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PIR IFRS 9 Impairment Project update

Objective

- 1 To provide the EFRAG FRB members with an update on the forthcoming Request for Information (RFI) for the post-implementation review of the impairment requirements in IFRS 9 *Financial Instruments* (the PIR) as well as the preliminary analysis performed at EFRAG.

Background of the IASB project

- 2 In November 2021, the IASB decided to begin the PIR of the ECL requirements in IFRS 9 in the second half of 2022. In July 2022, the IASB discussed the plan for identification of matters to be examined ([AP27](#)).
- 3 Between September 2022 and February 2023, the IASB conducted outreach to ask stakeholders what matters the IASB should examine within the context of the objectives of the PIR and, consequently, on which issues to collect further information in the form of a RFI (i.e., phase 1 of a PIR).
- 4 In February 2023, the IASB considered the feedback from the outreach and defined the matters on which it will seek feedback through a public consultation.
- 5 In April 2023, the IASB approved the publication of a RFI and set a 120-day comment period ([AP27](#)).
- 6 The IASB expects to publish the RFI by the end of May 2023.

Objective and process of post-implementation reviews

- 7 The objective of a PIR is to assess whether the effects of applying the new requirements on users of financial statements, preparers, auditors, and regulators are as intended when the IASB developed those new requirements.
- 8 In order to make this assessment the IASB needs to know whether there are any:
 - (a) fundamental questions (i.e., fatal flaws) about the core objectives or principles – their clarity and suitability – that indicate that the new requirements are not working as intended; or
 - (b) specific application questions which not necessarily prevent the IASB from concluding that the new requirements are operating as intended but may nonetheless need to be addressed if they meet the criteria for taking further action.
- 9 The PIR process consists of two phases:
 - (a) Phase 1 — the IASB identifies matters to be examined, drawing on discussions with the Interpretations Committee, the IASB's advisory groups and other interested parties. The IASB consults publicly on the matters identified in the first phase of the PIR by publishing an RFI.

- (b) Phase 2 — the IASB considers the comments from the public consultation along with the information it has gathered from any additional analysis and other consultative activities.
- 10 As part of the Phase 2, the IASB will consider whether to take action on its findings, based on the extent to which: (a) the objective of the new requirements is not being met; (b) benefits to users are significantly lower than expected; and (c) costs of applications are significantly higher than expected.

RFI content

- 11 As illustrated in paragraph 6 of the [AP27](#) for the IASB April 2023 meeting, the RFI will seek information in particular on the following matters:
- (a) the general approach to recognition of expected credit losses (ECL), specifically:
 - (i) the effects of the general approach on the usefulness of information about changes in credit risk to the users of the financial statements; and
 - (ii) the costs and benefits of applying the general approach to particular financial instruments;
 - (b) significant increases in credit risk, specifically:
 - (i) the use of judgement in determining significant increases in credit risk; and
 - (ii) the evidence about the causes of and the extent of diversity in how entities assess significant increases in credit risk;
 - (c) the measurement of ECL, specifically:
 - (i) using multiple forward-looking scenarios; and
 - (ii) measuring ECL in periods of enhanced economic uncertainty, including the use of post-model adjustments or management overlays;
 - (d) the prevalence of particular questions from entities on how to apply the ECL requirements to purchased or originated credit-impaired financial assets;
 - (e) the simplified approach to recognition of ECL for trade receivables, contract assets and lease receivables, specifically:
 - (i) the effects of the relief provided by the IASB through the simplified approach; and
 - (ii) the use of forward-looking information when applying the simplified approach;
 - (f) the accounting for loan commitments, collateral and other credit enhancements held, and issued financial guarantee contracts that are in scope of IFRS 9;
 - (g) the application of the ECL requirements alongside other requirements in IFRS 9 or in other IFRS Accounting Standards;
 - (h) the effects of transition reliefs provided by the IASB and the balance between reducing costs for preparers of financial statements and providing useful information to users of financial statements; and
 - (i) the disclosure requirements for credit risk in IFRS 7 Financial Instruments: Disclosures, specifically
 - (i) whether the combination of disclosure objectives and minimum disclosure requirements achieves an appropriate balance between comparable information and relevant information for users of financial

statements about the effect of credit risk on the amount, timing, and uncertainty of future cash flows; and

- (ii) the compatibility of the requirements with digital reporting.

Background of the EFRAG discussions

- 12 In anticipation of the publication of RFI and as a preliminary work, EFRAG reached out to its constituents and working groups to collect issues that they think should be raised during this process.
- 13 In April-June 2022, the EFRAG Secretariat has held several meetings with EFRAG constituents and working groups and came up with a first comprehensive list of issues that have been discussed with EFRAG FR TEG-CFSS members in the June and September 2022 meetings.
- 14 After considering the feedback received during these meetings, the EFRAG Secretariat presented and discussed an assessment on the categorisation and prioritisation of issues collected during the preliminary work with EFRAG FIWG, EFRG IAWG, and EFRAG FR TEG. The assessment was based on pervasiveness and prevalence of the issues in Europe and took into account the IASB's criteria for addressing the PIR findings (see paragraph 10 of this paper).
- 15 An updated [list of 19 issues](#) was presented at the meeting of EFRAG FR TEG on 16 March 2023.

Main results of the EFRAG's preliminary work

- 16 The preliminary work performed highlights that the ECL model works generally as intended. In other words, there are not fatal flaws on the clarity and suitability of the core objectives or principles and the impairment requirements have solved the issues of “too little too late” that they were designed to address.
- 17 Nonetheless, some application issues or diversity in practice should be addressed by the IASB with high priority. Namely:

- (a) **Interaction between ECL and other requirements**

The interaction between modification, impairment, and derecognition requirements needs clarification. The allocation of the accounting effects to the three events (and the consequent presentation in the statement of profit or loss) depends on several factors and interpretations (e.g., the reason that causes the modification and/or the derecognition – commercial opportunities, financial difficulties of the borrower – or the order in which an entity considers the different elements).

- (b) **Determination of credit risk**

There is diversity in practice regarding the extent to which cash shortfalls should be considered in the calculation of ECL. In particular, the IFRS IC [Agenda Decision](#) approved in October 2022 (the “AD”) Lessor Forgiveness of Lease Payments (IFRS 9 and IFRS 16) creates uncertainty on what the boundaries of credit risk are. This AD could have wider implications than lease receivables and cause undue disruption to long-standing general accounting practices for financial assets.

Therefore, the IASB should clarify whether the expression “all cash shortfalls” used in the AD should be interpreted within the scope of concessions from the lender due to financial difficulties of the borrower.

- (c) **Consistency and comparability of disclosures**

Important diversity in the level of details and content of disclosures provided by the entities is noted. The information provided in the disclosures is

important in understanding the credit risk management practices and their impact on the ECL numbers. Users need high quality information, which is reliable and comparable.

Areas that could be considered to increase consistency and comparability of disclosures are, for example:

- (a) how the ECL model parameters (e.g., PD, LDG, and EAD) were defined and their interaction with the definition of default;
- (b) criteria applied in determining significant increase in credit risk in presence of modifications or forbearance measures;
- (c) probability-weighted outcome and approaches to incorporate multiple economic scenarios;
- (d) sensitivity analysis, back-testing, and reconciliation forms; and
- (e) post model adjustments.

- 18 The table in Appendix 1 summarises the issues presented at the meeting of EFRAG FR TEG on 16 March 2023 and the EFRAG preliminary assessment on prevalence and priority in Europe.

Questions for EFRAG FRB

- 19 Does EFRAG FRB have comments on the summary above?

Next steps

- 20 The EFRAG Secretariat will closely monitor the developments of the IASB project and continue discussions with EFRAG FR TEG, EFRAG working groups and EFRAG constituents to select and prioritise the issues to be included in its DCL.

Appendix 1: Summary of issues

- 1 The table below summarises the issues that will be reported to the IASB in response to the forthcoming RFI of the PIR of IFRS 9 – Impairment and the EFRAG preliminary assessment on prevalence and priority in Europe.

#	Issue	IASB Category	Criterion	Prevalence in Europe	Priority in Europe
1.1	Integral vs non-integral and way of paying the premium	Loan commitments and financial guarantees	Requirements and application guidance difficult to be applied consistently	Prevalent	Medium
1.2	Joint and several guarantees	Loan commitments and financial guarantees	Diversity in practice	Some prevalence	Medium
2	Interaction between ECL and other requirements	Interaction between ECL and other requirements	Requirements and application guidance difficult to be applied consistently	Prevalent	High
3	Collective assessment of SICR: bottom-up vs top-down approach	Determining significant increases in credit risk	Wording not entirely consistent within the Standard	Some prevalence	Medium
4	Discount rate to be used for ECL in case the asset is floating rate based	Measurement of ECL	Diversity in practice	Some prevalence	Low
5	Simplified rules for corporates	Simplified approach for trade in lease receivables	Requirements and application guidance difficult to be applied consistently	Not prevalent	Low
6	Determination of credit risk	General approach to impairment Interaction between ECL and other requirements	Diversity in practice	Prevalent	High

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#	Issue	IASB Category	Criterion	Prevalence in Europe	Priority in Europe
7.1	Revolving credit facilities – Scope of the exception	Loan commitments and financial guarantees	Diversity in practice	Prevalent	Medium
7.2	Revolving credit facilities – Interaction with derecognition	Loan commitments and financial guarantees	Diversity in practice	Prevalent	Medium
7.3	Revolving credit facilities – Educational video of IASB Staff	Loan commitments and financial guarantees	Diversity in practice	Prevalent	Medium
8	Calculating ECL on intragroup loans	General approach to impairment	Requirements and application guidance difficult to be applied consistently	Prevalent	Medium
9	Contractually Linked Instruments (CLI and SPEs investments) – definition of default	Measurement of ECL	Requirements and application guidance difficult to be applied consistently	Prevalent	Medium
10	Timing to move to stage 3 (next reporting date or during the reporting period)	Other topics	Diversity in practice	Not prevalent	Low
11	Purchased or originated credit-impaired financial assets (POCI), alternative treatment of ECL	POCI financial assets	Requirements not working as intended	Some prevalence	Medium
12	Portfolios of high credit quality exposures	General approach to impairment	Requirements not working as intended	Some prevalence	Medium

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#	Issue	IASB Category	Criterion	Prevalence in Europe	Priority in Europe
13	Credit risk and portfolio performance	General approach to impairment	Requirements not working as intended	Not prevalent	Low
14	Exposures in stage 1 and stage 2 simultaneously	General approach to impairment	Requirements not working as intended	Not prevalent	Low
15	Consistency and comparability of disclosures	Disclosures	Diversity in practice	Prevalent	High
16	Impact of climate-related risk factors	Measurement of ECL	Requirements and application guidance difficult to be applied consistently	Prevalent	Medium