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Post-implementation Review of IFRS 9 Classification and Measurement

EFRAG's final comment letter - Cover Note

Objective and detailed agenda of this session

- 1 The session will include two different topics:
 - (a) From 8.35 am to 8.55 am the participants will receive a presentation by EBA on main takeaways from the IFRS 9 monitoring report recently issued;
 - (b) From 8.55 to 11.30 participants will discuss and approve EFRAG final comment letter on the PIR of IFRS 9 Classification and Measurement.
- 2 The objective of the second topic is twofold:
 - (a) to discuss the feedback received in response to EFRAG's draft comment letter relating to the *Post-Implementation Review of IFRS 9: Classification and Measurement*;
 - (b) to agree upon EFRAG's final comment letter to be shared with the IASB.
- 3 For the second topic, after a joint discussion by EFRAG TEG and EFRAG Board of the feedback obtained from the consultation and the changes to the DCL proposed by the EFRAG Secretariat, EFRAG TEG and EFRAG Board members will be asked to vote (first EFRAG TEG, after the EFRAG Board).

Background

EFRAG Due Process

- 4 The effective date of IFRS 9 was set as annual reporting periods beginning on or after 1 January 2018. Insurers and EU financial conglomerates have the possibility to defer the application date of IFRS 9 till 1 January 2023 (subject to fulfilling particular conditions).
- 5 In October 2020, the IASB decided to begin the PIR of the IFRS 9 classification and measurement requirements only, and not of impairment and hedge accounting requirements.
- 6 During [January – March](#) 2021, the EFRAG Secretariat consulted EFRAG TEG and EFRAG working groups (Academic Panel, EFRAG FIWG, EFRAG IAWG, EFRAG User Panel, EFRAG CFSS) and had an exchange with the IFRS 9 Task Force of Accountancy Europe. This consultation has allowed to prepare a first comprehensive list of issues that have been reported to the IASB Staff, including at the ASAF meeting in [March](#) 2021.

- 7 On 9 [June](#) 2021, the EFRAG Board decided that the future EFRAG response to the RFI on IFRS 9 *Financial Instruments* should include views about the technical merits of some of the key issues reported. The remaining issues are to be reported to the IASB without an accompanying assessment.
- 8 The EFRAG Board further decided that the technical assessment should be focused on providing indications as to whether standard setting is considered necessary to solve the issue, without providing indications of the possible standard setting solution itself.
- 9 When assessing the technical merits, to the extent possible, the EFRAG response to the RFI should also provide indications of the type of standard-setting activity needed (e.g., amendments to the standard, educational material).
- 10 It was noted that for some issues EFRAG has already developed views and it would be sufficient to repeat the existing positions. This relates to:
 - (a) Recycling the changes in FV accumulated in OCI for equity instruments; and
 - (b) FVTPL treatment for equity-type instruments (e.g., units of funds).
- 11 The list of issues has been assessed by EFRAG TEG in [June](#), [July](#) and [September](#) 2021, with inputs from EFRAG FIWG and EFRAG IAWG.
- 12 The final list of issues was agreed by the EFRAG Board on 6 [October](#) 2021.
- 13 The [Request for Information on IFRS 9](#) was published on 30 of September 2021 with comments to be delivered by **28 January 2022**.
- 14 EFRAG's [draft comment letter](#) was issued on 8 November 2021, with a comment deadline till **14 January 2022**.
- 15 In addition to the comment letter process, the EFRAG Secretariat has collected views from different constituents with regard to the i) financial instruments with ESG features and ii) equity-type financial instruments.

Main messages expressed in the DCL

- 16 EFRAG considers that the combination of the cash flow characteristics of the assets together with the assessment of the entity's business model has proved to generally provide an appropriate basis to align the measurement of financial instruments with how they are managed by the entity. However, there are some areas that require attention.
- 17 In EFRAG's view, the IASB should re-evaluate whether the classification and measurement principles and the accompanying guidance in IFRS 9 have kept up with e.g., recent market developments.
- 18 EFRAG has been made aware of some circumstances where the application of the business model concept is challenging. However, EFRAG does not consider that further standard-setting activity is needed, as overall the existing IFRS 9 requirements result in appropriate outcomes.
- 19 EFRAG considers that the effective interest rate method generally provides useful information. EFRAG notes that IFRS 9 includes scope limitations or corrections to the method for particular financial instruments. EFRAG also notes that more and more financial instruments incorporate clauses that may affect the future contractual cash flows when being fulfilled (or when they fail to be fulfilled) by the reporting entity or a third party.
- 20 EFRAG has identified a number of issues that deserve standard-setting activities. These issues are (in order of priority):
 - (a) Sustainable finance – SPPI test;
 - (b) Recycling changes in FV accumulated in OCI for equity instruments;

- (c) Treatment of equity-type instruments;
 - (d) Supply-chain financing – reverse factoring;
 - (e) Modification of contractual cash flows;
 - (f) Contractually linked instruments – non-recourse;
 - (g) Factoring of trade receivables;
 - (h) SPPI – use of administrative rates; and
 - (i) Financial guarantees.
- 21 In particular, for three issues particular attention is being asked as part of the comment letter:
- (a) Application of the SPPI test to sustainable finance products: it is expected that this issue will be so pervasive in Europe that, in EFRAG’s view, it should be lifted from the PIR process and treated as an urgent issue separately, so that the IASB can start working on it without waiting for the completion of the RFI process. EFRAG confirms its commitment and willingness to assist the IASB in the assessment of this issue.
 - (b) EFRAG considers the IASB should expeditiously review the non-recycling treatment of equity instruments within IFRS 9, testing whether the Conceptual Framework would justify the recycling of FVOCI gains and losses on such instruments when realised. If recycling was to be reintroduced, the IASB should also consider the features of a robust impairment model, including the reversal of impairment losses.
 - (c) EFRAG supports that similar fact patterns should be treated similarly, and notes that some mutual funds and puttable instruments, respond to movements in market variables in a similar way to equity instruments even though these do not meet the definition of an equity instrument under IAS 32 *Financial Instruments: Presentation*. EFRAG considers that any changes to the accounting for these instruments, aimed at allowing for equity and equity-type instruments to be treated similarly for accounting purposes, would require careful consideration. This would imply that equity-type instruments would be allowed to be accounted for at FVOCI, what is currently not the case.

Outreach and closed meeting

- 22 After the issuance of the DCL, the EFRAG Secretariat collected inputs and views from EFRAG’s working groups and had a number of closed meetings with experts from the banking and insurance industry, in addition to meetings with users’ groups, regulators and auditors. Please refer to Agenda papers 02-03 and 02-04.

Comment letters received

- 23 At the time of writing, EFRAG received comment letters from 13 respondents (and two drafts) representing national standard-setters, users, preparer organisations, preparers and one individual.

Question to the EFRAG TEG

- 24 Does the EFRAG TEG agree to recommend to the EFRAG Board for issuance the FCL in agenda paper 02-07 (marked-up version) subject to drafting changes that will be agreed in this meeting?

Question to the EFRAG Board

- 25 Does the EFRAG Board approve the FCL in agenda paper 02-07 (marked-up version) subject to drafting changes that will be agreed in this meeting?

Agenda Papers

- 26 In addition to this cover note, agenda papers for this session are:
- (a) Agenda paper 02-01B – EBA EFRAG Board presentation;
 - (b) Agenda paper 02-02 – Comment letter analysis;
 - (c) Agenda paper 02-03 – Comments received from EFRAG FIWG, IAWG and User Panel;
 - (d) Agenda paper 02-04 – Comments received during additional outreach in December 2021 and January 2022;
 - (e) Agenda paper 02-05 – The EFRAG Secretariat recommendations;
 - (f) Agenda paper 02-06 – Proposed final comment letter (clean); and
 - (g) Agenda paper 02-07 – Proposed final comment letter (compared).