STAFF PAPER

July 2016

IASB Meeting

Project	**Amendments to IFRS 4: Applying IFRS 9 *Financial Instruments* with IFRS 4 *Insurance Contracts***
Paper topic	Sweep issue: quantitative disclosures applicable for entities applying the temporary exemption from IFRS 9

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Objective

1. This Agenda Paper addresses a matter that has arisen following the initial review by Board members of the Amendments to IFRS 4 *Applying IFRS 9* Financial Instruments *with IFRS 4* Insurance Contracts (Amendments). In view of the urgency of the Amendments, and in order not to delay issuing the Amendments, the staff decided to bring this matter to the attention of the Board at its July 2016 meeting, even though this paper would be posted late.

Staff recommendation

2. The staff recommends aligning the scope for the fair value disclosures with the scope for the credit risk disclosures to simplify the disclosures applicable to entities applying the temporary exemption from IFRS 9 *Financial Instruments* (IFRS 9). Accordingly, an entity should disclose the fair value at the end of the reporting period and the change in the fair value during the reporting period for the following two groups of financial assets separately (*text in italics highlights the changes to the groups*):

   (a) Financial assets with contractual cash flows that <u>are</u> solely principal and interest (SPPI), *excluding financial assets that are held for trading or* *that are managed on a fair value basis*. [This is Group 2 in Table A below.]

(b) All financial assets excluding those described in (a). [This is Group 1 in Table A below.] That is, any financial assets:

(i) with contractual cash flows that are not solely principal and interest; or

(ii) *that are held for trading or managed on a fair value basis.*

3. Table A illustrates our recommendation on the financial assets grouped for the specified disclosures:

	SPPI	**Not SPPI**
Held for trading (HFT) or managed on a fair value basis (FVM)	Group 1	Group 1
Not HFT or FVM	Group 2 *	Group 1

* This is also the population subject to the credit risk disclosures. Our recommendation does not change the population for those disclosures.

Background

4. At a previous meeting, the Board tentatively confirmed the disclosures proposed in the Exposure Draft *Applying IFRS 9* Financial Instruments *with IFRS 4* Insurance Contracts (the ED) with minor amendments. Specifically, the Board tentatively decided that an entity applying the temporary exemption from IFRS 9 shall provide the following quantitative disclosures:

(a) the fair value at the end of the reporting period and the change in the fair value during the reporting period separately for the financial assets in the following groups:

(i) Financial assets with contractual cash flows that are not SPPI. [Group 1 in Table B below.]

(ii) All financial assets excluding those described in (i); that is, financial assets with contractual terms that are SPPI.
[Group 2 in Exhibit B below.]

(b) credit risk information for financial assets with contractual cash flows that are SPPI excluding those that are held for trading(HFT) as defined in IFRS 9 or that are managed on a fair value basis (FVM) as described in paragraph B4.1.6 of IFRS 9.

5. Table B illustrates the Board's tentative decision on the financial assets grouped for the specified disclosures:

	SPPI	**Not SPPI**
Held for trading (HFT) or managed on a fair value basis (FVM)	Group 2	Group 1
Not HFT or FVM	Group 2 *	Group 1

* This is the population subject to the credit risk disclosures.

6. The scopes for those disclosures (eg using the SPPI assessment for both the fair value disclosures and the credit risk disclosures but using HTF and FVM only for the credit risk disclosures) were proposed in the ED. The Board's objective was to propose disclosures for entities applying the temporary exemption from IFRS 9 that were similar to some of the disclosures required to be provided by entities applying IFRS 9, but to primarily rely on the assessment of the contractual terms of the financial assets. The proposals were intended to provide some comparability between entities applying the temporary exemption and those applying IFRS 9, without imposing excessive costs. Accordingly, the Board's proposals reduced the need for an entity to assess the business model for financial assets prior to the application of the new insurance contracts Standard and IFRS 9. Most respondents did not comment on the disclosures proposed in the ED. Those respondents that did comment had mixed views on the appropriateness of the disclosures and only a few of those respondents commented on the scope of the proposed disclosures.

7. However, since the Board has completed its planned redeliberations, some constituents have stated that performing the SPPI assessment on all financial

assets, as would be required to provide the disclosures described in paragraph 4(a), would be unduly burdensome. This because they think that when they eventually apply IFRS 9, they would no longer need to perform the SPPI assessment on some assets measured at fair value through profit or loss (FVPL). This is because those assets would be held in an 'other' business model and would be measured at FVPL irrespective of their contractual cash flows. Two common examples of an 'other' business model are assets that are HFT and assets that are FVM. They note that those assets are typically measured at FVPL applying IAS 39 and relate to investment contract liabilities measured at FVPL or insurance contract liabilities with unit-linking features. Such entities state that when they apply IFRS 9, they would perform the business model assessment first and then perform the SPPI assessment only for those assets in a 'hold to collect' or 'hold to collect and sell' business model.

Staff analysis

8. Staff recommend aligning the scopes used for the quantitative disclosures. That is, we recommend amending the fair value disclosures so that those disclosures are disaggregated using the same grouping of financial assets that are used for the credit risk disclosures (see Table A).

9. Staff think that aligning the scopes of those disclosures will make the fair value disclosures less complex to apply while continuing to meet the Board's objective of requiring disclosures that enable users of financial statements to compare entities applying the temporary exemption from IFRS 9 with entities applying IFRS 9, without imposing excessive costs on preparers.

10. Specifically, staff observes that separately presenting the fair value for the group of financial assets that meet any of the following:

    (a) do <u>not</u> meet the SPPI test; or

    (b) are HFT or FVM;

    would allow users of financial statements to usefully compare entities applying the temporary exemption from IFRS 9 to entities applying IFRS 9.

11. That is because entities applying IFRS 9 are required to separately disclose fair value information for financial assets that are mandatorily measured at FVPL applying IFRS 9 (see IFRS 7 *Financial Instruments: Disclosures* paragraph 8(a)(ii)). Financial assets that are mandatorily measured at FVPL applying IFRS 9 are those with any of the following characteristics:

    (a) do not meet the SPPI test; or

    (b) are held in an 'other' business model; ie a business model whose objective is neither to hold assets to collect contractual cash flow nor to hold to collect contractual cash flows and to sell. Two common examples of that 'other' business model are assets that are HFT and assets that are FVM.

12. Therefore, the staff think that our recommendation means that the disclosures required for entities applying the temporary exemption would be more consistent with the disclosures required for entities applying IFRS 9 and thus, better achieve the Board's objective of improving comparability. Entities applying IFRS 9 are not required to separately disclose the fair value just for financial assets that have cash flows that are not SPPI. This is because an entity applying IFRS 9 is not required to perform the SPPI assessment if it first determines that the assets are held in an 'other' business model.

13. Additionally, our recommendation would not impose any additional costs on preparers compared to what was proposed in the ED (and confirmed by the Board at a previous meeting) – and, in some cases, may be easier to prepare. That is because entities would not be required to perform the 'HFT/FVM assessment' for more assets than was proposed in the ED. Entities can identify Group 1 and Group 2 for the purposes of the fair value disclosures (see Table A) using the same HFT/FVM assessment that is needed to prepare the credit risk disclosures; ie the entity would perform the SPPI assessment for all financial assets and then perform the HFT/FVM assessment only for SPPI assets in the same way as it would have done to prepare the disclosures proposed in the ED. But if an entity does not want to perform the SPPI assessment for all financial assets, it can now choose to perform the HFT/FVM assessment first and then perform the SPPI assessment only for assets that are not HFT/FVM.

Question—Sweep issue

Does the Board agree that, to simplify the disclosures applicable to entities applying the temporary exemption from IFRS 9, the scope for the fair value disclosures should be aligned with the scope for the credit risk disclosures? Accordingly, an entity should disclose the fair value at the end of the reporting period and the change in the fair value during the reporting period for the following two groups of financial assets separately (*text in italics highlights the changes to the groups*):

(a) those financial assets with contractual cash flows that are solely principal and interest, *excluding financial assets that are held for trading or that are managed on a fair value basis*.

(b) all financial assets excluding those described in (a). That is, any financial assets:

(i) that are not solely principal and interest; or

(ii) that are held for trading or managed on a fair value basis.

Next steps

14. The staff will reflect the Board's decisions in the next draft of the Amendments. The staff aim to issue the final amendments to IFRS 4 in September 2016.