Interest Rate Benchmark Reform – Update on Phase 2 End of Phase 1, other IFRS Standards, Disclosure Issues Paper

Objective

1 The objective of this paper is to provide an update on the IASB's third deliberations on Phase 2 of the *Interest Rate Benchmark Reform* project at the January 2020 meeting.

The IASB tentative decisions taken in January 2020

2 The IASB met on 30 January to discuss the following issues that could result from IBOR reform:

(a) the relationship between the Board's tentative decisions taken so far in Phase 2 of the project and the end of application requirements for the Phase 1 amendments to IFRS 9 *Financial Instruments* and IAS 39 *Financial Instruments: Recognition and Measurement*;

(b) the potential effects of the IBOR reform on IFRS Standards other than those related to financial instruments accounting; and

(c) the potential disclosure requirements to accompany the Board's tentative decisions for Phase 2 of the project.

End of application—Phase 1 exceptions

3 The IASB tentatively decided to:

(a) amend IAS 39, only for the purpose of assessing retrospective effectiveness, to require entities to reset to zero the cumulative fair value changes of the hedging instrument and the hedged item at the date the exception to the retrospective assessment in paragraph 102G of IAS 39 ceases to apply; and

(b) make no amendments to the end of application requirements for the Phase 1 exceptions to the highly probable requirement for cash flow hedges and prospective assessments in IFRS 9 and IAS 39.

Feedback from EFRAG FIWG

4 EFRAG FIWG members welcomed the IASB's tentative decisions.

Question for EFRAG TEG

5 Does EFRAG TEG share the view of EFRAG FIWG?

Other IFRS Standards

6 The IASB tentatively decided:

(a) For IFRS 16 *Leases,* to require a lessee to apply paragraphs 42(b) and 43 of IFRS 16 [i.e. remeasure the lease liability using a discount rate that reflects the changes in the interest rate] to account for lease modifications to the interest rate benchmark on which lease payments are based that are required as a direct consequence of IBOR reform and done on an economically equivalent basis (modifications directly required by IBOR reform).

(b) For IFRS 4 *Insurance Contracts,* to require insurers that apply the temporary exemption from IFRS 9 to apply the amendments resulting from the Board's tentative decisions in Phase 2 of the project in accounting for modifications directly required by IBOR reform.

7 The IASB also tentatively decided that no amendments should be made in the context of IBOR reform to:

(a) IFRS 13 *Fair Value Measurement* because it provides sufficient guidance to determine if and when a financial asset or financial liability should be transferred to a different level within the fair value hierarchy. These transfers reflect the economic effects of IBOR reform, therefore providing useful information to users of financial statements.

(b) IFRS 17 *Insurance Contracts* because it provides an adequate basis for an entity to account for insurance contract modifications in the context of the IBOR reform. Such accounting results in useful information to users of financial statements.

(c) the current requirements in IFRS Standards with respect to discount rates as they already provide adequate guidance to determine the appropriate accounting treatment for the potential effects of changes to the discount rates resulting from the replacement of interest rate benchmarks (i.e. be treated as change in an accounting estimate that applies prospectively in accordance with IAS 8).

Feedback from EFRAG FIWG

8 EFRAG FIWG members welcomed the IASB's tentative decisions.

Question for EFRAG TEG

9 Does EFRAG TEG share the view of EFRAG FIWG?

Disclosures

10 The IASB tentatively decided to amend IFRS 7 *Financial Instruments: Disclosures* to require an entity to provide disclosures that enable users of financial statements to understand:

(a) the nature and extent of risks arising from IBOR reform to which the entity is exposed, and how it manages those risks; and

(b) the entity's progress in completing the transition from interest rate benchmarks to alternative benchmark rates, and how the entity is managing the transition.

11 To achieve this objective, an entity would disclose information about:

(a) how it is managing the transition from interest rate benchmarks to alternative benchmark rates and the progress made at the reporting date, and the risks arising from this transition;

(b) the carrying amount of financial assets and financial liabilities, including the nominal amount of the derivatives, that continue to reference interest rate benchmarks subject to the reform, disaggregated by significant interest rate benchmark;

(c) for each significant alternative benchmark rate to which the entity is exposed, an explanation of how the entity determined the base rate and relevant adjustments to the rate to assess whether the modifications to contractual cash flows were required as a direct consequence of IBOR reform and have been done on an economically equivalent basis; and

(d) to the extent that IBOR reform has resulted in changes to an entity's risk management strategy, a description of these changes and how is the entity managing those risks.

The EFRAG Secretariat analysis on disclosures

12 The EFRAG Secretariat observes that the disclosure requirements will be included in IFRS 7, which relates to disclosures on financial instruments as defined in the scope of IFRS 7. While it is expected that the majority of items affected from the IBOR reform will be financial instruments in scope of IFRS 7, it is less clear whether items scoped out from IFRS 7 (e.g. insurance contracts) will equally be subject to the additional disclosure requirements.

Feedback from EFRAG FIWG

13 On paragraph 11(c), EFRAG FIWG members noted that this rather relates to the scope of the amendments. These disclosures are expected to be very similar across entities affected and hence may be of limited use to users of financial statements.

Questions for EFRAG TEG

14 Does EFRAG TEG share the views of EFRAG FIWG?