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Amendments to the Classification and Measurement of Financial Instruments

Cover Note

Objective

- 1 The objective of this session is to discuss and agree to recommend for approval to the EFRAG FRB the Draft Endorsement Advice ('DEA') on the *Amendments to the Classification and Measurement of Financial Instruments* (Amendments to IFRS 9 and IFRS 7).

Background

- 2 The IASB has carried out a post-implementation review of the classification and measurement requirements in IFRS 9 *Financial Instruments* and related requirements in IFRS 7 *Financial Instruments: Disclosures* ('PIR'). The work performed by the IASB and the conclusions reached are summarised in the [Project Report and Feedback Statement—Post-implementation Review of IFRS 9 Financial Instruments—Classification and Measurement](#), published in December 2022.
- 3 To address the issues identified during PIR, in March 2023 the IASB published [the ED Amendments to the Classification and Measurement of Financial Instruments – Proposed amendments to IFRS 9 and IFRS 7 \(the ED\)](#).
- 4 EFRAG issued its [Final comment letter](#) (FCL) on 19 July 2023.
- 5 On 30 May 2024, the IASB issued [Amendments to the Classification and Measurement of Financial Instruments \(Amendments to IFRS 9 and IFRS 7\)](#) ('the Amendments'), where it took into account the feedback received from its stakeholders.

Summary of main changes in the Amendments

- 6 Early application of the Amendments is allowed for the set of amendments to solely payments of principal and interest ('SPPI') principles, not only for financial instruments with ESG-linked features, but also to non-recourse financial assets and contractually linked instruments ('CLI') altogether.
- 7 In paragraph B3.3.9 of the Amendments "the time between the entity initiating a payment instruction and the cash being delivered to the counterparty is short" was replaced by "the time between the criteria in paragraphs B3.3.8(a) and (b) being met" to accommodate the situations when the payment instruction is created in advance.
- 8 In paragraph B4.1.8A the IASB elaborated on when "contractual cash flows are inconsistent with a basic lending arrangement". The IASB added "if they are indexed to a variable that is not a basic lending risk or cost (for example, the value of equity instruments or the price

of a commodity)”. In the EFRAG Secretariat view this addition is important in the light of the overall interpretation of the changes.

- 9 Two additions were made to paragraph B4.1.10: first: “irrespective of the probability of the change in contractual cash flows occurring” for SPPI assessment (moved from paragraph B4.1.10A) and the second: the clarification that for the cash flows to be SPPI, the direction of changes of contractual cash flows should be the same as the direction of changes in basic lending risks and costs.
- 10 Paragraph B4.1.10A was significantly changed. The example of a loan where interest is linked to a contractually specified reduction in carbon emissions is added. This example with the reference to carbon emissions is included also in BC and amendments to IFRS 7. This paragraph also addressed the need for qualitative vs quantitative assessment of contractual cash flows.
- 11 The examples in paragraphs B4.1.13 and B4.1.14 are further elaborated, especially the example EA with the references to the related paragraphs of IFRS 9 added.
- 12 The main idea of the changes is that if the nature of contingent event does not relate directly to changes in basic risk and costs (with an example of reduction of carbon emissions), then further assessment of whether the contractual cash flows are SPPI is necessary. To make this assessment the contractual cash flows should be SPPI before and after a contingent event and, in all contractually possible scenarios, be not significantly different from the contractual cash flows on a financial instrument with identical contractual terms, but without such a contingent feature.
- 13 Some clarifying changes were also made to paragraphs on non-recourse financial assets and CLIs. They clarified the interrelations between the two and explained what paragraphs of IFRS 9 should be applied in each case. Also, an example of when lease receivables can be included in the underlying pool of financial instruments was added.
- 14 Some wording changes without changing the substance were made to the disclosure requirements for financial instruments measured at FVOCI. It was clarified that the disclosure is required by class of financial asset.
- 15 Disclosure of contractual cash flows: former paragraph 20C of the ED was split in two and part of it brought in front of the section, otherwise no significant changes were made. The IASB kept financial assets measured at FVOCI and credit-impaired financial assets within the scope of disclosure requirements which continue to refer to “gross carrying amount of financial assets”.
- 16 It is a first time the consequential amendments to IFRS 19 *Subsidiaries without Public Accountability* are included in the Amendments. The EC in its letter did not ask EFRAG to provide endorsement advice on amendments to IFRS 19.

EFRAG FIWG-IAWG feedback

- 17 EFRAG FIWG and EFRAG IAWG had a joint meeting on 7 June 2024 to discuss the first version of the DEA prepared by the EFRAG Secretariat.
- 18 Members welcomed the Amendments and noted that the overall package represented a significant improvement compared to the ED. Members considered that the Amendments fit for purpose for the EU.
- 19 Members agreed with the DEA as drafted by the EFRAG Secretariat and appreciated the quick turnaround.
- 20 EFRAG IAWG members noted that it is too early for them to comment on the implementation of IFRS 9 and that it will be done later as part of the PIR of IFRS 17 *Insurance*

Contracts and suggested to mention that non-recycling of equity instruments measured at FVOCI remains an important issue for European insurers.

- 21 Members commented that although the effective date of the amendments with regard to electronic payment systems may be challenging, especially if entity uses many different payment systems, it should not be an obstacle to recommend endorsing the amendments.
- 22 A member welcomed in particular, with a reference to example in paragraph B4.1.13, that non-significant differences in contractual cash flows for the purposes of SPPI assessment should be assessed on cumulative basis instead period by period.

Next steps

- 23 Following the recommendation of EFRAG FR TEG, the EFRAG Secretariat will bring the DEA for approval to the EFRAG FRB at its meeting on 25 June 2024 and will publish it for consultation as soon as possible after the approval. The expected deadline for comments will be 13 September 2024.

Questions to EFRAG FR TEG

- 24 Does EFRAG FR TEG have any comments on the drafting of the DEA?
- 25 Does EFRAG FR TEG agree to recommend the DEA for approval to the EFRAG FRB?

Agenda Papers

- 26 In addition to this Cover Note the Agenda Paper 01-02 - *Amendments to the Classification and Measurement of Financial Instruments DEA – Letter to the EC* is presented for this session.