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PIR IFRS 9 *Classification and Measurement* - Other matters raised in PIR feedback
Issues Paper

Objective

1 To obtain the EFRAG FR TEG members view on the IASB decisions in relation to the matters raised by respondents to the RFI on PIR *IFRS 9 - Classification and Measurement* that were not covered previously and on two application questions related to contractual cash flow characteristics of financial assets.

Information for EFRAG FR TEG

2 In its September meeting, the IASB considered six following matters raised in the feedback about how entities would apply requirements not specifically covered in the RFI on PIR *IFRS 9 - Classification and Measurement*:

(a) application of the derecognition requirements to financial assets;

(b) cash received via electronic transfer as settlement for a financial asset;

(c) contracts to buy or sell non-financial items;

(d) accounting for transaction costs on equity investments for which an entity has elected to present changes in fair value in other comprehensive income;

(e) financial assets and financial liabilities held for trading; and

(f) purchased or originated credit-impaired financial assets.

3 Where the topics related to specific application questions, the IASB staff have consulted ASAF members during their July 2022 meeting to determine whether any of these issues would meet the criteria for a financial reporting issue to be addressed by the IFRS IC, i.e.:

(a) is the matter widespread and expected to have a material effect; and

(b) is the matter sufficiently narrow in scope and can be resolved efficiently.

Description of the other matters raised in PIR feedback

(a) Derecognition of financial assets

4 A few respondents asked:

(a) to clarify which risks need to be considered when assessing whether 'substantially all risks and rewards' of a financial asset has been transferred;

(b) for more application guidance on assessing whether an entity has retained control over the financial asset (especially in the case of financial assets transferred to special purpose vehicles and in the case of complex risk-sharing and reverse factoring transactions); and

(c) for more guidance on accounting for an entity's 'continuing involvement' in a financial asset since IFRS 9 only provides illustrative examples for some specific forms of continuing involvement but does not clearly articulate general principles.

5 The IASB acknowledged that applying the IFRS 9 derecognition requirements for financial assets can be complex and involve significant judgement, especially when applied to structured transactions involving special purpose vehicles.

6 However, the IASB staff did not find any evidence that these issues were material or widespread and, therefore, concluded that the cost of standard-setting in this regard will outweigh the benefits. Therefore, the IASB decided **to take no further action on this matter.**

(b) Cash received via electronic transfer as settlement for a financial asset

7 A few respondents to the RFI referred to the discussion at the September 2021 meeting of the IFRS IC on Cash Received via Electronic Transfer as Settlement for a Financial Asset (IFRS 9 Financial Instruments). These respondents asked the IASB to consider the implications of the IFRS IC tentative agenda decision ('TAD') because in their view, the application of the requirements set out in this TAD will have significant impacts on long-standing and established practice and would therefore lead to significant operational challenges and costs to apply.

8 Having considered the IFRS IC discussions and respondents comments, the IASB decided to explore narrow-scope standard setting as part of PIR of IFRS 9. This issue is discussed in detail in the agenda paper 08-04 for this session.

(c) Contracts to buy and sell non-financial items ('own use exemption')

9 A few respondents to PIR:

(a) Mentioned practical challenges in applying the requirements in paragraphs 2.5(b) and 2.6 of IFRS 9 and asked for more guidance on what constitutes 'similar' contracts and what degree of past practice would invalidate the use of the 'own use exception' for future contracts.

(b) Asked for additional guidance with regards to the 'unit of account' in applying paragraphs 2.4–2.7 of IFRS 9 especially in case of 'oversized contracts' resulting from erratic energy supply. These respondents argued that recognising the entire contract as a derivative will not provide useful information to users.

(c) Asked for guidance on how to account for a change in management's intention for such a contract after initial recognition.

10 The IASB noted that the requirements relating to contracts to buy or sell non-financial items have been carried forward unchanged from IAS 39, acknowledged that some diversity in practice exists and more guidance could be helpful but as ASAF members did not consider these issues to be a priority, concluded that **no further action be taken on this as the matter is not widespread or expected to have a material effect.**

(d) Equity investments and OCI – transaction costs

11 A few respondents reported diversity in practice due to insufficient guidance on:

(a) the accounting for transaction costs on the disposal of equity instruments for which the entity has elected to present gains and losses in OCI (P&L vs OCI);

(b) the accounting for the difference between the fair value of the equity investment on the date of disposal and the transaction price.

12 The IASB considers that diversity in practice may result from the requirement in paragraph 3.2.12 of IFRS 9 that the difference between the carrying amount of a financial asset at the date of derecognition and the consideration received shall be recognised in profit or loss. This requirement was carried over unchanged from IAS 39, which did not have the option to present gains and losses on equity instruments through profit or loss without recycling these gains to profit or loss on disposal.

13 Some ASAF members confirmed that there is diversity in practice in their jurisdictions, but did not expect the matter to be widespread or have a material effect, therefore the IASB decided **not to take any further action on this issue**.

(e) Financial assets and financial liabilities held for trading

14 A respondent to the RFI asked for more guidance on the term held for trading in the following situations:

(a) structured liabilities issued by a bank to satisfy clients' investment needs, with limited repurchases by the bank to provide liquidity as a market maker; and

(b) a gradual reduction in an equity stake where the entity has the intention to sell the remaining stake (less than 20%) within the next 12 months.

15 The IASB analysed the existing requirements in IFRS 9 for the assets and liabilities held for trading and noted that financial assets and financial liabilities that are held-for-trading are a subset of those instruments measured at FVTPL.

16 The IASB also noted that it is clear that the definition of' held for trading' in Appendix A of IFRS 9 applies to financial assets and financial liabilities that are held with a specific trading purpose.

17 In addition, the IASB considered it important to distinguish financial assets and financial liabilities that are 'held for sale' applying IFRS 5 *Non-current Assets Held for Sale and Discontinued Operation* from financial instruments that are 'held for trading' in terms of IFRS 9.

18 As a result of this analysis the IASB concluded that IFRS 9 provides an adequate basis to determine whether a financial instrument is held for trading and decided **not to take a further action on these items.**

(f) Purchased or originated credit-impaired financial assets ('POCI')

19 A few respondents asked for more guidance on:

(a) accounting for POCI financial assets that arise because of the derecognition and re-recognition of an existing exposure due a substantial modification in contractual cash flows; and

(b) calculating the credit-adjusted EIR at the appropriate level of granularity in the case of purchasing a portfolio of consumer debt rather than individual exposures.

20 Respondents also raised conceptual questions on the presentation of movements in expected credit losses on POCI financial assets, especially in the case where there is an improvement in credit quality in excess of the entity's expectations at initial recognition.

21 As the requirements for POCI financial assets are closely related to the application of the impairment requirements in IFRS 9, the IASB decided **to consider them as part of the upcoming PIR on the impairment requirements.**

Application questions related to the contractual cash flow characteristics of financial assets

Contractual inflation adjustments and leverage

22 In some jurisdictions, it is common for the interest rate of financial instruments to be contractually linked to an index that adjusts for the time value of the money based on a market interest rate and/or inflation rate. Respondents questioned whether such adjustments introduce leverage in the context of recent significant rises in inflation rates.

23 In its April Agenda Paper 3A, the IASB staff expressed the view that contractual link to an unleveraged inflation index represents consideration for the time value of money on the principal amount outstanding and remains relevant regardless of the level of inflation.

24 The ASAF members were not aware about the widespread diversity in practice in this respect.

25 Therefore, the IASB decided **not to take any further action on this matter.**

Regulated interest rates and leverage

26 In some jurisdictions, financial instruments with regulated interest rates can include a leverage factor imposed by the government. Respondents asked whether such interest rates are regulated rates applying paragraph B4.1.9E of IFRS 9, and if so, how to consider whether the rate provides exposure to risks or variability in the contractual cash flows that are inconsistent with a basic lending arrangement applying the SPPI requirements in IFRS 9.

27 The IASB recognised that a diversity and practice exist and that impacts can be material in some jurisdictions. Therefore, the IASB consulted ASAF members, who responded that the issue only appears to be prevalent in specific countries such as Hungary. Therefore, the IASB believes that the application question does not meet the criteria for a submission to the IFRS IC and decided **not to take any further action on this matter.**

EFRAG FR TEG-CFSS discussion

28 EFRAG FR TEG-CFSS discussed the issues (a), (c) and (d) in paragraph 2 and the two application questions at the meeting on 28 June 2022 and provided the following comments.

(a) Derecognition of financial assets

29 Members noted that there is a diversity in practice in relation to the definition and accounting of the "continuing involvement". However, they do not believe that the IASB should prioritise this issue.

(c) Contracts to buy or sell non-financial items

30 Members noted that additional guidance is needed in relation to the accounting for these contracts when there is a change in management's intention for the contract. However, they do not believe that the IASB should prioritise this issue.

(d) Equity investments and OCI - accounting for transaction costs

31 Members were not aware of any kind of diversity in practice with a material effect with regards to the accounting for transactions costs on equity instruments for which the entity had chosen the OCI presentation election.

Application questions related to the contractual cash flow characteristics of financial assets

Contractual inflation adjustments and leverage

32 Members noted that this issue was not relevant to European jurisdiction.

Regulated interest rates and leverage

33 Members noted that the issue was only present in few countries in Europe (i.e., Hungary), so it was not widespread and relevant to European jurisdiction.

EFRAG working groups discussions

EFRAG FIWG

34 EFRAG FIWG discussed the topic at its 25 October meeting and on balance agreed with the IASB decision not to take further action on the matters described given the PIR criteria and other priorities.

35 Nonetheless, members noted that more guidance on derecognition of non-financial assets would have been appreciated as diversity in practices led to a significant number of application questions, especially given the rising energy prices, particularly for the corporates.

36 It was also noted that nowadays the discussions on the use of 'own use exemption' are increasing due to the trend in the energy prices and the evolution of energy market.

37 Members also acknowledged that these issues were not a priority for the IASB at this stage.

EFRAG IAWG

38 EFRAG IAWG discussed this topic at its meeting on 3 November 2022. The update from this discussion will be provided to EFRAG FR TEG orally.

The EFRAG Secretariat analysis

39 The EFRAG Secretariat does not have an information that the issues (a) and (c) – (e) and two application questions discussed above are widespread and pervasive in Europe and, therefore, agrees with the IASB staff analysis and the IASB decision not to take any further actions on these matters described above.

40 The EFRAG Secretariat also supports the IASB decision to consider the accounting for POCI financial assets during PIR of impairment requirements of IFRS 9.

Questions for EFRAG FR TEG

41 Does EFRAG FR TEG agree with the IASB decision not to take any action on the issues (a) and (c) – (e)?

42 Does EFRAG FR TEG agree with the IASB decision not to take any action on the two application questions?

43 Does EFRAG FR TEG agree with the IASB decision to consider the accounting for POCI financial assets during PIR of impairment requirements of IFRS 9?