

This paper has been prepared by the EFRAG Secretariat for discussion at a public meeting of EFRAG TEG. The paper forms part of an early stage of the development of a potential EFRAG position. Consequently, the paper does not represent the official views of EFRAG or any individual member of the EFRAG Board or EFRAG TEG. The paper is made available to enable the public to follow the discussions in the meeting. Tentative decisions are made in public and reported in the EFRAG Update. EFRAG positions, as approved by the EFRAG Board, are published as comment letters, discussion or position papers, or in any other form considered appropriate in the circumstances.

Interest Rate Benchmark Reform – Phase 2

Cover Note

Background and objective

- 1 The comment period on the ED IBOR Phase 2 ended the 25 May. The IASB has planned two Board meetings (June and July) to finalize the Amendments.
- 2 The objective of this session is to identify, if any, any material issue that needs to be considered in preparation of the DEA, on the basis of the IASB staff analysis and tentative decisions of the IASB during the IASB June meeting and on the basis of how the IASB will likely finalise the proposals in the Exposure Draft ED/2020/1 on IBOR Phase 2.
- 3 This paper has been prepared on the basis of the IASB Staff Papers. The EFRAG Secretariat will provide an oral summary of the IASB's tentative decisions during this session.

Comments by FIWG members

- 4 The proposals in the IASB agenda papers were discussed at EFRAG FIWG on 22 June 2020:
 - (a) FIWG members appreciated that many issues addressed in EFRAG's comment letter were covered, e.g. relocation of the modifications guidance or responding to the concerns expressed by EFRAG on disclosures. In general, the suggestions from the IASB staff were perceived as being balanced.
 - (b) While the IASB staff did not recommend changes to few issues raised such as historical fallback rates, EFRAG FIWG members observed that these issues are not to be considered as a blocking factor for the endorsement advice. The priority is to get the core proposals endorsed as soon as possible.
 - (c) Against this background, FIWG members concluded that, based on the proposals of the IASB staff in the IASB agenda papers, no major obstacles were identified that would outweigh the benefits from the IBOR amendments in general.

Endorsement plan

- 5 Considering the urgency of these amendments, which are needed at the latest in time for the approval of 2020 accounts, EFRAG has been requested to issue the FEA by the 15 September 2020, in order to allow for the fastest possible legislative approval process. The following table shows the proposed endorsement plan.

22 July 2020	Joint TEG and FIWG drafting session on the DEA (closed session)
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28 July	EFRAG Board will be updated on the outcome of the joint TEG/FIWG session and, if appropriate, provide drafting inputs
24 August	Two separate sessions of EFRAG TEG (morning) and EFRAG Board (afternoon) to approve the DEA subject to non-significant drafting changes.
End of August	IASB will issue the final amendments. EC will send to EFRAG the letter requesting the endorsement. EFRAG will issue the DEA.
7 September	End of comment period for the DEA. EFRAG will host a public outreach event (webcast) to collect inputs on the DEA.
14 September	Two separate sessions of EFRAG TEG (morning) and EFRAG Board (afternoon) to approve the FEA.
15 September	EFRAG will issue the FEA.

Key contents of the IASB Agenda papers

Modifications (IASB Agenda Paper 14A):

- 6 The IASB Staff recommends that the IASB make no substantial changes to the proposals in the Exposure Draft related to modifications of financial assets and financial liabilities. However, the IASB staff have identified some drafting suggestions that the IASB Staff will consider when preparing the final amendments (if the IASB decides to proceed).
- 7 Subject to the IASB approval and final drafting of the amendments, EFRAG Secretariat observes that the IASB Staff's proposals correspond to the suggestions raised in EFRAG's comment letter on:
 - (a) relocating the paragraphs on modifications to section 5.4 (paragraph 5 of EFRAG's comment letter);
 - (b) clarifying the term "required" (paragraph 9 of EFRAG's comment letter);
 - (c) reconsidering the wording used in BC25 of the ED (paragraph 11 of EFRAG's comment letter);
 - (d) reconsidering the wording used in BC35 of the ED (paragraph 16 of EFRAG's comment letter)
- 8 EFRAG Secretariat observes that the IASB Staff is not proposing to reflect in the final amendments the suggestions on historical fallback rates (paragraph 15 of EFRAG's comment letter). Preliminary feedback from FIWG members indicate that while not ideal, this is not seen as an obstacle for the endorsement.

Amendments to hedging relationships (IASB Agenda Paper 14B):

- 9 The IASB staff is not recommending any substantial changes to the amendments proposed in the Exposure Draft that would require an entity to amend the formal designation of a hedging relationship to incorporate the changes required as a result of the reform. However, the IASB Staff is recommending the following minor drafting changes to the proposed amendments in paragraphs 6.9.7–6.9.10 of IFRS 9 and 102O–102R of IAS 39:
- (a) refer to the examples of modifications required by the reform (in proposed paragraph 6.9.4(a)–(d)) as part of the changes required to the hedging relationship;
 - (b) include the designated hedged portion as a required change to the hedged item; and
 - (c) clarify that entities must make the changes to hedging relationships by the end of the reporting period during which uncertainty with respect to a specific element of the relationship has been resolved.
- 10 EFRAG Secretariat observes that the proposed changes would not counteract EFRAG’s previous conclusions on amendments to hedging relationships and instead would be helpful to clarify application of the amendments in practice.

Designation of risk components (IASB Agenda Paper 14D):

- 11 The IASB staff recommends finalising the proposals in the Exposure Draft, subject to clarifying that the 24-month period applies to the individual alternative benchmark rate and hence, begins from the date that an entity designates a particular alternative benchmark rate as the hedged risk for the first time.
- 12 EFRAG Secretariat observes that the IASB staff has considered the comments in EFRAG’s comment letter (paragraph 37 and 39) on introducing application guidance in the Basis for Conclusions that goes beyond IBOR-related issues. The IASB staff clarified that the intention was not for the proposed amendments to be interpreted as changing the current requirements in IFRS 9 or IAS 39 in this regard.
- 13 EFRAG Secretariat further observes that the comment in EFRAG’s comment letter (paragraph 40) to continue monitoring the future developments of alternative rate markets considering feedback was considered by the IASB staff after receiving current feedback on transition from parties involved in the transition process.
- 14 EFRAG Secretariat observes that the clarification proposed to the wording used in the Basis for Conclusions (EFRAG comment letter, paragraph 36) was not addressed in the IASB’s agenda paper.

Effective date and transition (IASB Agenda Paper 14E):

- 15 The IASB Staff recommends that the IASB finalises the effective date and transition requirements proposed in the Exposure Draft with one change as follows (underlined text indicates the change):

An entity would reinstate a discontinued hedging relationship if and only if:

(a) the entity discontinued that hedging relationship solely due to changes required by interest rate benchmark reform and, therefore, the entity would not have been required to discontinue that hedging relationship if the amendments had been applied at that time; and

(b) at the date of initial application of the amendments, that discontinued hedging relationship:

(i) still meets the risk management objective on the basis of which it qualified for hedge accounting (ie the entity still pursues the risk management objective for that hedging relationship); and

(ii) continues to meet all other qualifying criteria (after taking into account the amendments).

- 16 EFRAG Secretariat notes that the IASB Staff's recommendation relates to an issue previously discussed by EFRAG TEG during the March 2020 meeting (AP 06-03, Issue 1) and was deliberately not included in EFRAG's comment letter. EFRAG Secretariat observes that the proposed change would not counteract these previous conclusions and instead would be helpful to clarify application of the retrospective reinstatement in practice.

Modification/replacement of derivatives (IASB Agenda Paper 14F):

- 17 IASB staff recommends the IASB to clarify that, for the purpose of the changes required to a hedging instrument (as contemplated by proposed paragraphs 6.9.7(c) and 102O(c)), modifications required by the reform could be effected in ways other than modifying the contractual terms of the hedging instrument as long as the outcome is economically equivalent to modifying the hedging instrument to refer to an alternative benchmark rate.
- 18 EFRAG Secretariat observes that this is a new issue not addressed in the Exposure Draft. It was previously discussed by EFRAG TEG during the March 2020 meeting (AP 06-03, Issue 2) and, due to the conclusions reached, was deliberately not included in EFRAG's comment letter.
- 19 EFRAG Secretariat understands that the IASB staff's conclusions reached on replacement of derivatives correspond to the conclusions reached by EFRAG TEG during the March 2020 Meeting. A clarification as proposed by the IASB Staff could nevertheless be helpful to clarify application in practice.

Disclosures (IASB Agenda Paper 14G):

- 20 The IASB staff recommends that the IASB finalise the proposed disclosures in paragraphs 24I-24J of the Exposure Draft subject to the following two changes:
- (a) Amend paragraph 24J(b) to require disclosure of quantitative information¹ about non-derivative financial assets, non-derivative financial liabilities and derivatives (each shown separately) that, at the end of the reporting period, remain referenced to interest rate benchmarks subject to the reform. This information would be disaggregated by significant interest rate benchmark. For the purposes of this disclosure, an entity would choose the representative basis for disclosing the quantitative information and explain the basis applied in the financial statements.
 - (b) Delete the proposed disclosure in paragraph 24J(c) of the Exposure Draft.
- 21 Subject to IASB approval and final drafting of the amendments, EFRAG Secretariat observes that the IASB staff's proposals correspond to the suggestions raised in EFRAG's comment letter in paragraphs 47 and 50.
- 22 In addition, the IASB staff have clarified in the agenda paper that the proposed disclosures:
- (a) would not be applicable for the comparative period, which corresponds to the comment made in EFRAG's comment letter, paragraph 46;
 - (b) not meant to relate to hedge accounting only, which corresponds to the comment made in EFRAG's comment letter, paragraph 51.

Other comments (IASB Agenda Paper 14H):

- 23 The IASB Staff recommends no substantial changes to the proposed amendments in response to the issues discussed on this paper. However, the IASB Staff has identified some drafting suggestions which the IASB Staff will consider when drafting the final amendments.

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- 24 The EFRAG Secretariat observes that the conclusions reached by the IASB Staff on other comments would not counteract EFRAG's previous positions.
- 25 The IASB agenda papers can be downloaded (as an optional background reading) at the following [link](#).

Questions for EFRAG TEG

- 26 Does EFRAG TEG agree with the observations of FIWG as outlined in paragraph 4?
- 27 Does EFRAG TEG have further comments on the IASB's tentative decisions and on the endorsement plan?