IASB Update

Financial instruments projects

June 2023

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Overview

Projects of the IASB Financial Instruments team

		Next milestone
Amendments to the Classification and Measurement of Financial Instruments	Maintenance	ED Published on 21 March 2023 Comment period ends 19 July 2023
Post-implementation review of IFRS 9—Impairment	Research	Publish Request for Information May 2023
Dynamic Risk Management	Standard-setting	Further discussions on the DRM model
Financial Instruments with Characteristics of Equity	Standard-setting	Publish Exposure Draft

Amendments to the Classification and Measurement of Financial Instruments

Objectives

The IASB's objectives

To respond to feedback on the PIR of the classification and measurement requirements in IFRS 9 by improving:

- the understandability of some of these requirements; and
- the usefulness of related information disclosed by an entity applying the requirements in IFRS 7

Exposure Draft published in March 2023

The IASB proposes amendments relating to:

- derecognition of financial liabilities settled through electronic transfer;
- classifying financial assets through assessing whether contractual cash flows are solely payments of principal and interest on the principal amount outstanding (SPPI);
- disclosure of information about some financial instruments

Derecognition of financial liabilities

When can an entity derecognise a financial liability?

- IFRS 9 usually requires ***settlement date*** accounting for financial assets and financial liabilities
- An entity is permitted to deem a financial liability that is settled using an electronic payment system to be discharged ***before the settlement date*** if, and only, if the entity has initiated the payment instruction and there is:
  - no ability to withdraw, stop or cancel the payment instruction
  - no practical ability to access the cash
  - insignificant settlement risk

Classification of financial assets

When can an entity measure a financial asset with ESG-linked features at amortised cost?

- No exemption from SPPI requirements for ESG-linked features
- The IASB is clarifying the guidance on how to assess whether contractual cash flows are ***SPPI***, including considering:
  - elements of interest in a basic lending arrangement
  - contractual terms that change the amount or timing of contractual cash flows

What other amendments are the IASB proposing to the SPPI requirements?

- The IASB is proposing clarifications to the assessment of contractual cash flows for financial assets with non-recourse features and contractually linked instruments.

IFRS Accounting

Disclosures

What disclosure requirements are the IASB proposing?

- information about the fair value change of ***equity investments designated at FVOCI*** derecognised during the period
- qualitative and quantitative information about financial assets and financial liabilities with contractual terms that could ***change the timing or amount of contractual cash flows based on a contingent event*** that is specific to the debtor

Next step

- The IASB will consider the comments it receives on the Exposure Draft and will decide whether to proceed with the proposed amendments
- The comment letter deadline is ***19 July 2023***
- The ED and supporting material is available on the project website.

Post-implementation review of IFRS 9—Impairment

The IFRS 9 journey

2009 — **Post-financial crisis**

2014 — **IFRS 9 issued**

2018 — **IFRS 9 effective**

2020 — PIR of IFRS 9—Classification and Measurement started

2022 — PIR of IFRS 9—Impairment started

IFRS 9 developed in three phases
IASB accelerates project to improve accounting for financial instruments, including address the ‘too little, too late’ problem

Completed in 2022
IASB concluded that the requirements are generally working well but some clarifications are needed. IASB proposed amendments considering the stakeholders’ feedback

PIR of IFRS 9—Hedge accounting will follow

PIR—what is the objective?

OBJECTIVE	To **assess** whether the effects of applying the new requirements on users of financial statements, preparers, auditors and regulators are as intended when the IASB developed those new requirements
Overall, are the requirements working as intended?	**Fundamental questions** (fatal flaws) about the core objectives or principles—their clarity and suitability—would indicate that the new requirements are not working as intended
Are there specific application questions?	**Specific application questions** would not necessarily prevent the IASB from concluding that the new requirements are operating as intended but may nonetheless need to be addressed, if they meet the criteria for whether the IASB would take further action

Post-implementation review of IFRS 9—Impairment

Objective

Opportunity to assess the effects of the new requirements on companies, investors, auditors and regulators

Scope

Impairment requirements only

Request for information

RFI

Expected to be published
End of May 2023

Comments would be due
End of September 2023

Request for Information—what topics are being examined?

1 Overall—impairment

2 General approach to recognising ECL

3 Determining significant increases in credit risk

4 Measuring ECL

5 Simplified approach for trade and lease receivables

6 Purchased or originated credit-impaired financial assets

7 Applying ECL requirements with other requirements

8 Transition

9 Credit risk disclosures

10 Other matters

Request for Information—what questions is the IASB asking?

A **Are there fundamental questions (fatal flaws) on the clarity and suitability of the core objectives or principles in the impairment requirements?**

- Do the requirements achieve its objective of providing useful information about changes in credit risk and timely recognition of expected credit losses?
- Have the requirements addressed the issues they were designed to address?

B **Are the benefits to investors arising from applying the requirements significantly lower than expected?**

C **Are the costs of applying some or all of the requirements and auditing and enforcing their application significantly greater than expected?**

- Are the ongoing costs of applying the requirements significantly greater than expected or the benefits of the resulting information significantly lower than expected?
- Are the requirements and application guidance capable of being applied consistently?
- If diversity in practice exists, what is the cause and what is the effect?

Dynamic Risk Management

Objective and current status of the DRM project

The objective of the DRM project is to better reflect:

- How interest rate risk management affects amount, timing and uncertainty of cash flows
- Effect of risk management activities on the financial statements

2014	2017-2019	Q4 2020-Q2 2021	Q2 2021-Q2 2022	May 2022	Q3 2022 - present
DP: Portfolio Revaluation Approach	Developed DRM core model	Identified key issues through outreach	Discussed key issues and suggested refinements	Project status changed to 'Standard setting'	Working towards Exposure Draft

What is it about?

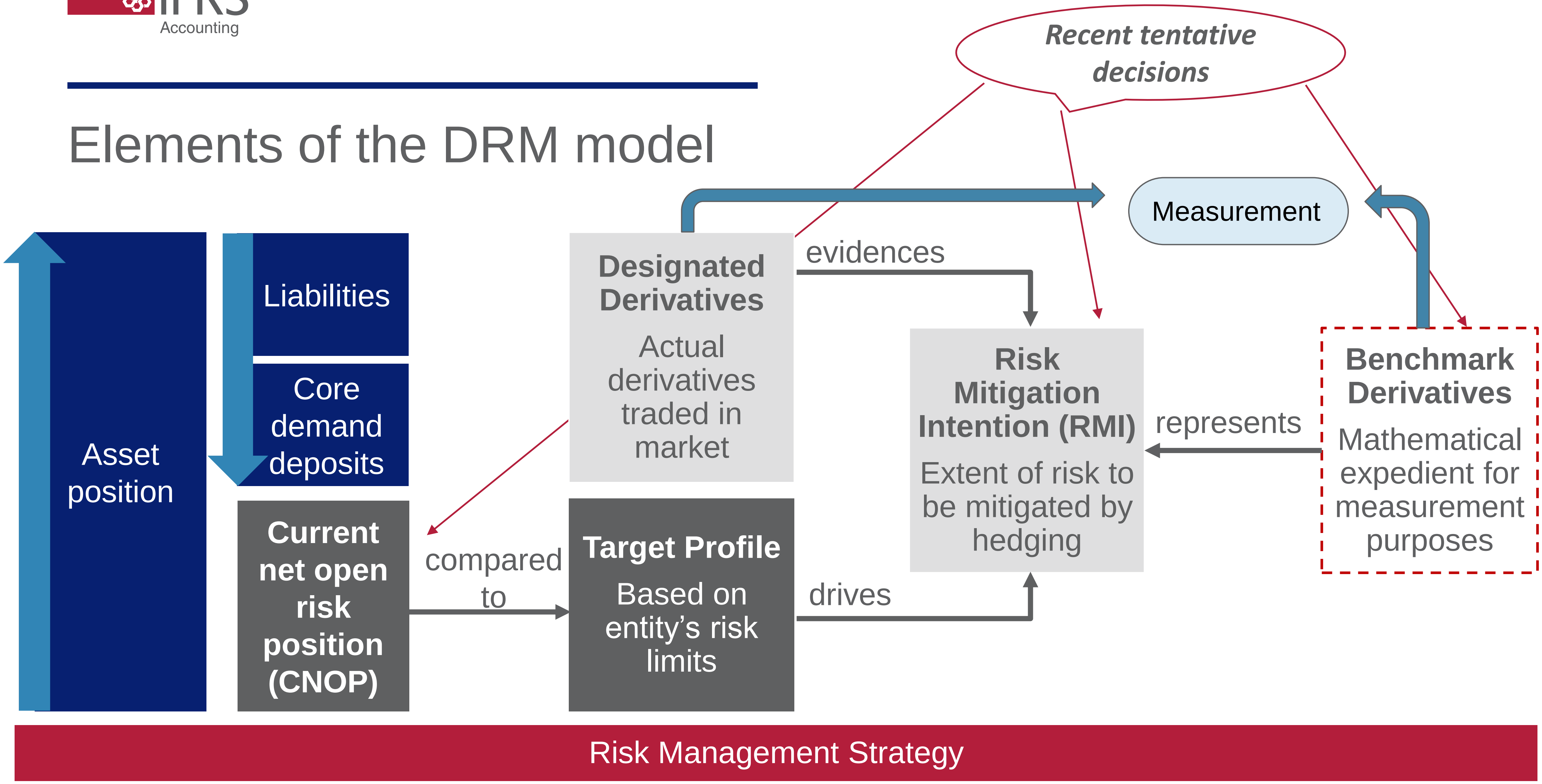
It is about dynamic interest rate risk management

- Process to manage repricing risk in financial assets and liabilities due to changes in interest rate risk
- Risk mitigating activities done using pre-defined risk limits set out in risk management strategy
- DRM model aims to better reflect the effect of these activities in the financial statements

Challenges the DRM model tries to address

- ***Transparency*** — add transparency to the financial statements
- ***Eligible items*** — widening of the scope of eligible items to better reflect risk management
- ***Dynamic nature*** — better depict the dynamic nature of portfolios of assets and liabilities
- ***Performance measurement*** — definition of reliable metric demonstrating if management was successful in achieving the risk management strategy

Elements of the DRM model



Mechanics of the DRM Model—Measurement

What to measure?

Risk Mitigation Intention

Extent of **risk** to be mitigated by hedging

Benchmark Derivatives

Compare Fair Values

Designated Derivatives

Derivatives traded in the market to mitigate **risk**

Calculate the 'lower of':

a) the **cumulative gain or loss** on the designated derivatives from inception of the DRM model; and

b) the **cumulative change in fair value** of the risk mitigation intention attributable to repricing risk from inception of the DRM model.

Where to recognise the aligned portion?

The aligned portion—the lower of (a) and (b)—is recognised in the statement of financial position as the DRM adjustment (subject to the 'capacity test')

Where to recognise the misaligned

The misaligned portion (ie changes in fair value of designated derivatives exceeding the aligned portion) is recognised in profit or loss

Next steps

Continuous engagement with our stakeholders

The staff engages with our stakeholders through:

- Publication of webcasts explaining the DRM model:
    - Webcast October 2022
    - Update April 2023
- Formal and informal outreach with stakeholders

Further deliberations of the IASB

The IASB will continue its discussion on the topics identified in the project plan, such as:

- The target profile and its alignment with an entity's risk management strategy
- Designated derivatives
- Performance assessment and the capacity test
- Presentation and disclosure requirements
- Transition requirements

Financial Instruments with Characteristics of Equity

IFRS Accounting

Objective, challenges and sensitivities

Objective

- Improve information provided in financial statements about issued financial instruments
- Address **known practice issues** applying IAS 32 *Financial Instruments: Presentation* by clarifying underlying principles and not fundamentally rewriting IAS 32

Challenges and sensitivities

- IAS 32 is not completely broken
- There is no one classification approach that everyone will agree on
- New terminology and descriptions lead to new questions
- If classification were to change this is a big deal vs if classification were to remain mostly the same, why do we need all the work to get to the same classification outcome?
- Economically similar instruments but different classification outcomes
- Consistency with other standards, eg Conceptual Framework
- Consistency within IAS 32
- The need to address many unresolved IFRS Interpretations Committee issues

Project update: Classification

IASB tentative decisions (April 2020—February 2023)

- Financial instruments settled in own equity instruments (including ‘fixed-for-fixed’ condition)
- Obligations that arise only on liquidation (eg perpetual instruments)
- Financial instruments with contingent settlement provisions
- The effects of applicable laws on contractual terms
- Financial instruments for which settlement of the contractual obligation is at the discretion of the issuer’s shareholders
- Reclassification of issued financial instruments
- Financial instruments containing obligations to redeem own equity instruments (including put options on non-controlling interests)

Project update: Presentation

IASB tentative decisions (December 2022—February 2023)

- Financial liabilities containing contractual obligations to pay amounts based on an entity’s performance or changes in its net assets and that are measured at fair value through profit or loss
- Issued equity instruments

Project update: Disclosures

IASB tentative decisions (April 2021—April 2023)

- Terms and conditions for financial instruments with characteristics of both financial liabilities and equity instruments
- Nature and priority of claims against an entity
- Terms and conditions about priority on liquidation for particular financial instruments
- Potential dilution
- Other terms and conditions
- Additional disclosures to complement the classification and presentation proposals

Transition and next step

Transition

- The IASB tentatively decided:
  - to require a company to apply the proposed amendments *retrospectively with the restatement of comparative information*.
  - to provide some transition relief and require some disclosure on transition for entities already applying IFRS Accounting Standards
  - not to provide any additional transition relief for first-time adopters

Next step

- The IASB will publish an Exposure Draft of amendments to IAS 32, IAS 1 and IFRS 7 in Q4 2023 with a *comment period of 120 days*.

Primary Financial Statements - Overview

Project overview

Q4 2019	Q1–Q3 2020	Q4 2020 – Q3 2022	Q4 2022	2023
Exposure Draft published	Consultation period	Discussion of feedback and key redeliberations	Targeted outreach on specific topics	Discussion of feedback and complete redeliberations

Objective

- Improve communication in financial statements
- Focus on information included in the statement of profit or loss

Main proposals

1. Require additional **defined subtotals** in statement of profit or loss
2. Require disclosures about **management performance measures**
3. Strengthen requirements for **disaggregating information**

Statement of profit of loss

Statement line item	Category
Revenue	Operating
Other income	Operating
Changes in inventories of finished goods and work in progress	Operating
Raw materials used	Operating
Employee benefits	Operating
Depreciation	Operating
Amortisation	Operating
Operating profit	
Income and expenses from associates and joint ventures	Investing
Operating profit and income and expenses from investments accounted for using the equity method *(specified subtotal)*	
Income and expenses from investments	Investing
Income and expenses from cash and cash equivalents	Investing
Profit before financing and income tax	
Income and expenses from liabilities that arise from transactions that involve only the raising of finance	Financing
Unwinding of discount on provisions	Financing
Profit before tax	
Income tax	
Profit for the year	

Line items illustrate what is included in each category and do not necessarily denote specified line items. An entity would present line items that provide an understandable overview of the entity's income and expenses.

Definition of MPMs

Subtotals of income and expenses not specified by IFRS Accounting Standards that:

Are used in public communications outside financial statements (excluding oral communications, transcripts and social media posts)

=

Communicate management's view of an aspect of an entity's financial performance

Rebuttable presumption that a subtotal used in public communications represents management's view of an aspect of an entity's financial performance—rebutted with reasonable and supportable evidence (including management communicating or using a subtotal in a way that is consistent with the assertion that the subtotal does not communicate management's view).

The rebuttable presumption is intended to:

- reduce the subjectivity involved in identifying the subtotals that represent management's view; and
- avoid requiring entities to include as management performance measures, subtotals of income and expenses that do not represent management's view of an aspect of the entity's performance

What disclosures will be required for MPMs?

Reconciliation	Reconciliation between MPM and the most directly comparable subtotal or total specified by IFRS Accounting Standards, including the income tax effect and effect on non-controlling interests
Why an MPM communicates management's view	Includes an explanation of how the MPM is calculated and how the measure provides useful information about the entity's performance. Explanation should refer to individual reconciling items where necessary
Not necessarily comparable with other entities	A statement that MPM provides management's view of an aspect of the entity's financial performance and is not necessarily comparable with measures provided by other entities
Changes in calculation	Explanation of and reasons for any changes in how the entity calculates its MPMs or which MPMs it provides

What will be the disaggregation requirements?

General requirements and specified line items	Roles of the primary financial statements (PFS) and the notes	Principles for aggregation and disaggregation
	Specified line items	Aggregating items and using meaningful labels
Specific requirements	Disclosure of amounts included in each function line item in statement of profit or loss for depreciation, amortisation, employee benefits, impairments and write-downs of inventory	Present operating expenses by nature and by function (mixed presentation permitted)

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