STAFF PAPER

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IASB® meeting

Project	**IBOR Reform and the Effects on Financial Reporting – Phase 2**
Paper topic	Project plan and preliminary timing

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Introduction

1. The purpose of this paper is to provide the Board with a project plan that sets out the potential issues that the Board will need to consider in the second phase of the *IBOR Reform and the Effects on Financial Reporting* project. This paper also provides the indicative timing of when the staff plan to present these issues to the Board for discussion. In light of that, this paper summarises:
   - (a) The preliminary scope of potential issues to be considered in the second phase of the project; and
   - (b) A high-level project timeline with the indicative timing and key areas for discussion with the Board at future meetings.
2. This paper does not include any staff analysis or recommendations to the Board and thus the staff is not asking the Board to make any decisions based on this paper. Nevertheless, the staff welcome any questions or comments that the Board members may have on the preliminary scope and the high-level project timeline.
3. The scope of Phase 2 of this project is broader than the previous phase as it will encompass different areas in financial instruments accounting and could also include other areas of accounting. At future Board meetings, the staff will analyse each of the potential accounting issues listed in this paper and make

recommendations to the Board on how these issues could be addressed. However, this does not mean that all those accounting issues will result in amendments to IFRS Standards to provide relief through exceptions to existing requirements. In particular, when IFRS Standards provide an adequate basis to account for a particular issue and the accounting outcome results in useful information to users of financial statements by faithfully representing the economic effects of the reform, the staff do not believe that any amendments to current IFRS Standards are needed.

4. The staff also note that, should the Board decide to propose an amendment to IFRS Standards in the form of a narrow-scope exception or additional application guidance, any such amendment would be subject to the Board's due process for developing an Exposure Draft.

5. This paper is structured as follows:

   (a) Background (paragraphs 6–9);

   (b) Objective of Phase 2 (paragraphs 10–12);

   (c) Preliminary scope of issues (paragraphs 13–16); and

   (d) High-level project timeline (paragraphs 17–18).

Background

6. When developing the exceptions proposed in the Exposure Draft *Interest Rate Benchmark Reform* ('IBOR ED'), published in May 2019, the Board acknowledged the increasing level of uncertainty about the long-term viability of some interest rate benchmarks and identified two groups of issues that could have financial reporting implications, those being:

   (a) issues affecting financial reporting in the period before the replacement of an existing interest rate benchmark with an alternative benchmark rate (pre-placement issues); and

   (b) issues that might affect financial reporting when an existing interest rate benchmark is replaced with an alternative benchmark rate (replacement issues).

7. At the time of adding the *IBOR Reform and the Effects on Financial Reporting* project to its standard-setting workplan, the Board noted that it had not yet considered whether and, if so, how to address any issues that might affect financial reporting when an interest benchmark rate is replaced with an alternative rate (Phase 2). The Board acknowledged that a range of issues could arise at different points in time because of the uneven timing of the reform in various jurisdictions, coupled with different approaches to reform the different interest rate benchmarks being considered. Therefore, the Board decided to monitor the developments in this area while progressing with the pre-replacement issues (Phase 1).

8. At its August 2019 meeting, the Board completed its redeliberations on the amendments to IFRS 9, IAS 39 and IFRS 7 for the pre-replacement issues and gave the staff permission to commence the balloting process to finalise and issue the final amendments.

9. As Phase 1 of the project moves towards its finalisation, the staff considered the potential financial reporting implications that could arise when an interest rate benchmark is replaced with an alternative benchmark rate (Phase 2) based on our research to date. In view of this, this paper set out the preliminary scope of the potential issues to be considered by the Board at future meetings, including the proposed order in which the staff will bring these issues to the Board for discussion.

Objective of Phase 2

10. As the scope of the issues to be considered by the Board in Phase 2 is broader than the previous phase, thereby increasing the opportunity for 'scope creep', the staff believe that defining the objective of Phase 2 would be important as this will help to guide the Board in determining if, and how, to address the various potential issues.

11. Consistent with the overall objective of financial reporting as set out in the Conceptual Framework, the staff are of the view that the objective of Phase 2 should be to provide useful and relevant financial information about the effects of the transition to alternative benchmark rates on an entity's financial statements.

This will assist the Board in assessing whether it should take any action in the form of amendments to IFRS Standards, which could include narrow-scope exceptions, additional application guidance or illustrative examples.

12. To achieve the objective set out in paragraph 11 above, the staff analysis will focus on the following steps:

(a) Identification of potential accounting issues that may arise when an existing interest rate benchmark is reformed or replaced with an alternative benchmark rate;

(b) Consideration as to whether IFRS Standards provide an adequate basis to determine how to account for the accounting issues that may arise due to the reform; and

(c) Assessment of whether the accounting outcome resulting from the application of IFRS Standards would provide the most useful information to users of financial statements. [1]

Preliminary scope of issues

13. The staff engaged with securities regulators, central banks, audit firms, industry groups and financial institutions to obtain an understanding of the effects of the reform on financial reporting. The staff also gathered inputs from the Accounting Standards Advisory Forum (ASAF) on potential accounting implications of the reform that should be considered by the Board in the second phase of the project.

14. In addition, as part of the summary of feedback from comment letter on the IBOR ED presented to the Board at the July 2019 meeting, the staff noted that most respondents commented not only on the specific questions asked in the IBOR ED, but also on potential issues for the Board to consider as part of the next phase of the IBOR project.[2] Accordingly, the staff also considered the feedback received

[1] Per paragraph 2.4 of the Conceptual Framework ‘if financial information is to be useful, it must be relevant and faithfully represent what it purports to represent. The usefulness of financial information is enhanced if it is comparable, verifiable, timely, and understandable.’

[2] For further information, refer to the July 2019 Agenda Paper 14A *Summary of feedback from comment letters* and Agenda Paper 14B *Additional issues for consideration before finalising the proposed amendments*.

from comment letters to identify potential issues that could affect financial reporting due to the reform.

15. Based on these activities, the staff developed the following preliminary list of potential accounting issues to be considered by the Board in the second phase of the project:

Area	Topic	Potential accounting issues
Classification and measurement of financial instruments	Determining what a modification is	i) In applying IFRS 9, what is considered to represent a ‘modification of a financial instrument’? ii) When does a modification result in the derecognition of a financial instrument? iii) How should amendments to the interest rate benchmark be accounted for? iv) How should other modifications be accounted for? v) In what order should modifications be accounted for?
	Assessment of SPPI	Would changes to reset dates and compounding periods cause financial assets to fail the SPPI assessment?
	Reassessment of business model	Would modifications that result in derecognition impact the business model assessment?
	Embedded derivatives	Would changes to reset dates and compounding periods for financial liabilities give rise to embedded derivatives?
Hedge accounting	Hedge designations	i) Would a change to the hedged risk in the hedge documentation require discontinuation of hedge accounting? ii) Are flexible hedged risk designations permissible (eg designating both IBOR and an alternative interest rate benchmark as the hedged risk)? iii) What are the implications when some loans within a portfolio of designated loans are amended to reflect an alternative benchmark and other loans within the same portfolio are not? iv) Application of other qualifying criteria to new hedging relationships.

Area	Topic	Potential accounting issues
Hedge accounting (*cont.*)	End of relief	i) How does the end of relief in Phase 1 interact with hedge designations under Phase 2? ii) How should the amount in OCI be recycled when an entity ceases to apply the exceptions provided in Phase 1? iii) If a change in the hedged risk does not require discontinuation, how should the valuation adjustments on the hypothetical derivative and fair value hedge adjustment be accounted for?
Other IFRS Standards		What are the potential impacts of IBOR reform on other IFRS Standards (eg IAS 19, IFRS 16 and IFRS 17)?
Disclosures	Disclosures	Considering whether additional disclosure requirements should be developed.

16. As some specific conditions and details of the reform have yet to be finalised, it is possible that the preliminary scope discussed in this paper will need to be adjusted to incorporate other potential accounting issues that may arise. Nevertheless, the staff think that the likely scope of issues is important to establish the expected general direction of the project upfront.

High-level project timeline

17. The staff note that the discussion about the classification of financial instruments, including whether the modification of a financial instrument gives rise to derecognition, will have consequential impacts on other areas. For example, determining how the end of application of a Phase 1 exception should be accounted for is subject to whether the relevant hedging relationship should be discontinued or not. This question is in turn subject to whether the designated hedged item and hedging instrument should be derecognised following a modification event. Therefore, the staff believe it would be more efficient to first consider the issues affecting the classification and measurement of financial instruments and then move on to other issues. The order in which these issues will be discussed with the Board, as proposed in the table above, already considers these interactions.

18. The table below summarises the indicative timing and the key areas for discussion that will require decisions from the Board at future meetings.

Timeline	Key areas for discussion (*)
October 2019	1) Classification and measurement of financial instruments
November 2019	2) Hedge accounting
December 2019	3) Hedge accounting (continued) 4) Other IFRS Standards
January / February 2020	5) Other/ new issues identified 6) Disclosures

(*) Refer to paragraph 15 of this paper for further details on the key areas for discussion.

Question for the Board

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1) Does the Board have any comments on the proposed high-level project timeline and the preliminary scope of potential accounting issues to be considered in the second phase of the project?