EFRAG SECRETARIAT PAPER FOR PUBLIC EFRAG BOARD MEETING

EFRAG Research activities

Research activities and consultation update

Objective

1 The objective of this session is to provide a short update on status of the various projects in the Research activities.

Research project – Equity instruments: Impairment and Recycling

2 The main project on the EFRAG Research agenda is the *Equity instruments – Impairment and Recycling*. Following the request of technical advice from the European Commission, the project is currently organised in two phases:

(a) Phase 1, which is due by the end of 2017, consists of information about the significance of the equity portfolio for long-term investors under IAS 39 and whether the new requirements in IFRS 9 will affect asset allocation decisions;

(b) In Phase 2, which is due by the end of mid-2018, the EC wants EFRAG to assess, from a conceptual perspective, the significance of an impairment model to the re-introduction of recycling. If an impairment model is considered to be a precondition for recycling, then the EC wants EFRAG to consider possible alternatives of a robust impairment model.

3 In relation to the collection of data, EFRAG launched a public consultation open until 30 September. At the date of this report, we have received 22 replies with a few other respondents committing to answer in the next few days.

4 Most of the respondents are financial institutions and located in France, Germany and Belgium.

5 Besides the public consultation, the EFRAG Secretariat has also:

(a) investigated the potential use of the FVOCI designation in its 2013 field test on classification and measurement of financial assets (37 participants, half of them from the banking sector and the other half from the insurance and other industries);

(b) obtained some aggregated data on total equity instruments, total AFS instruments and related OCI balances held by approximately 150 financial institutions from 28 member states of the European Union and one country of the European Economic Area for the period 30 September 2014 to 30 September 2016, by the European Banking Authority ('EBA');

(c) reviewed the financial statements of 2015 of 45 public entities in Europe to collect the relevant data and investigate how these entities apply the IAS 39 impairment requirements, and in particular how they articulate the 'significant or prolonged' criterion;

(d) reviewed other publicly available reports, including:

  (i) the ESMA report *Review of Accounting Practices: Comparability of IFRS Financial Statements of Financial Institutions in Europe* on the 2012; financial statements of 39 major European financial institutions;

  (ii) the Mercer 2017 asset allocation survey, that includes data from 1,240 institutional investors across 13 countries in Europe and reports information on asset allocation by class of assets;

  (iii) the 2015 Pensions Europe statistics on pension funds in the private sector in 21 European countries.

6 The EFRAG Secretariat will present a full analysis of the replies at the October EFRAG TEG meeting. There are a few elements to consider in relation to the consultation:

(a) It is difficult to assess if and to what extent accounting requirements affect asset allocation decisions. Economic factors, tax regimes and other regulations are likely to influence these decisions, possibly to a bigger extent than accounting Standards;

(b) The European Commission in its request for advice refers to the impact of IFRS 9 on long-term investors, and the data collection request repeatedly mentions 'long-term portfolios' or 'the proportion of equity instruments considered to be held for the long-term'. However, the long-term notion is neither defined nor relevant in IFRS Standards, that make a distinction only between current and non-current assets and liabilities, based on the entities' operating cycle. Non-current assets are commonly interpreted to be assets expected to be realised on more than twelve months from the reporting date, but the EFRAG Secretariat does not consider that 'long-term' is intended to have this meaning;

(c) The same applies to 'long-term investors' that are not defined for accounting purposes. Finally, long-term investments is not equivalent to investments of long term investors – some entities may have different portfolios.

7 In relation to Phase 2, EFRAG TEG has discussed two basic accounting models:

(a) one model under which all fair value changes below the original purchase cost are carried through profit or loss, and all changes above the original purchase cost are carried through OCI;

(b) one model under which entities are required to account for decreases in value that are impairment losses in profit or loss. Different features of the model were discussed, such as the use of quantitative impairment triggers or non-rebuttable presumptions.

8 EFRAG had also launched a call for an academic literature review on the topic. The deadline to apply was extended to 9 October. At the date of this report, we had received two applications.

Other projects

9 In July the Pensions Advisory Panel met to continue discussions on possible accounting approaches to plans with benefits that are based on asset returns. The next meeting of the Panel will occur in November and the EFRAG Secretariat plans to bring back the topic to EFRAG TEG in December.

10 The Panel suggested to have a discussion on the scope of the project, that some Panel members believe should encompass a wider range of 'hybrid' plans. The current scope is aligned to the IASB project currently in their Research pipeline.

11 The July EFRAG TEG included a session on the *EFRAG Research project – Transactions other than Exchanges of Equal Value*. EFRAG TEG discussed a conceptual model that applies to both cost and revenue-generating transactions. EFRAG TEG raised a number of suggestions to be addressed by the Secretariat. A new session is planned for the November meeting.

12 The EFRAG Secretariat has started to consult the different Working Groups on possible topics for new Research projects. We plan to bring a formal proposal to the Board early next year.