

## **Attachment HE-10 - TAB 7 Part 16 & Supplemental Item 7b: GASBS No. 53, *Accounting and Financial Reporting for Derivative Instruments***

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### **Purpose**

The purpose of GASBS No. 53 is to provide financial reporting standards for derivative instruments. GASBS No. 59, *Financial Instruments Omnibus*, GASBS No. 64, *Derivative Instruments: Application of Hedge Accounting Termination Provisions*, and GASBS No. 72, *Fair Value Measurement and Application*, include amendments to GASBS No. 53. Any reference to GASBS No. 53 in this document is referring to GASBS No. 53 as amended by GASBS No. 59, GASBS No. 64, and GASBS No. 72. Per GASBS No. 53 paragraph 19 the classification of derivative instruments depends on whether they represent an asset or liability and should be reported on the statement of net position.

According to current generally accepted accounting principles, derivative instruments should be measured at fair value, except for fully benefit-responsive synthetic guaranteed investment contracts (SGICs). Changes in the fair value of investment derivative instruments, including derivative instruments that are determined to be an ineffective hedge, should be reported on the investment revenue line item. Changes in fair value of hedging derivative instruments (effective hedge) should be reported on either the deferred inflows of resources or deferred outflows of resources line items on the statement of net position. GASBS No. 53 paragraphs 67 and 79 provide guidance on the reporting and disclosures for SGICs.

This document is provided for informational purposes and is not authoritative. HEIs must refer to GASBS No. 53 for reporting requirements. In addition, the Implementation Guide No. 2015-1 and Implementation Guide No. 2016-1 include information on this statement.

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### **Applicability**

Higher Education Institutions (HEIs) are required to properly report any activity/balances related to this statement in their individually published financial statements as well as the financial statement template.

Attachment HE-10, Financial Statement Template, TAB 7 Part 16 is for HEIs to answer certain questions regarding this GASB statement.

Supplemental Item 7b is for HEIs that have derivative instrument activity/balances during and/or as of June 30, 2017, to provide additional information/disclosures. This Supplemental Item 7b is an Excel file available on DOA's website after the Attachment HE-10.

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**Definitions**

Per GASBS No. 53 paragraph 7, a derivative instrument is defined as a financial instrument or other contract that has the following characteristics:

- Settlement factors
- Leverage
- Net settlement

GASBS No. 53 paragraphs 9 through 13\* provide additional information on these characteristics. GASBS No. 53 paragraphs 63 to 66\* provide additional information regarding a derivative instrument that is embedded in a financial instrument or contract.

Note\*: GASBS No. 59 includes amendments to paragraphs 13 and 64.

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**Not applicable**

Per GASBS No. 53 paragraphs 14 through 18\*\* this statement **does not apply to the following**:

- 1) Normal purchases and normal sales contracts
- 2) Insurance contracts
- 3) Certain financial guarantee contracts
- 4) Certain contracts that are not exchange-traded

Refer to GASBS No. 53 for information regarding the scope and applicability of this statement.

Note \*\*: GASBS No. 59 includes amendments to paragraphs 16 & 17.

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**Overall  
derivative  
instrument  
categories**

The following are overall categories of derivative instruments referred to in Attachment HE-10 – TAB 7 Part 16:

- Hedging derivative instrument – effective hedge
  - Investment derivative instrument – ineffective hedge
  - Investment derivative instrument – a) held primarily for the purpose of income or profit, and b) has a present service capacity based solely on its ability to generate cash or to be sold to generate cash
  - Fully benefit-responsive SGICs
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**Hedging  
derivative  
instrument –  
effective hedge**

Per GASBS No. 53, a hedging derivative instrument is a derivative instrument that is associated with a hedgeable item and significantly reduces an identified financial risk by substantially offsetting changes in cash flows or fair values of the hedgeable item (see GASBS No. 53 paragraphs 28 to 30 for additional information on hedgeable items). Per GASBS No. 53 paragraph 27, a hedging derivative instrument exists if both of the following criteria are met:

- The derivative instrument is associated with a hedgeable item.
- The potential hedging derivative instrument is effective in significantly reducing the identified financial risk.

This overall category of derivative instruments will be referred in the Attachment HE-10 – TAB 7 Part 16 as a hedging derivative instrument – effective hedge.

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**Potential  
hedging  
derivative  
instrument**

A potential hedging derivative instrument represents a derivative instrument that is associated with a hedgeable item prior to the determination of whether the derivative instrument is effective in significantly reducing the identified financial risk.

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**Effectiveness  
evaluation  
method**

A potential hedging derivative instrument must be evaluated to determine if it is a hedging derivative instrument – effective hedge **or** an investment derivative instrument – ineffective hedge at the end of a reporting period. GASBS No. 53 paragraphs 31 to 62 provide guidance on evaluating the effectiveness of a potential hedging derivative instrument. Some effectiveness evaluation methods are as follows:

- Consistent critical terms method
- Synthetic instrument method\*
- Dollar offset method\*
- Regression analysis method\*

Note\*: These represent quantitative methods. Per GASBS No. 53 paragraph 48 other quantitative methods may be used if they meet certain criteria.

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**Effectiveness  
evaluation  
method,  
*continued***

**First reporting period:** GASBS No. 53 paragraph 31a states that if an institution uses the consistent critical terms method in the first reporting period and the potential hedging derivative instrument does not meet the effectiveness criteria, it must be evaluated using at least one quantitative method before concluding that it is ineffective. If a potential hedging derivative instrument is first evaluated using a quantitative method and does not meet the criteria for effectiveness, it may be evaluated using another quantitative method(s) before concluding that it is ineffective. If the potential hedging derivative instrument is determined to be effective, it is considered a hedging derivative instrument – effective hedge and in future years it must be re-evaluated to determine effectiveness. If the potential hedging derivative instrument is determined to be an ineffective hedge, it is considered an investment derivative instrument – ineffective hedge and will not have to be reevaluated for effectiveness in future years.

**Second reporting period:** Per GASBS No. 53 paragraph 31b, a hedging derivative instrument – effective hedge as of the end of the prior reporting period must be re-evaluated at the end of the current reporting period using the same method that was applied in the prior reporting period. If it is determined that the prior year’s hedging derivative instrument – effective hedge is no longer effective as of the end of the current reporting period, the institution may apply another method(s) before concluding that the hedging derivative instrument is no longer effective.

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**Financial  
statement  
template line  
items**

Below is some general guidance on the reporting of derivative instruments on the financial statement template (FST) for the HEI:

**Derivative Instrument** – If the FST does not have a line item that properly classifies the derivative instrument, report the derivative instrument on the “Other Assets” or “Other Liabilities” FST line item and provide a description of the derivative instrument on the applicable Attachment HE-10 TAB 7 Parts 9a or 10a.

**Changes in fair values: Hedging derivative instrument – effective hedge:** The “Deferred Outflows of Resources” or “Deferred Inflows of Resources” FST line items are to report the change in fair values for derivative instruments that are an effective hedge.

**Changes in fair values: Investment derivative instrument – ineffective hedge & investment derivative instrument – a) held primarily for the purpose of income or profit, and b) has a present service capacity based solely on its ability to generate cash or to be sold to generate cash:** These changes in fair values should be reported on the “Investment Earnings” FST line item.

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**TAB 7  
Part 16**

**Derivative instruments:** Attachment HE-10 – TAB 7 Part 16 is to determine whether the HEI had derivative activity/balances to be reported.

Overall Derivative Instrument Categories:

- Hedging derivative instrument – effective hedge
- Investment derivative instrument – ineffective hedge
- Investment derivative instrument – a) held primarily for the purpose of income or profit, and b) has a present service capacity based solely on its ability to generate cash or to be sold to generate cash
- Fully benefit-responsive synthetic guaranteed investment contracts (SGICs)

Note: If “yes” to Part 16, Supplemental Information Item 7b must also be completed and submitted along with the Attachment HE-10 submission.

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**Supplemental  
information 7b-  
derivative  
instruments as  
of June 30,  
2017**

**Supplemental Information Item 7b is to provide more detailed information/disclosures on the derivative instruments that existed as of June 30, 2017, and/or activity during fiscal year 2017.**

**Part 1a** is to provide information on the following categories of derivative instruments: **hedging derivative instrument – effective hedge, investment derivative instrument – ineffective hedge, and/or investment derivative instrument – a) held primarily for the purpose of income or profit, and b) has a present service capacity based solely on its ability to generate cash or to be sold to generate cash.**

The FST line item for the FY 2017 change in fair value for the following categories should be “**Investment Earnings**”:

- Investment derivative instrument – ineffective hedge and/or
- Investment derivative instrument – a) held primarily for the purpose of income or profit, and b) has a present service capacity based solely on its ability to generate cash or to be sold to generate cash.

The FST line item for the FY 2017 change in fair value for the following category should be the applicable “**Deferred Inflows of Resources**” or “**Deferred Outflows of Resources**” FST line items:

- Hedging derivative instruments – effective hedges.

**Parts 1b and 1c** are to indicate if the HEI has a **fully benefit-responsive synthetic guaranteed investment contract (SGIC)** as of June 30, 2017, and to confirm that the SGIC was reported in accordance with GASBS No. 53 which states the combination of the underlying investments and the wrap contract should be reported at contract value. Also, footnote disclosures must be provided.

**Part 1d** is to indicate if there are any **contingent features** included in any derivative instrument as of June 30, 2017, and to provide disclosures of the contingent features.

**Part 1e** is to indicate if any derivative instrument as of June 30, 2017, is part of a **hybrid instrument (embedded derivative instrument and a companion instrument)** and to provide a description of the companion instrument.

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**Supplemental information 7b- hedging derivative instruments – effective hedge**

**Parts 1f, 1g, 1h, 1i** are to provide the information on **hedging derivative instruments – effective hedge** that existed as of June 30, 2017, to identify what types of risks the HEI is exposed to that could give rise to financial loss, and to provide disclosures as required by GASBS No. 53.

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**Supplemental information 7b- investment derivative instruments**

**Part 1j:** For **investment derivative instruments (ineffective hedge or a) held primarily for the purpose of income or profit, and b) has a present service capacity based solely on its ability to generate cash or to be sold to generate cash)** identify what types of risks as of June 30, 2017, the HEI is exposed to that could give rise to financial loss and provide disclosures as required by GASBS No. 53.

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**Supplemental information 7b- termination of hedge accounting**

**Part 2:** This part is to indicate if the HEI had hedging derivative instrument – effective hedge as of June 30, 2016, and there was a **termination of hedge accounting during FY 2017**. If there was a termination of hedge accounting during FY 2017, a description of the termination event, the deferral amount, and how the amount was reported on the financial statement template must be provided.

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**Supplemental information 7b- derivative instruments – other activity**

**Part 3:** This part is to indicate if the HEI had any **other derivative instrument activity during FY 2017** not already provided in the previous parts and to provide a description of the other activity.

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**Supplemental information 7b- Hedged debt tab**

The **Hedged debt** tab is to provide the future principal and interest payments on the hedged debt as well as the hedging derivative instrument’s net cash flows as required by GASBS No. 53 paragraph 74. This tab is also to provide a description and principal amount of the hedged debt.

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**Supplemental information 7b- CAFR footnote tabs**

**UVA CAFR footnote, VCU CAFR footnote, and VCUHSA CAFR footnote** tabs have been added with prior year CAFR footnote wording to be updated for the current year.

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