STAFF PAPER

March 2019

IFRS® Interpretations Committee meeting

Project	**Curing of a credit-impaired financial asset (IFRS 9)**		
Paper topic	Comment letters		
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1. For ease of reference, this paper reproduces comment letters received on the tentative agenda decision published by the IFRS Interpretations Committee in November 2018 on ‘Curing of a credit-impaired financial asset’.

MASB MALAYSIAN ACCOUNTING STANDARDS BOARD
LEMBAGA PIAWAIAN PERAKAUNAN MALAYSIA

1 February 2019

Ms. Sue Lloyd
Chair
IFRS Interpretations Committee
Columbus Building
7 Westferry Circus
Canary Wharf
London E14 4HD
United Kingdom

Dear Ms. Lloyd

IFRS Interpretations Committee Tentative Agenda Decisions

The Malaysian Accounting Standards Board (MASB) welcomes the opportunity to provide comments on the following Tentative Agenda Decisions published in IFRIC Update December 2018:

(1) Credit enhancement in the measurement of expected credit losses (IFRS 9 *Financial Instruments*).

(2) Curing of a credit-impaired financial asset (IFRS 9 *Financial Instruments*).

(3) Physical settlement of contracts to buy or sell a non-financial item (IFRS 9 *Financial Instruments*).

(4) Sale of output by a joint operator (IFRS 11 *Joint Arrangements*).

(5) Customer's right to access the supplier's software hosted on the cloud (IAS 38 *Intangible Assets*).

We agree with the Committee's decision not to take these issues onto its agenda and we agree with the Tentative Agenda Decisions.

If you need further clarification, please contact the undersigned by email at beeleng@masb.org.my or at +603 2273 3100.

Thank you.

Yours sincerely,

TAN BEE LENG
Executive Director

Unit 13A-1, Menara MBMR, No. 1, Jalan Syed Putra, 58000 Kuala Lumpur.
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Global Financial Reporting Collective
incorporating the Pacioli Initiative

globalfrcollective@gmail.com

4 February 2019

IFRS Interpretations Committee
IFRS Foundation
Columbus Building
7 Westferry Circus
Canary Wharf
London
E14 4HD
United Kingdom

The Global Financial Reporting Collective is pleased to offer its comments on the Tentative Agenda Decision—Curing of a credit-impairment

We agree with conclusions reached by the Committee that that IFRS 9 is clear on this point. We also think that the tentative Agenda Decision is drafted clearly.

We Thank you for considering our comments.

Global Financial Reporting Collective

4 February 2019

About the Global Financial Reporting Collective

The **Global Financial Reporting Collective** is a coalition of academics who support global financial reporting standards and who are motivated to help the IASB to develop high quality standards. The Collective does not have a jurisdictional base. It operates as a virtual, global network.

The Collective was established in 2018. In its initial phase it is managed by a small group of volunteers who analyse IASB proposals and collate comments into comment letters to the IASB. In the second phase the Collective plans to develop a website that will enable a broader range of academics, and practitioners, to provide analysis of proposals. Any comments and input received will not be attributed to an individual. We plan to provide mechanisms to allow individuals to make observations which can then be assessed on their merits, rather than be influenced by the reputation of the submitter—a blind review process.

The primary focus of comments from the Collective is on the clarity and internal and conceptual consistency of proposals, mainly informed from experience with teaching from IFRS Standards or applying them in practice. The Collective does not represent any sector and will not lobby on behalf of any entity or sector to support a particular view.

The purpose of the **Pacioli Initiative** is to make research and learning resources available to the broader community of people using global financial reporting standards. A portal for sharing these resources is being developed as part of the second phase of the Collective. We welcome any input on IFRS-related matters that could be helpful to those who teach or research in this area.

POSITION PAPER

IASB Tentative Agenda Decision — Curing of a credit-impaired financial asset

WSBI (World Savings and Retail Banking Group)
ESBG (European Savings and Retail Banking Group)
Rue Marie-Thérèse, 11 - B-1000 Brussels

ESBG Transparency Register ID 8765978796-80

01.02.2019

WSBI

ESBG

WSBI-ESBG agrees with the technical analysis made by the IFRS Interpretation Committee based on the current IFRS 9 requirements concluding that unrecognised interest should be presented as a credit impairment gain in the profit and loss account following the cure of a credit-impaired financial asset.

Notwithstanding the technical analysis made by the Committee, we believe that the question submitted may lead to a further and deeper analysis of whether the presentation as a credit impairment gain faithfully depicts the economics of companies using IFRS financial statements. In particular, we believe there may be strong arguments in certain jurisdictions to present such amounts in the net interest margin – NIM - based not only on giving more predominance to the nature of the cash flows being recovered but also considering (i) whether the originator of the credit has a contractual unconditional right to deduct from the unrecognised interests the amounts recovered from the debtor, and (ii) internal management practices that rank the precedence of those amounts.

WSBI-ESBG further develops this view below and provides additional comments for your consideration:

- Income and expenses are presented in the profit and loss account usually based on their nature, therefore, the expectation would be that all contractual interests accrued during the life of the credit are reflected, if applicable, within interest margin.
- Interest margin typically reflect the results of financing activity of banks. Registering unrecognised interest in the loss allowance caption would lead users of financial data to distorted ratios for example on the loan average profitability.
- Users also expect that 'reversal of loss allowance' corresponds to the amounts previously recognised for this concept in the profit and loss account. Impairment gains, although possible in accordance with IFRS 9, are not very understandable and difficult to explain.
- General accepted practice is to allocate the amounts recovered first to past due interests when such a right is established within contractual terms or prior to beginning with the formal recovery process for a credit-impaired financial assets that is past-due In such cases, financial entities may consider that first they recover the interests accrued for late payment, then the contractual interest, and lastly the pending principal. Among other reasons for setting up such a rank would be increasing the probability to recover the unrecognised interests if a claim was filled with the debtor in case of new defaults.
- Once the debtor is no longer in the repayment process, but in the recovery phase, then we would agree that general accepted practice is to give precedence in any amounts being recovered (either in cash or forborne assets) to the pending principal before considering that any interests were recovered. In such cases the expected loss is very probable and financial entities-objective is to minimize such loss.
- As stated in B.5.5.2 of IFRS 9, typically, credit risk increases significantly before a financial instrument becomes past due or other lagging borrower-specific factors are observed (for example, a modification or restructuring). In those cases lifetime expected credit losses are recognised and interests are calculated by applying effective interest rate to the amortized cost of the asset. It can be misleading for users of financial statements that part of contractual interests of financial assets in which a significant increase in credit risk have been identified but which are paying in accordance of the contractual terms, are recognised in the loss allowance caption of the profit and loss account and not in interest margin. Such types of debtors have not yet entered into the repayment or recovery process.
- We note that the Committee decision is silent on whether written-off loans – off-balance sheet figures – that may be recovered later should be also treated in the same way. We believe that for these written-off loans that are subsequently cured, any amount recovered is expected to reduce the cost of risk previously recognised and would agree only for these type of exposures

to recognise a credit impairment gain. Recognising these amounts in the interest margin will distort average ratios of the loan portfolio on balance.

As a consequence WSBI-ESBG considers that it would be reasonable if entities could apply an accounting policy choice that permits a better alignment of the amounts presented in NIM with their credit risk management practices, in particular, considering the order of payment priority that entities have internally defined and the contractual terms of their loan portfolios, allowing to recognize in NIM the amounts recovered when there is economic substance and/or contractual evidence.

About WSBI (World Savings and Retail Banking Institute)

(Boiler plate)

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About ESBG (European Savings and Retail Banking Group)

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Published by WSBI-ESBG. [Date]

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IFRS Interpretations Committee
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5 February 2019

Re: IFRS Interpretations Committee tentative agenda decisions published in the November 2018 IFRIC Update

Dear Ms Lloyd,

We are pleased to have the opportunity to provide our comments on the IFRS Interpretations Committee ("the Committee") tentative agenda decisions included in the September 2018 IFRIC Update.

Our comments refer to the following issues:

a. *Physical settlement of contracts to buy or sell a non-financial item (IFRS 9 Financial Instruments);*
b. *Customer's right to access the supplier's software hosted on the cloud (IAS 38 Intangible Assets);*
c. *Curing of a credit-impaired financial asset (IFRS 9 Financial Instruments).*

[...]

[...]

Curing of a credit-impaired financial asset (IFRS 9)

In summary, in its tentative agenda decision the Committee observes that:

- applying paragraph 5.5.8 of IFRS 9, an entity recognises in profit or loss as a reversal of expected credit losses the adjustment required to bring the loss allowance to the amount that is required to be recognised in accordance with IFRS 9 (zero if the asset is paid in full).
- The amount of this adjustment includes the effect of the unwinding of the discount on the loss allowance during the period that the financial asset was credit-impaired.
- Accordingly, following the curing of the credit-impaired financial asset, an entity is required to present in the statement of profit or loss the difference between the interest calculated on the gross carrying amount and the interest income recognised for credit-impaired financial assets ("the unrecognised interest") as a reversal of impairment losses.
- The requirements in existing IFRS Standards are adequate.

We think that IFRS 9 does not specify that the amount of adjustment referred to in paragraph 5.5.8. of IFRS 9 includes the effect of the unwinding of the discount on the loss allowance. Consequently, we disagree with the Committee's conclusion that the requirements in existing IFRS Standards are adequate. Indeed, we have been informed that there are diverging views on this issue. Some share the view of the Committee, whilst some other believe that such a reversal should be presented as interest revenues. We believe that both the views are correct being IFRS 9 not sufficiently clear on this.

We are aware that this issue is material in the banking industry; thus we think that the Committee should:

- propose an amendment to IFRS 9 to clarify the presentation in the statement of profit or loss of the unrecognised interest; and
- amend its decision in order to permit entities (in the meantime) to present the unrecognised interest as a reversal of impairment losses or as interest revenue (ie entities have an accounting policy choice in presenting the unrecognised interest).

Should you need any further information, please do not hesitate to contact us.

Yours sincerely,

Angelo Casò
(Chairman)

6th February, 2019

To,
Ms Sue Lloyd,
Chair, IFRS Interpretations committee,
IFRS Foundation,
London, UK

Dear Ms Sue,

Subject: Tentative Agenda Decision (TAD) Nov 2018 – Public Comments by Feb 6th, 2019

Thank you for giving us an opportunity to comment on the six tentative agenda decisions of IFRS Interpretation Committee published in Nov 2018. Our comments and concerns on TADs are given in the attachment and we hope you will find those useful and relevant. IFRIC Interpretation Committee is requested to consider our concerns appropriately to depict true and fair view and economic substance of the transactions/events.

The Institute of Chartered Accountants of India (the ICAI) , is the premier accounting body of India established way back 1949 as one of the primary building block of nation building, of Independent India. Over the last seven decades, the ICAI has grown in many professional areas and today it is second largest body of accountants in the World. The ICAI with its great vision and relentless mission to serve the public interest, domestic and global, has earned title of "Partner in Nation Building" in an emerging economy which is sixth largest by GDP and the fastest growing capital market in Asia.

Please feel free to contact CA. Vidhyadhar Kulkarni, Head, Technical Directorate, (email: vidhyadhar.kulkarni@icai.in or asb@icai.in) for any clarifications or discussion.

Thanking you,

Yours faithfully,

CA.S.B.Zaware,

Chairman, ASB, ICAI

New Delhi, India

ICAI Comments on IFRS IC Tentative Agenda Decisions
Due date Feb 6, 2019

Tentative agenda decision (TAD): Presentation of unrecognised interest following the curing of a credit-impaired financial asset (IFRS 9)

In our view, while the TAD may appear to be broadly in line with the text of the IFRS 9, but when one looks at it from the fundamental concepts of preparation of general purpose financial statements such true and fair view, economic substance etc, it raises some discomfort highlighted below. Therefore, we are unable to support the conclusion drawn in the above referred TAD.

1) Primary reason for our concern is that the TAD completely changes the true underlying nature of the income from "Interest income" to "Impairment Gain" simply due to the way certain definitions (Amortised Cost, Gross Carrying Amount etc.) are drafted. In particular, Staff Paper supporting the TAD conclusion heavily relies on the definition of gross carrying amount, which in the context of Credit Impaired Assets has limited relevance in the context of disclosure under paragraph 35 of IFRS 7 Financial Instruments Disclosure. Therefore, we are of the view that it is not appropriate that the underlying end nature of an income suddenly changes its colour completely just because a particular financial asset was classified as credit-impaired during some part of its life cycle.

2) We also have some concerns about the staff conclusion and suggestion in paragraphs 34-38 of Agenda Paper 7 of Nov 2018 meeting. Paragraph 36 of the Agenda paper states that unrecognised interest will be debited to Impairment charge in profit or loss with corresponding credit to ECL. Secondly, reading of paragraph 40 in the Agenda paper suggests to credit the Impairment Charge in P/L to account for the missing account for credit entry in paragraph 34 to record the unrecognised interest. As a result, there is no net charge to P/L as Impairment Charge in relation to unrecognised interest. It is this supposition in paragraph 40 of the TAD (that the corresponding entry for increasing the GCA by the amount of unrecognised interest should also be made to the credit impairment line), which ultimately leads the Staff's argument in para 43 that "…the entity also reverses the unwinding of discount on the ECL through the same line in which it was initially presented. When the asset cures, the entity records the following journal entries, which in our view faithfully reflect that all impairment losses previously recognised are now fully reversed…". In our view, an alternate accounting solution needs to be found out which leads to recognition of the received amounts as per their true nature. We do understand the challenge to find a sound technical solution when the text of standard appears to portray significantly different result from the economic substance of the transaction/event.

3) In our view, on an overall consideration of the theoretical and practical aspects, View 2 i.e. to credit the unrecognised interest to 'interest in suspense' account in the statement of financial position and not in profit or loss through the credit impairment line, is the most appropriate one. Incidentally, this approach is similar to an option given in US GAAP to place certain credit impaired financial assets on 'Non-Accrual' basis and the practice followed under IAS 39 by many Banks and Financial Institutions.

4) At the end, we strongly recommend IFRS IC NOT to issue this TAD and refer the matter to IASB for making narrow scope amendments to IFRS 9, if required in the light of above concerns.

Deloitte.

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6 February 2019

Sue Lloyd
Chair
IFRS Interpretations Committee
Columbus Building
7 Westferry Circus
Canary Wharf
London
United Kingdom
E14 4HD

Dear Ms Lloyd

Tentative agenda decision – IFRS 9 *Financial Instruments*: Curing of a credit-impaired financial asset

Deloitte Touche Tohmatsu Limited is pleased to respond to the IFRS Interpretations Committee's publication in the November IFRIC Update of the tentative decision not to take onto the Committee's agenda the request for clarification on how to present amounts recognised in profit or loss when a credit-impaired financial asset is either paid in full or is determined to be no longer credit-impaired.

We agree with the IFRS Interpretations Committee's decision not to add this item onto its agenda for the reasons set out in the tentative agenda decision.

If you have any questions concerning our comments, please contact Veronica Poole in London at +44 (0) 20 7007 0884.

Yours sincerely

Veronica Poole
Global IFRS Leader

6th February 2019

Mrs Sue Lloyd

IFRS Interpretation Committee

Columbus Building
7 Westferry Circus - Canary Wharf
London E14 4HD - UNITED KINGDOM

Re: Tentative Agenda Decision – Curing of a credit-impaired financial asset (IFRS 9)

Dear Sue,

We are pleased to provide our comments on the above Tentative Agenda Decision.

The issue that has been brought to the IFRS IC is related to both interest income and income and expense on credit risk allowances (also called "cost of risk" in the income statement of financial institutions). The question raised does not affect the net income of the entity, but only the presentation of these two components in the income statement. Similarly, it does not affect the value of the net amortised cost of the debt financial assets measured at amortised cost, but only the respective amounts of their gross amortised cost and of the related credit risk allowances.

When answering to the question about the curing of a credit-impaired financial asset, the Interpretation Committee observed that, applying paragraph 5.5.8 of IFRS 9, an entity recognises in profit or loss as a reversal of expected credit losses the adjustment required to bring the loss allowance to the amount that is required to be recognised in accordance with IFRS 9 (zero if the asset is paid in full). The Interpretation Committee also concluded that the reversal of impairment losses may exceed the impairment losses recognised in profit or loss over the life of the asset.

Such effect is based on the application of the conclusions of previous ITG agenda papers dealing with the presentation of interest income on credit-impaired financial assets which leads to increasing the amount of credit risk allowances without any counterparty in the income statement. We find quite surprising that the Interpretation Committee endorsed such conclusions of the ITG whereas the ITG is not supposed to issue guidance or assimilated interpretation. For being considered as an applicable interpretation, such previous conclusions should have been issued by the Interpretation Committee itself after the usual due process.

We consider that the previous conclusions of the ITG are questionable due to some inconsistencies that currently exist in the standards between different definitions. You will find in appendix 1 our analysis of the ITG conclusions. Assuming no further loss is expected, the approach endorsed by the ITG results in an increase in the amount of the credit risk allowance over time that is not presented as an impairment loss, even though all movements in the allowance are required by IAS 1 to be reported in a separate line in the income statement. We also provide an alternative view on that question and we have disclosed in appendix 2 the references we used in IFRS 9 and IAS 1. Indeed, we consider that since the expectations of cash-flow recoveries remain unchanged (because the creditworthiness of the borrower remains unchanged, without subsequent improvement and without subsequent deterioration), there should be no further loss for credit risk.

We have understood that the Interpretation Committee has built its conclusion about the curing of credit-impaired financial assets on the basis of the ITG's previous conclusions. As far as according to these conclusions, credit risk allowances are supposed to grow over time without recognising any additional impairment loss in the income statement, the Interpretation Committee has concluded that the reversal of impairment losses may exceed the impairment losses recognised in profit or loss over the life of the cured financial asset.

In appendix 3, we have developed the illustrative example provided in Staff Paper 7 (November 2018) and we have built an alternative proposal based on the impairment gains or losses definition provided by paragraph 5.5.8 of IFRS 9 and on the requirement of paragraph 82 of IAS 1 requiring the presentation on a single line of the income statement of impairment losses (including reversals of impairment losses or impairment gains) determined in accordance with Section 5.5 of IFRS 9.

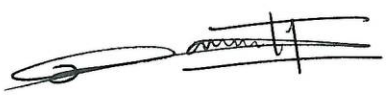
This alternative proposal illustrated in appendix 3 leads to a cumulative impairment loss of zero in case of a full recovery of all amounts due (curing of the credit-impaired asset). We consider that a loan at amortised cost that might have been temporarily credit-impaired and subsequently cured, i.e. transferred from Stage 3 to Stage 2 or fully recovered, should depict the same cumulative economic return as a loan maintained in Stage 2. It means that in both cases, this economic return should be reflected as an interest income rather than an impairment gain.

It should be underlined that in both approaches (the ITG / Interpretation Committee's one, and the alternative approaches illustrated in the appendices here below), the measurement of the financial assets is the same (amortised cost measurement), and the impact of credit risk assessment is the same as well (based on the expected loss approach of IFRS 9). In both cases, the net income is the same, and the amortised cost of the asset (after deduction of credit-risk allowance) is the same as well. It means that beyond the debate around definitions, the issue could also be addressed from the angle of Better Communication. Consequently, we think that the issue could be addressed on a more comprehensive way to include consideration that are closed to the purpose of the Better Communication project currently held by IASB (What is meaningful in the Income Statement? How to make information clear and understandable? Etc…).

Should the Interpretation Committee share these fact that some unintended inconsistencies currently exist between the different definitions provided by IFRS 9 and the accompanied amendments introduced in IAS 1, we would then encourage the Committee to extend its analysis and to measure how our proposed approach could contribute to a better communication. Should the definitions introduced in the newly applicable standards be a potential obstacle to the objective of providing a better communication through financial statements, the Interpretation Committee could also assess whether the issue should be addressed to the board itself.

We hope you will find our comments and illustrations useful to the Interpretation Committee. If you have any query regarding our comments, please do not hesitate to contact me at:
Pierre-Henri.Damotte@socgen.com

Sincerely yours,



Pierre-Henri DAMOTTE

Accounting Public Affairs

IFRIC Update – November 2018

Curing of a credit-impaired financial asset (IFRS 9 Financial Instruments)—Agenda Paper 7

The Committee received a request about how an entity presents amounts recognised in the statement of profit or loss when a credit-impaired financial asset is subsequently cured (ie paid in full or no longer credit-impaired).

When a financial asset becomes credit-impaired, paragraph 5.4.1(b) of IFRS 9 requires an entity to calculate interest revenue by applying the effective interest rate to the amortised cost of the financial asset. This results in a difference between (a) the interest that would be calculated by applying the effective interest rate to the gross carrying amount of the credit-impaired financial asset, and (b) the interest revenue recognised for that asset. The request asked whether, following the curing of the financial asset, an entity can present this difference as interest revenue or, instead, is required to present it as a reversal of impairment losses.

Appendix A to IFRS 9 defines a credit loss as 'the difference between all contractual cash flows that are due to an entity in accordance with the contract and all the cash flows that the entity expects to receive (ie all cash shortfalls), discounted at the original effective interest rate...'. Appendix A also defines the gross carrying amount as 'the amortised cost of a financial asset, before adjusting for any loss allowance'. The Committee noted that, based on the definitions in Appendix A to IFRS 9, the gross carrying amount, amortised cost and loss allowance are discounted amounts, and changes in these amounts during a reporting period include the effect of the unwinding of the discount.

Paragraph 5.5.8 of IFRS 9 requires an entity to 'recognise in profit or loss, as an impairment gain or loss, the amount of expected credit losses (or reversal) that is required to adjust the loss allowance at the reporting date to the amount that is required to be recognised in accordance with this Standard'.

The Committee observed that, applying paragraph 5.5.8 of IFRS 9, an entity recognises in profit or loss as a reversal of expected credit losses the adjustment required to bring the loss allowance to the amount that is required to be recognised in accordance with IFRS 9 (zero if the asset is paid in full). The amount of this adjustment includes the effect of the unwinding of the discount on the loss allowance during the period that the financial asset was credit-impaired, which means the reversal of impairment losses may exceed the impairment losses recognised in profit or loss over the life of the asset. Accordingly, the Committee concluded that, in the statement of profit or loss, an entity is required to present the difference described in the request as a reversal of impairment losses following the curing of a credit-impaired financial asset.

The Committee concluded that the requirements in existing IFRS Standards provide an adequate basis for an entity to recognise and present the reversal of expected credit losses following the curing of a credit-impaired financial asset in the fact pattern described in the request. Consequently, the Committee [decided] not to add this matter to its standard-setting agenda.

Appendix 1

IFRS 9 – An analysis for the presentation of income and expense related to credit risk

The issuance of IFRS 9 has also introduced amendments to existing standards. Paragraph 82 of IAS 1 has been updated to include new requirements for the presentation in the income statement of a separate line for impairment losses (including reversals of impairment losses or impairment gains).

Definition of *impairment gains or losses* is provided in the appendix A of IFRS 9. This definition refers to paragraph 5.5.8 of IFRS 9.

According to paragraph 5.5.8, these *impairment gains or losses* are the amount of *expected credit losses (or reversal)* that is required to adjust the *loss allowance* at the reporting date.

In appendix A, definitions of *expected credit losses* and of *loss allowance* then lead to refer to the definition of *credit loss*. According to this definition, *credit loss* is the difference between (i) all contractual cash flows that are due to an entity in accordance to the contract and (ii) the discounted amount of all the cash flows that the entity expects to receive. It shall be noted that contractual cash flows that are due shall then include all contractual interests that are due and that still remain unpaid.

Consistently with the definition of *credit loss*, the *gross carrying amount* is defined as the amortised cost of the of the financial asset before adjusting for any *loss allowance*.

Applying these definitions for determining the amount of the amortised cost of the asset before allowance and the amount of the allowance mechanically leads to present on the line *Impairment loss* in the income statement some losses that are linked to the time flow and not to any change in the creditworthiness of the counterparty.

Illustration:

Case 1 based on the example provided by the ITG

Contractual terms of the loan							
Full reimbursment in fine							
Yearly payment of interest							
Principal	100						
EIR	10%						
		31/12/N before depreciation	**31/12/N after depreciation**	**31/12/N+1**	**31/12/N+2**	**31/12N+3**	**31/12/N+4**
Contractual cash flows				10	10	10	110
Expected cach flows as at 31/12/N,				0	0	0	60
(expectations remain unchanged until 31/12/N+4)							
Present value of expected cash flows		100	41,0	45,1	49,6	54,5	60,0
(at the end of each period)							
Balance sheet - Assets							
Gross carrying amount (including amounts due but unpaid)			100	110	120	130	140
Depreciation (loss allowance)			-59,0	-64,9	-70,4	-75,5	-80,0
Net amortised cost			41,0	45,1	49,6	54,5	60,0
Coverage rate (depreciation / gross carrying amount)			*-59%*	*-59%*	*-59%*	*-58%*	*-57%*
Income statement							
Interest income			0	10	10	10	10
Cost of risk (impairment losses)			-59,0	-5,9	-5,5	-5,0	-4,5
Net income before tax			-59,0	4,1	4,5	5,0	5,5
Variations of the present value of expected cash flows			*-59,0*	*4,1*	*4,5*	*5,0*	*5,5*

Case 2 illustrating an extreme situation where the expected recoverable amounts are very low

Contractual terms of the loan	
Full reimbursment in fine	
Yearly payment of interest	
Principal	100
EIR	10%

	31/12/N before depreciation	31/12/N after depreciation	31/12/N+1	31/12/N+2	31/12N+3	31/12/N+4
Contractual cash flows			10	10	10	110
Expected cach flows as at 31/12/N, (expectations remain unchanged until 31/12/N+4)			0	0	0	10
Present value of expected cash flows (at the end of each period)	100	6,8	7,5	8,3	9,1	10,0
Balance sheet - Assets						
Gross carrying amount (including amounts due but unpaid)		100	110	120	130	140
Depreciation (loss allowance)		-93,2	-102,5	-111,7	-120,9	-130,0
Net amortised cost		6,8	7,5	8,3	9,1	10,0
Coverage rate (depreciation / gross carrying amount)		*-93%*	*-93%*	*-93%*	*-93%*	*-93%*
Income statement						
Interest income		0	10	10	10	10
Cost of risk (impairment losses)		-93,2	-9,3	-9,2	-9,2	-9,1
Net income before tax		-93,2	0,7	0,8	0,8	0,9
Variations of the present value of expected cash flows		*-93,2*	*0,7*	*0,8*	*0,8*	*0,9*

In these two examples, the credit risk is supposed to have been correctly assessed since 31/12/N and expected recoverable cash flows are supposed to be effectively received without any enhancement or degradation of the counterparty's creditworthiness. Applying definitions provided by IFRS 9 then leads to present a stable ratio of coverage (credit allowance / gross carrying amount of the asset).

But, in the same time, the presentation on a single line of the income statement of impairment losses (including reversals of impairment losses or impairment gains), as required by IAS 1, leads to present a Cost of risk on this line that is not nil between year N+1 and N+4 : there are credit losses presented on this line each year, despite the absence of any further deterioration of the counterparty's creditworthiness. In these examples, the sole time flow is the cause of a credit loss presented as such in the income statement. Looking at such recurring credit losses, users of financial statements may question the quality and the relevance of the risk management and of the estimation of credit risk at the end of year N.

The counterparty for the annual increase of credit allowance is an enhancement of interest income: in the income statement, interest income is then still presenting all contractual interest. It seems inconsistent with the increase of the net amount of the asset due to the sole time flow (as far as the counterparty's creditworthiness remains unchanged), this increase which then corresponds the reversal of the discounting effect of expected cash flows using the effective interest rate.

This symmetrical adjustment of credit losses (to reflect the mechanical increase of the allowance) and interest income is inconsistent with the definition of interest revenues provided by paragraph 5.4.1 b) of IFRS 9: "for those financial assets, the entity shall apply the effective interest rate to the amortised cost of the financial asset in subsequent reporting periods". The EIR is said to be applied to the amortised cost of the asset (i.e.; after adjustment for credit allowance), and not to its gross carrying amount.

Such inconsistency, and the related counterintuitive effects for users of financial statements, are stressed when expected recoverable amounts are low (Cf. case 2).

Solution provided by the ITG:

The approach provided by the ITG consists in

(i) recognising interest income in the income statement by applying the EIR to the net amortised cost of the loan (i;e; after deduction of allowance for credit risk), and
(ii) incrementing the gross carrying amount of the loan in the balance sheet with all contractual interest, and
(iii) incrementing the depreciation for credit risk in the balance sheet for the difference between these two previous amounts.

Application to the example provided in case 2 is the following:

Contractual terms of the loan	
Full reimbursment in fine	
Yearly payment of interest	
Principal	100
EIR	10%

	31/12/N before depreciation	31/12/N after depreciation	31/12/N+1	31/12/N+2	31/12N+3	31/12/N+4
Contractual cash flows			10	10	10	110
Expected cach flows as at 31/12/N, (expectations remain unchanged until 31/12/N+4)			0	0	0	10
Present value of expected cash flows (at the end of each period)	100	6,8	7,5	8,3	9,1	10,0
Balance sheet - Assets						
Gross carrying amount (including amounts due but unpaid)		100	110	120	130	140
Depreciation (loss allowance)		-93,2	-102,5	-111,7	-120,9	-130,0
Net amortised cost		6,8	7,5	8,3	9,1	10,0
Coverage rate (depreciation / gross carrying amount)		*-93%*	*-93%*	*-93%*	*-93%*	*-93%*
Income statement						
Interest income		0	0,7	0,8	0,8	0,9
Cost of risk (impairment losses)		-93,2	0,0	0,0	0,0	0,0
Net income before tax		-93,2	0,7	0,8	0,8	0,9
Variations of the present value of expected cash flows		*-93,2*	*0,7*	*0,8*	*0,8*	*0,9*

But in such a case, adjustments of impairment losses (depreciation) during the year N+1, N+2, N+3 and N+4 are not recognised in the income statement as they should be according to paragraph 5.5.8 of IFRS 9 and paragraph 82 of IAS 1.

Alternative approach that could be considered:

To solve the issue, another approach could be considered that would treat consistently the interest in the income statement and in the balance sheet by recognising an amount of interest determined by applying the EIR to the only net amortised cost of the loan (i.e. after deduction of allowance for credit risk).

Application to the example provided in case 2 is the following:

Contractual terms of the loan	
Full reimbursment in fine	
Yearly payment of interest	
Principal	100
EIR	10%

	31/12/N before depreciation	31/12/N after depreciation	31/12/N+1	31/12/N+2	31/12N+3	31/12/N+4
Contractual cash flows			10	10	10	110
Expected cach flows as at 31/12/N, (expectations remain unchanged until 31/12/N+4)			0	0	0	10
Present value of expected cash flows (at the end of each period)	100	6,8	7,5	8,3	9,1	10,0
Balance sheet - Assets						
Gross carrying amount (including amounts due but unpaid)		100	100,7	101,4	102,3	103,2
Depreciation (loss allowance)		-93,2	-93,2	-93,2	-93,2	-93,2
Net amortised cost		6,8	7,5	8,3	9,1	10,0
Coverage rate (depreciation / gross carrying amount)		*-93%*	*-93%*	*-92%*	*-91%*	*-90%*
Income statement						
Interest income		0	0,7	0,8	0,8	0,9
Cost of risk (impairment losses)		-93,2	0,0	0,0	0,0	0,0
Net income before tax		-93,2	0,7	0,8	0,8	0,9
Variations of the present value of expected cash flows		*-93,2*	*0,7*	*0,8*	*0,8*	*0,9*

Interest income in the income statement would be then the same as the one presented according to IASB's approach.

But the Cost of risk in the income statement would be different as far as it would be nil between N+1 and N+4 consistently with the absence of any increase or decrease of depreciation in the balance sheet, but also consistently with the absence of any deterioration or improvement of the creditworthiness of the counterparty during these periods.

Curing of the loan:

In this alternative approach, if the loan is cured by a full repayment at the beginning of year N+5, the reversal of impairment losses previously recognised would be recorded in the income statement under Cost of risk (as required by IAS 1) for an amount of 93,2.

The payment of all amounts due would generate an additional income of 36,8 (140 – 103,2), presented as interest income. Then, the cumulative interest income recognised over all the reporting periods between the issuance of the loan and its full reimbursement would be equal to 40, which would be then the same amount as the cumulative interest income that would have been recognised as interest income if the loan would have remained performing during all these reporting periods.

Similarly, the cumulative cost of risk (impairment losses and gains) would be equal to zero, as if the loan would have remained performing during all the reporting periods. This is consistent with the analysis performed for credit risk management purpose which consider that the lender has not suffer from any credit risk over the life of the loan if all amounts due are fully paid at the end of the day (including interest in arrear that have been ignored in the examples provided here-before in order to simplify their reading).

Appendix 2

References to IFRS 9, and course between definitions

1st step: IFRS 9 – Appendix C

C22:

IAS 1 *Presentation of Financial Statements*

82 In addition to items required by other IFRSs, the profit or loss section or the statement of profit or loss shall include line items that present the following amounts for the period :
(a) revenue, presenting separately interest revenue calculated using the effective interest method ;
(aa) gains and losses arising from the derecognition of financial assets measured at amortised cost ;
(b) finance costs ;
(ba) impairment losses (including reversals of impairment losses or impairment gains) determined in accordance with Section 5.5 of IFRS 9 ;
(c) share of the profit or loss of associates and joint ventures accounted for using the equity method ;
(ca) if a financial asset is reclassified out of the amortised cost measurement category so that it is measured at fair value through profit or loss, any gain or loss arising from a difference between the previous amortised cost of the financial asset and its fair value at the reclassification date (as defined in IFRS 9) ;
(cb) if a financial asset is reclassified out of the fair value through other comprehensive income measurement category so that it is measured at fair value through profit or loss, any cumulative gain or loss previously recognised in other comprehensive income that is reclassified to profit or loss ;
(d) ...

2nd step: IFRS 9 – Appendix A

Impairment gain or loss

Gains or losses that are recognised in profit or loss in accordance with paragraph 5.5.8 and that arise from applying the impairment requirements in Section 5.5.

3rd step: IFRS 9

5.5.8 An entity shall recognise in profit or loss, as an impairment gain or loss, the amount of expected credit losses (or reversal) that is required to adjust the loss allowance at the reporting date to the amount that is required to be recognised in accordance with this Standard.

4th step: IFRS 9 – Appendix A

Loss allowance
The allowance for **expected credit losses** on financial assets measured in accordance with paragraph 4.1.2, lease receivables and **contract assets,** the accumulated impairment amount for financial assets measured in accordance with paragraph 4.1.2A and the provision for expected credit losses on loan commitments and **financial guarantee contracts.**

Expected credit losses

The weighted average of **credit losses** with the respective risks of a default occurring as the weights.

Credit loss

The difference between all contractual cash flows that are due to an entity in accordance with the contract and all the cash flows that the entity expects to receive (ie all cash shortfalls), discounted at the original **effective interest rate** (or **credit-adjusted effective interest rate** for **purchased or originated credit-impaired financial assets**). An entity shall estimate cash flows by considering all contractual terms of the financial instrument (for example, prepayment, extension, call and similar options) through the expected life of that financial instrument. The cash flows that are considered shall include cash flows from the sale of collateral held or other credit enhancements that are integral to the contractual terms. There is a presumption that the expected life of a financial instrument can be estimated reliably. However, in those rare cases when it is not possible to reliably estimate the expected life of a financial instrument, the entity shall use the remaining contractual term of the financial instrument.

5th step: IFRS 9 – Appendix A

Gross carrying amount of a financial asset

The **amortised cost of a financial asset,** before adjusting for any **loss allowance.**

Interest revenue dans IFRS 9

5.4.1

Interest revenue shall be calculated by using the effective interest method (see Appendix A and paragraphs B5.4.1-B5.4.7). This shall be calculated by applying the effective interest rate to the gross carrying amount of a financial asset except for:

(a) purchased or originated credit-impaired financial assets. For those financial assets, the entity shall apply the credit-adjusted effective interest rate to the amortised cost of the financial asset from initial recognition.
(b) financial assets that are not purchased or originated credit-impaired financial assets but subsequently have become credit-impaired financial assets. For those financial assets, the entity shall apply the effective interest rate to the amortised cost of the financial asset in subsequent reporting periods.

Amortised cost of a financial asset or financial liability

The amount at which the financial asset or financial liability is measured at initial recognition minus the principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between that initial amount and the maturity amount and, for financial assets, adjusted for any loss allowance.

Appendix 3

Development of the illustrative example provided in Staff Paper 7 (November 2018) and alternative proposal

The development presented here are based on the illustrative example provided by the Staff in the agenda paper 7 issued for the IFRS IC meeting of November 2018.

Based on the data of the example, the accounting entries are detailed, and final balance sheets are presented at the end of each reporting period. The following

IFRS IC preferred view

Year 1

Origination of the loan	Debit	B/S	Customer loan	100	
	Credit	B/S	Funding		100
Interest payment	Debit	B/S	Cash	26,4	
	Credit	B/S	Customer loan		16,4
	Credit	P/L	Interest income		10
Credit risk	Debit	P/L	Cost of risk	66	
	Credit	B/S	Allowance for credit risk		66

Balance sheet at the end of Year 1

Customer loan (gross amount)	83,6	Funding		100
Allowance for credit risk	-66			
		Interest income	*10*	
Net	17,6	*Cost of risk*	*-66*	
Cash	26,4	Net income		-56
Total	44	Total		44

Year 2

Interest recognition	Debit	B/S	Customer loan	1,8	
	Credit	P/L	Interest income		1,8
Credit risk	Debit	B/S	Customer loan	6,6	
	Credit	B/S	Allowance for credit risk		6,6

Balance sheet at the end of Year 2

Customer loan (gross amount)	92		Funding	100
Allowance for credit risk	-72,6		Retained earnings	-56
Net	19,4			
			Interest income	*1,8*
Cash	26,4		Net income	1,8
Total	45,8		Total	45,8

Year 3

Interest recognition	Debit	B/S	Customer loan	1,9	
	Credit	P/L	Interest income		1,9
Credit risk	Debit	B/S	Customer loan	7,3	
	Credit	B/S	Allowance for credit risk		7,3

Balance sheet at the end of Year 3

Customer loan (gross amount)	101,2		Funding	100
Allowance for credit risk	-79,9		Retained earnings	-54,2
Net	21,3			
			Interest income	*1,9*
Cash	26,4		Net income	1,9
Total	47,7		Total	47,7

Year 4

Full reimbursment	Debit	B/S	Cash	101,2	
	Credit	B/S	Customer loan		101,2
Credit risk	Debit	B/S	Allowance for credit risk	79,9	
	Credit	P/L	Cost of risk		79,9

Balance sheet at the end of Year 4

Customer loan (gross amount)	0	Funding	100
Allowance for credit risk	0	Retained earnings	-52,3
Net	0		
		Cost of risk	*79,9*
Cash	127,6	Net income	79,9
Total	127,6	Total	127,6

Cumulative amount over years 1 to 4:

Interest income	13,7
Cost of risk	13,9
Net income	27,6

Comments:

- this illustration shows that even if the loan if fully repaid, including interest due and compound interest for late payment, the cumulative cost of risk (net amount of income and expense on allowances for credit risk) is not zero.
- It also illustrates that allowances are incremented each year for an amount that is not recognized in P&L, as far as the ITG approach is applied, leading to a counterintuitive presentation (the credit risk is not growing, but the allowances are).

An alternative approach is illustrated hereafter, based on the same example.

Alternative view

Year 1

Origination of the loan	Debit	B/S	Customer loan	100	
	Credit	B/S	Funding		100
Interest payment	Debit	B/S	Cash	26,4	
	Credit	B/S	Customer loan		16,4
	Credit	P/L	Interest income		10
Credit risk	Debit	P/L	Cost of risk	66	
	Credit	B/S	Allowance for credit risk		66

Balance sheet at the end of Year 1

Customer loan (gross amount)		83,6	Funding		100
Allowance for credit risk		-66			
	Net	17,6	*Interest income*	*10*	
			Cost of risk	*-66*	
Cash		26,4	Net income		-56
Total		44	Total		44

Year 2

Interest recognition	Debit	B/S	Customer loan	1,8	
	Credit	P/L	Interest income		1,8

Balance sheet at the end of Year 2

Customer loan (gross amount)		85,4	Funding		100
Allowance for credit risk		-66	Retained earnings		-56
	Net	19,4			
			Interest income	*1,8*	
Cash		26,4	Net income		1,8
Total		45,8	Total		45,8

Year 3

Interest recognition	Debit	B/S	Customer loan	1,9	
	Credit	P/L	Interest income		1,9

Balance sheet at the end of Year 3

Customer loan (gross amount)		87,3	Funding		100
Allowance for credit risk		-66	Retained earnings		-54,2
	Net	21,3			
			Interest income	*1,9*	
Cash		26,4	Net income		1,9
Total		47,7	Total		47,7

Year 4

Full reimbursement	Debit	B/S	Cash	101,2	
	Credit	B/S	Customer loan		87,3
	Credit	P/L	Interest income		13,9
Credit risk	Debit	B/S	Allowance for credit risk	66	
	Credit	P/L	Cost of risk		66

Balance sheet at the end of Year 4

Customer loan (gross amount)	0	Funding	100
Allowance for credit risk	0	Retained earnings	-52,3
		Interest income	*13,9*
Net	0	*Cost of risk*	*66*
Cash	127,6	Net income	79,9
Total	127,6	Total	127,6

Cumulative amount over years 1 to 4:

Interest income	27,6
Cost of risk	0
Net income	27,6

Cumulative amount of contractual interest at the end of year 3 would have been:	25
Difference with cumulative amount of interest income recognised in P/L:	2,7

=> these additional interests are compound interest on amounts paid later than contractually due.

Comments:

- Cumulatively, the cost of risk (net amount of income and expense on allowances for credit risk) is nil. This is consistent with the fact that the lender has not suffered any loss at the end of the story (all contractual amounts are paid, including additional interest for late payments). This is also consistent with a loan that would have been fully repaid but without the borrower having suffered from temporary difficulties.
- In this approach, allowances are not growing while credit risk remains stable. It leads to show no cost of risk in P&L and no increase of allowances when credit risk remains stable, which is consistent with requirement of IAS 1 – paragraph 82. Additionally, this alternative approach is in line with credit risk management performed by Risk Departments of financial institutions.
- It also helps to deliver through the balance sheet and through the income statement a better and more understandable communication about the performance of the entity regarding credit risk.

Rio de Janeiro, February 06, 2019

CONTRIB 0009/2019

Ms Lloyd
International Accounting Standards Board
Columbus Building
7 Westferry Circus
Canary Wharf
London
E14 4HD, UK.

Subject: Tentative Agenda Decision

Reference: Curing of a credit-impaired financial asset

Dear Ms Lloyd,

Petróleo Brasileiro S.A. - Petrobras welcomes the opportunity to comment on the IFRS Interpretations Committee's tentative agenda decision - Curing of a credit-impaired financial asset.

We believe this is an important opportunity for all parties interested in the future of IFRS and we hope to contribute to the progress of the Board's activities.

We do not agree with the Committee's conclusion that the requirements in existing IFRS Standards provide an adequate basis for an entity to recognise and present the difference between the interest that would be calculated by applying the effective interest rate to the gross carry amount and the interest revenue recognised for the credit-impaired financial asset when this asset is cured.

If you believe we can be of any assistance regarding this matter, do not hesitate to contact us (contrib@petrobras.com.br).

Respectfully,

/s/Rodrigo Araujo Alves

_____

Rodrigo Araujo Alves

Chief Accounting and Tax Officer

Deutsches Rechnungslegungs Standards Committee e.V.

Accounting Standards Committee of Germany

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Sue Lloyd
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IFRS Technical Committee
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Berlin, 06 February 2019

Dear Sue,

RE: The IFRS IC's tentative agenda decisions in its November 2018 meeting

On behalf of the Accounting Standards Committee of Germany (ASCG), I am writing to comment on the tentative agenda decisions taken by the IFRS Interpretations Committee (IFRS IC) and published in the November 2018 IFRIC Update.

We agree with four of the tentative agenda decisions. However, in respect of two tentative agenda decisions we have concerns with the decision and the reasons cited, namely the tentative decisions on physical settlement of contracts (IFRS 9) and cloud computing (IAS 38).

Please find our detailed comments in the appendix to this letter. If you would like to discuss our views further, please do not hesitate to contact Jan-Velten Große (grosse@drsc.de) or me.

Yours sincerely,

Andreas Barckow

President

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Paris, 6 February 2019

Mrs Lloyd
IFRS Interpretations Committee Chair
7 Westferry Circus, Canary Wharf
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November 2018 - IFRS-IC tentative agenda decisions

Dear Mrs Lloyd, Dear Sue,

I am writing on behalf of the Autorité des Normes Comptables (ANC) to express our views on the IFRS-IC tentative decisions published in November 2018 IFRIC Update regarding IFRS 9 – *Physical settlement of contracts to buy or sell a non-financial item*, IAS 38 – *Customer's right to access the supplier's software hosted on the cloud* as well as IFRS 9 – *Curing of a credit-impaired financial asset*. This letter sets out some of the most critical comments raised by interested stakeholders involved in ANC's due process.

Physical settlement of contracts to buy or sell a non-financial item (IFRS 9)

ANC does not disagree with the tentative decision. ANC notes however that in the energy industry, when neither the own-use exception nor the hedge accounting is applied, entities often manage contracts measured at fair value through P&L (IFRS 9.2.5) to achieve an economic hedge. Upon physical settlement, there is a common practice to present the accumulated fair value gain or loss on the derivative on one line in the P&L that differs from the one where the sale/purchase is recorded (at contract's value instead of the fair value retained in the fact pattern).

ANC understands that this current accounting practice reflects the way performance is analysed, both by management and by external users of the financial statements. The Committee's suggested accounting treatment might have significant impact on this current practice and be disruptive. ANC is concerned that this could result in increasing the use of non-GAAP information to meet user's expectations.

The issue is partially linked to the dual practice in the industry to settle net and physically. ANC suggests that IASB considers, as part of its standard-setting activity, the accounting treatment of these contracts that are neither held for trading nor eligible to the own-use exception and that are eventually physically settled.

[...]

Presentation of unrecognised interest following the curing of a credit-impaired financial asset (IFRS 9)

In order to analyse properly the accounting treatment of the reversal of previously "suspended interests" (i.e. the difference between contractual interests and interests recognised in accordance with IFRS 9.5.4.1b), it is important to clarify how these suspended interests were initially recorded. We note the following definitions in IFRS 9:

The gross carrying amount (GCA) is "the amortised cost before adjusting for any loss allowance";

The loss allowance (LA) corresponds to the expected credit losses (ECL) that shall be measured for credit impaired financial asset "as the difference between the asset's gross carrying amount and the present value of estimated future cash flows discounted at the financial asset's original effective interest rate" (IFRS 9.B5.5.33);

The amortised cost (AC) has been defined as "the amount at which the financial asset (…) is measured at initial recognition minus the principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between that initial amount and the maturity amount and, (…) adjusted for any loss allowance" ;

By way of exception for financial assets that have become credit-impaired, the effective interest method applies to the AC and not to the GCA (IFRS9.5.4.1(b)).

Applying the above definitions to credit-impaired financial assets, we consider that there is no evidence that the GCA of a credit impaired asset shall reflect the contractual interests accrued instead of the interest revenue determined in accordance with IFRS 9.5.4.1(b). This is a strong assumption in the tentative agenda decision that needs to be further analysed.

Actually, IFRS 9 does not give any evidence about how "suspended interests" interact with both the GCA and the AC, and how they shall be presented either in the balance sheet or in the P&L. There are even situations where it may be impossible to comply with both (i) the interest revenue definition in IFRS 9.5.4.1 and (ii) the impairment gain or loss definition in IFRS 9.5.5.8. Assuming that on a

stage 3 financial asset, the GCA has increased applying the effective interest rate; the impairment allowance should also increase to achieve interest revenue at amortised cost in the P&L (see also accompanying example in Appendix). In such case:

- either the change in impairment allowance for the period is recognised in "impairment gain or loss" but in this case the recognised interest revenue shall be based on the GCA instead of the AC to get the right final impact in the P&L; or
- interest revenue is recognised based on the AC, but in this case it is impossible to reflect in the line "impairment gain or loss" the change in impairment allowance for the period.

In our view, this inconsistency has to be clarified (via standard-setting) before addressing the way curing credit impaired financial asset should be accounted for.

Moreover, ANC considers that a loan at amortised cost that might have been temporarily credit-impaired and subsequently cured, i.e. transferred from Stage 3 to Stage 2 or fully recovered out of Stage 3, should depict the same cumulative economic return as a loan maintained in Stage 2. We also have concerns about the intelligibility of presenting a reversal that exceeds the impairment. Thus this economic return would be better reflected as an interest income than an impairment gain.

We therefore encourage the Committee to investigate further this topic in a more comprehensive way to address both the presentation on the balance sheet and on the P&L over the life of the instrument (interest revenue recognition in Stage 2 and 3, coupon payment occurring while the instrument is in Stage 3, scenario of a cured financial asset…).

Please do not hesitate to contact us should you want to discuss any aspect of our letter.

Kind regards.

Yours sincerely,

Patrick de Cambourg

Appendix: Illustrative example relating to the presentation of unrecognised interest following the curing of a credit-impaired financial asset

Contractual terms of the loan	
Yearly payment of interest	
Principal	100
EIR	10%

	31/12/N	31/12/N	31/12/ N+1	31/12/ N+2	31/12/ N+3	31/12/ N+4		**Curing on 31/12/N+4**
	Before impairment	After impairment						
Contractual cash flows			10	10	10	10		
Expected Cash Flows as at 31/12/N			0	0	0	**40**		
(Expectations remaining unchanged until 31/12/N+4)								
Present value of expected cash flows at the end of each period	100	27,3	30,1	33,1	36,4	40,0		

Reversal exceeds initial allowance

1) Balance sheet - Assets : APPROACH RESULTING FROM IFRIC POSITION

Gross Carrying Amount (including amounts due but unpaid)	100,0	110,0	120,0	130,0	140,0		0	
loss allowance	-72,7	-79,9	-86,9	-93,6	-100,0		0	
Net amortised cost	27,3	30,1	33,1	36,4	40,0			
					71%			
Income statement						total		**∑ P&L**
Interest income (EIR)	0,0	2,7	3,0	3,3	3,6	12,7		**12,7**
Cost of risk	-72,7					-72,7	100,0	**27,3**
	-72,7	2,7	3,0	3,3	3,6	-60,0	100,0	**40,0**

2) Balance sheet - Assets : ALTERNATIVE APPROACH

Gross Carrying Amount (including amounts due but unpaid)	100,0	102,7	105,7	109,0	112,7		0	
loss allowance	-72,7	-72,7	-72,7	-72,7	-72,7		0	
Net amortised cost	27,3	30,1	33,1	36,4	40,0			
					65%			
Income statement						total		**∑ P&L**
Interest income (EIR)	0,0	2,7	3,0	3,3	3,6	12,7	27,3	**40,0**
Cost of risk	-72,7					-72,7	72,7	**0,0**
	-72,7	2,7	3,0	3,3	3,6	-60,0	100,0	**40,0**

MAZARS

Mrs Sue Lloyd
IFRS Interpretations Committee
Columbus Building,
7 Westferry Circus, Canary Wharf
London E14 4HD
United Kingdom

La Défense, February 6, 2019

Tentative Agenda Decisions – IFRIC Update November 2018

Dear Sue,

MAZARS is pleased to comment on the various IFRS Interpretations Committee tentative agenda decisions published in the November 2018 IFRIC Update.

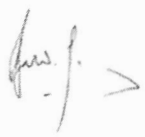
We have gathered all our comments as appendices to this letter, which can be read separately and are meant to be self-explanatory.

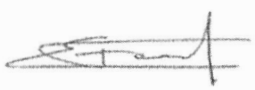
We would like to draw your attention to two issues that are worth considering:

- The tentative decision on physical settlement of contracts to buy or sell a non-financial item (see Appendix 2 to this letter) is contrary to the practice applied by large companies in the energy sector, and we think it necessary to undertake a comprehensive analysis of the issue and the rationale for their current practice before finalizing any decision;
- The issue of the accounting for the curing of a credit-impaired financial asset is not an easy one, and when diving into examples, it appears that there exist within IFRS 9 some unclear requirements or even inconsistencies between the definitions involved. We have tried to develop examples evidencing those difficulties, and we stand ready to present them and our concerns in a dedicated meeting with IFRS IC Staff / members.

Should you have any questions regarding our comments on the various tentative agenda decisions, or should you want us to participate in a meeting as proposed above, please do not hesitate to contact Michel Barbet-Massin (+33 1 49 97 62 27) or Edouard Fossat (+33 1 49 97 65 92).

Yours faithfully





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Appendix 6

Curing of a credit-impaired financial asset (IFRS 9 Financial Instruments*)— Agenda Paper 7*

We have several comments regarding that Tentative Agenda Decision on curing of a credit-impaired financial asset. We are concerned that the proposed clarifications go beyond a simple application of the existing framework and may create inconsistencies with the existing guidance in IFRS 9 (see Issue 2 below).

Description of our main areas of concern

ISSUE 1: a need for a consistent approach both for reversal and initial recognition of "interest in suspense"

Firstly, we believe that the IFRS IC cannot properly analyse the question of the reversal of "interest in suspense" following the collection of all the contractual interest on "stage 3" financial assets without considering beforehand how the "interest in suspense" should be accounted for **initially**, when accounting for interest on a net basis rather than on a gross basis. The corresponding entries should in our opinion be consistent both for the initial recognition and the reversal of "interest in suspense" (i.e. if the interest in suspense is not included within the loss allowance initially, then its reversal upon recovery / curing should not be treated as an impairment gain either).

In its agenda paper the staff seems to think that there has been in the past an allocation of impairment allowance in relation to interest in suspense, and that it is justified to take it back / reverse it. In our example we figure out that such entries are not obvious and maybe unjustified (see Issue 2 below).

ISSUE 2: we disagree with the proposal to present the reversal of "interest in suspense" as an impairment gain

We consider that "interest in suspense" **may not** be accounted for **initially** as part of the impairment allowance. Existing guidance in IFRS 9.5.5.8 and IFRS 9.B5.5.33 requires that all changes in loss allowance go through the profit or loss statement as an impairment gain or loss.

IFRS 9.5.5.8 (emphasis added): *"An entity shall recognise **in profit or loss**, as an impairment gain or loss, the amount of expected credit losses (or reversal) that is required to adjust the loss allowance at the reporting date to the amount that is required to be recognised in accordance with this Standard."*

IFRS 9.B5.5.33 (emphasis added): *"For a financial asset that is credit-impaired at the reporting date, but that is not a purchased or originated credit-impaired financial asset, an entity shall measure the expected credit losses as the difference between the asset's gross carrying amount and the present value of estimated future cash flows discounted at the financial asset's original effective interest rate. Any adjustment is* ***recognised in profit or loss*** *as an impairment gain or loss."*

In our opinion, impairment gains and losses correspond to the change in discounted expected cash shortfalls, in accordance with the definition of credit losses in Appendix A of IFRS 9. Therefore, interest in suspense, which is created by a change in the way interest revenue is recognised rather than by a change in expected cash shortfalls, do not relate to an impairment gain or loss. The Basis for Conclusions of IFRS 9 clearly state that the loss allowance should be calculated in the same manner for Stage 2 and Stage 3 assets, the distinction between the two stages having an impact only on the calculation of interest revenue, as per the extract below:

IFRS 9 BC5.75 (emphasis added): *The IASB received feedback on the 2013 Impairment Exposure Draft that showed the majority of respondents agreed that the interest revenue calculation should change to a calculation on a net basis for some financial assets, because it best supported faithful representation.* ***These requirements only affect the calculation and presentation of interest revenue and not the measurement of the loss allowance****.*

This is further illustrated by our example 1. No additional impairment gain or loss needs to be recorded on the date on which interest in suspense is recognised. As a result, applying IFRS 9.5.5.8 and IFRS 9.B5.5.33 the interest in suspense should neither be included in the loss allowance amount nor as an impairment gain or loss.

As the initial accounting of interest in suspense is not recognised through impairment loss, we disagree with the IFRS IC tentative decision to recognise the reversal of the interest in suspense upon recovery against an impairment gain.

We note that the staff's example provided in the Agenda Paper AP7 is simplified. This could be source of some misunderstandings, for example in relation to the unwinding of discounting mentioned. We strongly recommend to the IFRS IC and its Staff to perform a comprehensive example, over the life of the instrument, with annual interest payment (rather than a zero-coupon profile) and taking into account discounting effects.

ISSUE 3: what is the appropriate initial accounting for the "interest in suspense"?

We have prepared numerical examples 1 and 2 that are attached to this comment letter that illustrate the initial accounting scenarios for interest in suspense for Stage 3 assets (the third example, example 0, is only included for reference / control purposes to show what the accounting entries would have been for a stage 2 asset where there is no interest in suspense). **To facilitate the understanding of our reasoning, we stand ready to present this example step-by-step during a dedicated meeting with the IFRS IC Staff, should you wish so.**

Example 2 shows that the suspended interest would be included within the gross carrying amount in order to comply with the definition of amortised cost and impairment allowance. We would ask the IFRS IC to provide additional guidance as to which of these calculations is more appropriate / prohibited. In our opinion, only example 2 fully complies with the existing definitions of gross carrying amount, loss allowance and amortised cost in the Appendix A of IFRS 9.

- **Example 1**
  - Presentation & assumptions:
    - It is similar in its underlying assumptions to the example discussed by the ITG in its December 2015 meeting, meaning that the *gross carrying amount* is calculated as a present value / sum of discounted contractual cash flows (without considering credit losses and the specific interest revenue mechanism for credit impaired asset).
    - The *loss allowance* is calculated as the discounted expected credit losses / cash shortfalls.
    - The *amortised cost* is the present value / sum of expected cash flows taking into account credit losses.
  - The issues:
    - As the gross carrying amount and amortised cost include a coupon on a gross basis and the P&L includes a coupon on a net basis, this gives rise to an "interest in suspense" amount (a negative asset)
    - Contrary to the 2015 ITG discussion, we do not agree that this negative asset should be included within the loss allowance for the reasons explained in Issue 2 above.
    - If the IFRS IC confirms the calculation of gross carrying amount in Example 1, additional guidance is needed on where / how this negative asset should be presented upon its initial recognition.

- **Example 2:**
  - Presentation & assumptions:
    - The *loss allowance* calculation is identical to the one in Example 1 (i.e. present value of expected cash shortfalls)
    - Upon transfer to Stage 3, we calculate the *amortised cost* as defined in Appendix A of IFRS 9 (i.e. amortised cost of previous year-end plus change in loss allowance during the period plus interest revenue using the EIR method, i.e. on a net basis, minus repayments of coupon)
    - So the *gross carrying amount* equals the amortised cost plus impairment allowance. Mechanically, "interest in suspense" (interest in P&L minus interest in cash) is included within the gross carrying amount.
  - The issue:
    - This example is not in line with the 2015 ITG discussion, as the gross carrying amount is a balancing figure rather than the present value of contractual cash flows.

- However, this calculation seems to us in line with the definitions provided in Appendix A of IFRS 9 (which do not define gross carrying amount as a present value; reference to present value is only provided in IFRS.5.4.3 and IFRS 9.B5.4.6 on modified / revised contractual cash flows).
- Upon recovery, assuming all contractual cash flows are recovered the same question arises as to where the gain upon recovery should be recorded (as the asset's net carrying amount is below the recovered amount). This topic is similar to the reversal of the interest in suspense amount upon recovery (see Issue 4 below).

To sum up the issue, the real question according to us is **the definition of gross carrying amount** in IFRS 9. Should interest in suspense be included within the gross carrying amount (this is in our view the sole possibility given current definitions in IFRS 9 Appendix A), its initial recognition would no longer be an issue, contrary to Example 1.

ISSUE 4: where in P&L should the gain upon recovery / curing be presented?

When "interest in suspense" is recognised on B/S separately from the impaired asset (see **Example 1** in Issue 3 above), the current IFRS framework does not provide sufficient guidance as to how the reversal of this interest should be recorded[1].

In our view, this gain may not be presented as an *impairment gain* in accordance with IAS 1.82(ba) as it is not related to a change in impairment allowance. Moreover, it did not give rise to an impairment loss initially (see Issue 2 for more arguments on this specific aspect).

In our opinion, this gain may be presented as *interest revenue.* Even if it is not directly calculated using the effective interest method in accordance with IAS 1.82(a)(i), we see it as a reversal of the specific interest revenue mechanism required by IFRS 9 for credit-impaired assets.

We acknowledge that this presentation issue is not straightforward in IAS 1 / IFRS 9 requirements and recommend to the IFRS IC to provide further guidance on this topic in a way consistent with the answers provided to the above-mentioned issues.

ISSUE 5: minor additional comments on the wording of November's TAD

The proposed TAD raised another concern to us, in particular the part we underlined hereafter: "*The amount of this adjustment includes the effect of the unwinding of the discount on the loss allowance during the period that the financial asset was credit-impaired, which means the reversal of impairment losses may exceed the impairment losses*

[1] Similarly, if we follow the alternative approach / **Example 2** presented in Issue 3 above (i.e. when the gross carrying amount is calculated as the balancing figure / sum of amortised cost and impairment allowance rather than as the sum of contractual cash flows discounted at the initial effective interest rate – which means that the interest in suspense is presented as a deduction from the gross carrying amount rather than a separate item on B/S), the net book value of the instrument will be lower than the amount recovered. Therefore, the question is here where to account for this gain / positive difference between the cash inflow and the reversal of a smaller net carrying amount. Our opinion here as to the appropriate line in P&L to present this gain is the same as for Example 1.

We note that under the general model of impairment of IFRS 9 the unwinding of the discounting (assuming an unchanged undiscounted credit loss estimates) gives rise to a complementary impairment loss at each closing of accounts. Should the losses be eventually reversed, the reversal may not exceed the previously recognised amount of impairment loss. We encourage the IFRS IC to review this position and clarify the wording in the final Agenda Decision in this respect. To our knowledge, the only scenario where impairment gains may outweigh previously recognised impairment losses is in the case of POCI (purchased or originated credit-impaired assets), as per IFRS 9.5.5.14, but POCI follow a specific impairment model, whereas the scope of the submission is limited to the general impairment model.

Last but not least, we would prefer that the scope of the issue in the first paragraph be reduced to only deal with cured assets that are **paid in full**. The case of no longer credit-impaired (i.e. assets that are transferred back to Stage 2 or Stage 1) is not really dealt with in the TAD, as in addition to the presentation issue (i.e. where in P&L to present the gain upon curing) there is the issue of the timing of reversal of "interest in suspense" (i.e.. upon transfer out of Stage 3, upon final recovery or some time in between?). We are not sure this issue may be resolved within the confines of existing IFRS 9 guidance.

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Appendix 6Bis – page 1/4

Numerical example to illustrate our comments on Agenda Paper 7, Curing of a credit-impaired financial asset (IFRS 9 Financial Instruments*)—*

DEFINITIONS

Amortised Cost

amortised cost of a financial asset or financial liability — The amount at which the financial asset or financial liability is measured at initial recognition minus the principal repayments, plus or minus the cumulative amortisation using the **effective interest method** of any difference between that initial amount and the maturity amount and, for financial assets, adjusted for any **loss allowance**.

Gross Carrying amount :

gross carrying amount of a financial asset — The **amortised cost of a financial asset**, before adjusting for any **loss allowance**.

Loss allowance

loss allowance — The allowance for **expected credit losses** on financial assets

Expected credit losses

expected credit losses — The weighted average of **credit losses** with the respective risks of a default occurring as the weights.

Credit Losses:

credit loss — The difference between all contractual cash flows that are due to an entity in accordance with the contract and all the cash flows that the entity expects to receive (ie all cash shortfalls), discounted at the original **effective interest rate** (or **credit-adjusted effective interest rate** for **purchased or originated credit-impaired financial assets**). An entity shall

Interest revenue

5.4.1 **Interest revenue shall be calculated by using the *effective interest method* (see Appendix A and paragraphs B5.4.1–B5.4.7). This shall be calculated by applying the *effective interest rate* to the *gross carrying amount* of a *financial asset* except for:**

(b) financial assets that are not purchased or originated credit-impaired financial assets but subsequently have become *credit-impaired financial assets*. For those financial assets, the entity shall apply the effective interest rate to the amortised cost of the financial asset in subsequent reporting periods.

Impairment gain or Loss

5.5.8 An entity shall recognise in profit or loss, as an *impairment gain or loss*, the amount of expected credit losses (or reversal) that is required to adjust the loss allowance at the reporting date to the amount that is required to be recognised in accordance with this Standard.

B5.5.33 For a financial asset that is credit-impaired at the reporting date, but that is no a purchased or originated credit-impaired financial asset, an entity sha measure the expected credit losses as the difference between the asset's gro carrying amount and the present value of estimated future cash flow discounted at the financial asset's original effective interest rate. An adjustment is recognised in profit or loss as an impairment gain or loss

THE ASSUMPTIONS

3 year Loan, *in fine*
Nominal 100
Issued 31th december N
Contractual interest and EIR = 10%
Interest paid each year on 31th december

Expected loss of 60 on final repayment
(assumption unchanged from N+1 to N+3)

THREE EXAMPLES

	YE N+1	YE N+2	YE N+3
Ex0	Stage 2	Stage 2	Stage 2
Ex1	Stage 2	Stage 3	Stage 3
Ex2	Stage 2	Stage 3	Stage 3

Difference between Ex1 and Ex2:
- Ex1. GCA = present value of contractual cash flows
- Ex2. GCA = amortised cost + loss allowance (includes interest in suspense)

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Appendix 6Bis – page 2/4 – Numerical example 0 (asset in Stage 2 at all closings)

SITUATION AT THE END OF N+1

Gross Carrying Amount : 100
Credit Loss = 60 x $(1+10\%)^{-2}$ = 50
Amortised Cost = 100 – 50 = 50
Interest revenue = 10 = (100*10%)
Impairment Gain or Loss = - 50

B/S as at 31 December N+1 stage 2			
GCA (including accrued coupon)	110	Capital	100
Coupon payment	-10	Retained earnings	0
GCA (after coupon payment)	100		
Loss allowance	-50		
Loan's NCA	50		
		Interest revenue	10
		Impairment gains / losses	-50
Cash	10	Profit or loss for the year	-40
Total	60	Total	60

SITUATION AT THE END OF N+2

GCA : 100
Credit Loss = 60 x $(1+10\%)^{-1}$ = 55
Amortised Cost = 100 – 55 = 45
Interest revenue = 10 = (100*10)
Impairment Gain or Loss = -5 = 50 – 55

B/S as at 31 December N+2 stage 2			
GCA (including accrued coupon)	110	Capital	100
Coupon payment	-10	Retained earnings	-40
GCA (after coupon payment)	100		
Loss allowance	-55		
Loan's NCA	45		
		Interest revenue	10
		Impairment gains / losses	-5
Cash	20	Profit or loss for the year	5
Total	65	Total	65

SITUATION AT THE END OF N+3
(JUST BEFORE CASH REPAYMENT)

GCA : 100 + 10 Accrued coupon
Credit Loss = 60 x $(1+10\%)^{0}$ = 60
Amortised Cost = 110 – 60 = 50
Interest revenue = 10 = (100*10)
Impairment Gain or Loss = -5 = 55 – 60

B/S as at 31 December N+3 stage 2 just before recovery of 50			
GCA (including accrued coup	110	Capital	100
Coupon payment	0	Retained earnings	-35
GCA (after coupon payment)	110		
Loss allowance	-60		
Loan's NCA	50		
		Interest revenue	10
		Impairment gains / losses	-5
Cash	20	Profit or loss for the year	5
Total	70	Total	70

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Appendix 6Bis – page 3/4 – Numerical example 1 (Stage 3 + GCA = present value)

SITUATION AT THE END OF N+1

Gross Carrying Amount : 100
Credit Loss = 60 x $(1+10\%)^{-2}$ = 50
Amortised Cost = 100 – 50 = 50
Interest revenue = 10 = (100*10%)
Impairment Gain or Loss = - 50

B/S as at 31 December N+1 stage 2			
GCA (including accrued coupon)	110	Capital	100
Coupon payment	-10	Retained earnings	0
GCA (after coupon payment)	100		
Loss allowance	-50		
Loan's NCA	50		
		Interest revenue	10
		Impairment gains / losses	-50
Cash	10	**Profit or loss for the year**	-40
Total	60	Total	60

SITUATION AT THE END OF N+2

GCA : 100
Credit Loss = 60 x $(1+10\%)^{-1}$ = 55
Amortised Cost = 100 – 55 = 45
Interest revenue = 5 = (50*10%)
Impairment Gain or Loss = -5 = 50 – 55

B/S as at 31 December N+2 Stage 3			
GCA (including accrued coupon)	110	Capital	100
Coupon payment	-10	Retained earnings	-40
GCA (after coupon payment)	100		
Loss allowance	-55		
Loan's NCA	45		
Suspended interest	-5	Interest revenue	5
		Impairment gains / losses	-5
Cash	20	**Profit or loss for the year**	0
Total	60	Total	60

SITUATION AT THE END OF N+3
(JUST BEFORE CASH REPAYMENT)

GCA : 100 + 10 Accrued coupon
Credit Loss = 60 x $(1+10\%)^{0}$ = 60
Amortised Cost = 105 – 60 = 45
Interest revenue = 5 = (45*10%)
Impairment Gain or Loss = -5 = 55 – 60

B/S as at 31 December N+3 Stage 3 - just before the recovery of 50			
GCA (including accrued coup	110	Capital	100
Coupon payment	0	Retained earnings	-40
GCA (after coupon payment)	110		
Loss allowance	-60		
Loan's NCA	50		
Suspended interest	-11	Interest revenue	5
		Impairment gains / losses	-5
Cash	20	**Profit or loss for the year**	-1
Total	59	Total	59

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Appendix 6Bis – page 4/4 – Numerical example 2 (Stage 3 + GCA includes interest in suspense)

SITUATION AT THE END OF N+1

Gross Carrying Amount : 100
Credit Loss = 60 x $(1+10\%)^{-2}$ = 50
Amortised Cost = 100 – 50 = 50
Interest revenue = 10 = (100*10%)
Impairment Gain or Loss = - 50

B/S as at 31 December N+1 stage 2			
GCA (including accrued coupon)	110	Capital	100
Coupon payment	-10	Retained earnings	0
GCA (after coupon payment)	100		
Loss allowance	-50		
Loan's NCA	50		
		Interest revenue	10
		Impairment gains / losses	-50
Cash	10	**Profit or loss for the year**	-40
Total	60	Total	60

SITUATION AT THE END OF N+2

Interest revenue = 5 = (50*10%)
Cash received = 10 of which 5 of interest revenue, 5 remaining considered as principal repayment
GCA : 95 = 100 – 5 cash income not recognised as interest revenue
Credit Loss = 60 x $(1+10\%)^{-1}$ = 55
Amortised Cost = 95 – 55 = 40
Impairment Gain or Loss = -5 = 50 – 55

B/S as at 31 December N+2 Stage 3			
GCA (including accrued coupon at EI	105,0	Capital	100,0
Coupon payment	-10,0		
GCA (after coupon payment)	95,0		
Loss allowance	-54,5	Retained earnings	-39,6
Loan's NCA	40,5		
Suspended interest	0,0		
		Interest revenue	5,0
		Impairment gains / losses	-4,9
Cash	20,0	**Profit or loss for the year**	0,1
Total	60,5	Total	60,5

SITUATION AT THE END OF N+3

Interest revenue = 4 = (40*10%)
GCA : 99 = 95 + 4 as interest revenue
Credit Loss = 60
Amortised Cost = 99 – 60 = 39
Impairment Gain or Loss = -5 = 55 – 60

B/S as at 31 December N+3 Stage 3 - just before the recovery of 50			
GCA (including accrued coupo	99,1	Capital	100,0
Coupon payment	0,0		
GCA (after coupon payment)	99,1		
Loss allowance	-60,0	Retained earnings	-39,5
Loan's NCA	39,1		
Suspended interest	0,0		
		Interest revenue	4,0
		Impairment gains / losses	-5,5
Cash	20,0	**Profit or loss for the year**	-1,4
Total	59,1	Total	59,1