

November 19th, 2025

Ms. Hillary Salo
Chair of the Emerging Issues Task Force
Financial Accounting Standards Board
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EITF Agenda Request – Application of the Spot Method of Net Investment Hedging

Dear Ms. Salo:

The International Swaps and Derivatives Association's ("ISDA")¹ North American Accounting Committee (the "Committee") requests the Emerging Issues Task Force ("EITF") to add a project to its agenda to clarify that FASB Accounting Standards Codification ("ASC") Topic 815, *Derivatives and Hedging* does not preclude certain hedges of net investments in foreign operations from being eligible to be assessed for hedge effectiveness based on changes in spot exchange rates (i.e., the "spot method").

Specifically, under ASC 815-35-35-5, a hedging relationship is considered to be perfectly effective and no quantitative assessment of hedge effectiveness is required at hedge inception if certain conditions are met :

The change in the fair value of the derivative instrument attributable to changes in the difference between the forward rate and spot rate would be excluded from the assessment of hedge effectiveness if all of the following conditions are met:

- a. The notional amount of the derivative instrument designated as a hedge of a net investment in a foreign operation matches (that is, equals) the portion of the net investment designated as being hedged.*

¹ Since 1985, ISDA has worked to make the global derivatives markets safer and more efficient. Today, ISDA has over 990 member institutions from 78 countries. These members comprise a broad range of derivatives market participants, including corporations, investment managers, government and supranational entities, insurance companies, energy and commodities firms, and international and regional banks. In addition to market participants, members also include key components of the derivatives market infrastructure, such as exchanges, intermediaries, clearing houses and repositories, as well as law firms, accounting firms and other service providers. Information about ISDA and its activities is available on the Association's website: www.isda.org. Follow us on [Twitter](#), [LinkedIn](#), [Facebook](#) and [YouTube](#).

- b. *The derivative instrument's underlying exchange rate is the exchange rate between the functional currency of the hedged net investment and the investor's functional currency.*
- c. *When the hedging derivative instrument is a cross-currency interest rate swap, it is eligible for designation in a net investment hedge in accordance with paragraph [815-20-25-67](#).*

In that circumstance, the hedging relationship would be considered perfectly effective, and no quantitative effectiveness assessment is required at hedge inception. (See paragraph [815-20-25-3\(b\)\(2\)\(iv\)\(01\)](#).)

The above guidance implies, but does not explicitly state, that the difference between the forward rate and spot rate (or interest rate differential) may be excluded from the assessment of hedge effectiveness only when a hedge relationship is perfectly effective.

ASC 815-35-35-9 enumerates three conditions whereby a hedge of a net investment in a foreign operation *would not* be considered to be perfectly effective. In that circumstance, ASC 815-35-35-10 requires entities to perform a quantitative assessment of hedge effectiveness by comparing the change in fair value of the hypothetically perfect derivative instrument and the change in fair value of the actual derivative instrument. ASC 815-35-35-9 and 35-10 state:

35-9 The hedging relationship would not be considered perfectly effective, and the guidance in paragraph 815-35-35-10 shall be applied if any of the following conditions exist:

- a. *The notional amount of the derivative instrument does not match the portion of the net investment designated as being hedged.*
- b. ***The derivative instrument's underlying exchange rate is not the exchange rate between the functional currency of the hedged net investment and the investor's functional currency.***
- c. *When the hedging derivative instrument is a cross-currency interest rate swap eligible for designation in a net investment hedge in accordance with paragraph 815-20-25-67, both legs are not based on comparable interest rate curves (for example, pay foreign currency based on the three-month London Interbank Offered Rate [LIBOR], receive functional currency based on three-month commercial paper rates).*

*35-10 If any of the conditions in paragraph 815-35-35-9 exist, the change in fair value of the hypothetical derivative instrument that does not incorporate those differences shall be compared with the **change in fair value** of the actual derivative instrument in assessing hedge effectiveness.*

The Committee has observed an emerging practice issue associated with certain net investment hedge strategies that involve the use of derivatives that do not meet the three criteria in ASC 815-35-35-5.

Specifically, companies seeking to hedge their net investments in Chinese Renminbi (“CNY”)-functional currency operations are effectively required to use a hedging instrument denominated in China-Hong Kong (“CNH”). This is because CNY is the onshore currency used within mainland China, while CNH is a highly correlated offshore proxy currency used for international trade and investment transactions outside of mainland China, including derivative transactions.

Certain practitioners have concluded that this difference between onshore CHY exposures and offshore CNH derivatives denotes a derivative with an “underlying exchange rate not the same as the exchange rate between the functional currency of the hedged net investment and the investor’s functional currency”.

As a result, these practitioners have concluded that paragraph 815-35-35-10 effectively requires the hedging entity to assess hedge effectiveness using the hypothetical derivative method and precludes the ability to apply the spot method (that is, recognize the excluded spot-forward difference or interest rate differential in earnings), even if the hedge is deemed highly effective.

In the Committee’s view, ASC 815-35-35-5 creates unnecessary ambiguity that may be eliminated by amending that paragraph to distinguish between the implications of an imperfect hedge on the assessment of hedge effectiveness versus the recognition of hedge results under the spot method when a hedge is deemed to be highly effective. The Committee requests the EITF to amend ASC 815-35-35-5 as such to clarify that reporting entities would be permitted to apply the spot method and recognize excluded components in earnings in accordance with 815-35-35-5A or 35-5B, as long as the hedge is highly effective.

Additionally, ASC 815-35-35-9 and 35-10 retained the guidance in ASC 815-35 prior to the issuance of Accounting Standards Update (“ASU”) 2017-12—*Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities* that requires a comparison of changes in the fair value of the hedging instrument designated under the spot method when there is any mismatch between the actual hedge and the hypothetically perfect hedging derivative, even though the portion of the hedge gain or loss “included” in the assessment of hedge effectiveness pertains solely to spot foreign currency movements (refer to ASC 815-35-35-8). We believe the retention of the phrase “fair value” in ASC 815-35-35-9 and 35-10 was unintentional post the issuance of ASC 2017-12 and request the EITF amend existing guidance in ASC Topic 815 replace this language with “value of the included component”.

The practice issue we have highlighted herein affects all multinational companies that hedge their net investments in foreign subsidiaries that have a functional currency that:

- is not readily accessible to hedge by the reporting entity or its affiliates, such as those subject to currency controls or onshore restrictions,
- trades in less liquid markets, or
- trades “in tandem” with the currency denomination of the hedging instrument (as contemplated in ASC 815-20-25-33 and ASC 815-35-35-19)

While this issue has existed since the effective date of ASU 2017-12, its relevance to reporting entities has become more prominent in the wake of increased geopolitical risk and trade policy shifts, both of which have catalyzed companies to increase the scope of foreign currency hedging.

The Committee would greatly appreciate the EITF’s willingness to consider our agenda request and welcomes the opportunity to share additional perspectives on the matters discussed herein. Should you have any questions concerning this request, please contact the undersigned.

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