

TO: Sam Woods
Chair
International Accounting Standards Board (IASB)

Dear Mr Woods,

Exposure Draft: Risk Mitigation Accounting, proposed amendments to IFRS 9 and IFRS 7

About the European Banking Federation

The European Banking Federation (EBF) is the voice of the European banking sector, bringing together 33 national banking associations representing approximately 3,500 banks and around 2.7 million employees across Europe.

The EBF welcomes the opportunity to comment on the Exposure Draft and recognises the substantial effort invested by the International Accounting Standards Board (IASB) in developing a comprehensive approach to accounting for dynamic interest-rate risk management. We support the Board's objective of improving the alignment between financial reporting and risk management and remain committed to constructive engagement on a workable solution.

Executive summary

We support the objective of improving the alignment between accounting and risk management. In our view, however, the objective should be expanded and stated more completely by reference to the accounting outcome and the practical operation of the model. Better representation of risk management is important, but is not sufficient on its own.

Expanded objective: RMA outcomes should represent the economic effect of an entity's repricing-risk management, materially mitigate artificial accounting volatility arising from the different accounting treatment of managed exposures and risk management derivatives, and be operationally viable.

When assessed against this expanded objective, the Exposure Draft does not yet provide an effective and operationally feasible replacement for existing portfolio hedge accounting. This conclusion arises from the combined operation of the model's eligibility, measurement and safeguard mechanisms, rather than from one isolated requirement.

When revising the model, the identified issues and suggested approaches should be considered as a package to achieve the expanded objective. Should such comprehensive revisions not be achievable, alternative approaches to RMA should be explored.

The proposals come up short along three connected axes:

Accounting volatility: The combined mechanics will create, or fail to remove, profit-or-loss and other comprehensive income volatility, even where the entity continues to manage its interest-rate risk effectively.

Operational complexity and cost: The proposals will require granular attribution, repeated adjustment and extensive tracking within portfolios managed on a net basis, with implementation and continuing costs that are not proportionate to the reporting benefit.

Disclosures: The proposed disclosures provide only a partial view of an institution's interest-rate risk management, when compared with the broader scope of the institution's interest-rate risk management and applicable prudential frameworks and may require commercially sensitive information to be disclosed.

We acknowledge that the Exposure Draft contains constructive developments. However, substantial revision is needed before the model can credibly replace the existing approaches. Therefore, any revised package should be subject to sufficient practical assessment and stakeholders should have an opportunity to assess it through re-exposure.

Basis for assessment

The EBF Expert Group was formed to perform a collective assessment of RMA. The Group consisted of 13 EU and non-EU banks representing a total asset base EUR17 trillion. The work this group performed drew on the expertise of 35 specialists from these banks who invested upwards of 1,500 hours in this evaluation work.

Our collective work focused on interpreting and evaluating the Exposure Draft on Risk Mitigation Accounting through the preparation of a series of detailed accounting interpretation papers with examples, which are included in Appendix 2 of this document. During this phase, the EBF identified several conceptual issues that could be demonstrated through these focused examples, these issues are presented in the body of this letter.

Background and current accounting approaches

Banks manage interest-rate risk in the banking book dynamically and on a portfolio basis. The accounting challenge arises because the managed exposures and the derivatives used to mitigate their risk are not necessarily measured on the same basis.

The accounting for banking book exposures reflects the applicable IFRS 9 classification and measurement requirements. Risk management derivatives are generally measured at fair value through profit or loss. Economically related positions may therefore affect profit or loss differently and at different times, producing volatility that is not caused by ineffective risk management and does not reflect the economics of the managed position.

Banks currently address this effect through different hedge accounting approaches, depending on the requirements available to them and the risk being managed. These include portfolio fair value hedge accounting under IAS 39, the EU-endorsed version of IAS 39 and hedge accounting approaches under IFRS 9. Existing approaches are not uniform, are not without limitations and may not fully reflect modern portfolio risk management. Nevertheless, they are firmly embedded in institutions' systems, governance and reporting processes and, over many years, have been refined to provide a generally effective and operationally robust representation of risk management activities and the underlying economics of managed portfolios in financial statements.

This is not an argument that existing accounting should remain unchanged indefinitely. Improvement is desirable. We recognise the potential benefits of a single globally applicable accounting model for repricing-risk management and would support such a globally consistent approach, particularly if its primary objective were to eliminate the artificial accounting volatility created by current accounting requirements. The relevant test, however, is whether the proposed replacement produces a demonstrably equivalent or better accounting outcome, reflects risk management more faithfully, addresses that accounting volatility and can be operated reliably in practice.

Constructive developments in the Exposure Draft

The Exposure Draft contains important developments that provide a constructive foundation. We welcome:

- the continued pursuit of a comprehensive solution for dynamic portfolio risk management;
- the recognition of net exposures and open portfolios;
- the inclusion of non-maturing deposits using behavioural assumptions, subject to appropriate governance;
- the greater use of risk management concepts in the model; and
- the separation of the frequency of designation from the frequency of measurement and accounting.

These developments move the accounting closer to aspects of risk management. They do not, however, overcome the effects created by the interaction of the proposed mechanisms.

Why the combined mechanisms do not yet achieve the expanded objective

The concern is not one isolated requirement. The eligible underlying portfolios define the accounting population. The net repricing risk exposure is measured within time bands. The risk mitigation objective is constrained by that exposure. Benchmark derivatives are constructed and adjusted, including for changes in dynamic portfolios. The resulting accounting amount is then subject to the lower-of mechanism and the RMA excess test, while other changes may result in discontinuance and restart.

Each element may have an intended disciplinary purpose when considered separately. The concern is the cumulative effect. Eligibility restrictions, individual time-band constraints, benchmark derivative adjustments, the treatment of unexpected changes, the lower-of mechanism, the excess test and discontinuance requirements can interact in a way that produces accounting results disconnected from portfolio-level risk management and creates residual artificial accounting volatility and involves a significant operational burden.

1. Accounting mismatch and artificial or undue accounting volatility

We are concerned that the proposed model will generate accounting results that do not faithfully reflect the underlying economics of the managed portfolio. Risk management objectives are primarily focused on the stability and predictability of future NII and the economic value of banking book positions.

In our view, the objective should be to reduce accounting mismatches arising from asymmetrical measurement requirements in IFRS 9 to the extent necessary for the resulting accounting outcomes to faithfully represent an entity's IRRBB risk management activities, rather than to eliminate all accounting volatility. Furthermore, volatility arising solely from the mechanics of the accounting model does not provide useful information to management or to users of financial statements.

For banking book activities, the vast majority of positions are managed and assessed on a hold-and-collect basis and measured internally using amortised cost concepts.

The objective is neither to suppress nor defer legitimate economic volatility. Rather, it is to avoid accounting outcomes that are disconnected from the economics of the exposures being managed and therefore reduce the decision-usefulness of financial reporting.

Accounting volatility should be a consequence of economic volatility, not a consequence of accounting mechanics.

Structured item & Relevant WG document (see appendix 2)	Issue description	Alternative approach(es) for discussion
RMA excess test WG2 – RMA Excess	The proposed excess test will create accounting outcomes that are disconnected from actual risk management activities and may result in accounting volatility even where risk management objectives continue to be achieved effectively.	We recommend a removal of the excess test as is, and design an effective, principles-based recoverability test.
NRRE alignment with risk management practices incl. leases and AT1 WG6 – Interaction IFRS and RMA	Any misalignment between the NRRE and risk management practices will result in accounting outcomes that do not faithfully represent an entity's risk management activities and may introduce unnecessary accounting volatility.	Re-examine alignment with risk management practices to also include currently non-eligible items such as leases and AT1 items which are actual elements of risk management practices
Benchmark derivatives WG3 – Transition Benchmark Derivative Initial Fair Value of Zero	The current Exposure Draft gives rise to a fundamental challenge in relation to benchmark derivatives through the requirement that benchmark derivatives are constructed with an initial fair value of zero.	The requirement for benchmark derivatives to start at a fair value of zero should be reconsidered. A pull-to-par approach should be explored.
Risk measure per bucket WG5 – Risk Measure per Time Bucket	The proposed determination of risk measures at bucket level will create outcomes that are disconnected from actual risk management practices and may affect the representational	Entities should not be restricted to a single risk measure per time bucket, where risk management uses multiple measures.

Lower-of test WG3 – Cumulative Lower Of	faithfulness of the resulting accounting outcomes. In certain cases, the lower-of test will constrain the ability of the model to reflect managed exposures and contribute to artificial accounting volatility.	We recommend removing the cumulative lower of requirements from the Exposure Draft and reconsidering them only if field testing demonstrates a clear need and a workable alternative. No such replacement has yet been identified.
Non-linear risk management WG8 – Non-linear Risk RMA	The wording of the Exposure Draft is insufficiently well-developed to facilitate effective representation of non-linear risk management strategies.	Clarification of the treatment of non-linear instruments and related risk management activities.
Over-hedging WG9 – Over-hedge vs Under-hedge within Limits and Optimisation Strategy	The treatment of so-called over-hedging at bucket level will generate accounting outcomes that do not faithfully represent economic risk management and can lead to artificial volatility.	Our general recommendation is to address or remove artificial over-hedging limitations. Alternatively, introduce an entity-defined RMA eligibility threshold that redefines the boundary of eligible risk mitigation on a gross level. A hedge within the threshold is then not an over-hedge for RMA purposes.
Unexpected changes WG10 – Unexpected Changes	The treatment of unexpected changes will generate accounting outcomes that are inconsistent with how dynamic portfolios are managed in practice and result in accounting volatility unrelated to underlying economics, also due to the lack of clarity around what constitutes an unexpected change.	Restrict the definition of unexpected changes to actual and material realised deviations from expectations and unexpected portfolio disposals.
Intercompany hedges WG7 – Intra Group Application of RMA	The proposed treatment of intercompany hedges could create accounting outcomes that differ from the economic risk management activities undertaken at group level and therefore warrants further consideration.	We conclude that the model should better accommodate intra-group risk management arrangements.

2. Operational complexity and implementation cost

Replacing current practices will be costly, and in the absence of net positive benefits, would not justify the initial and ongoing operational costs.

Structured item	Issue description	Alternative approach(es) for discussion
Dynamic balance-sheet changes WG10 – Unexpected Changes & WG4 – RMA Cycle Run Frequency	The proposed model introduces significant operational complexity when dealing with continuously changing portfolios and evolving risk positions.	Much closer alignment with risk management would reduce complexity by relying on established methodologies, rather than introducing new synthetic

System and data requirements

Multiple: **WG11, WG10, WG4, WG3 & WG9**

RMA discontinuance

WG1 – Changes in Risk Management Strategy, Discontinuance and Restart of RMA and RMA Cycle Accounting Entries

Implementation of the model is likely to require substantial investment in systems, controls and data architecture, creating significant operational burden with uncertain reporting benefits.

Circumstances that require discontinuance and restarting of the model introduce additional operational complexity and may generate outcomes that are difficult to explain.

accounting-only mechanisms and/or requirements.

An “RMA system” would also be simplified by closer alignment of RMA with risk management to rely upon established methodologies, rather than introducing new synthetic accounting-only mechanisms and/or requirements.

Normal portfolio and risk management changes should not automatically trigger discontinuation.

3. Disclosure concerns

Certain disclosures associated with the model may not achieve their intended objective of providing users of financial statements with a complete and coherent view of an institution’s risk management activities.

Structured item	Issue description	Alternative approach(es) for discussion
Partial scope and sensitivity analysis	Because RMA may represent only a subset of the exposures actually managed within an institution's overall IRRBB framework, the resulting disclosures may not provide users with a complete picture of the institution's risk position and, if so, would be inconsistent with disclosures prepared under the IRRBB framework.	The proposed RMA disclosure package should be significantly streamlined. The IFRS 7.30K sensitivity analysis should be removed because it does not reflect a bank's overall IRRBB exposure and is likely to be misunderstood as a headline interest-rate-risk measure.
Commercial sensitivity	Several of the proposed disclosures require entities to reveal commercially sensitive information regarding portfolio construction, hedging strategies, behavioural assumptions, management actions and other aspects of proprietary risk management practices.	The IASB should therefore reassess whether the transparency benefits of these requirements justify the potential commercial harm and should limit disclosures to information that is necessary for users to understand the accounting effects of RMA.

Please see the document “WG11 – Disclosure Requirements Impact Assessment” in Appendix 2 for further details.

Additional topics

Following the Expert Group assessment, additional observations were received on topics that were not considered in detail during that phase. These observations included whether the proposed model adequately accommodates portfolios managed on a gross basis. They also included whether the disclosure requirements for entities eligible for RMA, but choosing not to apply it, are proportionate to the benefits provided. Further observations concerned linking the withdrawal of existing portfolio hedge accounting approaches to completion of a broader model. Such a model would need to address additional risks, products and reporting entities beyond banking-book interest rate risk.

These observations do not affect the overall conclusions in this letter. However, they merit further consideration by the IASB in any future development of the model.

Conclusion and requested direction

Taken as a package, the current proposals in the RMA Exposure Draft do not yet meet the expanded objective. In particular, they do not yet demonstrate that RMA will materially mitigate artificial accounting volatility, operate reliably and provide coherent and useful disclosures. Consequently, the proposals do not yet provide an effective and operationally feasible replacement for existing portfolio hedge accounting.

We kindly request that the IASB addresses all of the following:

- strengthen the RMA objective to align accounting with risk management to the extent that artificial accounting volatility is mitigated, while ensuring that the model is operationally viable;
- improve the scope of the model to completely align with risk management practices;
- reconsider the interlinkages between the model components and address the mechanics as a package;
- remove the RMA excess test and introduce a proper backstop;
- address the artificial effects of over-hedging limitations and the lower-of test;
- reconsider the requirement for benchmark derivatives to start at a fair value of zero and consider a pull-to-par approach;
- clarify the treatment of non-linear instruments and related risk management activities;
- ensure that normal portfolio and risk management changes do not automatically trigger discontinuation;
- reassess the proposed disclosures in light of their usefulness and potential commercial sensitivity, limiting them to information necessary for users to understand the accounting effects of RMA; and
- issue a re-exposure document.

Withdrawal of IAS 39 and contingency planning

Withdrawal of IAS 39 should be considered only once a replacement has been demonstrated to reduce artificial accounting volatility, operate reliably in practice and provide a meaningful improvement over existing requirements. The Exposure Draft has not yet met that threshold. Any implementation pathway should require the replacement model to be validated before existing portfolio hedge accounting is withdrawn.

Alternative approaches for consideration

If a viable RMA model cannot be achieved, alternative approaches should be explored. We respectfully list here alternatives which could be considered for selection and further development, without indicating an order of preference.

- Incorporation of the principles of IAS39 (EU endorsed) within IFRS9.
- Incorporation of the principles of IAS39 (EU endorsed) + additional hedged items within IFRS9.
- A direct business model alignment for accounting for IRRBB derivatives termed as "Held for Hedging".
- Assist users in understanding the results by judiciously improving current disclosures.

Closing remarks

We have sought to provide a balanced, evidence-based and practical perspective, grounded in the experience of preparers. We remain committed to constructive engagement in further development of the model.

We also note the broader public interest dimension of portfolio hedge accounting. A robust and operable solution supports the efficient use of interest rate derivatives, enabling banks to continue offering customers banking products and risk management solutions that meet their financing needs while managing interest rate risk in a prudent manner.

The views expressed reflect a carefully balanced position developed across participating institutions, seeking to provide a clear message while recognising the diversity of perspectives within the European banking sector.

Yours faithfully,



Gonzalo Gasos
EBF Senior Director Prudential
Policy and Supervision



Ricardo Sanchez
EBF Accounting Committee
Chair



Suresh Chadda
EBF Hedge Accounting Expert
Group Chair

Structure of Supporting Material

Appendix 1: Responses to EFRAG questions

Appendix 2: Supporting technical analysis in the form of Accounting Interpretation Papers

1. **WG1 – Changes in Risk Management Strategy, Discontinuance and Restart of RMA and RMA Cycle Accounting Entries**
Assesses when RMA should be discontinued or restarted following changes in risk management strategy or portfolio composition. Concludes that normal portfolio and risk management changes should not automatically trigger discontinuation.
2. **WG2 – RMA Excess**
Evaluates the proposed RMA Excess mechanism and concludes that it is structurally flawed. Recommends redesign or removal of the excess test to avoid unintended accounting outcomes.
3. **WG3 – Cumulative Lower Of**
Analyses the cumulative lower-of mechanism and its impact on accounting outcomes. Identifies situations where the approach creates distortions that do not reflect economic risk management.
4. **WG3 – Transition Benchmark Derivative Initial Fair Value of Zero**
Examines the requirement to use benchmark derivatives with an initial fair value of zero when transitioning into RMA. Highlights operational complexity and unintended accounting consequences.
5. **WG4 – RMA Cycle Run Frequency**
Assesses the frequency with which the RMA process should be run and updated. Concludes that the model is workable if the operational requirements are clarified and practical.
6. **WG5 – Equity Model Book**
Examines the treatment of equity within interest rate risk management and accounting. Explores how equity modelling approaches can be reflected more faithfully within RMA.
7. **WG5 – Risk Measure per Time Bucket**
Evaluates the use of risk measures within individual repricing buckets. Concludes that entities should not be restricted to a single risk measure where risk management uses multiple measures.
8. **WG6 – Interaction IFRS and RMA**
Analyses the interaction between existing IFRS requirements and the proposed RMA model. Identifies areas where inconsistencies may arise and clarifications are required.
9. **WG7 – Intra Group Application of RMA**
Examines the use of RMA within group structures and internal transactions. Concludes that the model should better accommodate intra-group risk management arrangements.

10. WG8 – Non-linear Risk RMA

Assesses how the model deals with options and other non-linear risk positions. Recommends clarifications to ensure that non-linear risk management strategies can be represented appropriately.

11. WG9 – Over-hedge vs Under-hedge within Limits and Optimisation Strategy

Demonstrates that the distinction between over-hedges and under-hedges at bucket level is inconsistent with IRRBB risk management. Concludes that these restrictions create artificial volatility and should be removed.

12. WG10 – Unexpected Changes

Examines the treatment of unexpected changes in exposures, assumptions and risk positions. Concludes that the proposed treatment may generate accounting results that do not reflect actual risk management.

13. WG11 – Disclosure Requirements Impact Assessment

Evaluates the proposed disclosure requirements from both preparer and user perspectives. Concludes that some disclosures may reveal commercially sensitive information without providing proportionate benefits.