STAFF PAPER

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IASB® meeting

Project	Post-implementation Review of IFRS 9—Classification and Measurement
Paper topic	Other matters raised in PIR feedback

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Introduction

1. The IASB has been discussing feedback to the *Request for Information Post-implementation Review of IFRS 9 – Classification and Measurement* (the RFI) since March 2022.

2. The purpose of this paper is to cover questions relating to matters raised by respondents to the RFI that are not covered by other staff papers presented to the IASB. The paper does not analyse application questions that relate to specific fact patterns included in the feedback on the RFI.

3. This paper also provides feedback from the July 2022 meeting of the Accounting Standards Advisory Forum (ASAF) on topics related to the contractual cash flow characteristics of financial assets, first discussed during the April 2022 IASB meeting.

4. This paper is structured as follows:

   (a) reminder of the requirements for assessing feedback raised in a post-implementation review (PIR);

   (b) summary of staff recommendations and a question for the IASB;

(c) staff analysis of questions on other matters; and

(d) updated staff analysis of questions related to contractual cash flow characteristics of financial assets.

PIR Requirements

5. At its June 2022 meeting, the Trustees of the IFRS Foundation considered the recent revisions to the description of PIRs (including the prioritisation of PIR findings) in the Due Process Handbook. These principles were previously discussed by the IASB in January 2022.

6. In order to respond to findings identified in PIRs, the IASB considers a two-step approach in deciding whether to take action on any of the findings and the prioritisation of any such action:

   (a) step 1—assess whether the findings from the PIR provides evidences that:

      (i) an objective of the new requirements is not being met;

      (ii) the benefits to users of financial statements of the information arising from applying the new requirements are significantly lower than expected (for example, there is significant diversity in application); or

      (iii) the costs of applying some or all of the new requirements and auditing and enforcing their application are significantly greater than expected (or there is a significant market development since the new requirements were issued for which it is costly to apply the new requirements consistently).

   (b) step 2—if finding evidence of any of those characteristics described in step 1, the timing of any action would depend on the prioritisation of the finding as high, medium or low, based on the extent to which evidence indicates:

      (i) the finding has substantial consequences;

(ii) the finding is pervasive;

(iii) the finding arises from a financial reporting issue that can be addressed by the IASB or the Interpretations Committee; and

(iv) the benefits of any action would be expected to outweigh the costs. To determine this, the IASB would consider the extent of disruption and operational costs from change and the importance of the finding to users of financial statements.

Summary of staff **recommendations** and **question** for IASB

7. The table below summarises the staff recommendations on the six questions on other matters discussed in this paper:

Application question	Staff recommendation
A. Derecognition of financial assets	No further action, as matter is not widespread or expected to have a material effect.
B. Cash received via electronic transfer as settlement for a financial asset	No recommendation made in this paper.
C. Contracts to buy and sell non-financial items	No further action, as matter is not widespread or expected to have a material effect.
D. Equity investments and OCI – transaction costs	No further action, as matter is not widespread or expected to have a material effect.
E. Financial assets and financial liabilities held for trading	No further action, as IFRS 9 provides sufficient guidance.
F. Purchased or originated credit-impaired financial assets	Consider this matter as part of the upcoming PIR on the impairment requirements in IFRS.

8. This staff also recommend no further action on the following two SPPI questions, based on outreach with ASAF members that indicated that these questions are neither widespread nor expected to have a material effect on entities' financial statements:

   (a) contractual inflation adjustments and leverage; and

   (b) regulated interest rates and leverage.

Question for the IASB
Do you agree with the staff's recommendations as summarised in paragraphs 7 and 8 of this paper?

Staff analysis of questions raised on other matters

9. This paper analyses six questions that were raised by respondents to the RFI on matters not covered in other staff papers. For each of these questions, the following tables:

   (a) summarise the requirements to which the question relates;

   (b) explain the question; and

   (c) provide staff analysis and recommendations on whether—and what— further action the IASB could take in response to the question.

10. Where the topics discussed in this section relate to specific application questions, the staff have consulted ASAF during their July 2022 meeting to determine whether any of these issues would meet the criteria for a financial reporting issue to be addressed by the Interpretation Committee (see paragraph 5(b)(iii)): The criteria to be considered are:

   (a) if the matter is widespread and expected to have a material effect; and

   (b) if the matter is sufficiently narrow in scope and can be resolved efficiently.

11. The responses from ASAF members are included in the staff analysis below.

A. Derecognition of financial assets

Requirements
IFRS 9 includes detailed requirements for when an entity should derecognise a financial asset. When an entity transfers a financial asset to another entity, paragraph 3.2.6 of IFRS 9 requires the entity to evaluate the extent to which it retains the risks and rewards of ownership of the financial asset. If the entity neither retains nor transfers substantially all risks and rewards of ownership of the financial asset, the entity shall determine whether it has retained control of the financial asset to determine whether it needs to account for its continuing involvement in the financial asset.
Application question
The RFI did not include specific questions on the requirements in IFRS 9 relating to the derecognition of financial assets. This is because IFRS 9 carried over the requirements in IAS 39 without amendment. However, a few respondents used the opportunity to raise longstanding questions regarding the interpretation and application of some aspects of the requirements. A few respondents said it would be useful if the IASB clarified which risks need to be considered when assessing whether 'substantially all risks and rewards' of a financial asset has been transferred. Furthermore, a few respondents asked for more application guidance on assessing whether an entity has retained control over the financial asset if the entity concludes that it has neither transferred nor retained substantially all the risks and rewards. Respondents mentioned that this assessment can be especially difficult in the case of financial assets that are transferred to special purpose vehicles and in the case of complex risk-sharing and reverse factoring transactions. Finally, a few respondents argued that the guidance on accounting for an entity's 'continuing involvement' in a financial asset could be improved since IFRS 9 only provides illustrative examples for some specific forms of continuing involvement, but

does not clearly articulate general principles, which makes it difficult to ensure that other transactions that result in continuing involvement in financial assets are accounted for in a consistent manner.
Staff analysis
The staff acknowledge that applying the derecognition requirements for financial assets in IFRS 9 can be complex and involve significant judgement. However, notwithstanding the application questions raised by a few respondents to the RFI, the derecognition requirements have been applied to a wide variety of transactions over a long period. The staff is not aware of any evidence that the derecognition criteria are not meeting the objective of providing useful information to users of financial statements about transactions which involve the transfer of financial assets to another entity. In the staff's view, extensive analysis and judgement is often required due to the complexity of specific fact patterns, especially in the case of structured transactions involving special purpose vehicles. Therefore, the staff do not believe that the cost of complying with the requirements is significantly greater than expected, or that there is a clear approach for simplifying the requirements through standard-setting. The staff acknowledges that additional application guidance on accounting for continuing involvement, could enable greater consistency. However, in the absence of any evidence that this issue is widespread or expected to have a material effect, we think the cost of standard-setting in this regard will outweigh the benefits to be gained. When asked about the prevalence and significance of these questions, some ASAF members acknowledged that there is diversity in practice on certain questions, but did not consider the issue to be a priority for the IASB to address. **The staff recommend that no further action be taken on this as the matter is not widespread or expected to have a material effect.**

B. Cash received via electronic transfer as settlement for a financial asset

Requirements
The recognition and derecognition criteria in IFRS 9 apply to all financial assets and financial liabilities in the scope of IFRS 9, including cash. According to paragraph 3.1.1 of IFRS 9, an entity shall recognise a financial asset or a financial liability when, and only when, the entity becomes party to the contractual provisions of the instrument. Paragraph 3.2.3 of IFRS 9 states that an entity shall derecognise a financial asset when, and only when, the contractual rights to the cash flows from the financial assets have expired or it transfers the financial asset in a manner set out in paragraphs 3.2.4 to 3.2.6 of IFRS 9. Paragraph 3.3.1. states that an entity shall remove a financial liability (or part of a financial liability) from its statement of financial position when, and only when it is extinguished – ie when the obligation specified in the contract is discharged or cancelled or expires.
Application question
A few respondents to the RFI referred to the discussion at the September 2022 meeting of the Interpretations Committee on *Cash Received via Electronic Transfer as Settlement for a Financial Asset (IFRS 9 Financial Instruments)*. These respondents asked the IASB to consider the implications of the tentative decision of the Interpretation Committee because in their view, the application of the requirements set out in the tentative decision will have significant impacts on long-standing and established practice and would therefore lead to significant operational challenges and costs to apply.
Staff analysis
The staff note that the respondents to the RFI did not express disagreement with the Interpretations Committee's analysis on how the IFRS 9 requirements are applied to the

recognition and derecognition of financial asset and financial liabilities. However, the respondents argued that the tentative decision could have widespread and costly implications because it implies a treatment that is different from some long-established practices. These concerns are similar to comments received by the Interpretations Committee on their tentative decision in September 2021 before finalising their decision in June 2022.

Agenda Paper 12A for this meeting:

(a) provides the IASB with a summary of the Interpretations Committee's discussions;

(b) reports to the IASB respondents' comments on the potential outcomes of finalising the agenda decision, together with our analysis of those comments; and

(c) asks the IASB whether it would like to explore narrow-scope standard-setting in response to respondents' comments.

As this matter is subject to the IASB's decision on Agenda paper 12A for this meeting, we are not making any recommendations on this matter in this paper.

C. Contracts to buy and sell non-financial items

Requirements
Paragraph 2.4 of IFRS 9 requires IFRS 9 to be applied to those contracts to buy or sell a non-financial item that can be settled net in cash or another financial instrument, or by exchanging financial instruments, as if the contracts were financial instruments, with the exception of contracts that were entered into and continue to be held for the purpose of the receipt or delivery of a non-financial item in accordance with the entity's expected purchase, sale or usage requirements (ie the 'own use exemption').

Paragraph 2.6 of IFRS 9 sets out various ways in which a contract to buy or sell a non-financial item can be settled net in cash, including ways that prohibits the use of the own use exemption.
Application question
Although not new requirements in IFRS 9, a few respondents to the PIR mentioned practical challenges in applying the requirements in paragraphs 2.5(b) and 2.6 of IFRS 9 which state that an entity cannot use the ‘own use exemption’ for contracts to buy or sell non-financial items if the entity has a practice of settling similar contracts net in cash or another financial instrument or by exchanging financial instruments. These respondents asked for more guidance on what constitutes ‘similar’ contracts and what degree of past practice would invalidate the use of the ‘own use exception’ for future contracts. A few respondents also asked for additional guidance with regards to the ‘unit of account’ in applying paragraphs 2.4–2.7 of IFRS 9. A respondent gave the example of oversized contracts, where the contracted volume is higher than the entity’s expected usage. This may be done because the type of energy supply is erratic (as in the case of renewable energy relying on weather conditions) and the entity therefore wants to ensure that they are supplied with the volumes needed to carry out their normal operations. The respondent argued that it does not provide useful information to users of the financial statements to recognise the entire contract as a derivative measured at fair value through profit or loss solely because the volume of the contract exceeds the entity’s expected usage and part of the contract may be net settled in cash. Furthermore, a few respondents also asked for guidance on how to account for a change in management’s intention for such a contract after initial recognition.
Staff analysis
As with the derecognition requirements in IAS 39, the requirements relating to contracts to buy or sell non-financial items have been carried forward unchanged to IFRS 9. The staff is aware of some questions about the application of particular aspects of these requirements.

However, the staff believes that the requirements meet the objective of ensuring that contracts with the economic characteristics of a financial instrument are accounted for appropriately.

The staff asked ASAF members about the prevalence and significance of these questions in their jurisdictions. ASAF members acknowledged that there exists diversity in practice on some of these issues and that more guidance would be helpful, but did not consider the issues to be a priority for the IASB to address.

Although there is some evidence of diversity in practice, the staff is not aware of evidence that the findings are widespread of expected to have a material effect on entities' financial statements. Furthermore, these are long-standing questions and practice has developed to address areas of judgement. The staff therefore does not believe that the benefit of additional guidance will outweigh the costs of developing and implementing the new guidance, including the potential disruption of existing practice.

The staff recommend that no further action be taken on this as the matter is not widespread or expected to have a material effect.

D. Equity investments and OCI – transaction costs

Requirements
According to paragraph 5.7.1(b) of IFRS 9, a gain or loss on a financial asset that is measured at fair value shall be measured in profit or loss unless it is an equity instrument on which the entity has elected to present gains and losses in other comprehensive income (OCI).
Application questions
A few respondents said that due to insufficient guidance, there is diversity in practice in the accounting for transaction costs on the disposal of equity instruments for which the entity has elected to present gains and losses in OCI, with some entities recognising these costs in profit or loss and others recognising the costs in OCI. A few respondents also

noted diversity in practice in accounting for the difference between the fair value of the equity investment on the date of disposal and the transaction price (for example, as a result of volume discounts).
Staff analysis
The IASB discussed the feedback received on the OCI presentation election for equity investments in Agenda paper 3A for the June 2022 meeting. However, the staff viewed this question to be unrelated to the feedback in that paper as it relates to the mechanics of the presentation election. We therefore decided to consider the matter separate from the other feedback. In the staff's view, one reason for the reported diversity in practice may be the requirement in paragraph 3.2.12 of IFRS 9 that the difference between the carrying amount of a financial asset at the date of derecognition and the consideration received shall be recognised in profit or loss. This requirement was carried over unchanged from IAS 39, which did not have the option to present gains and losses on equity instruments through profit or loss without recycling these gains to profit or loss on disposal. However, we think the requirements for equity investments for which the entity has elected the option to present gains or loss in OCI, provide an adequate basis for an entity to determine the appropriate accounting treatment. Some ASAF members confirmed that there is diversity in practice in their jurisdictions, but did not expect the matter to be widespread or have a material effect. **The staff recommend that no further action be taken on this as the matter is not widespread or expected to have a material effect.**

E. Financial assets and financial liabilities held for trading

Requirements
According to Appendix A to IFRS 9, a financial asset or financial liability is held for trading if it is: (a) is acquired or incurred principally for the purpose of selling or repurchasing it in the near term; (b) on initial recognition is part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking; or (c) is a derivative (except for a derivative that is a financial guarantee contract or a designated and effective hedging instrument). Paragraphs BA.6 to BA.8 of IFRS 9 and question B.11 of the Implementation Guidance of IFRS 9 provides further guidance on financial liabilities held for trading.
Application question
A respondent to the RFI said that more guidance on the term held for trading would be useful to ensure consistent application. The respondent gave two examples of where diversity in practice may occur: (a) structured liabilities issued by a bank to satisfy clients' investment needs, with limited repurchases by the bank to provide liquidity as a market maker. The risk positions embedded in the liabilities and related hedges are managed by the bank's trading desk. (b) a gradual reduction in an equity stake where the entity has the intention to sell the remaining stake (less than 20%) within the next 12 months.

Staff analysis
A financial asset is measured at fair value through profit or loss unless it meets the requirements to be measured at amortised cost or fair value through other comprehensive income (paragraph 4.1.4 of IFRS 9) or is designated under the fair value option applying paragraph 4.1.5 of IFRS 9. In contrast, a financial liability is measured at amortised cost unless it is: (a) a financial liability at fair value through profit or loss as mentioned in paragraph 4.2.1(a) and defined in Appendix A to IFRS 9 (which includes liabilities held for trading); (b) one of the financial liabilities mentioned in paragraph 4.2.1(b)–(e) of IFRS 9; or (c) designated at fair value through profit or loss in accordance with paragraph 4.2.2 of IFRS 9. Based on these requirements in IFRS 9, the staff note that financial asset and financial liabilities that are held-for-trading are a subset of those instruments measured at fair value through profit or loss. Equally, financial instruments designated under the fair value option is a particular sub-set of instruments measured at fair value through profit or loss. In our view, it is clear from the definition of held for trading in Appendix A of IFRS 9 that this classification applies to financial assets and financial liabilities that are held for with a specific trading purpose. It is also important to distinguish financial assets and financial liabilities that are 'held for sale' applying IFRS 5 *Non-current Assets Held for Sale and Discontinued Operation* from financial instruments that are 'held for trading' in terms of IFRS 9. Classifying a financial instrument as held for sale reflects management's intention to realise cash flows on individual instruments through sale, whereas held for trading is considered as one of the 'Other business models' discussed in paragraphs B4.1.5 and

B4.1.6 of IFRS 9. In that context, classifying an instrument as held for trading is part of the business model considerations as required in paragraphs B4.1.1–B4.12B of IFRS 9.

In the staff's view, IFRS 9 provides an adequate basis to determine whether a financial instrument is held for trading.

The staff recommend that no action is taken on these items, as IFRS 9 provides an adequate basis to determine whether a financial instrument is held-for-trading.

F. Purchased or originated credit-impaired financial assets

Requirements

IFRS 9 has specific measurement requirements for the recognition of interest revenue on purchased or originated credit-impaired (POCI) financial assets. Unlike the effective interest rate (EIR) for other financial assets, paragraph 5.4.1(a) of IFRS 9 requires an entity to apply a credit-adjusted effective interest rate to the amortised cost of these financial assets from initial recognition.

A credit-adjusted EIR includes an entity's estimates of expected credit losses in calculating the rate that discounts estimated future cash flows through the expected life of a financial asset.

Application questions

A few respondents reported difficulties in applying the requirements relating to POCI financial assets in practice and asked for more guidance in the following scenarios:

(a) accounting for POCI financial assets that arise because of the derecognition and re-recognition of an existing exposure due a substantial modification in contractual cash flows; and

(b) calculating the credit-adjusted EIR at the appropriate level of granularity in the case of purchasing a portfolio of consumer debt rather than individual exposures.

Respondents also raised conceptual questions on the presentation of movements in expected credit losses on POCI financial assets, especially in the case where there is an improvement in credit quality in excess of the entity's expectations at initial recognition.
Staff analysis
The requirements for POCI financial assets are closely related to the application of the impairment requirements in IFRS 9. We do not believe that questions around the application of the credit-adjusted EIR can be analysed without considering the relevant impairment requirements. **The staff therefore recommend that questions about POCI financial assets are considered as part of the upcoming PIR on the impairment requirements in IFRS 9.**

Application questions related to the contractual cash flow characteristics of financial assets

12. The two application questions below related to the contractual cash flow characteristics of financial assets and were first discussed in Agenda Paper 3A for the April 2022 IASB meeting. The IASB agreed to seek input from ASAF members about the prevalence and significance of these questions in different jurisdictions in order to determine whether to submit these questions to the Interpretations Committee.

Contractual inflation adjustments and leverage

13. In some jurisdictions, it is common for the interest rate of financial instruments to be contractually linked to an index that adjusts the time value of the money based on a market interest rate and/or inflation rate. Some respondents expressed the view that linking principal and interest payments to such an index result in a 'current level' time value of money (ie the 'real' interest rate). Respondents therefore questioned whether such adjustments introduce leverage in the context of recent significant rises in inflation rates.

14. In the April paper, the staff expressed the view that the conclusion in IFRS 9 that a contractual link to an unleveraged inflation index represents consideration for the time value of money on the principal amount outstanding, remains relevant regardless of the level of inflation.

15. ASAF members confirmed that inflation-linked financial instruments are common in some jurisdictions, but they are not aware of widespread diversity in practice in assessing the contractual cash flow characteristics of these instruments. The staff therefore recommend that no further action is taken on this matter.

Regulated interest rates and leverage

16. In some jurisdictions, financial instruments with regulated interest rates can include a leverage factor imposed by the government. For example, the interest rate on a loan is determined based on a factor of say 1.3 x the government bond yield at disbursement + a spread. Respondents asked whether such interest rates are regulated rates applying paragraph B4.1.9E of IFRS 9, and if so, how to consider whether the rate provides exposure to risks or variability in the contractual cash flows that are inconsistent with a basic lending arrangement applying the SPPI requirements in IFRS 9.

17. In the April paper, the staff noted that the feedback indicates that diversity in practice exists and that there could be a material effect in specific jurisdictions. The staff further observed that it would be helpful to understand whether this matter has widespread and material effect in other jurisdictions.

18. The ASAF members reported that the issue is not widespread across jurisdictions and only appears to be prevalent in specific countries such as Hungary. The staff therefore believes that the application question does not meet the criteria for a submission to be made to the Interpretations Committee and recommends that no further action is taken on this matter.