EFRAG Secretariat: Almudena Alcalá,
Didier Andries (teamleader), Galina
Borisova

Post-Implementation Review of IFRS 9 – BACS issue
Issues Paper

Objective

1 This paper describes the tentative agenda decision (TAD) by the IFRS IC of September 2021 about the recognition of cash received via an electronic transfer (payment) system as settlement for a financial asset (IFRS 9). The expected date for input to this TAD is February 2022.

2 At the meeting of EFRAG TEG of 20-21 October 2021 one EFRAG TEG member suggested [through written input] to address the BACS issue as part of the Post-Implementation Review of IFRS 9. The reason for this being that the TAD might bring a change in current practices in several jurisdictions on when to derecognise a trade receivable and when to recognise cash.

3 To avoid such a consequence, one might consider proposing an amendment to IFRS 9 to allow the current practice as an accounting policy choice between recognising the cash on initiation date of the transfer or receipt.

4 In their meeting of 20-21 October 2021 EFRAG TEG members agreed not to include this issue in the draft comment letter, but to discuss it separately, including the merit of covering this topic in the final comment letter.

Description of the issue

5 Many payment systems around the world have formal automated settlement processes that take at least one day to settle a cash transfer. The submission considers one example of such a payment system, the BACS payment system in the UK. The submitter says BACS follows a strict three working-day cycle to settle a cash transfer, which it describes as follows:

(a) Day 0—submission: a payment instruction is submitted to BACS and distributed to the relevant parties overnight.

(b) Day 1—processing: after receiving the instruction, the paying and receiving banks prepare to debit and credit the payer and receiver's accounts, respectively.

(c) Day 2—action: all parties take the action required—thus, the paying bank debits the payer's account and the receiving bank simultaneously credits the receiver's account.

6 The submitter notes that, because of the three working-day cycle described above, if an entity receives a payment via BACS after the reporting date but within two days of it, the payer will necessarily have initiated the payment before the reporting date.

7 The submitter then describes the following fact pattern:

(a) on 30 November 20X0, an entity sells goods to a customer and recognises a trade receivable of CU100.

(b) on 31 December 20X0 (the entity's reporting date), the customer notifies the entity that it has initiated a payment of CU100 via BACS to settle the trade receivable.

(c) on 2 January 20X1, the entity receives CU100 into its bank account.

8 The submitter asks whether it is acceptable for the entity to derecognise the trade receivable and recognise cash of CU100 on the date the cash transfer is initiated (31 December 20X0), rather than the date the cash transfer is settled (2 January 20X1). The submitter outlines two views, summarised below:

(a) View 1—yes, it is acceptable: there are no requirements in IFRS Standards that specifically apply to the timing of recognition of cash in an entity's financial statements. The entity therefore applies paragraphs 10–11 of IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors and uses its judgement in developing and applying an accounting policy. In doing so, the entity refers to the requirements in IFRS Standards dealing with similar and related issues. Paragraph 3.1.2 of IFRS 9 Financial Instruments states that a 'regular way purchase or sale of financial assets shall be recognised and derecognised, as applicable, using trade date accounting or settlement date accounting'. Applying these requirements and considering the established time frame for cash settlement in the BACS payment system, an entity receiving cash via BACS is permitted to adopt an accounting policy under which it derecognises its trade receivable and recognise cash upon initiation of the transfer by the payer. Such an accounting policy would be similar to applying 'trade date accounting'.

(b) View 2—no, it is not acceptable: an entity recognises cash based on an assessment of control of the cash. This approach to the recognition of cash received is consistent with the definition of an asset in the Conceptual Framework for Financial Reporting (Conceptual Framework), which an entity considers in developing and applying an accounting policy in accordance with paragraphs 10–11 of IAS 8. The entity obtains control of the cash only on 2 January 20X1 when it receives the cash, and therefore recognises the cash only on that date. It would be inappropriate to refer to the requirements in paragraph 3.1.2 of IFRS 9 because the receipt of cash is not a regular way purchase of a financial asset.

The proposed Tentative Agenda Decision

The applicable requirements in IFRS 9

9 The fact pattern described in the request involves the receipt of cash as settlement for a trade receivable. Both the trade receivable, and the cash the entity receives, are financial assets within the scope of IFRS 9. The entity therefore applies paragraph 3.2.3 of IFRS 9 in determining the date on which to derecognise the trade receivable and paragraph 3.1.1 of IFRS 9 in determining the date on which to recognise the cash as a financial asset.

10 The Committee observed that, in the fact pattern described in the request, the entity is neither purchasing nor selling a financial asset. Therefore, paragraph 3.1.2 of IFRS 9— which specifies requirements for a regular way purchase or sale of a financial asset—is not applicable.

Derecognition of the trade receivable

11 Except when an entity transfers a financial asset, paragraph 3.2.3 of IFRS 9 requires an entity to derecognise a financial asset when, and only when, 'the contractual rights to the cash flows from the financial asset expire'. In the fact pattern described

in the request, the entity therefore derecognises the trade receivable on the date on which its contractual rights to the cash flows from the trade receivable expire.

12 Determining the date on which the entity's contractual rights to those cash flows expire is a legal matter, which would depend on the specific facts and circumstances including the applicable laws and regulations and the characteristics of the electronic transfer system.

13 The Committee however expects that an entity would typically derecognise the trade receivable on the transfer settlement date (the date it receives the cash in its bank account) because, in the fact pattern described in the request, it would expect the entity's contractual right to receive cash from the customer to expire when the entity receives that cash, and not before.

Recognition of cash (or another financial asset)

14 Paragraph 3.1.1 of IFRS 9 requires an entity to recognise a financial asset when, and only when, 'the entity becomes party to the contractual provisions of the instrument'. In the fact pattern described in the request, the entity is party to the contractual provisions of an instrument—its bank account—under which it has the contractual right to obtain cash from the bank for amounts it has deposited with that bank. It is therefore only when cash is deposited in its bank account that the entity would have a right to obtain cash from the bank. Consequently, in the fact pattern described in the request, the entity recognises cash as a financial asset on the transfer settlement date, and not before.

15 The Committee observed that, if an entity's contractual rights to the cash flows from the trade receivable expire before the transfer settlement date, the entity would recognise any financial asset received as settlement for the trade receivable (for example, a right to receive cash from the customer's bank) on that same date. An entity would not however recognise cash (or another financial asset) received as settlement for a trade receivable before it derecognises the trade receivable.

Conclusion

16 In the fact pattern described in the request, the Committee concluded that, applying paragraphs 3.2.3 and 3.1.1 of IFRS 9, the entity:

(a) derecognises the trade receivable on the date on which its contractual rights to the cash flows from the trade receivable expire; and

(b) recognises the cash (or another financial asset) received as settlement for that trade receivable on the same date.

17 The Committee concluded that the principles and requirements in IFRS Standards provide an adequate basis for an entity to determine when to derecognise a financial asset and recognise cash received via an electronic transfer system as settlement for that financial asset. Consequently, the Committee [decided] not to add a standard-setting project to the work plan.

Questions for EFRAG TEG

18 Do EFRAG TEG members think this issue should be considered in EFRAG's final comment letter?