

# Technical Accounting Alert

## Accounting for Hedge Transactions

### Overview

The conditions for hedge accounting under AASB 139 Financial Instruments: Recognition and Measurement are onerous and can be separated into:

- Documentation requirements
- Effectiveness monitoring.

Given that many entities are unable to satisfy these conditions, this brief has been compiled to illustrate the journals required to accounting for hedge derivatives where hedge accounting has not been applied.

### Relevant accounting standards

- AASB 121: The Effects of Changes in Foreign Exchange Rates
- AASB 132: Financial Instruments: Presentation
- AASB 139: Financial Instruments: Recognition and Measurement

### Accounting Treatment

The theme of this standard is to recognise all financial instruments on the balance sheet and ensure that these items are recognised at fair value at reporting dates.

In order to describe the accounting treatment, an example has been used:

### Facts

- Sale was made on 30 November 2008 of US\$150,000, cash expected to be received on 31 January 2009
- Spot rate at 30 November 2008 = 0.75
- Forward contract taken out on 30 November 2008 for US\$150,000 @ 0.76 expiring on 31 January 2009
- Spot rate at balance date 31 December 2008 = 0.77
- Fair value of forward contract at balance date = 0.78
- Spot rate at 31 January 2009 = 0.79

### Journals

#### *Inception date*

- Dr: Hedge debtor 197,368
- Cr: Hedge creditor 197,368

Being the fair value of the hedge at inception date (i.e. 150,000 / 0.76).

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- Dr: Trade receivable 200,000
- Cr: Revenue 200,000

Being the sale recorded at the spot rate (i.e. 150,000 / 0.75)

*Year end*

- Dr: Income statement – Foreign Exchange Loss 5,195
- Cr: Trade receivable 5,195

Being the revaluation of the trade receivable to year end spot rate (i.e. 200,000 – (150,000 / 0.77))

- Dr: Hedge creditor 5,060
- Cr: Income statement – Foreign Exchange Gain 5,060

Being the revaluation of the hedge creditor to the fair value of the contract at the year end (i.e. 197.368 – (150,000 / 0.78))

*Settlement*

- Dr: Cash 189,873
- Dr: Income statement – Foreign Exchange Loss 4,932
- Cr: Trade receivable 194,805

Being the recognition of cash received from customer, clearing of trade receivable and resulting foreign exchange loss (i.e. 150,000 / 0.79)

- Dr: Hedge creditor 2,435
- Cr: Income statement – Foreign Exchange Gain 2,435

Being the revaluation to fair value of the hedge derivative at settlement date (i.e. 192,308 – (150,000 / 0.79))

- Dr: Hedge creditor 189,873
- Cr: Cash 189,873

Being the amount required to pay to the bank (i.e. 150,000 / 0.79) and clearing the hedge creditor.

- Dr: Cash 197,368
- Cr: Hedge debtor 197,368

Being the amount received from the bank which was fixed at the inception date.

AASB 132 allows the offset of financial instruments under the following conditions:

“42. A financial asset and a financial liability shall be offset and the net amount presented in the balance sheet when, and only when, an entity:

- (a) currently has a legally enforceable right to set off the recognised amounts; and
- (b) intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously.”

It is therefore likely that the hedge debtor and hedge creditor can be offset in the balance sheet.

**Assumptions/Limitations**

- The conditions for hedge accounting have not been satisfied.

**FURTHER INFORMATION**

For further information on any of the information included in this TA alert, please contact your local Grant Thornton Australia representative or a member of the National Audit Support team at [NAS@grantthornton.com.au](mailto:NAS@grantthornton.com.au)