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FAS 133 Overview

In June 1998, the Financial Accounting Standards Board (FASB) released FAS 133: Accounting for Derivative Instruments and Hedging Activities. FAS 133 requires that all derivatives be recognized as assets or liabilities on the balance sheet and be measured and reported at fair value.

General Accounting Treatment

The general accounting treatment of a derivative depends upon its use. Derivatives use falls into one of 4 main categories:

- Not used for hedging purposes;
- Hedging changes in the fair value of an asset or liability;
- Hedging exposure to forecasted cash flows; and,
- Hedging foreign currency exposures.

Not Designated as a Hedge

Derivative gains and losses are marked to market and are realized in current period earnings.

Fair Value Hedges

Derivative gains and losses, together with the offsetting gains and losses of the hedged item, are reflected in current period income. The net result is that reported earnings reflect only the extent to which the hedge is not effective.

Cash Flow Hedges

The effective portion of derivative gains/losses initially reported in other comprehensive income (OCI) and then reclassified into earnings when the forecasted cash flows affect earnings. Ineffective derivative gain/loss is immediately reported in earnings.

Foreign Currency Hedges

Gains and losses are reported in OCI with cumulative currency translation adjustments.

FAS 133 applies to all entities. In order to elect hedge accounting treatment, you are required to establish at the inception of the hedge the method to be used for assessing hedge effectiveness and the measurement approach to determine the ineffective amount of the hedge. All methods must be consistent with your risk management approach.

Wondering how these rules apply to you? Call us today for a free analysis and consultation at 1.800.971.1378, We'll help you understand these complex standards and then advise you on the right approach for your financial situation — ultimately helping you maximize your financial potential.