IFRS Foundation

Staff paper

Agenda reference 2

IFRS Foundation Trustees meeting—Due Process Oversight Committee

Date	**December 2022**
Project	**Post-implementation Review of IFRS 9—Classification and Measurement**
Topic	**Draft Project Report and Feedback Statement**
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Confirmation requested from the Due Process Oversight Committee (DPOC)

At its November 2022 meeting the International Accounting Standard Board (IASB) decided that sufficient work had been completed to conclude the Post-implementation Review and requested the staff prepare the Project Report and Feedback Statement on the Post-implementation Review of IFRS 9—*Classification and Measurement* (the Report).

The IASB expects to finalise the Report in the near future, if the DPOC is satisfied the IASB has completed the Post-implementation Review satisfactorily.

Does the DPOC agree, based on the materials provided, that the IASB has completed the Post-implementation Review satisfactorily and that the Report can be finalised and published?

Introduction

1. The purpose of this paper is to report on the due process undertaken in the Post-implementation Review of IFRS 9—Classification and Measurement.
2. The IFRS Foundation Due Process Handbook (*Due Process Handbook*) requires the IASB to report to the DPOC when it has completed a post-implementation review and provide the DPOC with a draft of the Report. A draft of the Report has been circulated to the DPOC (but not as a public paper, given that it is still draft).
3. The DPOC is asked to confirm, based on the materials provided, that the IASB has completed the Post-implementation Review satisfactorily and that the Report can be finalised and published.

Background

4. The IFRS Foundation's *Due Process Handbook* states that a post-implementation review has two phases. During both phases, the IASB reviews relevant academic research and other reports.
   (a) Phase 1— the IASB identifies matters to be examined, drawing on discussions with the Interpretations Committee, the IASB's advisory groups and other interested parties. The IASB consults publicly on the matters identified in the first phase of the PIR.

(b) Phase 2— the IASB considers the comments from the public consultation along with the information it has gathered from any additional analysis and other consultative activities.

5. A post-implementation review ends when the IASB presents its findings and sets out the steps it plans to take, if any, as a result of the review.

Purpose of a post-implementation review

6. When the IASB issues a new requirement, it includes an effects analysis of the likely benefits and costs arising from the new requirement. Costs comprise initial and ongoing financial and other costs.

7. The objective of a post-implementation review is to assess whether the information a company provides when it applies the new requirements affects users of financial statements, preparers, auditors and regulators in the way the IASB intended when it developed those new requirements.

8. A post-implementation review includes consideration of how contentious matters that the IASB considered during development of the new requirements, and how market developments since those new requirements were issued, are being addressed in practice.

9. A post-implementation review concludes with a determination of whether:

(a) overall, the new requirements are working as intended. Fundamental questions (ie 'fatal flaws') about the clarity and suitability of the core objectives or principles in the new requirements would indicate that they are not working as intended; and

(b) there are specific questions about application of the new requirements. If there are specific application questions, the IASB may still conclude that the new requirements are working as intended. However, those specific application questions would be addressed if they meet the criteria for whether the IASB would take further action.

10. A post-implementation review is not a standard-setting project and does not automatically lead to standard-setting. It is also not intended to lead to the resolution of every application question.

11. However, post-implementation reviews can identify improvements that can be made to a new requirement, to the standard-setting process or the structure of Accounting Standards.

The IASB's objectives when issuing IFRS 9—Classification and Measurement

12. IFRS 9 *Financial Instruments* was finalised and issued in 2014 and became effective for annual periods beginning on or after 1 January 2018.

13. IFRS 9 was developed with the overall objective of improving the requirements for financial reporting of financial instruments to enhance the relevance and understandability of information about financial instruments for users of financial statements. IFRS 9 was issued in three discrete stages reflecting the key areas of the requirements: classification and measurement, impairment and hedge accounting.

14. The IASB's overall objective when issuing the classification and measurement requirement in IFRS 9 was to improve financial reporting of financial instruments by providing a logical, single classification and measurement approach for financial assets that reflects the business model in which they are managed and their cash flow characteristics. The IASB also introduced a reclassification approach to reflect changes in an entity's business model, to replace complicated

reclassification rules in IAS 39 *Financial Instruments: Recognition and Measurement*. In addition, IFRS 9 addresses the issue of volatility in profit and loss that resulted from entities measuring their own debt at fair value (so called 'own credit' issue) by requiring that the effects of changes in the credit risk of financial liabilities designated under the fair value option are presented in other comprehensive income (OCI).

How the Post-implementation Review was conducted

15. In October 2020, the IASB began the first phase of the Post-implementation Review of *IFRS 9: Financial Instruments—Classification and Measurement.* At its December 2020 meeting, the IASB discussed the plan for the first phase of the Post-implementation Review.

16. In the first phase of the Post-implementation Review the IASB members and staff held over 20 meetings with a wide range of stakeholders to understand and gather evidence on the experience of implementing and applying the classification and measurement requirements of the Standard. Stakeholders consulted included academics, investors, preparers, regulators, auditors and standard-setters, and the IFRS consultative bodies (Capital Markets Advisory Committee, Global Preparers Forum, Accounting Standards Advisory Forum).

17. Generally, stakeholders said that the classification and measurement requirements work well in practice and are an improvement to the rule-based approach that applied previously under IAS 39.

18. As part of the first phase of the Post-implementation Review, the IASB reviewed academic research and other literature; materials published alongside IFRS 9; and Agenda Decisions issued by the IFRS Interpretations Committee to understand empirical evidence on implementation and application of the classification and measurement requirements of the Standard.

19. In September 2021 the IASB approved the publication of the *Request for Information Post-implementation Review of IFRS 9—Classification and Measurement* (the RFI). Based on the evidence gathered in the first phase, the IASB decided to focus the RFI on particular matters relating to the classification and measurement requirements of the Standard. The RFI was published on 30 September 2021, with comments due on 28 January 2022 (a 120-day comment period).

20. After publishing the RFI, in October 2021 the IASB entered the second phase of the Post-implementation Review in which it began extensive and focused consultation with stakeholders—consulting again with the IFRS consultative bodies (Islamic Finance Consultative Group, Emerging Economies Group, Capital Markets Advisory Committee, Accounting Standards Advisory Forum). During this period, the IASB members and staff also continued its consultation with stakeholders, participating in more than 20 events with preparers, regulators, auditors, standard-setters and industry representative bodies.

21. The IASB received 95[1] comment letters on the RFI. Although the IASB received only one comment letter from users of financial statements, IASB members and staff participated in a number of discussions with investors and analysts as part of the outreach activities.

22. In March 2022, the IASB discussed the summary of feedback received on the RFI.

23. At its meeting in June 2022, an academic literature review update was presented to the IASB. In addition to the literature considered during the first phase of the PIR, this review also included five additional papers, three of which were accepted for publication in the Special Issue of the *Australian*

[1] Including one comment letter that was received after the deadline.

Accounting Review that focused on academic research related to the application and impact of IFRS 9.[2]

24. Between April 2022 and November 2022, the IASB considered the findings from the second phase to decide what, if any, action to take.

25. At its November 2022 meeting the IASB decided that sufficient work has been completed to conclude the Post-implementation Review and requested the staff to prepare the Report. The IASB expects to publish the Report in December 2022.

26. Appendix A of this paper sets out the due process steps followed in the post-implementation review. Appendix B of this paper sets out the distribution of respondents and participants by stakeholder type and by geographical region.

Approach to assessing evidence

27. In September 2022, the IASB discussed a clarified description of the objective, process and outcome of a post-implementation review reflecting discussions with the DPOC in May and June 2022[3]. For this Post-implementation Review, the IASB applied the following two-step approach—set out in the clarified description—to identify and prioritise matters arising in the second phase of the Post-implementation Review. The IASB assessed:

    (a) whether matters warrant further action; and

    (b) how such matters should be prioritised.

Assessing whether matters warrant further action

28. The IASB takes action, subject to the prioritisation criteria (detailed in paragraph 29 of this paper), if there is evidence that:

    (a) there are fundamental questions (ie 'fatal flaws') about the clarity and suitability of the core objectives or principles in the new requirements; or

    (b) 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

    (c) 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).

Assessing the priority of the matters that warrant further action

29. The prioritisation of matters as high, medium or low depends on the extent to which evidence gathered during the Post-implementation Review indicates:

    (a) the matter has substantial consequences;

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[2] Australian Accounting Review is an independent peer reviewed academic journal which publishes research relevant to academics and practitioners https://onlinelibrary.wiley.com/journal/18352561

[3] For further detail refer to September 2022 meeting of the IASB, AP8A: Post-implementation reviews—Objectives and process

(b) the matter is pervasive;

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

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

30. The prioritisation of matters as high, medium or low determines how and when the matter is addressed.

Findings from the Post-implementation Review

31. After analysing the evidence gathered in the Post-implementation Review, the IASB concluded that the classification and measurement requirements in IFRS 9 are working as intended. In particular, the IASB concluded that:

(a) there are no fundamental questions (ie 'fatal flaws') about the clarity or suitability of the core objectives or principles in the new requirements;

(b) the requirements can be applied consistently apart from those requirements that are, or will be, subject to a narrow-scope standard setting or research project (see paragraphs 32–35 of this paper);

(c) the information provided by the Standard is useful to users of financial statements; and

(d) no unexpected costs arose when applying or enforcing the classification and measurement requirements of IFRS 9, nor when using or auditing information the Standard requires an entity to provide.

32. Applying the approach in paragraphs 27–30 of this paper to the matters arising from the Post-implementation Review, the IASB considered the matter of assessing contractual cash flow characteristics of a financial asset with ESG[4]-linked features to be of high priority (paragraphs 37–39). The IASB decided to start a standard-setting project to clarify requirements in relation to this matter before diversity in practice becomes embedded.

33. The IASB also identified lower-priority matters that require standard-setting:

(a) application of the contractual cash flow characteristics assessment to contractually linked instruments (Question 3 of the Request for Information). The requirements for contractually linked instruments are part of, and therefore need to be consistent with, the clarifications to the contractual cash flows characteristics requirements (paragraphs 37–39);

(b) cash received via electronic transfer as settlement for a financial asset (Question 9 of the Request for Information) because it is pervasive and relates to a financial reporting issue that can be addressed by the IASB in a timely manner (paragraphs 40–43); and

(c) disclosures of fair value changes on equity instruments a company has presented in other comprehensive income rather than in profit or loss (OCI presentation election) (Question 4 of the Request for Information). These additional disclosures will ensure that users of financial

[4] Environmental, Social and Governance (ESG)

statements are provided with more transparent information about the performance of such investments (paragraphs 44–49).

34. Although these matters would not, on their own, justify immediate action as they were not considered high priority items, the IASB decided it would be most efficient for stakeholders (for the reasons explained in paragraph 33 of this paper) to include these proposed amendments in a single exposure draft (Amendments to the Classification and Measurement of Financial Instruments), with the amendments to clarify requirements for financial instruments with ESG-linked features. The IASB started work on this project concurrently with analysing feedback on the other areas of the Post-implementation Review and the exposure draft is expected to be published in the first half of 2023.

35. In considering the prioritisation criteria in paragraph 27–30 of this paper, the IASB classified the application of the findings related to amortised cost measurement and modifications of financial assets and financial liabilities as a medium priority. It decided to add a project to its research pipeline to explore whether these requirements could be clarified in an effective manner (paragraphs 50–54). There are likely to be interdependencies between the scope of this project and the expected credit loss requirements in IFRS 9. The IASB is of the view that this will likely be a wider scope project that will require more time to resolve and therefore decided to only start this project after considering the findings on the post-implementation review of the impairment requirements.

36. The IASB decided no further action was required on other matters identified in the Post-implementation Review.

Contractual cash flow characteristic of a financial asset (including ESG-linked financial assets and contractually linked instruments)

37. At its meeting in April 2022, the IASB discussed feedback received on the application of the contractual cash flow characteristics requirements in IFRS 9. Consistent with the IASB's understanding before commencing the Post-implementation Review, two types of financial instruments were noted as areas where stakeholders are experiencing application challenges:

    (a) financial instruments with ESG-linked features—challenges relate to interest rates that are adjusted depending on the borrower meeting a pre-determined ESG target that is specific to the borrower and whether these financial instruments would meet the requirements in IFRS 9 to be measured at amortised cost.

    (b) contractually linked instruments (CLI)—respondents requested clarification on the scope of transactions to which the CLI requirements apply and how to apply those requirements. This includes questions on the interaction between the requirements for CLIs and for financial assets with non-recourse features.

38. In May 2022, the IASB decided to start a project to clarify particular aspects of the IFRS 9 requirements for assessing a financial asset's contractual cash flow characteristics. These clarifications seek to support consistent application of requirements to determine whether to measure financial assets at fair value or amortised cost

39. This project will not seek to provide an exemption from existing requirements for financial instruments with particular features (eg sustainability) but rather to clarify the principles in IFRS 9.

Cash received via electronic transfer as settlement for a financial asset

40. Respondents to the RFI asked the IASB to consider the implications of the tentative (ie draft) agenda decision of the Interpretations Committee published in September 2021 in relation to cash received via electronic transfer in settlement of a financial asset. In their view, the application of the requirements set out in the tentative agenda decision would have significant impacts on long-standing and established practice and would therefore lead to significant operational challenges and costs to apply.

41. Although the Interpretations Committee's tentative agenda decision focussed on applying the derecognition requirements in IFRS 9 to financial assets, most of the practical concerns raised by stakeholders related to financial liabilities.

42. In response to this feedback, the IASB—at its October 2022 meeting—tentatively decided to permit entities (through an accounting policy choice) to derecognise a financial liability before it delivers cash on the settlement date when specified criteria are met[5].

43. However, to reduce diversity in practice and assist with the consistent application of the derecognition requirements in IFRS 9 to both financial assets and financial liabilities, the IASB tentatively decided at its November 2022 meeting to also clarify that for the derecognition of financial assets and financial liabilities, an entity applies settlement date accounting (that is the date the cash delivered by or to the entity).

Disclosures for equity instruments for which the OCI presentation election was made

44. At its meetings in June 2022 and October 2022, the IASB discussed feedback and evidence on accounting for investments in equity instruments for which an entity has elected to present subsequent changes in fair value in other comprehensive income (OCI) rather than profit or loss. Applying IFRS 9, the gains or losses presented in OCI whilst the entity holds the investment are not subsequently taken out of OCI and recognised in profit or loss ('recycled') when the investment is sold.

45. This was one of the areas that attracted the most feedback and respondents' views were split between those that agree that the requirements are working as intended and those that think gains or losses on disposal should be recycled to profit or loss. Most of the respondents that asked for recycling to profit or loss to be required, were from the insurance industry. In their view, the requirements for equity investments for which the OCI presentation election was made, do not provide users of financial statements with the most useful information about the performance of equity instruments that an entity intends to hold for the long-term. They believe that the best information about such equity instruments would be provided by presenting fair value changes in OCI over the period the entity holds the instrument and recycling those gains and losses to profit or loss in the period of disposal.

46. However, some respondents, notably prudential and securities regulators, said that they have not identified any evidence that suggests the IFRS 9 requirements had impacted entities' investment decisions. This view was consistent with findings of some of the academic studies referred to in paragraph 23 of this paper.

47. After considering the feedback, the IASB decided not to make any changes to the requirements in IFRS 9 because it did not identify any evidence that there are fundamental questions about the suitability or clarity of the requirements for equity investments or that the benefits to users of

[5] The IASB will consider this matter further in AP16B of the November 2022 IASB meeting.

financial statements, or costs of applying the requirements, are significantly different from what the IASB expected. However, the IASB will continue to monitor and evaluate any new evidence—as and when it becomes available (for example when insurance companies have applied IFRS 9)—that indicates that users of financial statements consider the information provided is not relevant or is not a faithful representation of entities' performance.

48. The IASB acknowledged respondents' feedback that the current disclosure requirements for equity instruments to which the OCI presentation option is applied, are not necessarily adequate in communicating all the relevant and useful information about the performance of the investments to users of the financial statements. Although IFRS 7 requires disclosure of the gain or loss on disposal of such an equity investment, it does not require disclosure of information about fair value changes presented in OCI during the reporting period on investments the entity continues to hold.

49. The IASB therefore decided to propose additional disclosure requirements in IFRS 7 to improve transparency of the information presented in OCI and provide users of the financial statements with a more comprehensive view of the performance of these investments in equity instruments.

Amortised cost measurement and modifications

50. At its meeting in July 2022, the IASB discussed the findings of the Post-implementation Review on the requirements for amortised cost measurement and the effective interest method as well as modifications of financial assets and financial liabilities.

51. Respondents to the RFI stated that further clarification and additional application guidance are needed to resolve existing diversity in practice with regards to particular aspects of the modification requirements in IFRS 9.

52. Respondents also said that the effective interest method is an area that gives rise to many application questions in practice due to the lack of guidance and clear principles to determine how to account for adjustments to contractual cash flows.

53. In response to the feedback, the IASB decided to add a project on amortised cost measurement to its research pipeline to clarify the requirements for applying the effective interest method and modifications of financial assets and liabilities.

54. The IASB acknowledge the potential interaction between the application questions on modifications and amortised cost measurement, and the expected credit loss requirements in IFRS 9. Therefore, any forthcoming project will also consider the potential findings from the Post-implementation Review of IFRS 9—Impairment that recently started.

Appendix A—Confirmation of Due Process Steps

Table A1—Due process steps			
Step	**Required/optional due process step**	**IASB**	**DPOC**
Timeline for the post-implementation review established.	Required	The IASB added the Post-implementation Review to its work plan in October 2020. At its meeting in December 2020, the IASB discussed the objectives, activities and timeline for the first phase of the Post-implementation Review.	The DPOC was informed in March 2021 that the work on the first phase of the Post-implementation Review had commenced.
Establishment of scope, including identifying the important or contentious issues that arose during development of the Standard	Required	In the first phase, more than 20 meetings were held with stakeholders including preparers, auditors, investors, standard-setters and regulators. This included meetings with the IASB's consultative bodies. The history of the development of the Standards together with matters subsequently brought to the attention of the IASB and/or the IFRS Interpretations Committee were analysed to identify the important and contentious issues. The IASB also performed an academic literature review to understand empirical evidence on implementation and application of the Standards. The IASB considered a summary of feedback from its phase 1 outreach and identified matters it	The DPOC were reminded of activities being undertaken in the first phase of the Post-implementation Review at its June 2021 meeting.

		considered warranted further examination at its July 2021 meeting.	
After the initial assessment, one of two routes may be taken: (d) a request for information published to invite public comment, with appropriate response period; or (e) after its initial assessment, the IASB may decide that it would be premature to undertake a review at the time.	Required	At its September 2021 meeting, the IASB approved the publication of the RFI and set a 120-day comment period.	The DPOC were informed in October 2021 that the RFI was published with a comment period of 120 days.
The IASB considers whether it is necessary to supplement the findings from the Request for Information with other evidence, such as an analysis of financial information, a review of academic or other related research on the implementation of the Standard being reviewed, or consultations with relevant parties.	Optional	During the second phase of the Post-implementation Review the IASB conducted extensive and focused consultation with stakeholders, including the IFRS consultative bodies. At its June 2022 meeting, the IASB discussed an update to the academic literature review conducted in the first phase of the Post-implementation Review, including five additional academic research papers.	Not applicable
Project teams analyse and summarise comment letters for the IASB's consideration. The IASB posts all	Required	The IASB discussed a summary of the feedback received on the RFI at its March 2022 meeting.	The DPOC were informed, at its March 2022 meeting, that the staff were analysing feedback from comment letters and outreach, with plans to

comment letters in relation to the Request for information online.		All comment letters and summaries of the feedback were posted on the project page on the IFRS Foundation's website.	begin discussions with the IASB at its March 2022 meeting.
Follow up action after concluding the Post-implementation Review.	Required	The IASB discussed what action, if any, it should take at its meetings between April 2022 and November 2022. The IASB's decisions are summarised in paragraphs 31–54 of this paper.	The DPOC were provided with an update on the IASB's decisions on matters identified in the RFI at its meetings in June 2022 and October 2022.
IASB meetings are held in public and papers are publicly available. All decisions are made in a public session.	Required	The Post-implementation Review was discussed at public IASB meetings held between October 2020 and November 2022. The project page on the IFRS Foundation's website has been maintained throughout the project.	The DPOC was informed about progress on the Post-implementation Review at its meetings in March 2021, October 2021, March 2022, June 2022 and October 2022.
The IASB presents its findings in a public report.	Required	The draft report has been circulated to the DPOC.	The DPOC is asked to confirm that the IASB may finalise the Report at this meeting.
Recommendations to DPOC about changes to the IASB's procedures (such as how the effects of a Standard should be assessed or additional steps that should be taken in developing a Standard).	Optional	None identified	Not applicable

Appendix B—Respondents and participants by stakeholder type and by geographical region

Public consultation through a Request for Information

In September 2021, the IASB published a RFI for public comment. The RFI was open for comment until 28 January 2022. The IASB received 95[6] comment letters, which are available on the IFRS Foundation's website.

The data in these tables should be considered in conjunction with the stakeholder engagement events to gather feedback during the Post-Implementation Review.

Respondents to the Request for Information represented various stakeholder groups:

Table B1 – Respondents by stakeholder type

Type of respondent	Number of respondents	Percentage of respondents (%)
Accounting firm	9	10
Preparer	36	38
Regulator	8	8
Standard-setting and/or accountancy body	33	35
User	1	1
Other	8	8
Total	95	100

Table B2 – Respondents by geographical region

Geographical region	Number of respondents	Percentage of respondents (%)
Africa	2	2
Asia	21	22
Europe	49	52
Latin America	6	6
North America	4	4
Oceania	4	4
Global	9	10
Total	95	100

[6] Included in this total is one comment letter which was received after the comment period deadline.

Stakeholder engagement

During the Post-implementation Review, IASB members and technical staff met with a wide range of stakeholders, which included participating in 24 stakeholder-engagement events during Phase one and 21 events during Phase two of the Post-implementation Review. Stakeholders consulted included academics, investors, preparers, regulators, auditors and standard-setters, and the IFRS consultative bodies (Capital Markets Advisory Committee, Global Preparers Forum, Accounting Standards Advisory Forum). Some of the events were facilitated by standard-setters or professional accountancy bodies.

The events included participants from various stakeholder groups:

Table B3—Participants by stakeholder type

Type of participant	Number of events	Percentage of events (%)
Academics	3	7
Accounting firms	6	13
Preparers and industry organisations	19	42
Regulators and government agencies	2	5
Standard-setters	6	13
Users of financial statements	3	7
Mixed[7]	6	13
Total	45	100

The events included participants from various geographical regions:

Table B4—Participants by geographical region

Geographical region	Number of events	Percentage of events (%)
Asia	3	7
Europe	19	42
North America	1	2
Global[8]	22	49
Total	45	100

[7] Includes various types of participants, including investors and analysts
[8] Includes participants from across the world