)
- d. Net written options as hedging instruments
- e. Foreign-currency-denominated debt instrument as hedging instrument and hedged item (dual hedge).

BC7. The Board received 22 comment letters in response to the 2024 proposed Update. Overall, respondents supported the proposed amendments, noting that the amendments would better align hedge accounting with entities' risk management strategies. The Board also received input on how to make the proposed amendments more operable and has addressed most of that feedback in this Update. However, some respondents suggested that certain amendments would be of limited utility if they were not expanded to apply to broader fact patterns and circumstances faced in practice. In considering that feedback, the Board determined that the changes that would be necessary to address those suggestions would require providing exceptions to the core principles of the Topic 815 hedge accounting model. The Board decided that those changes are beyond the scope of a targeted Update and would be better addressed as part of a separate project to reconsider the hedge accounting model more comprehensively. Therefore, in this Update, the Board focused on finalizing the amendments in the 2024 proposed Update, with certain targeted changes and clarifications.

## Benefits and Costs

BC8. 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 benefits and costs of issuing new guidance is unavoidably more qualitative than quantitative because there is no method to objectively quantify the value of improved information in financial statements or to measure the costs to implement new guidance.

BC9. The purpose of the amendments in Update 2017-12 was to improve the financial reporting of hedging relationships to better portray the economic results of an entity's risk management activities in its financial statements. As part of its objective to better align the hedge accounting guidance with entities' risk management activities, the Board included amendments in both Update 2017-12 and the 2019 proposed Update that were intended to allow entities greater flexibility to retain hedge accounting once a highly effective hedging

relationship is established (through the proposed change in hedged risk guidance). This proposed guidance was intended to address stakeholders' concern that current guidance increases the prevalence of missed forecasted transactions for otherwise highly effective hedging relationships, thus resulting in less decision-useful information for investors.

BC10. However, after considering stakeholders' concerns that certain of those amendments deviated from the core principles of Topic 815 and would have been challenging to operationalize, the Board decided to take a different approach in this Update and identify more targeted solutions for different types of hedges. Accordingly, certain amendments in this Update are intended to allow an entity's financial reporting to more closely reflect economic hedging strategies for highly effective cash flow hedges of groups of forecasted transactions, including nonfinancial forecasted transactions. Other amendments in this Update are intended to facilitate application of cash flow hedge accounting to commonly issued debt instruments with terms that allow entities to change their interest rate over the life of the debt instrument. The Board believes that these solutions will achieve the goal of reducing unintuitive missed forecasts, which will provide more decision-useful information to investors and other financial statement users about entities' risk management activities and the relative success of entities' hedging programs. In addition, these solutions will be more operable for preparers and auditable for auditors compared with the 2019 proposed Update.

BC11. The Board also believes that the clarity provided by the amendments in this Update will result in a more faithful representation of hedging activities in a cost-efficient manner for preparers. In some cases, the amendments provide the benefit of improving consistent application of GAAP by clarifying guidance that already exists within GAAP. In other cases, the amendments necessitated by LIBOR cessation provide the benefit of allowing Topic 815 to remain operable after the effects of global reference rate reform.

BC12. Because hedge accounting is optional, not all entities will bear the costs of implementing the amendments in this Update. For entities that elect to apply hedge accounting, the Board does not anticipate that they will incur significant costs as a result of the amendments. However, the Board acknowledges that certain reporting entities will incur costs. Those costs may include initial costs to educate employees, establish new accounting methods, and update systems and processes. The Board believes that after

implementing the amendments, entities will have minimal, if any, incremental costs to comply with the amendments on an ongoing basis. Moreover, entities largely will be able to leverage existing systems and processes. The elective nature of hedge accounting permits entities to independently determine whether the benefits of applying the amendments outweigh the costs.

BC13. The basis for conclusions related to each amendment in this Update provides the relevant benefit-cost analysis for that amendment.

## Basis for Conclusions

### Issue 1: Similar Risk Assessment for Cash Flow Hedges

#### *Current GAAP*

BC14. Currently, Topic 815 permits entities to designate cash flow hedges of groups of forecasted transactions using a single derivative as the hedging instrument. To qualify for that approach, the individual forecasted transactions in the group must share the same risk exposure in addition to meeting all other requirements for applying hedge accounting. Stakeholders informed the Board that beyond the temporary relief provided in Topic 848, Reference Rate Reform, after the cessation of LIBOR, permanent amendments to Topic 815 would be needed to maintain the ability to apply the guidance to hedges of groups of individual forecasted transactions, given the increased variety of alternative reference rates and iterations of those rates that have emerged.

BC15. Before LIBOR cessation, hedges of variable-rate loan pools were established to hedge forecasted interest cash flows based on a particular tenor (that is, reset frequency) of LIBOR. Because LIBOR was the predominant reference rate and financial institutions could continuously replenish LIBOR-based loans, entities could readily assert that the designated forecasted interest cash flows shared the same risk exposure and were probable of occurring.

BC16. Stakeholders observed that the shared risk exposure requirement, and the related example in paragraph 815-20-55-23 that has been commonly applied in practice to restrict hedges of interest receipts to only those based on the same index, is unnecessarily restrictive in a post-LIBOR environment. Financial institution stakeholders indicated that because of the increased

variety of alternative reference rates after LIBOR cessation, more granular groups (or pools) are necessary to comply with the shared risk exposure requirement to apply cash flow hedge accounting.

BC17. As loan origination terms have shifted after LIBOR cessation, pools of loans have generally become smaller and more granular because of the wider variety of alternative reference rates, resulting in an increased risk of missed forecasted transactions. In some cases, concerns about the ability to accurately forecast probable transactions at the pool level has reduced the extent to which hedge accounting has been applied. Stakeholders stated that, in their view, these challenges will persist as it remains unclear how the interest rate landscape will continue to evolve.

### *2019 Proposed Update*

BC18. The 2019 proposed Update would have amended paragraph 815-20-55-23 to remove the example that indicates that interest payments hedged in a group need to vary with the same index to qualify for hedging with a single derivative. At that time, the Board noted that while it may be common for forecasted transactions in a group to vary with the same index, it did not intend to prohibit the application of hedge accounting in instances in which forecasted transactions with different interest rate indexes or commodity indexes are highly correlated. That is, the Board did not intend for the “same index” example to be interpreted as a requirement to qualify for hedge accounting.

BC19. Stakeholders who commented on the 2019 proposed Update supported the Board’s decision to remove the same index example. Stakeholders noted that removing that example would increase the degree to which the desired level of hedge accounting can be achieved by allowing the aggregation of risks within a single portfolio. In addition, stakeholders observed that it would reduce the cost and complexity of managing their hedge accounting programs and ease the burden of hedge accounting post-LIBOR cessation.

BC20. Some stakeholders noted that the term *shared* risk exposure used to describe the eligibility assessment for hedges of groups of forecasted transactions should be changed to *similar* risk exposure because removing the same index example clarifies the Board’s intent that hedged risks in a pool need not share the same risk exposure.

## *2024 Proposed Update*

BC21. In the 2024 proposed Update, the Board decided to carry forward its decision from the 2019 proposed Update to remove the same index example. In addition, as suggested by stakeholders, the Board decided to change the term *shared* risk exposure to *similar* risk exposure to avoid confusion in practice and to better reflect the intent of the amendments in the 2024 proposed Update. As a result, the amendments in the 2024 proposed Update expanded the hedged risks permitted to be aggregated in a group of individual forecasted transactions in a cash flow hedge by changing the requirement to designate a group of individual forecasted transactions from having a shared risk exposure to having a similar risk exposure.

BC22. The 2024 proposed Update provided guidance for applying the similar risk exposure requirement. The Board proposed guidance on the required frequency of the similar risk assessment, the quantitative threshold, and parameters for performing that assessment and whether a qualitative assessment may be performed. As to the frequency of the assessment, the Board decided that the similar risk assessment should be performed initially at hedge inception and on an ongoing basis (that is, a quarterly assessment at a minimum under Topic 815). That decision affirmed the amendment in the 2019 proposed Update and restored the requirement for initial and ongoing assessment that was in place before the amendments in Update 2017-12 were implemented. The Board acknowledged that the requirement for ongoing similar risk assessments is necessary to address groupings of individual forecasted transactions that may include diverse contractually specified risks or overall price risks. Furthermore, stakeholders noted, and the Board agreed, that if one or more risks is dissimilar in subsequent periods, then it would be conceptually inconsistent to permit the continuation of existing hedges but not permit new hedges on the same pool to be established. The Board also proposed guidance to require that entities apply the selected method of assessing similarity consistently to similar hedges. The Board observed that this is consistent with the guidance under current GAAP that requires the selected method of assessing effectiveness to be applied consistently to similar hedges. The Board also acknowledged that a change in method of assessing effectiveness or similarity is not a change in accounting principle under Topic 250.

BC23. Current GAAP does not specify the threshold necessary to conclude that forecasted transactions in a group share the same risk exposure, and the Board understands that after LIBOR cessation some diversity in practice has been observed. To address that issue, in the 2024 proposed Update, the Board decided that the quantitative threshold necessary to determine that risks in a group of forecasted transactions have a similar risk exposure should be consistent with the highly effective threshold.

BC24. While the term *similar risk* suggests that an entity should validate that all risks in a pool are highly correlated with one another, the Board decided that entities may conclude that the risk exposures in a group of forecasted transactions are deemed similar if the hedging instrument is highly effective against each risk in the group. The Board concluded that if all hedged risks in the pool are highly effective against the hedging instrument, then each risk is sufficiently similar to every other risk in the group to be eligible to apply hedge accounting as a group. Furthermore, if each risk is highly effective against the designated hedging instrument, then an entity could achieve hedge accounting for those forecasted transactions by designating a discrete hedging relationship for each forecasted transaction.

BC25. The Board understood that this approach aligns the amendments in the 2024 proposed Update with an approach commonly applied in current practice under which the same assessment will be applied to satisfy both the hedge effectiveness assessment and the similar risk assessment, which will have the benefit of reducing the cost and complexity of applying hedge accounting for this type of strategy. That is, the Board understood that, in practice, some entities utilize a dual-purpose assessment commonly referred to as a “test to worst” approach, the premise of which is that if the derivative designated as the hedging instrument is highly effective against the least effective risk in the pool (the identification of which requires judgment that may change over time), it may be considered highly effective against every risk in the pool. However, the Board decided that if an entity elects not to utilize a dual-purpose assessment, then it would be required to assess whether the risks in the group are similar separately from its assessment of hedge effectiveness. Whether individual forecasted transactions in a group are determined to have a similar risk exposure may differ depending on the assessment method selected. The Board decided that if an entity applies one of the qualitative methods applicable to cash flow hedges of a group of individual forecasted transactions in paragraph 815-20-25-3(b)(2)(iv)(01) for

purposes of assessing hedge effectiveness, it also may assume that the hedged risks related to a group of forecasted transactions are similar. In that circumstance, the Board observed that because those methods generally require that the derivative match the items in the group, application of those methods generally apply only to pools containing a single risk exposure.

BC26. The Board also decided that entities should be permitted to assess whether risk exposures in a group of forecasted transactions are similar using ongoing qualitative assessments, on a hedge-by-hedge basis, in a manner similar to the guidance in paragraphs 815-20-35-2A through 35-2F. The Board noted that in specifying a quantitative threshold, it did not intend to prohibit an entity from performing qualitative ongoing assessments and believed that the concepts in those paragraphs are appropriate for performing the similar risk assessment.

BC27. Under the amendments in the 2024 proposed Update, if as part of an entity's ongoing similar risk assessment one or more hedged risks included in a pool became dissimilar, the entity would be required to fully dedesignate the entire hedging relationship. The Board observed that under a dual-purpose test of similarity and effectiveness, not requiring a full dedesignation if one or more risks test dissimilar would permit an ineffective hedging relationship to continue to achieve hedge accounting. Therefore, the Board believed that full dedesignation in that circumstance is necessary to remain in line with the core hedge accounting model.

### *Feedback on the 2024 Proposed Update and Redeliberations*

BC28. Stakeholders supported the amendments in the 2024 proposed Update and viewed the change from the shared risk assessment to the similar risk assessment as a necessary amendment to allow entities to hedge broader pools of forecasted transactions. Stakeholders similarly supported the proposed criteria for performing a similar risk assessment.

BC29. Some financial institution stakeholders highlighted that the requirement to fully dedesignate all cash flow hedges related to a pool of variable rate loans if one or more of the risks designated as being hedged tested dissimilar may limit the utility of the guidance for some entities in practice. Those stakeholders noted that in situations in which there are sufficient forecasted transactions (for example, interest payments) related to a

pool that satisfy a similar risk assessment to support the hedging relationship despite one or more of the hedged risks no longer being similar, hedge accounting should be permitted to continue without requiring a full dedesignation of the hedging relationship. Those stakeholders noted the considerable operational burden associated with dedesignating hedging relationships for a pool of loans for an entity with a sophisticated cash flow hedging program using a first-payments-received technique under which a significant number of individual hedges may be designated against a single pool. Furthermore, redesignation of those hedging relationships using the same derivatives (that generally contain off-market terms) introduces complications into the hedge accounting mechanics and may affect hedge effectiveness assessments.

BC30. The Board considered stakeholders' requests to permit the continuation of hedge accounting without a full dedesignation of the hedging relationship if one or more of the risks designated as hedged became dissimilar. The Board observed that to achieve that result an exception would need to be made to certain core principles of hedge accounting guidance in Topic 815. Specifically, that exception would involve the ability to use hindsight to identify hedged transactions. Although Board members acknowledged that the amended hedge accounting requirements may not fully reflect the economics of entities' risk management strategies without that exception, the Board decided to finalize the amendments as proposed including the requirement to fully dedesignate a hedging relationship related to a pool if one or more of the risks test dissimilar. While some Board members supported providing exceptions to the core principles of the hedge accounting model, the majority of the Board reasoned that providing those exceptions is beyond the scope of this Update, which was intended to address issues arising from Update 2017-12 and from LIBOR cessation, and could have delayed providing the intended relief. Furthermore, based on feedback received in comment letters and stakeholder outreach, while some entities view the cost of a possible full dedesignation as potentially outweighing the benefits of the amendments, the Board understands that some entities expect to benefit from the ability to hedge broader pools.

BC31. By expanding the risks that may be included in a group, the Board viewed its decisions as improving GAAP by allowing hedge accounting to be applied more broadly. The Board continues to believe that this is an improvement over current GAAP because investors will receive more relevant information about an entity's risk management activities. Furthermore, by clarifying the guidance necessary to conclude that a group of forecasted transactions has a similar risk exposure, the Board believes that stakeholders will be able to apply hedge accounting to more economic hedges in a more cost-effective and efficient manner. Also, while this issue was initially raised in the context of interest rate risk hedges of variable-rate loan pools, the Board observed that guidance related to the similar risk assessment would apply equally for commodity price risk hedges designated on a pool basis when the forecasted transactions are future purchases or sales of nonfinancial assets.

BC32. While the Board understands that the amendments in this Update will not address all potential issues encountered in practice on hedges of variable-rate loan pools, stakeholders indicated that the proposed amendments would be important incremental improvements because they would provide the flexibility to expand pools relative to current practice, which may enable entities to reduce potential missed forecasts in some circumstances.

BC33. The Board believes that the expected benefits of its decisions on the similar risk assessment justify the expected implementation costs because stakeholders noted that the amendments in this Update will improve the degree to which the desired level of hedge accounting can be achieved by removing the impediment to aggregate certain risks within a single pool, while simultaneously reducing the costs and complexities of managing hedge programs.

BC34. The decisions reached on this issue are not intended to introduce a more rigorous analysis to determine whether individual transactions in a group have similar risks. Rather, they are meant to allow entities to assemble larger pools, while simplifying and providing greater clarity on how assessments of similar risk exposure should be performed. The Board does not foresee significant costs for education or establishing accounting policies on this issue because the revised guidance is generally consistent with the use of dual-purpose assessments in practice.

## Issue 2: Hedging Forecasted Interest Payments on Choose-Your-Rate Debt Instruments

### *Current GAAP*

BC35. Before the issuance of Update 2017-12, paragraph 815-20-55-56 included a broad prohibition against changing the critical terms of a hedging relationship after initial hedge designation without dedesignating and redesignating the hedging relationship. Update 2017-12 amended Topic 815 to permit entities to continue applying hedge accounting in a cash flow hedge, without dedesignation, if the designated hedged risk changes during the life of the hedging relationship and the hedging instrument is highly effective at offsetting the cash flows attributable to the revised hedged risk.

BC36. The Board's objective was to introduce flexibility into Topic 815 to enable an entity to avoid missed forecasts when the entity did not anticipate the change in hedged risk upon hedge designation but the hedging relationship remained highly effective (considering the new risk) and continued to achieve the original risk management objective.

### *2019 Proposed Update*

BC37. Stakeholders' feedback following the issuance of Update 2017-12 indicated operability concerns about the change in hedged risk guidance, which led to the issuance of the 2019 proposed Update to clarify its application. Comment letter respondents to the 2019 proposed Update conveyed numerous concerns about the amendments in that proposed Update. Some stakeholders expressed concern that the amendments, which would have permitted an entity to identify a hedged forecasted transaction with an undocumented hedged risk after the forecasted transaction occurred, would be inconsistent with the core principles underlying Topic 815 that were established when hedge accounting was first introduced. In addition, among other concerns, many stakeholders indicated that requiring application of the change in hedged risk guidance, rather than permitting elective application, could disrupt existing practice for certain cash flow hedges.

BC38. The Board acknowledged that the change in hedged risk model in the 2019 proposed Update was intended to be a broad solution to address the risk of missed forecasted transactions. Some stakeholders noted that for the

change in hedged risk model to be operable, auditable, and aligned with the existing cash flow hedging framework, it would need to be revised to be significantly more limited and prescriptive.

### *2024 Proposed Update*

BC39. In the 2024 proposed Update, the Board decided to narrow the change in hedged risk model to apply only to a particular hedging strategy. The Board decided that revising the change in hedged risk model that was proposed in the 2019 proposed Update in the manner that stakeholders suggested would not meet the Board's stated objectives. Furthermore, the Board recognized that other amendments in the 2024 proposed Update would address the risk of missed forecasts for certain types of hedges, thereby minimizing the need for a broader solution.

BC40. Accordingly, in the 2024 proposed Update, the Board decided to propose that the change in hedged risk model should focus on one pervasive hedging strategy for which stakeholders highlighted that the application of hedge accounting has been limited in practice and diversity exists when it is applied. Specifically, the Board decided to address cash flow hedges of individual variable-rate debt instruments that permit the borrower to change either or both the interest rate index and interest rate tenor upon which interest is accrued. That type of instrument is commonly referred to as "choose-your-rate" debt. The Board decided to focus on that particular hedging strategy because it believed that a change in hedged risk model is well suited for application to that hedging strategy because the terms of the debt instrument explicitly allow a borrower to change either or both the interest rate index and interest rate tenor and also specify the rates and tenors that may be selected. Furthermore, the approach for applying cash flow hedge accounting to this type of instrument is not specified in Topic 815, which has led to diversity in practice.

BC41. In the 2024 proposed Update, the Board decided that the central provision of a change in hedged risk model for choose-your-rate debt was that upon hedge designation, the terms of the issued debt instrument establish the parameters of the hedging relationship and the complete set of risks that an entity may change to during the hedging relationship. The Board also decided that an entity should be permitted to continue hedge accounting for a replacement of a choose-your-rate debt instrument upon a refinancing to the extent that, upon replacement, the entity selects a rate that is captured within

the terms of the original debt issuance and the interest payments remain probable of occurring over the hedge period. The Board believed that replacement of a choose-your-rate debt instrument should be accommodated because refinancings are commonplace and the replacement debt (whether a variable-rate debt instrument with a single interest rate index or a choose-your-rate debt instrument) may be viewed as linked to the original hedged debt if the selected rate is present in the terms of the original debt instrument and the interest payments remain probable of occurring over the hedge period.

BC42. Because the terms of the originally issued debt instrument establish the parameters of the hedging relationship, to continue hedge accounting without dedesignation, the Board believed that the original notional amount designated as being hedged and the original term of the hedging relationship may not be changed upon replacement of the originally designated choose-your-rate debt instrument. That is, the replacement debt instrument must have a notional amount equal to or greater than the amount of the principal hedged under the original choose-your-rate debt instrument, and the replacement debt instrument must mature on or after the last interest payment hedged under the original choose-your-rate debt instrument.

BC43. The Board decided that at hedge inception the assessment of hedge effectiveness would be based on the single rate on which interest is accrued, ignoring the optionality embedded in the debt instrument, including alternative rates previously selected or rates anticipated to be selected in the future. The Board believed that would simplify the assessment and permit entities to assess hedge effectiveness on a qualitative basis. The Board also observed that an entity would not need to assess the similarity of all interest rates available to be selected because only the selected interest rate is designated as the hedged risk at any given point in time.

BC44. When an entity changes to a new interest rate index or interest rate tenor in accordance with the terms of the debt agreement giving rise to the interest cash flows designated as the hedged forecasted transactions, it would perform a final retrospective assessment based on the previously selected contractually specified rate and then begin prospectively assessing hedge effectiveness based on the revised contractually specified interest rate. In performing those assessments using the revised rate, the entity would create the terms of the instrument used to estimate changes in the cash flows of the revised hedged risk based on the market data as of the inception of the hedging

relationship, which would avoid an off-market element being captured in effectiveness assessments.

BC45. If an entity fails the final retrospective assessment but passes the prospective assessment using the revised rate, the entity should not apply cash flow hedge accounting for the period covered by that final retrospective assessment but may apply cash flow hedge accounting prospectively without dedesignating the hedging relationship. That is because the derivative is expected to be highly effective in offsetting forecasted cash flows based on the entity's decision to change the rate upon which interest accrues going forward, in accordance with the terms of the debt instrument.

BC46. The Board decided that the assessment of the probability of forecasted transactions occurring should be based on the likelihood that interest payments on the choose-your-rate debt instrument (or replacement debt) will occur at one of the documented eligible interest rates and interest rate tenors, without consideration of the likelihood that an entity will exercise the option to change the selected rate and tenor on which interest is accrued. The Board decided that the interest rate tenor is permitted to change if the revised payments are accrued over the hedge period. Although a change in tenor of an interest rate also represents a change in the number and timing of interest payments, the Board decided that within the confines of this model, an entity may view the interest accruals on that discrete debt instrument (or replacement debt) as the hedged cash flows. Accordingly, a change in the number and frequency of hedged cash flows that results from an entity selecting a different interest rate index, including tenor, will not result in a missed forecast within this model.

BC47. The Board decided that entities should be required to apply (rather than have the election to apply) the change in hedged risk model in the amendments in the 2024 proposed Update when hedging interest payments on choose-your-rate debt under Topic 815, given the implicit benefits of the model. The Board believed that the proposed amendments would establish a model for hedging interest payments on choose-your-rate debt that would reduce operational complexity, mitigate the risk of unintuitive missed forecasts or dedesignation events, and more consistently reflect risk management strategies in the financial information provided to investors. The Board decided that because the elements of this model have been tailored to the features of variable-rate debt instruments that permit a borrower to select at each reset period the interest rate index (including the interest rate tenor) from a

contractually specified list upon which interest is accrued (that is, choose-your-rate debt), the model should not be applied by analogy to other hedging relationships, including relationships in which forecasted transactions are identified in accordance with the first-payments-received technique.

### *Feedback on the 2024 Proposed Update and Redeliberations*

BC48. Some respondents provided feedback on the 2024 proposed Update that the choose-your-rate debt model should be made optional on an instrument-by-instrument basis instead of required as proposed. Those respondents expressed concerns about the clarity of the guidance for transitioning between the core hedge accounting model when hedging the forecasted issuance of choose-your-rate debt and the guidance applicable to existing choose-your-rate debt once the debt is issued as discussed in paragraph BC50. In outreach conducted following the comment letter period, stakeholders generally agreed with making the choose-your-rate debt model optional and similarly noted that an optional model would alleviate concerns that entities may be penalized for not updating their hedge documentation following the issuance of this Update.

BC49. To address stakeholders' concerns, the Board decided to allow entities to choose whether to apply the choose-your-rate debt model. The Board understands that without making the choose-your-rate debt model optional, entities would still have been able to hedge choose-your-rate debt outside the choose-your-rate debt model through designation of the debt instrument under the first-payments-received technique. However, the Board believes that making the choose-your-rate debt model optional is less complex.

BC50. Stakeholders were concerned that the proposed choose-your-rate debt model would relate only to hedges of existing choose-your-rate debt instruments and did not contemplate hedges of forecasted issuances of choose-your-rate debt. That is, the proposed amendments would not have permitted an entity to apply the choose-your-rate debt model when hedging the forecasted issuance of choose-your-rate debt unless that debt is considered replacement debt. As a result, under the proposed amendments, an entity wishing to hedge the forecasted issuance of choose-your-rate debt would have been required to dedesignate the initial cash flow hedge of the forecasted issuance of debt and then redesignate a new hedging relationship under the choose-your-rate debt model once the choose-your-rate debt was issued.

BC51. Under current hedge accounting guidance, an entity that hedges the forecasted issuance of variable-rate debt can continue hedge accounting when the variable-rate debt is issued. That ability to continue hedge accounting allows an entity to retain the economics of the hedging relationship that it established when it entered into the derivative instrument for the duration of the hedge period.

BC52. Comment letter respondents noted that requiring dedesignation and redesignation when applying the choose-your-rate debt model could limit the utility of the proposed guidance, especially because dedesignation and redesignation are not required if an entity is applying current hedge accounting guidance. Specifically, stakeholders noted that it is common for entities to hedge issuances of choose-your-rate debt in the forecasted period and highlighted that requiring dedesignation could result in an entity having an off-market derivative, which could cause the hedging relationship to fail effectiveness assessments if redesignated.

BC53. On the basis of feedback received, the Board decided to allow the choose-your-rate debt model to apply to forecasted issuances of choose-your-rate debt and hedge accounting to continue once choose-your-rate debt is issued. An entity that wishes to hedge the forecasted issuance of choose-your-rate debt is required at hedge inception to (a) document the interest rates that it expects to be included in the choose-your-rate debt when issued on the basis of the terms of choose-your-rate debt available in the marketplace and (b) assert that it is probable that it will issue choose-your-rate debt and pay interest at one of those rates.

BC54. The Board decided that once the choose-your-rate debt is issued, which is the point at which an entity would select the initial rate to accrue interest from among the rates specified in the contractual terms of the debt instrument, hedge accounting can continue without dedesignation as long as the entity selects a rate to accrue interest that also was documented at hedge inception on the basis of the rates in the market in the forecast period. After the initial selection of a rate to accrue interest, an entity applies the model for outstanding choose-your-rate debt instruments and alternative rate selections in subsequent periods are governed by the interest rate options within the initially issued choose-your-rate debt agreement. However, if it becomes probable that an entity will select a rate at issuance that was not included in the list of rates documented at hedge inception or that the debt issued will not be

choose-your-rate debt, the entity would have a missed forecast and would not be able to apply hedge accounting under the existing hedging relationship.

BC55. The Board believes that providing a mechanism to continue cash flow hedge accounting once the choose-your-rate debt is issued provides a better portrayal of an entity's economic hedging activity. The Board did not want the mechanics of hedge accounting to preclude entities from applying hedge accounting to forecasted issuances of choose-your-rate debt. Furthermore, on the basis of stakeholder feedback, the Board expects that the forecast period will be minimal in most cases. Therefore, the Board concluded that the market interest rates documented at the inception of the hedge of the forecasted issuance will often not significantly differ from the interest rates included in the choose-your-rate debt that is ultimately issued.

BC56. The Board understands that the amendments in this Update create a separate model and separate documentation requirements for the hedged forecast period and when the choose-your-rate debt is ultimately issued. However, in permitting a change in hedged risk model for this particular hedging strategy, the Board placed significant weight on the fact that the contractual terms of the debt instrument specifically allow a borrower to change either or both the interest rate index and interest rate tenor and also specify the full complement of rates and tenors that may be selected. Therefore, the Board decided that when the choose-your-rate debt is issued, the contractual rates in the debt agreement appropriately ring-fence the flexibility available during the remainder of the hedge period and the rates documented at inception of the hedge of the forecasted issuance no longer apply. The flexibility in the model for existing choose-your-rate debt also is limited by the requirement for the hedged forecasted interest payments to have begun accruing. This requirement, which only applies to the existing choose-your-rate debt model, excludes interest payments from being hedged in a forward starting period in that model and appropriately limits the application of that model to hedged interest payments accruing at the currently selected contractual rate (rather than involving a best estimate of the rate at which hedged interest payments will accrue).

BC57. In addition, comment letter respondents questioned the proposed requirement for replacement debt to mature on or after the last interest payment hedged under the original choose-your-rate debt instrument because that condition is not required in the current hedging model for cash flow hedges of replacement debt. Stakeholders indicated that entities commonly execute interest rate hedges after the origination of a debt instrument with hedging periods that extend beyond the maturity of the debt. In those situations, an entity would still be required to demonstrate that forecasted interest cash flows beyond the existing choose-your-rate debt instrument are probable of occurring as a condition of qualifying for hedge accounting. Furthermore, stakeholders noted that the outcome of a missed forecast in situations in which the maturity date of the replacement choose-your-rate debt does not meet or exceed the maturity of the hedging instrument does not appear to be consistent with the Board's objectives to align hedge accounting with entities' risk management strategies.

BC58. The Board agreed with that feedback and decided to remove the requirement that the maturity date of the replacement debt must be on or after the last interest payment hedged under the original choose-your-rate debt instrument. The Board believes that allowing hedge accounting to continue if the replacement debt instrument matures before the end of the hedge period avoids placing restrictions on the use of the choose-your-rate debt model, is more operable in practice, and better reflects the economics of entities' risk management strategies.

BC59. The Board acknowledges that the choose-your-rate debt model for replacement debt differs from the model for forecasted issuances of choose-your-rate debt. While the model for forecasted issuances of choose-your-rate debt is bound by rates in the market documented at hedge inception, the model for replacement debt is bound by the rates in the originally issued choose-your-rate debt agreement. Consistent with the Board's view in the 2024 proposed Update, the interest rates included in the terms of the initial choose-your-rate debt instrument serve as the anchor for all future rates to be selected in replacement debt. If it becomes probable that a rate will be selected in choose-your-rate or other variable-rate replacement debt that was not included as a rate in the initial choose-your-rate debt instrument, an entity would have a missed forecast. Also, if it becomes probable that replacement debt will be fixed-rate debt, the entity would have a missed forecast.

BC60. The Board believes that the expected benefits of the amendments in this Update for hedges of choose-your-rate debt justify the expected implementation costs. The Board understands that stakeholders have been seeking clarification of this cash flow hedging strategy for many years and anticipates that the amendments will simplify application of a common hedging strategy in a manner that best aligns with the economics of entities' risk management activities. On the basis of outreach with stakeholders, the Board expects that in instances in which an entity decides to apply the choose-your-rate debt model, the amendments will eliminate much of the diversity in practice that currently exists about the application of cash flow hedge accounting to choose-your-rate debt instruments. In instances in which an entity decides not to apply the choose-your-rate debt model, the Board understands that diversity in practice may continue to exist. However, the Board expects that most entities will prefer the flexibility provided under the choose-your-rate debt model and believes that the benefits of the optionality of the model outweigh the costs of potential continued diversity in practice when the model is not applied. The Board acknowledges that there will be costs for education and establishing processes, internal controls, and accounting policies related to the new model. The Board believes that the potential benefits justify such potential implementation costs because they mitigate the risk of hedge dedesignation events and missed forecasts occurring for hedges of choose-your-rate debt and, as a result, allow entities to more consistently reflect risk management strategies in their financial statements.

### Issue 3: Cash Flow Hedges of Nonfinancial Forecasted Transactions

#### *Current GAAP*

BC61. For cash flow hedges of the forecasted purchase or sale of a nonfinancial asset, current GAAP (introduced in Update 2017-12) allows entities to designate hedges of a contractually specified component of the pricing formula within a purchase or sale agreement. The central element of this model is that the contractually specified component must be explicitly referenced (or expected to be explicitly referenced) in the pricing formula of an agreement that supports the nonfinancial asset's transaction price. In introducing this model in Update 2017-12, the Board sought to better align hedge accounting with an entity's risk management activities.

BC62. The Board selected this approach for hedging nonfinancial price components in Update 2017-12 because it believed that designating the variability in cash flows attributable to changes in a contractually specified component as the hedged risk is objective and relatively straightforward to apply (that is, a contractually specified component has a direct and measurable effect on the transaction price). In addition, the amendments in Update 2017-12 required that for an entity to designate a component in a forward contract that is a derivative in its entirety, the entity must apply the normal purchases and normal sales (NPNS) scope exception to ensure that no extraneous or speculative price component would be eligible for cash flow hedging.

### *2019 Proposed Update*

BC63. Following the issuance of Update 2017-12, stakeholders asked the Board to clarify several issues on the contractually specified component hedging model. Those issues included specifying the type of contract or agreement necessary to support the existence of a contractually specified component and when that contract or agreement must be received, how the guidance interacts with the NPNS scope exception, how an entity should assess whether a contractually specified component determines the transaction price of a nonfinancial asset, and how the contractually specified component guidance should be interpreted for forecasted transactions consummated in the spot market.

BC64. The 2019 proposed Update sought to clarify those matters. The amendments in that proposed Update indicated that any documentation that supports the price at which a nonfinancial asset is purchased or sold may be evidence of a contractually specified component. Furthermore, the proposed amendments specified that an entity would be required to apply only the portion of the NPNS scope exception that requires all underlyings in the agreement to be clearly and closely related to the asset being purchased or sold (rather than being required to qualify for and elect the NPNS scope exception, which includes meeting additional conditions). In response to some practitioners' concerns about the operability and auditability of the model for spot transactions, the Board sought to clarify that agreements supporting the contractually specified component need not be legally binding or executed in advance of the transaction and provided examples of the type of documentation (such as a spot-market receipt) that would satisfy this requirement.

BC65. Stakeholders expressed concerns about the operability of the nonfinancial component hedge accounting model under both Update 2017-12 and the 2019 proposed Update. The ability to hedge component risks in spot-market transactions was the most pervasive issue raised by stakeholders. Some stakeholders expressed that the existing contractually specified component model, which relies on written evidence that a price component is explicitly referenced in a pricing formula of an agreement governing the transaction, is incompatible with the mechanics of a spot market. The current model has created challenges in applying hedge accounting and diversity in practice for hedges of price components in forecasted nonfinancial transactions consummated in the spot market. Stakeholders consistently expressed support for a nonfinancial component hedging model that permits hedges of price components beyond those that are contractually specified in a pricing formula. Stakeholders indicated that permitting hedges of price components beyond contractually specified components would make it easier to achieve hedge accounting for forecasted transactions without the need to execute the purchase through a forward contract.

BC66. In outreach conducted after Update 2017-12 was issued, stakeholders also informed the Board of diversity in practice on whether a forecasted transaction for the purchase or sale of a nonfinancial asset that is in a contract accounted for as a derivative under Topic 815 (that is, where the NPNS scope exception is not applied) qualifies for hedge accounting. This diversity originates from different views on whether the guidance in paragraph 815-20-25-15(d) through (e) allows the forecasted purchase or sale of a nonfinancial asset accounted for as a derivative to be designated in a cash flow hedge.

BC67. Some stakeholders indicated that they interpret the guidance in paragraph 815-20-25-15(d) through (e) to allow the purchase or sale of a nonfinancial asset that is in a contract accounted for as a derivative under Topic 815 to qualify as a forecasted transaction if the physical settlement of that contract is probable and all other criteria for cash flow hedge accounting are satisfied. Those stakeholders maintained that an entity is not hedging the variability associated with the derivative gain or loss but rather the variability of the price risk associated with the forecasted purchase or sale of the nonfinancial asset that is recognized upon physical settlement. That interpretation may be analogized to an all-in-one hedge. In an all-in-one hedge, a fixed-price contract to purchase or sell an asset accounted for as a derivative under Topic 815 can be designated as the hedging instrument in a cash flow

hedge of the variability of the consideration to be paid or received in the forecasted transaction that occurs upon gross settlement of the derivative instrument itself if the contract involves gross settlement.

BC68. Other stakeholders stated that such an analogy to an all-in-one hedge is inappropriate because the all-in-one hedge guidance applies to a narrow fact pattern. Those stakeholders maintained that an entity cannot ignore the fact that the contract that gives rise to the purchase or sale may be accounted for as a derivative and, therefore, is not permitted to be an eligible hedged item under paragraph 815-20-25-15(e) unless the NPNS scope exception in Topic 815 is applied.

### *2024 Proposed Update*

BC69. In the 2024 proposed Update, the Board decided to develop a principles-based model for cash flow hedges of nonfinancial price components. The Board agreed with the views expressed by stakeholders, notably that a component hedging model that limits the application of hedge accounting for a population of forecasted transactions (that is, spot-market transactions) based on the selected marketplace for the transaction is not ideal because it precludes an entity from applying hedge accounting to a subset of risk management strategies. Accordingly, the Board decided to propose a revised nonfinancial component hedging model with eligibility based on the clearly-and-closely-related criteria in the NPNS scope exception under Topic 815. Under that model, entities may designate the variability in cash flows attributable to changes in a component of the price of a nonfinancial asset as the hedged risk if the component presents an exposure to cash flow variability that could affect reported earnings and is clearly and closely related (as described in paragraph 815-10-15-32(a) and (b)) to the purchase or sale price of the nonfinancial asset.

BC70. In evaluating whether the hedged price component presents an exposure to cash flow variability that could affect reported earnings, the Board observed that the assessment of whether cash flow variability exists would differ depending on the nature of the transaction used to purchase or sell the nonfinancial asset. The Board noted that the cash flow variability in a forecasted transaction executed through a forward agreement stems from the components that are explicitly referenced in that agreement's pricing formula. The Board acknowledged that this results in an inherent limitation of the

population of components eligible to be designated as the hedged risk because the existence of the contract evidences the source of cash flow variability in the forecasted purchase or sale transaction.

BC71. However, the Board decided that the components that may be designated are not limited to only the explicitly referenced variable components in the contract but also would include variable components that are clearly and closely related to an explicitly referenced component (that is, subcomponents as described in paragraph 815-20-25-22C(b)(2)). The Board believed that it is reasonable to consider factors such as ingredients, factors in production, or fair value inputs when applying the clearly-and-closely-related analysis for determining eligible subcomponents of explicitly referenced components. In addition, the Board observed that entities may not be able to identify whether a subcomponent is the highest-level ingredient, factor, or input to the explicitly referenced component and, therefore, did not impose a requirement for performing an assessment of whether a subcomponent is clearly and closely related to other higher-level subcomponents that make up the explicitly referenced component.

BC72. The Board also noted that the cash flow variability in a forecasted transaction consummated in the spot market stems from the total price that is ultimately paid or received. The Board believed that, relative to a forward contract, there is a broader population of eligible hedged risks for transactions executed in the spot market because the cash flow variability from the forecasted transaction is not inherently limited by a contractual pricing formula. Rather, an entity would be permitted to designate as the hedged risk any component that would be considered to create variability in the spot price depending on the nature of the commodity, the market, the location, and so forth, if the required hedge designation criteria are met.

BC73. The Board decided to base eligibility for nonfinancial component hedging on the clearly-and-closely-related criteria within the NPNS scope exception because it is a well-understood concept and would place appropriate limitations on the price components that can be designated. Specifically, the requirement in paragraph 815-10-15-32(a) would ensure that the price components are not extraneous to both the cost and changes in fair value of the asset being purchased or sold (including being extraneous to an ingredient or direct factor in the production of that asset). The requirement in paragraph 815-10-15-32(b) would ensure that there is no leverage present under the

requirement that the magnitude of the price adjustment based on the underlying is not significantly disproportionate to the effect of the underlying on the fair value or cost of the asset being purchased or sold (or of an ingredient or direct factor, as appropriate).

BC74. Some stakeholders expressed concern that paragraph 815-10-15-32(b) may require a quantitative correlation test, which in their view may not allow hedge accounting to be applied to the degree that the Board intended. However, the Board understood that using a quantitative assessment to support the clearly-and-closely-related assessment under the NPNS scope exception has generally been limited to determining whether any leverage features exist and would expect the same practice to be applied for purposes of assessing whether a nonfinancial component is eligible for hedge accounting.

BC75. The Board understood from stakeholders that a model based on the clearly-and-closely-related principle within the NPNS scope exception would be operable because it is a longstanding concept in GAAP. The Board noted that this decision will have a minimal effect on entities that want to continue to hedge an explicitly referenced component in a pricing formula according to a forward contract because, under current GAAP, entities already assess whether the component is clearly and closely related to the price of the nonfinancial item being purchased or sold.

BC76. Under current GAAP, depending on whether the contract meets the definition of a derivative, the clearly-and-closely-related assessment would be slightly different. If the contract meets the definition of a derivative, entities apply the clearly-and-closely-related guidance as part of the assessment of the NPNS scope exception to determine whether the contractually specified component within that contract can be designated as the hedged risk. However, if the purchase or sale contract does not meet the definition of a derivative, then entities assess whether the component is clearly and closely related to the host contract under the bifurcation guidance for embedded derivatives to determine whether the contractually specified component can be designated as the hedged risk.

BC77. The Board observed that in both cases the purpose is to identify extraneous components that the Board believes should not be eligible for hedge designation. Therefore, the Board observed that requiring the clearly-and-closely-related criteria under the NPNS scope exception would not be a

significant change from current practice and would extend the analysis already required for designating a contractually specified component under current GAAP for contracts that meet the definition of a derivative to forecasted transactions in the spot market.

BC78. The Board also considered an alternative that would have replaced the existing contractually specified component model with the guidance in International Financial Reporting Standard (IFRS) 9, *Financial Instruments*, that permits designation of a separately identifiable and reliably measurable component of the total price of the nonfinancial item. That approach permits designation of price components in a forecasted nonfinancial transaction that are distinct and contribute to the total price risk of the nonfinancial asset (that is, separately identifiable) and possess observable market prices (that is, reliably measurable).

BC79. The Board received feedback from stakeholders that developing a model grounded on the clearly-and-closely-related principle was preferable to incorporating the separately identifiable and reliably measurable principle under IFRS 9 for several reasons. Stakeholders noted that applying the separately identifiable and reliably measurable principle may differ under GAAP and IFRS Accounting Standards because of differences in the base hedging frameworks. Incremental guidance would be needed to incorporate defined terms and concepts used under IFRS 9, such as the terms *market structure* and *market convention*, to ensure that the FASB's stakeholders would understand and consistently interpret those concepts. Stakeholders also indicated that applying hedge accounting under IFRS Accounting Standards is largely limited to forecasted purchases or sales of nonfinancial assets consummated according to a forward contract, rather than spot transactions. Therefore, incremental analysis would be required to apply that model to spot market transactions in practice.

BC80. In contrast, stakeholders asserted that while the use of the clearly-and-closely-related principle in the context of hedge accounting would be a new application of that guidance that may require some different considerations, the judgments necessary would be grounded in experience with that principle in practice. The Board agreed with the observations made by stakeholders and, for those reasons, decided that the clearly-and-closely-related principle for hedging price components in nonfinancial forecasted transactions would achieve the desired goal of permitting more risk management strategies to

apply hedge accounting while avoiding any potential operability challenges that may result from incorporating the separately identifiable and reliably measurable principle into GAAP.

BC81. As part of a separate nonfinancial hedging issue, the 2019 proposed Update sought to clarify that a forecasted purchase or sale of a nonfinancial asset through a contract that is accounted for as a derivative under Topic 815 may be designated as the forecasted transaction in a cash flow hedge. The Board agreed with some stakeholders who commented on the 2019 proposed Update and maintained that the price variability associated with the forecasted purchase or sale of the nonfinancial asset that is recognized upon settlement should be eligible to be hedged because the variable component is always “at market” and, therefore, does not affect the fair value of the derivative.

BC82. The amendments in that proposed Update would have clarified that a future purchase or sale of a nonfinancial asset through a contract that is accounted for as a derivative under Topic 815 may be designated as the forecasted transaction in a cash flow hedge if physical settlement of the contract accounted for as a derivative is probable in accordance with paragraph 815-20-25-15(b) and the forecasted transaction is not the acquisition of a nonfinancial asset that subsequently will be remeasured with changes in fair value attributable to the hedged risk reported currently in earnings.

BC83. Stakeholders expressed concern that by specifying that the contract, as opposed to the forecasted transaction, must be probable of physical settlement, the amendments in the 2019 proposed Update would have prevented entities from applying hedge accounting to many common types of forecasted purchases and sales in which the forecasted transaction is probable of occurring but the entity is uncertain which specific contract is probable of physically settling.

BC84. The Board acknowledged that the proposed physical settlement requirement at a contract level unit of account is unnecessarily burdensome and arbitrary from a risk management perspective. Therefore, the Board decided to not finalize the amendments in the 2019 proposed Update. Instead, the Board decided to clarify in the amendments in the 2024 proposed Update that the guidance in paragraph 815-20-25-15(e), which prohibits hedge accounting from being applied to a forecasted transaction that relates to a recognized asset or liability that is remeasured in earnings for changes in fair value attributable to the hedged risk, does not preclude hedging a variable price

component in a forward contract accounted for as a derivative if that variable price component does not cause changes in the fair value of the derivative (and all other criteria for hedge accounting are satisfied). The Board believed that the amendment in the 2024 proposed Update would better align with the broader cash flow hedging framework.

### *Feedback on the 2024 Proposed Update and Redeliberations*

BC85. Respondents to the 2024 proposed Update indicated that the proposed amendments are both operable and an improvement to current GAAP and supported the increased ability to hedge nonfinancial spot market transactions using the clearly-and-closely-related criteria. Stakeholders emphasized that the clearly-and-closely-related principle is well understood in practice and that it would help alleviate the difficulties that entities experience under current GAAP to apply hedge accounting for transactions conducted in the spot market.

BC86. The Board decided to finalize the nonfinancial component model in the 2024 proposed Update. The Board continues to believe that a model based on the clearly-and-closely-related principle is a significant improvement over the existing contractually specified component model because it allows entities to apply hedge accounting regardless of the nature of the nonfinancial purchase or sale transaction that creates the risk being hedged. That is, relative to current GAAP, which limits designation of nonfinancial components to those that are contractually specified, the Board expects that the clearly-and-closely-related principle will expand hedge accounting for forecasted purchases and sales of nonfinancial items because it more broadly permits hedge accounting of components for forecasted spot transactions and expands eligible component hedges for forward contracts to include subcomponents of components explicitly referenced in a contract's pricing formula.

BC87. The Board observes that entities often enter into derivatives as hedges of price variability attributable to forecasted purchases of nonfinancial assets before entering into a forward contract, commonly referred to as a hedge of a "not-yet-existing" contract. The Board decided that for hedges of not-yet-existing contracts designated on a pool basis (as discussed in paragraph BC31), an entity may need to perform a similar risk assessment that considers the possible price components to be included in the not-yet-existing contracts. On the basis of feedback received, the Board decided to clarify in the example

of a nonfinancial hedge of not-yet-existing contracts (see paragraphs 815-30-55-160 through 55-164) that the similar risk assessment is required because the entity expects that the hedged forecasted transactions will have multiple risks occurring at the same time (for example, purchases of soybeans indexed to the ABC soybean index and the DEF soybean index included in the same portfolio hedge), but the entity is uncertain what combination of the designated hedged risks will be explicitly referenced in the contracts. The Board observes that the similar risk assessment would be required in comparable hedges of not-yet-existing financial contracts such as a cash flow hedge of a forecasted issuance of debt when an entity expects that the hedged forecasted transactions will have multiple risks occurring at the same time (for example, interest payments occurring at multiple interest rate indexes or tenors in the same portfolio hedge). The Board understands that there has been diversity in practice for hedges of not-yet-existing financial contracts when the hedged forecasted transactions will have only one risk that occurs but there is uncertainty about what that risk will be. The Board acknowledges that those types of hedges were not explicitly addressed as part of this project.

BC88. The Board also continues to believe that an important advantage of the nonfinancial component model relative to current GAAP is that it may allow entities to avoid missed forecasts for highly effective economic hedges in certain circumstances. For example, if an entity experiences an unexpected shortfall in the forecasted amount of a nonfinancial asset to be purchased under a forward contract and makes up the shortfall through a spot market purchase, hedge accounting could be preserved under a model based on the clearly-and-closely-related principle if the component being hedged is clearly and closely related to both the forward price and the spot price of the nonfinancial asset. Therefore, the Board believes that this model will achieve its objective of more closely aligning entities' economic hedging strategies with hedge accounting to better portray those strategies in financial reporting.

BC89. The Board also observes that more hedges may qualify for the critical terms match method of assessing hedge effectiveness with the expanded ability to designate a component or subcomponent as the hedged risk in a nonfinancial purchase or sale transaction. Therefore, stakeholders requested that the Board amend the current example demonstrating the critical terms match method to incorporate the amendments allowing component hedging under the clearly-and-closely-related criteria. The Board amended the example as a means of aligning the guidance in the Codification with the Board's

observation on the potential broadened use of the critical terms match method of assessing hedge effectiveness.

BC90. The Board also decided to finalize the amendments in the 2024 proposed Update to clarify the accounting for hedging nonfinancial components in contracts accounted for as derivatives, with minor clarifications, to explicitly allow an entity to designate a variable price component in a forecasted purchase or sale of a nonfinancial asset under a contract that is accounted for as a derivative as the hedged risk in a cash flow hedge (see paragraph 815-20-25-15(e)). Stakeholders generally supported the proposed amendment and viewed the limitation on the ability to hedge a variable price component in these circumstances as overly restrictive and inconsistent with entities' risk management strategies.

BC91. The Board does not foresee significant costs for education or establishing accounting policies related to the new principle-based model for cash flow hedges of nonfinancial price components. However, for entities that historically have not been able to hedge components of forecasted nonfinancial transactions, or otherwise elected not to apply hedge accounting for nonfinancial components, there may be costs incurred to introduce new or amend existing processes and internal controls to implement the new model and educate employees. Nevertheless, because cash flow hedge accounting is an election, only entities that elect to apply cash flow hedge accounting will be affected. The Board believes that the potential benefits of its decisions on cash flow hedges of forecasted nonfinancial purchases and sales justify the potential implementation costs because they expand the population of economic hedging strategies to which hedge accounting may be applied, thus allowing a greater number of entities to better reflect the results of their risk management activities in their financial statements.

## Issue 4: Net Written Options as Hedging Instruments

### *Current GAAP*

BC92. For a cash flow hedge involving a hedging instrument that is deemed to be a net written option to be eligible for cash flow hedge accounting, Topic 815 requires symmetry of the gain and loss potential of the combination of the hedged item and the net written option. Many lending institutions enter into interest rate swaps with mirror-image options to better mitigate their exposure

to interest rate risk arising from lending activity, which requires application of the net written option test to determine whether the compound derivative (the swap and the written cap or floor) is eligible for hedge accounting.

### *2024 Proposed Update*

BC93. Following the cessation of LIBOR and the introduction of the Secured Overnight Financing Rate (SOFR) in the United States, stakeholders highlighted an issue about the application of the net written option test for lending institutions that enter into loans and derivatives with “mirror image” caps or floors. When LIBOR was the predominant reference rate, both the variable leg of the interest rate swap and the variable loans were tied to the same LIBOR tenor. As a result, historically, assuming that all other relevant criteria were met, compound derivatives comprising swaps and interest rate floors satisfied the net written option test and were eligible to be designated in a cash flow hedging relationship because the potential for favorable cash flows stemming from this relationship would equal or exceed the potential for unfavorable cash flows. After LIBOR cessation, it became common for the variable leg of the interest rate swap to be tied to Daily SOFR, which often does not match the rate on the variable-rate loans (which may be tied to Term SOFR or Daily SOFR with a different compounding convention).

BC94. While the economic substance of the two relationships (pre- and post-LIBOR cessation) is similar, the relationship executed in a LIBOR environment would pass the net written option test to be eligible for hedge accounting, while the relationship executed in the post-LIBOR environment would not, rendering it ineligible for hedge accounting. This is because in the post-LIBOR environment, symmetry would not exist in all possible percentage changes in the underlying because the underlying interest rates do not match. Stakeholders requested that the net written option test be amended because, in their view, that guidance was not written to contemplate a post-LIBOR environment in which the underlyings in the hedged item and hedging instrument do not match.

BC95. To resolve this issue, the Board decided to propose a narrow amendment of the guidance for applying the net written option test when the designated hedging instrument in a cash flow hedge is a compound derivative made up of a written option and a non-option derivative to allow entities to assume that certain terms of the compound derivative and the hedged item are matched for purposes of applying the test.

BC96. Under the amendment in the 2024 proposed Update, the interest rate of the hedged transaction and hedging instrument would be considered to match if it is a derivation of the same index, and the timing of occurrence of the hedged transaction and the settlement of the hedging instrument (as well as reset dates) would be considered to match if they are within the same 31-day period or fiscal month. The Board believed that these were reasonable adjustments to accommodate differences in rates and minor differences in payment or reset dates associated with those rates as a result of reference rate reform, which would cause otherwise highly effective hedging strategies to fail the net written option test.

BC97. The Board considered an alternative that would have removed the net written option test from Topic 815. Some stakeholders noted that the test may not be necessary given that current guidance requires hedging relationships to be highly effective and that the test limits application of hedge accounting for certain risk management activities, thereby not reflecting the economics of those hedges. In addition, some stakeholders noted that eliminating the net written option test could reduce the cost burden associated with hedging using option contracts and could increase the application of hedge accounting for common highly effective hedging strategies.

BC98. The Board also considered another alternative that would have changed the scope of the net written option test by removing the requirement for compound hedging instruments made up of a written option and any other non-option derivative instrument (for example, an interest rate swap) to be presumed to be a net written option. This would have addressed the specific fact pattern raised by stakeholders in which (a) an interest rate swap with a written option is designated as a hedge of a loan with the same embedded purchased option and (b) the addition of the written option to the interest rate swap results in a better economic hedge but would cause the strategy to fail the net written option test.

BC99. The Board decided not to propose eliminating the net written option test or changing the scope of that test because the test serves an important purpose that is incremental to the hedge effectiveness assessment. Some Board members noted that the requirement for symmetry of the gain and loss potential of the combined hedged position was intended to preclude a written option that is used to sell a portion of the gain potential on an asset or liability from being eligible for hedge accounting. While some of those strategies are

explicitly prohibited in GAAP (for example, covered call strategies that are explicitly prohibited by paragraph 815-20-55-45), eliminating the test may permit other strategies involving options, combinations of options, or combinations of options and non-option derivatives to qualify for hedge accounting, which some may view as inconsistent with the original intent of the guidance.

### *Feedback on the 2024 Proposed Update and Redeliberations*

BC100. Stakeholders indicated that the amendments in the 2024 proposed Update related to the application of the net written option test were narrowly tailored, such that few cash flow hedges would qualify for the Board's intended relief. Respondents highlighted that limiting the timing of occurrence of the hedged transaction and the settlement of the hedging instrument window to the same 31-day period or fiscal month would exclude instruments with settlement windows exceeding 1 month, which are commonplace. Respondents also noted that to qualify for the relief, all loans in a hedged portfolio would need to have the same floor, regardless of whether loans with different floors are highly correlated. Some stakeholders noted that this could be viewed as inconsistent with the proposed amendments about the similar risk assessment.

BC101. Additionally, while this issue was initially raised in the context of cash flow hedging, certain stakeholders provided feedback that a SOFR mismatch in a fair value hedge also can result in automatic failure of the net written option test. In instances in which an interest rate swap (with a written cap or floor) designated as the hedging instrument is based on a SOFR Term rate, the mismatch with the SOFR-OIS benchmark rate will similarly result in the hedging relationship automatically failing the net written option test. Therefore, stakeholders supported incorporating in a final Update a solution to also address fair value hedges. The Board agreed with stakeholders that both cash flow hedges and fair value hedges should be addressed as part of this issue because both arise as the result of the cessation of LIBOR.

BC102. Some stakeholders suggested, and the Board considered, an alternative that would have expanded the proposed amendments such that the hedged forecasted transaction's and the hedging instrument's reset date, settlement date, or both dates match if they are expected to be in the same 181-day period for *cash flow hedges*. For *fair value hedges*, the alternative would have allowed entities to assume that the benchmark interest rate

designated matches the interest rate in the hedging instrument for the purposes of performing the net written option test if both interest rates are derivations of the same index. This would have addressed concerns about the settlement window as well as the issue that caused fair value hedges to fail the net written option test. However, the Board did not select this alternative because it concluded that it would have reduced the benefits of the proposed amendments to similar risk assessment guidance for entities seeking to hedge portfolios of floored loans with floored swaps.

BC103. Some comment letter respondents supported eliminating the net written option test. Other stakeholders expressed that it is inappropriate to reduce the potential for gains in return for an upfront cash payment and achieve hedge accounting, which would be allowed if the net written option test was eliminated. The Board believes that a blanket prohibition on applying hedge accounting to written options is inconsistent with other aspects of the hedge accounting model. Therefore, the Board decided to remove the presumption that a compound hedging instrument is a net written option if (a) the instrument is designated in either a cash flow hedge or fair value hedge of interest rate risk, (b) the instrument comprises a swap and a written option, and (c) the notional amounts of the swap and written option match. Hedging instruments that meet those requirements qualify for the relief even if a net premium is received. The Board established this approach to respond to feedback and better reflect the results of entities' economic hedging strategies. By narrowly defining the hedging instruments that would be eligible for relief from applying the net written option test, the Board believes that the effects on strategies outside those with known issues would be minimized. The Board also believes that current requirements for hedge documentation and effectiveness assessments provide sufficient guardrails in the absence of the net written option test in these circumstances.

BC104. The Board acknowledges that eliminating the net written option test for hedges that include a hedging instrument comprising a swap and a written option could result in entities being more selective of the risk corridors they choose to hedge. The Board observes that swaps with written options reduce risk when hedging a loan with a mirror-image option and that when a mirror-image option does not exist in the hedged item, reducing the protection offered by a swap by writing an option could be a valid risk management strategy.

BC105. The Board believes that the expected benefits of the changes to the net written option test justify the expected implementation costs because it is a practical solution to the problem facing practice. The Board observes that the net written option test was developed more than 25 years ago when LIBOR was the predominant reference rate. In that environment, both the variable leg of the interest rate swap and the variable loans were tied to the same LIBOR tenor. The Board believes that hedge accounting guidance should continue to be operable after LIBOR cessation and that the amendments achieve that outcome for cash flow and fair value hedges in which the designated hedging instrument is a compound derivative comprising a written option and a swap. The Board believes that its selected alternative to resolve this issue addresses many of the same concerns as removing the net written option test but takes a more targeted approach by excluding a particular compound instrument from the test to address the most common circumstance creating unintuitive outcomes under current GAAP. Because the amendments in this Update simplify the application of hedge accounting guidance by permitting entities to presume that a compound hedging instrument comprising a swap and a written option is not a net written option in a hedge of interest rate risk, the Board does not foresee significant implementation costs related to this issue.

## Issue 5: Foreign-Currency-Denominated Debt Instrument as Hedging Instrument and Hedged Item (Dual Hedge)

### *Current GAAP*

BC106. The amendments in Update 2017-12 eliminated the separate recognition and measurement of ineffectiveness for net investment hedges and required that amounts included in the assessment of effectiveness be recognized in accumulated other comprehensive income until the foreign entity is substantially liquidated. As a result, for a foreign-currency-denominated debt instrument that is designated as the hedging instrument in a net investment hedge and designated as the hedged item in a fair value hedge of interest rate risk (that is, a dual hedge), the gain or loss on the remeasurement of the fair value hedge basis adjustment at the spot exchange rate must be deferred in accumulated other comprehensive income.

BC107. Before the issuance of Update 2017-12, that foreign exchange remeasurement was recognized in current-period earnings because it was a source of ineffectiveness resulting from the notional mismatch in the net

investment hedge. The foreign exchange remeasurement of the fair value hedge basis adjustment was offset in earnings by the foreign exchange remeasurement of the derivative designated as the hedging instrument in the fair value hedge of interest rate risk. That resulting offset no longer exists under current GAAP as a result of the amendments in Update 2017-12.

### *2019 Proposed Update*

BC108. The Board did not intend to cause amounts previously recorded as ineffectiveness from the fair value hedge basis adjustment to be recognized in accumulated other comprehensive income for a net investment hedge when the debt instrument also is designated as the hedged item in a fair value hedge of interest rate risk. Therefore, to resolve that issue, the amendments in the 2019 proposed Update would have excluded the fair value hedge basis adjustment from the assessment of the effectiveness of the net investment hedge when the debt instrument also is designated as the hedged item in a fair value hedge of interest rate risk. Accordingly, the notional amount of the debt instrument that is designated as the hedging instrument in the net investment hedge would not change over time as a result of applying fair value hedge accounting. Therefore, the notional amount for the debt instrument may continue to match the notional amount of the investment in a foreign subsidiary that is designated in the net investment hedge. Because the debt instrument's fair value hedge basis adjustment would be excluded from the assessment of effectiveness of the net investment hedge, the remeasurement for changes in the spot rates on the fair value hedge basis adjustment would be recognized in earnings in accordance with Subtopic 830-20, Foreign Currency Matters—Foreign Currency Transactions.

### *2024 Proposed Update*

BC109. The Board decided to affirm the amendments in the 2019 proposed Update to require that an entity exclude the fair value hedge basis adjustment from the assessment of hedge effectiveness in a net investment hedge when the hedging instrument also is a hedged item in a fair value hedge of interest rate risk. The Board continues to believe that this was an unintended consequence of the amendments in Update 2017-12, which were not intended to diminish the utility of the dual hedge strategy.

BC110. In addition, the amendments in the 2019 proposed Update would have been applied only to foreign-currency-denominated debt instruments that are both a hedging instrument and a hedged item, and the proposed amendments specified that the guidance should not be applied by analogy to other circumstances. Accordingly, if the fair value hedge for interest rate risk is subsequently discontinued, an entity would have considered the debt instrument's fair value hedge basis adjustment when prospectively assessing the effectiveness of the net investment hedge. The Board decided to affirm the amendments in the 2019 proposed Update that specified that the guidance should not be applied by analogy to other circumstances and that if the fair value hedge for interest rate risk is subsequently discontinued, an entity would consider the debt instrument's fair value hedge basis adjustment when prospectively assessing the effectiveness of the net investment hedge because it ensures alignment of all net investment hedges once the source of the presentation mismatch has been eliminated.

### *Feedback on the 2024 Proposed Update and Redeliberations*

BC111. Stakeholders unanimously supported the amendments to dual hedges, and the Board decided to affirm the amendments. The Board continues to believe that the expected benefits of its decision on dual hedging relationships justify the expected implementation costs because it restores the ability to apply this hedging strategy without the earnings volatility for a hedge that may achieve a perfect economic offset of changes attributable to both interest rate risk and foreign exchange risk. The Board does not foresee significant implementation costs for education or establishing accounting policies because the Board's decision restores the guidance that had been in place before the issuance of Update 2017-12. That is, entities are already familiar with the strategy and mechanics necessary for its application.

### **Effective Date and Transition**

BC112. The amendments in this Update are effective for public business entities for annual reporting periods beginning after December 15, 2026, and interim reporting periods within those annual reporting periods. For entities other than public business entities, the amendments in this Update are effective for annual reporting periods beginning after December 15, 2027, and interim reporting periods within those annual reporting periods. Comment letter respondents supported an incremental one-year implementation period for

entities other than public business entities because it would allow more time for those entities to understand and implement the final guidance. The Board decided to provide an additional year for those entities to apply the amendments on the basis of that stakeholder feedback.

BC113. In the 2024 proposed Update, the Board proposed permitting early adoption for all entities on any date because it expects that some stakeholders may want to adopt the guidance before the mandatory effective date. In the final Update, the Board decided to affirm its decision to permit early adoption on any date on or after issuance of the final Update on the basis of support from comment letter respondents. The Board also observes that permitting early adoption provides entities with the flexibility to implement the guidance at their discretion.

BC114. The Board decided to affirm the proposed requirement that entities should apply the amendments in this Update on a prospective basis for all hedging relationships. The Board considered whether a retrospective transition approach would be necessary to provide for the consistent use of the same accounting methodology from one historical accounting period to another and to enhance the comparability of financial statements between periods. For each of the amendments in this project, the Board determined that a retrospective transition approach would not be necessary because affected hedging relationships already qualify for hedge accounting under the current guidance. Furthermore, the changes made to the critical terms of the hedging relationship in accordance with the amendments only affect the ongoing (that is, future) assessments necessary to retain hedge accounting and, therefore, do not result in adjustments to the financial statements at the date of adoption.

BC115. In the 2024 proposed Update, the Board proposed incremental guidance to facilitate transition for entities with existing hedges (that is, the hedging instrument has not expired, been sold, terminated, or exercised, or the entity has not removed the designation of the hedging relationship) that would be affected by the amendments. For the issue on the similar risk assessment for cash flow hedges, the Board decided to affirm the proposed transition guidance to permit entities to migrate some or all forecasted transactions associated with one or more risks from one existing pool or pools to a new pool or pools, existing pool or pools, or a combination of those pools and to reassign existing hedging instruments to those new or existing pools as appropriate. The Board understands that entities with existing hedges using a “first-of” approach

will have already assigned a significant portion of their forecasted transactions with common risk types to an existing pool; therefore, this provision is necessary to enable entities to obtain the benefit of the proposed amendments on the similar risk exposure assessment without dedesignating a significant portion of their existing hedging relationships.

BC116. On the basis of stakeholder feedback on the 2024 proposed Update, the Board decided to allow entities to reassign amounts in accumulated other comprehensive income associated with hedges that are dedesignated before the final Update is adopted in a manner that would allow entities to align accumulated other comprehensive income associated with dedesignated portfolio hedges and live hedges (see paragraph 815-20-65-7(f)). The Board acknowledged the benefit of allowing dedesignated pools to be aligned with newly repooled live hedges so that entities would be able to track dedesignated and live pools on a combined basis after adoption to determine when to reclassify amounts out of accumulated other comprehensive income into earnings. For example, an entity may currently hedge SOFR-OIS and Prime interest payments in separate pools and track those pools separately when determining when to reclassify amounts out of accumulated other comprehensive income into earnings. Upon adoption of the amendments in this Update, the entity may choose to hedge SOFR-OIS and Prime interest payments in a single pool if all requirements of hedge accounting are met. In this example, the Board's decision to allow entities to align accumulated other comprehensive income associated with dedesignated hedges and live hedges will allow the entity to track SOFR-OIS and Prime interest payments on a combined basis for both (a) individual pools that had been dedesignated before adoption of the amendments in this Update and (b) the combined pool designated upon adoption of the amendments. Entities are still required to reclassify amounts out of accumulated other comprehensive income into earnings when the hedged forecasted transaction affects earnings, which is consistent with current guidance.

BC117. In addition, the 2024 proposed Update provided entities with the option to amend existing hedging relationships to add an additional hedged risk or risks to an existing portfolio, which the Board believed would benefit those entities that were previously precluded from pooling transactions with similar risks. The Board decided to finalize that transition provision in this Update.

BC118. Additionally, in the 2024 proposed Update, the Board proposed requiring entities to change their similarity assessment method to one of the approaches specified in the amendments in the proposed Update. If an entity is already applying one of the proposed methods of assessing similar risk exposure, the Board proposed that the entity may change to the other method upon adoption. Also, if an entity wishes to perform one assessment that satisfies both the similar risk exposure assessment and the effectiveness assessment, it would be able to change its method of assessing hedge effectiveness to achieve that streamlined objective.

BC119. On the basis of stakeholder feedback on the 2024 proposed Update, the Board decided that adopting the specified methods for similar risk assessment should be optional, rather than required, for hedges existing as of the date of adoption. Respondents indicated that optionality would help avoid unintended outcomes for entities that may not update their hedge documentation in connection with adoption of this final Update. As a result of this decision, for existing hedges, entities may elect to continue to apply current GAAP until the end of the existing hedge. In outreach conducted during redeliberations, stakeholders supported that change. However, the Board observes that entities are still required to apply one of the two specified methods for similar risk assessment for hedges designated after the adoption of the final Update.

BC120. Because the 2024 proposed Update would have required application of the choose-your-rate debt model for applicable hedging relationships, the Board proposed that the transition provisions require that an entity apply the amendments in the proposed Update to existing hedging relationships involving choose-your-rate debt instruments that do not use the first-payments-received technique. The Board understood that a choose-your-rate debt instrument designated as part of an existing hedging relationship using the first-payments-received technique would not qualify for the amendments in the proposed Update. Accordingly, the Board proposed that an entity may choose to (a) change its designation approach in those circumstances in transition to qualify for the proposed amendments or (b) maintain its current designation approach and not apply the proposed amendments to those hedging relationships. In redeliberations, the Board decided to make the choose-your-rate debt model optional, as discussed in paragraph BC49. Therefore, the proposed transition provisions to require that an entity apply the amendments

to existing hedging relationships involving choose-your-rate debt instruments that do not use the first-payments-received technique are no longer relevant.

BC121. For the issue on cash flow hedges of nonfinancial forecasted transactions, the Board proposed and decided to finalize transition guidance that permits, but does not require, entities to amend their designated hedged risk for existing hedges to reflect the changes to the guidance given the overlap in eligibility criteria between the existing contractually specified component model and a model based on the proposed clearly-and-closely-related principle. The Board anticipates that existing hedges of contractually specified components generally will be eligible for hedge accounting under the clearly-and-closely-related guidance because of the current requirements for (a) the hedged risk to be explicitly referenced in the pricing formula of an agreement to purchase or sell a nonfinancial asset and (b) the price component to be clearly and closely related to the nonfinancial asset.

BC122. Although contracts that are not derivatives in their entirety were previously assessed under the clearly-and-closely-related guidance for bifurcation of embedded derivatives rather than the clearly-and-closely-related guidance on the NPNS scope exception, given the similar objectives of those assessments, the Board believes that an existing contractually specified component hedge is expected to also qualify under a model based on the clearly-and-closely-related principle. Therefore, the Board did not want to place an incremental burden on preparers to perform an analysis under the clearly-and-closely-related guidance on the NPNS scope exception in transitioning to the guidance in this Update in those circumstances.

BC123. For each of those discrete issues, the Board proposed and decided to finalize guidance requiring that prospective hedge effectiveness assessments be performed as though the revised relationship and the amendments in this Update had been in place since the hedge designation date, thereby avoiding any hedge ineffectiveness resulting from the passage of time between hedge inception and the date of adoption. That is, an entity should create the terms of the instrument used to estimate changes in the cash flows of the hedged risk on the basis of market data as of hedge inception. The Board believes that this accommodation will allow an entity to more accurately reflect its risk management activities in financial reporting immediately upon adoption. This transition approach was utilized by the Board in Update 2017-12 to address the same issue, with no known challenges emerging in practice.

BC124. The Board proposed and decided to finalize guidance that would clarify that if an entity is revising a hedging relationship's critical terms (including the hedged forecasted transactions or its method of assessing effectiveness or similar risk exposure) in accordance with the transition provisions in this Update, the entity also is permitted to revise the corresponding hedge documentation, without hedge dedesignation, to reflect those changes. Without that clarification, stakeholders indicated that it would be unclear whether an entity would be required to dedesignate all hedging relationships modified as a result of adopting the amendments when the entity updated its hedge documentation in transition. The Board understands that there could be situations in which the hedged forecasted transactions are defined by the designated hedge risk. Accordingly, if an entity changes the designated hedged risk as permitted upon adoption of the amendments, then it also will need to amend the hedged forecasted transactions without dedesignation to fully effectuate transition.

BC125. The Board decided that no specific transition guidance is needed for the amendments in this Update on dual hedging relationships and net written options as hedging instruments because the amendments are applicable only to hedges designated on or after the adoption date. The Board based this decision on stakeholders' feedback indicating that the dual hedging strategy lost its utility because of the recognition and presentation mismatch created by the amendments in Update 2017-12, and, as a result, the Board is unaware of dual hedging relationships currently existing in practice. The Board also is unaware of any existing hedging relationships in which a compound derivative made up of a written option and a non-option derivative has been designated as the hedging instrument in a cash flow hedge where there is a mismatch between the interest rate index on the hedged item and the derivative. The Board received stakeholder feedback indicating that this type of hedging relationship has also lost its utility following the LIBOR cessation.

BC126. For the transition disclosures, the Board considered the standard disclosure requirements in Topic 250, Accounting Changes and Error Corrections. Given a prospective transition approach, the Board decided to limit the transition disclosures to the nature of and reason for the change in accounting principle and the method of applying the change. The Board decided that an entity that issues interim financial statements must provide those disclosures in the financial statements of both the interim period of the change and the annual period of the change.

## Amendments to the GAAP Taxonomy

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The amendments to the *FASB Accounting Standards Codification*<sup>®</sup> in this Accounting Standards Update require improvements to the GAAP Financial Reporting Taxonomy and SEC Reporting Taxonomy (collectively referred to as the “GAAP Taxonomy”). Those improvements, which will be incorporated into the proposed 2026 GAAP Taxonomy, are available through [GAAP Taxonomy Improvements](#) provided at [www.fasb.org](http://www.fasb.org), and finalized as part of the annual release process.