STAFF PAPER

September 2012

IFRS Interpretations Committee Meeting

Project	**Review of comments received on agenda decision**		
Paper topic	**IAS 39 *Financial Instruments: Recognition and Measurement*—Accounting for different aspects of restructuring Greek Government Bonds**		
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Introduction

1. In April 2012, the IFRS Interpretations Committee (the Committee) received a request for guidance on the accounting for several different aspects of the restructuring of Greek government bonds (GGBs).

2. The principal issue raised was whether this transaction should result in derecognition of the whole asset, or only part of it, in accordance with IAS 39 *Financial Instruments Recognition and Measurement* (IAS 39).[1] In the fact pattern submitted, the relevant facts led the Committee to conclude that, in determining whether the transaction results in derecognition of the financial asset, both an assessment of extinguishment under paragraph 17(a) of IAS 39 as well as an assessment of a substantial change of the terms of the asset would result in derecognition of the whole asset. The Committee decided not to add the issue to its agenda.

3. A further issue raised was the request for guidance on the appropriate accounting for the GDP-linked security that was part of the restructuring of GGBs. The Committee did not opine on whether the indexation to the issuer's GDP meets the

[1] The issue was discussed at the Committee's May 2012 meeting. The related agenda paper series 10 is available under http://www.ifrs.org/Meetings/Pages/IFRSInterMay12.aspx.

definition of a derivative. However, the Committee concluded that if not regarded as a derivative, the GDP-linked securities are classified either as at fair value through profit or loss or as available for sale.

Comment letter summary

4. The comment period for the tentative agenda decision ended on 26 July 2012 and eight responses were received. All respondents agreed with the conclusion (ie derecognition of GGBs) but four of them requested that more guidance be provided on derecognition in the context of debt restructurings in general. These respondents noted that financial asset restructuring has become a frequent and significant issue in the context of the current economic environment so that diversity in practice might develop. One respondent disagreed with the rationale and stated that derecognition of the GGBs should be only based on extinguishment under paragraph 17(a) of IAS 39[2].

5. The accounting for the GDP-linked security that was part of the restructuring of the GGBs was only addressed in six comment letters. Five of them requested that the Committee add it to its active agenda or recommend to the International Accounting Standards Board (IASB) to perform further work. One respondent disagreed that it is unclear whether the GDP-linked security meets the definition of a derivative or not and instead believed the security meets the definition of a derivative under current IFRSs[3].

Derecognition: analysis of issues raised

6. Although all respondents agreed with the conclusion, ie derecognition of the GGBs, four of them requested more guidance. They noted that in the current economic environment financial asset restructuring has become a frequent and significant issue. In their view, the current lack of guidance leads to diversity in practice and weakens the comparability of IFRS financial statements and

[2] KPMG IFRG Limited

[3] Organismo Italiano di Contabilità – OIC – The Italian Standard Setter

enforceability of the standard. Some respondents ask for a change to IAS 39 or at a minimum that the issue be addressed in the IFRS 9 *Financial Instruments* project.

7. The staff note that debt restructuring was already part of a comprehensive derecognition project. In March 2009, the IASB published an exposure draft which proposed a new derecognition model for financial assets that was based on the aspect of control. The primary objectives of the project were:

   (a) firstly, to improve the derecognition requirements for financial assets in IAS 39, which have been perceived to be complex to understand and apply in practice;

   (b) secondly, to provide users with more information about an entity's exposure to the risks of transferred financial assets; and

   (c) thirdly, to facilitate convergence between IFRSs and US GAAP.

8. Given that the responses to the exposure draft were largely negative, the IASB decided to focus its efforts on increasing the transparency and comparability of accounting for derecognised financial assets by improving and converging the disclosure requirements under IFRSs and US GAAP. In October 2010, the IASB issued amendments to IFRS 7 *Financial Instruments: Disclosures* that increases the disclosure requirements for transactions involving the transfer of financial assets. The remainder of its comprehensive derecognition project is no longer on the IASB's agenda.

9. The staff think that the outcome of the IASB's derecognition project shows that this issue is difficult, controversial and encompasses a large topical area. The IASB's experience also demonstrates that the project would be a big project that would require significant time commitment and resources. The staff think that a narrower project scope that would only include the assessment of whether the appropriate accounting following changes to the terms of a contract is an impairment of the original asset or instead the derecognition of the original asset and recognition of a new asset:

   (a) could not be done in isolation without addressing the issue of changes in contractual terms more generally, which would have significant consequences for situations other than debt restructuring in the context of a borrower with financial difficulties;

(b) would raise the question of whether derecognition should be symmetrical for assets and liabilities, which relates to whether a bright-line test should be used; and

(c) because of the interaction with impairment, any new proposals would inevitably always result in significant judgment still being required to be applied, which is unlikely to satisfy those requesting that the issue be considered.

10. Therefore, the staff think that developing a new derecognition model for financial instruments goes beyond the type of issue that the Committee could address by way of an interpretation. Consequently, the staff conclude that the issue does not meet the Committee's agenda criteria because it cannot be resolved efficiently within the confines of existing IFRSs and the Framework, and the demands of the interpretation process.

11. One respondent holds the view that only one approach, namely derecognition under paragraph 17a of IAS 39, is the basis for derecognising the GGBs. However, the respondent's view would still use an analogy to paragraph 40 of IAS 39 to assess whether there has been a substantial change in the terms of the asset.

12. The staff think that the tentative agenda decision wording should be retained because:

(a) It answers the questions in the submission, one of which was about the application of IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* and possible analogies to the requirements for financial liabilities.

(b) It avoids creating inconsistencies that would arise from mixing the analogy to the requirements for financial liabilities with the application of IAS 39.17(a) (this argumentation is supported by an illustration in Appendix A). Using an analogy to financial liabilities in order to subsume the concept of a substantial change of the terms of the financial instrument (IAS 39.40) under the notion of "expiry" in IAS 39.17(a) would implicitly assert that this extinguishment is an expiry. In contrast, the source of the analogy (IAS 39.40) does not make an assertion what type of extinguishment applies (ie expiry, discharge or cancellation). Hence, the analogy would have the indirect effect of interpreting its source, which would create inconsistencies. A further consequence of this would be to implicitly opine on a legal question—which relates to the difference between expiry, discharge or cancellation.[4] This is not required nor do the staff consider it appropriate to indirectly opine on what is a matter of Greek law.

(c) The feedback requested the Committee to provide more guidance. In our view the structure of the tentative agenda decision, while focussing on the fact pattern in hand, provides guidance on different types of restructurings (ie irrespective of by way of exchange or modification). Some of this guidance would be lost if the structure of the tentative agenda decision was not retained.

Staff recommendation

13. We recommend that the Committee does *not* add the accounting treatment of restructurings to its agenda for the reasons described above. We think that if the Committee believes that more guidance on derecognising financial instruments should be provided this issue should be brought to the IASB's attention for its consideration.

14. The staff further recommend retaining the tentative agenda decision wording in order to avoid unintended consequences. If the Committee wants to recommend that the IASB addresses the accounting treatment of restructurings more comprehensively that could be added in finalising the agenda decision.

[4] See IAS 39.AG57.

Question to the Committee

Question for the Committee
1. Does the Committee agree with the staff recommendation that the accounting treatment of restructurings is not added to the Committee's agenda? 2. Does the Committee want to recommend the IASB to address this issue? 3. If the Committee agrees with the staff recommendation, does the Committee agree with the proposed rejection wording in Appendix B?

Definition of a derivative: analysis of issues raised

15. For the classification of the GDP-linked security a key question is whether the security's indexation to the issuer's GDP gives rise to an underlying that is a non-financial variable specific to a party to the contract:

  (a) if so, the security would have to be classified as a non-derivative financial asset into the appropriate one of the four categories for financial assets in IAS 39.

  (b) if not, the security would meet the definition of a derivative and classification as at fair value through profit or loss would be mandatory.

16. One respondent[5] noted that examples in IFRS 9 and the related implementation guidance use derivatives based on sales volume and concludes that sales specific to one party of the derivative are considered as a financial variable. In that respondent's view, by analogy GDP should also be a financial variable so that the GDP-linked security would meet the definition of a derivative. However, in July 2006 the IFRIC already considered whether EBITDA or revenue were financial or non-financial variables and acknowledged that this was unclear from IAS 39. The IFRS 9 examples cited by the respondent already existed under IAS 39 when the

[5] Organismo Italiano di Contabilità – OIC – The Italian Standard Setter

IFRIC considered the issue in 2006. Therefore, the response does not raise any new facts or circumstances; so the situation remains unchanged.

17. The other five respondents who commented on the derivative issue suggested that the Committee add it to its active agenda or recommend to the IASB that it perform further work. The staff note that this issue was on several previous occasions considered by the IFRIC and the IASB. Information on those previous deliberations is included in Appendix C.

18. The Committee already tentatively decided that the issue of whether an underlying is a non-financial variable specific to a party to the contract fails the agenda criteria. Given the previous unsuccessful attempts of the IFRIC and the IASB to address the issue the staff conclude that:

    (a) The issue cannot be resolved efficiently within the confines of existing IFRSs and the Framework, and the demands of the interpretation process.

    (b) It is not probable that the Committee will be able to reach a consensus on the issue on a timely basis.

    In the staff's view, the responses do not provide new information that would change this assessment.

19. Even if changes to IAS 39 were required, the Committee considered that IFRS 9 already used a different classification for financial assets[6]. The Committee further noted that the issue also relates to a current IASB project (the limited review of classification and measurement under IFRS 9).

Staff recommendation

20. The staff think that:

[6] Under IFRS 9 (even per the proposed amendments) the GDP security for the holder does not only have payments that are principal and interest and therefore would always have to be classified as FVPL.

(a) Only addressing the issue of whether the GDP is a non-financial variable specific to a party of the GDP-linked security would:

  (i) still be difficult and at best result in opining on an aspect that is very specific to a fact pattern that is not widespread; hence it would fail to provide guidance that would be of more general relevance (and could have unintended consequences because it would raise the question of when and to what extent it would be an appropriate basis for an analogy);

  (ii) only be relevant for the classification of a financial asset under a standard that is already being phased out (IAS 39) by a new standard (IFRS 9).

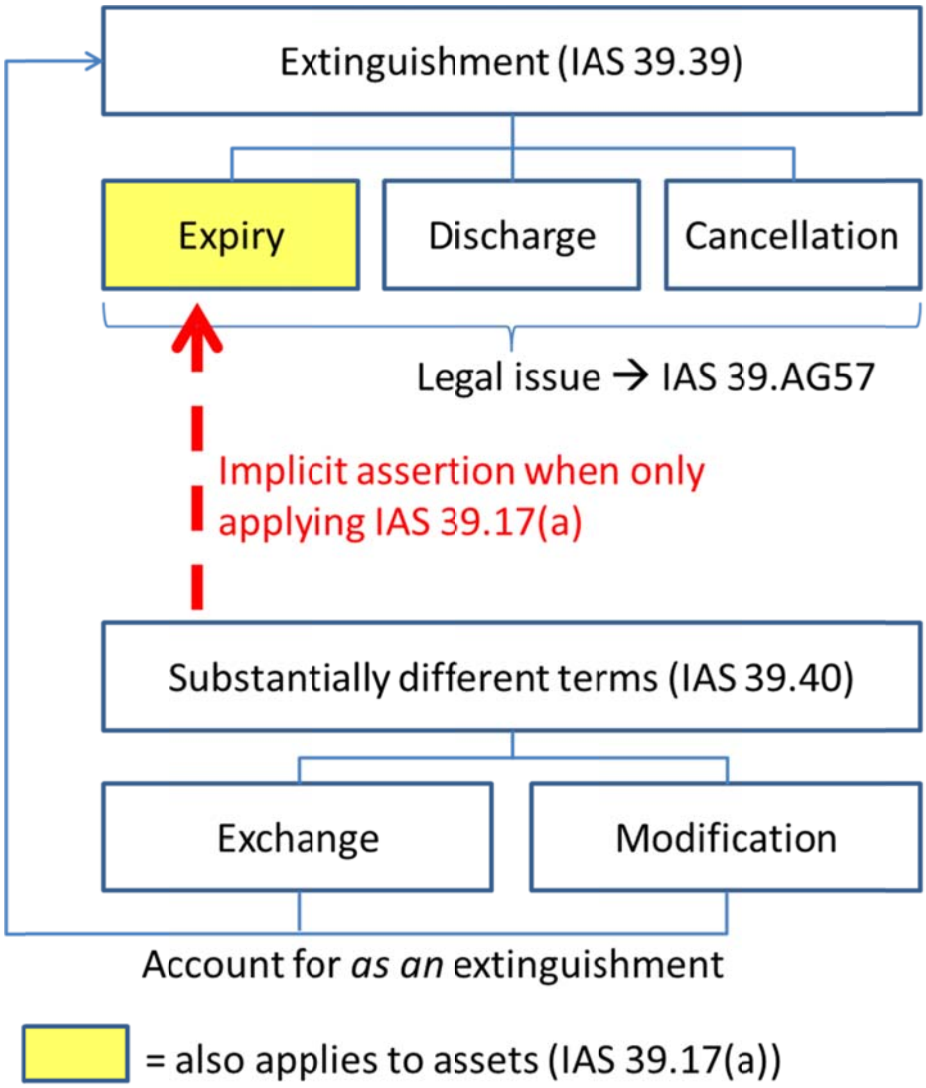
(b) Addressing more generally what underlyings are a non-financial variable specific to a party to the contract would fail the Committee's agenda criteria (see paragraph 18). The staff also think resolving the issue would require a time commitment and resources to the extent that is consistent with an IASB project.

21. The staff recommend confirming the tentative agenda decision, ie not adding this issue to the Committee's agenda. If the Committee considers that the issue should nevertheless be addressed, we think that the Committee should recommend that the IASB add it to its agenda.

Question for the Committee

Question for the Committee
1. Does the Committee agree with the staff recommendation that the issue of whether the GDP is a non-financial variable specific to a party of the GDP-linked security should not be added to the Committee's agenda? 2. Does the Committee want to recommend to the IASB that it address this issue? 3. If the Committee agrees with the staff recommendation, does the Committee agree with the proposed rejection wording in Appendix D?

Appendix A—Illustration of the different approaches leading to derecognition (referring to paragraph 12(b) of this paper)



Appendix B—Proposed wording for final agenda decision

D.1 The staff propose the following wording for the agenda decision:

IAS 39 *Financial Instruments: Recognition and Measurement*— Derecognition of financial instruments upon modification

The Committee received a request for guidance on the circumstances in which the restructuring of Greek government bonds (GGB) should result in derecognition of the whole asset, or only part of it, in accordance with IAS 39. In particular, the Committee has been requested to consider the following questions:

- Whether the portion of the old GGBs that are exchanged for twenty new bonds with different maturities and interest rates should be derecognised, or conversely accounted for as a modification or transfer that would not require derecognition?
- Whether IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors would be applicable in analysing the submitted fact pattern?
- Whether either paragraphs AG8 or AG62 of IAS 39 would be applicable to the fact pattern submitted if the GGBs were not derecognised?

Exchange of financial instruments: derecognition?

The Committee noted that the request has been made within the context of a narrow fact pattern. The narrow fact pattern highlights the diversity in views that has arisen in relation to the accounting for the portion of the old GGBs that is exchanged for twenty new bonds with different maturities and interest rates. The submitter asked the Committee to consider whether these should be derecognised, or conversely accounted for as a modification or transfer that would not require derecognition?

In addition, the Committee has been asked to consider whether IAS 8 would be applicable in analysing the submitted fact pattern, and whether the exchange can be considered a transfer within the scope of paragraph 17(b) of IAS 39.

The Committee observed that the term ‘transfer’ is not defined in IAS 39. However, the potentially relevant portion of paragraph 18 of IAS 39 states that an entity transfers a financial asset if it transfers the contractual rights to receive the cash flows of the financial asset. The Committee noted that in the fact pattern submitted, the bonds are transferred back to the issuer rather than a third party. Accordingly, the Committee believed that the transaction should be assessed against paragraph 17(a) of IAS 39.

In applying paragraph 17(a) of IAS 39, the Committee noted that in order to determine whether the financial asset is extinguished it is necessary to assess the changes made as part of the bond exchange against the notion of ‘expiry’ of the rights to the cash flows. The Committee also noted that if an entity applies IAS 8 because of the absence in IAS 39 of an explicit discussion of when a modification of a financial asset results in derecognition, applying IAS 8 requires judgement to develop and apply an accounting policy. Paragraph 11 of IAS 8 requires that in determining an appropriate accounting policy, consideration must first be given to the requirements in IFRSs dealing with similar and related issues. The Committee noted that in the fact pattern submitted, that requirement would lead to the development of an analogy to the notion of a substantial change of the terms of a financial liability in paragraph 40 of IAS 39.

Paragraph 40 of IAS 39 sets out that such a change can be effected by the exchange of debt instruments or by way of modification of the terms of an existing instrument. Hence, if this analogy to financial liabilities is applied to financial assets, a substantial change of terms (whether effected by exchange or by modification) would result in derecognition of the financial asset.

The Committee noted that if the guidance for financial liabilities is applied by analogy to assess whether the exchange of a portion of the old GGBs for twenty new bonds is a substantial change of the terms of the financial asset, the assessment needs to be made taking into consideration all of the changes made as part of the bond exchange.

In the fact pattern submitted, the relevant facts led the Committee to conclude that, in determining whether the transaction results in the derecognition of the financial asset, both approaches (ie extinguishment under paragraph 17(a) of IAS 39 or substantial change of the terms of the asset) would result in derecognition.

The Committee considered the following aspects of the fact pattern in assessing the extent of change that results from the transaction:

- A holder of a single bond has received in exchange for one portion of the old bond twenty bonds with different maturities and cash flow profiles as well as other instruments in accordance with the terms and conditions of the exchange transaction.
- All of the bondholders received the same restructuring deal irrespective of the terms and conditions of their individual holdings. This indicates that the individual instruments, terms and conditions were not taken into account. The different bonds

(series) were not each modified in contemplation of their respective terms and conditions but instead replaced by a new uniform debt structure.

- The terms and conditions of the new bonds are substantially different from those of the old bonds; this includes many different aspects such as the change in governing law, the introduction of contractual collective action clauses and the introduction of a co-financing agreement that affects the rights of the new bond holders, and modifications to the amount, term and coupons.

The Committee noted its analysis used as the starting point the assumption in the submission that the part of the principal amount of the old GGBs that was exchanged for new GGBs could be separately assessed for derecognition. The Committee emphasised that this assumption was more favourable for achieving partial derecognition than looking at the entirety of the old bond. Hence, its conclusion that the old GGBs should be derecognised would apply even more so when taking into account that the exchange of the old GGBs was as a matter of fact the result of a single agreement that covered all aspects and types of consideration for surrendering the old GGBs. As a consequence, the Committee noted that partial derecognition did not apply.

Consequently, the Committee ~~[~~decided~~]~~ not to add the issue to its agenda.

Application of paragraphs AG62 or AG8 of IAS 39 to the submitted fact pattern

The Committee noted that the questions raised by the submitter assume that the old GGBs in the fact pattern would not be derecognised. In the submitted fact pattern, the Committee concluded that the old GGBs are derecognised. The Committee noted that because of its conclusion on derecognition these questions did not need to be answered.

Appendix C—Previous deliberations on the definition of a derivative

Tentative IFRIC agenda decision in July 2006

C.1 A submitter asked the IFRIC whether contracts indexed to an entity's own EBITDA or own revenue meet the definition of a derivative. At its meeting in July 2006, the IFRIC considered two different aspects:

a. First, the IFRIC considered whether the reference to non-financial variables that are specific to a party to the contract was restricted to insurance contracts. The IFRIC did not believe that IAS 39 included that restriction. That meant that the question whether EBITDA or revenue are financial or non-financial variables was relevant (see (b) below). The IFRIC tentatively decided not to take this first issue on to its agenda because it did not expect significant diversity in practice to arise.

b. Second, the IFRIC considered whether EBITDA or revenue were financial or non-financial variables and acknowledged that this was unclear from IAS 39. However, the IFRIC tentatively decided not to take this second issue on to its agenda because it believed it would be unable to reach a consensus on a timely basis.

IFRIC agenda decision in January 2007

C.2 The IFRIC reconsidered the issue and at its January 2007 meeting decided to withdraw the tentative agenda decision. The IFRIC was concerned that taking no action would allow continued significant diversity in practice regarding how financial and non-financial variables were determined.

Consequently, the issue was referred to the IASB with the recommendation to amend IAS 39 (possibly as part of the annual improvements process). That amendment should have limited to insurance contracts the exclusion from the definition of a derivative of contracts linked to non-financial variables that are specific to a party to the contract.

IASB Annual Improvements project 2007/2008

C.3 As part of the Annual Improvements project in 2007/2008 the Board proposed amending IAS 39 as the IFRIC had recommended. However, the feedback was unsupportive[7] and significant issues were raised in the comment letters. There was significant concern that the proposed amendment:

a. would result in a significant change to current practice,

b. would result in many different types of contracts meeting the (new) definition of a derivative and likely have unintended consequences;

c. would require a separate project for a major amendment.

To keep the project to its timetable, the Board at its February 2008 meeting decided to exclude this issue from the final annual improvements.

[7] Out of 61 respondents 33 did *not* support and 28 objected to the proposal.

Appendix D—Proposed wording for final agenda decision

D.1 The staff propose the following wording for the agenda decision:

IAS 39 *Financial Instruments: Recognition and Measurement*— Classification of a GDP-linked security

The Committee received a request for guidance on the appropriate accounting for the GDP-linked security that was offered as part of the restructuring of GGBs.

The submitter noted that IAS 39 refers to a 'non-financial variable that is not specific to a party to the contract' but does not define the meaning of that term. The Committee noted that the four alternatives in the submitted fact pattern were based on the assumption that the indexation to the issuer's GDP is a non-financial variable specific to a party to the contract. The Committee noted that the question of what constitutes an underlying that is a non-financial variable specific to a party to the contract had been considered on several previous occasions by itself and the Board. Therefore, the Committee was concerned that it could not resolve the issue efficiently within the confines of existing IFRSs and the Framework, and the demands of the interpretation process and that it was not probable that it would be able to reach a consensus on the issue on a timely basis. The Committee considered that it would therefore remain an open question whether the assumption in the submission is appropriate.

However, the Committee thought that it could highlight some aspects that should be considered when assessing the accounting for the GDP-linked securities. The Committee highlighted the following aspects:

- The GDP-linked security is a structured option that entitles the holder to cash payments depending on the nominal and the real GDP of the issuer exceeding particular thresholds.
- Mandatory classification as at fair value through profit or loss only applies, by definition, if the GDP-linked security is a derivative or is otherwise held for trading.
- The definition of loans and receivables excludes those financial assets "for which the holder may not recover substantially all of its initial investment, other than because of credit deterioration, which shall be classified as available for sale".
- The definition of held-to-maturity investments requires that an entity has the positive intention and ability to hold that financial asset to maturity. The application guidance

in IAS 39 clarifies that "the criteria for classification as a held-to-maturity investment are met for a financial asset that is callable by the issuer if the holder intends and is able to hold it until it is called or until maturity and the holder would recover substantially all of its carrying amount".

- Unless the GDP-linked securities are classified as at fair value through profit or loss they would be classified as available for sale debt instruments.
- Entities should consider the operational complexities of applying the effective interest method to the GDP-linked securities owing to their complex cash flow profile.

The Committee considered that no clarification of IAS 39 was required. Even if changes were required, the Committee considered that IFRS 9 already used a different classification for financial assets. The Committee further noted that the issue also relates to a current IASB project (the limited review of classification and measurement under IFRS 9). Consequently, the Committee ~~[~~decided~~]~~ not to add the issue to its agenda.

Accounting Standards Board
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July 26, 2012

(via email to ifric@ifrs.org)

IFRS Interpretations Committee
30 Cannon Street, 1st Floor
London EC4M 6XH
United Kingdom

Dear Sirs:

Re: Tentative agenda decision on IAS 39 *Financial instruments: Recognition and Measurement* – Accounting for different aspects of restructuring Greek Government Bonds

This letter is the response of the staff of the Canadian Accounting Standards Board (AcSB) to the IFRS Interpretations Committee's tentative agenda decision on accounting for different aspects of restructuring Greek Government Bonds published in the May 2012 IFRIC Update.

The views expressed in this letter take into account comments from individual members of the AcSB staff but do not necessarily represent a common view of the AcSB or its staff. Views of the AcSB are developed only through due process.

We agree with the Committee's decision not to add this item to its agenda for the reasons provided in the tentative agenda decision. However, we think that the tentative agenda decision needs to be modified to clarify or remove the discussion of alternative treatments of the instrument issued as part (d) of the restructuring. The tentative agenda decision does not clearly establish whether a GDP-linked financial instrument meets the definition of a derivative.   Accordingly, we think that it is potentially confusing to comment that the instrument is a structured option, and therefore what many people would consider a derivative, while concurrently suggesting treatments that are not available to derivatives.

We think the notice should exclude all of the paragraph beginning "However, the Committee thought that it could highlight …." except for the statement that "The Committee considered that no clarification of IAS 39 was required." and the final two sentences: "The Committee further noted that the issue also relates to a current IASB project (the limited review of classification and measurement under IFRS 9). Consequently, the Committee [decided] not to add the issue to its agenda."

If the paragraph is not removed, we think that it should be modified as follows:

> However, the Committee thought that it could highlight some aspects that should be considered when assessing the accounting for the GDP-linked securities <u>if indexation to the issuer's GDP is a non-financial variable specific to a party to the contract</u>. The Committee highlighted…

We note that neither the Committee nor the Board have been able to reach a consensus on interpretation of the non-financial underlying variable exception in the definition of a derivative. We agree that the Committee's decision on this issue is appropriate in the circumstances. However, we think that the definition of a derivative should be revisited to resolve inconsistencies in practice relating to derivatives based on non-financial variables. We encourage either the Committee or the Board to undertake a project to provide more comprehensive and consistent guidance on accounting treatments for the broader range of derivative instruments. We think that it is particularly important to address derivative accounting as the Board reconsiders IFRS 9 because the definition of a derivative and thus, an embedded derivative, continues to exist in IFRS9.

We would be pleased to provide more detail if you require. If so, please contact me at +1 416 204-3276 (email peter.martin@cica.ca) or Kate Ward, Principal, Accounting Standards at +1 416 204-3437 (email kate.ward@cica.ca).

Regards

Peter Martin

Peter Martin, CA
Director, Accounting Standards

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Chairman
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n° 32

Paris, the 10 JUIL. 2012

Mr Wayne UPTON
Chairman
IFRS Interpretations committee
30 Cannon Street
LONDON EC4M 6XH

Re : Tentative Agenda Decision – IAS 39 – Accounting for different aspects of restructuring Greek Government Bonds

Dear Mr Upton,

I am writing on behalf of the Autorité des Normes Comptables (ANC) to express our views on the above-mentioned IFRS IC's Tentative Agenda Decision (TAD).

The ANC agrees with the IFRS IC's conclusions that the old Greek Government Bonds that are exchanged for new instruments must be fully derecognised in accordance with IAS 39.

However, we acknowledge that IFRS (namely IAS 39) are not specific about the wider subject of debt restructuring in the financial statements of the holder. Moreover, we note that the terms "non-financial variable that is not specific to a party to the contract" is not defined in IAS 39, whereas it is a key notion to assess whether GDP-linked instruments meet the definition of derivative instruments. Therefore, instead of providing too extensive a reasonning in the TAD, we suggest that the Interpretation Committee recommend to the IASB to address the accounting for debt restructuring or modifications for debt holders and clarify the definition of derivative instruments as regards the notion of "non financial variable".

If you have any questions concerning our comments, we would be pleased to discuss them.

Yours sincerely,

Jérôme HAAS

EFRAG
European Financial Reporting Advisory Group

26 July 2012

Wayne Upton, Chairman
IFRS Interpretations Committee
30 Cannon Street
London EC4M 6XH
United Kingdom

Dear Mr. Upton,

Re: IAS 39 Financial Instruments: *Recognition and Measurement* — Accounting for different aspects of restructuring Greek government bonds

On behalf of the European Financial Reporting Advisory Group (EFRAG), I am writing to comment on the IFRS Interpretations Committee's (Interpretations Committee) tentative decision not to proceed with the agenda item on a request for guidance to clarify the circumstances in which the restructuring of Greek government bonds should result in derecognition of the whole asset, or only part of it, in accordance with IAS 39.

This letter is submitted in EFRAG's capacity of contributing to the Interpretations Committee's due process.

We agree with the Interpretations Committee's conclusion that the old Greek government bonds should be derecognised in their entirety (since their terms and conditions are substantially different compared to those of the new Greek government bonds). We therefore support the Interpretations Committee's tentative decision not to add the issue to its agenda.

However, we believe that it would be helpful if the standards explicitly dealt with debt restructurings more generally, which would be particularly relevant in the light of the current financial crisis. In this respect we note the absence of certain definitions that are critical for the derecognition assessment process, and the lack of an explicit discussion in IAS 39 of when a modification of a financial asset (or exchange of debt instruments) results in derecognition. Therefore, we suggest that the Interpretations Committee recommend to the IASB that accounting for debt restructurings and modifications be addressed as part of the finalisation of IFRS 9 *Financial Instruments*.

If you would like to discuss our comments further, please do not hesitate to contact Panagiotis Papadopoulos or me.

Yours sincerely,

Françoise Flores
EFRAG Chairman

European Securities and Markets Authority

Date: 26 July 2012
ESMA/2012/465

Hans Hoogervorst
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Wayne Upton
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30 Cannon Street
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The IFRS Interpretations Committee's tentative agenda decision on IAS 39 Financial Instruments: *Recognition and Measurement* – Accounting for different aspects of restructuring Greek government bonds

The European Securities and Markets Authority (ESMA) is an independent EU Authority that contributes to safeguarding the stability of the European Union's financial system by ensuring the integrity, transparency, efficiency and orderly functioning of securities markets, as well as by enhancing investor protection.

ESMA has considered the IFRS Interpretations Committee's tentative decision not to add to its agenda the request for clarification it received on different aspects of the restructuring of Greek government bonds, as addressed in our letter dated 17 April 2012 (ESMA/2012/248). ESMA welcomes the Committee's swift reaction and would like to provide you with the following considerations aimed at improving the decision-usefulness of financial statements and the transparency and enforceability of IFRSs.

— **Exchange of financial instrument: modification or derecognition**

ESMA agrees with the Interpretations Committee's conclusion that the old Greek government bonds should be derecognised in their entirety. In the current economic climate, an increase in the number of restructuring transactions related to non-sovereign bonds and other loans has been observed.

Answering the question whether the restructuring transaction should be classified as a modification of the current financial instrument or as an exchange of financial assets resulting in the derecognition of the current financial instrument and the recognition of the new financial instrument in the books of the lender requires a significant amount of judgement under the current reporting framework.

In such context, European enforcers of IFRS note varying accounting practices for debt restructurings by lenders due to the lack of clear guidance which leads in turn to decreased comparability between financial statements. The differences might be immaterial on a loan by loan basis but could be material on a collective basis, taking into account the current economic climate.

ESMA believes that guidance on how to account for debt restructurings from the holder's perspective is needed. More specifically, ESMA thinks that a more practical articulation between derecognition and impairment of financial instruments would enhance consistency in applying IFRSs requirements. The lack of clear guidance combined with the possibility of application by analogy of the criteria used for financial liabilities (IAS 39 paragraph 40) may have consequential impacts that might weaken comparability of IFRS financial statements and enforceability of the standard.

— **Accounting for the GDP-linked securities as part of the restructuring of Greek government bonds**

IAS 39 – *Financial Instruments: Recognition and Measurement* refers to, but does not define, a non-financial variable that is not specific to a party to the contract. The Interpretations Committee notes that the question of what constitutes an underlying that is a non-financial variable specific to a party to the contract had been considered on several previous occasions by the Committee and the IASB.

ESMA welcomes the Committee's implicit agreement that there is divergence in practice on this particular issue but does not agree with the Committee's conclusion not to add it to its active agenda nor to recommend the Board to perform further work. We believe that further work is necessary.

ESMA notes that the IASB is currently revisiting the guidance on financial instruments. In order to promote transparency, achieve consistent application of IFRS and to set standards that are enforceable ESMA would strongly encourage the Board to consider the abovementioned concerns as part of its ongoing deliberations on IFRS 9 – *Financial Instruments*.

We would be happy to discuss all or any of these issues further with you.

Yours sincerely,

Steven Maijoor
Chair ESMA

Julie Galbo
Chair ESMA's Corporate Reporting Standing Committee

Mr Wayne Upton

IFRS Interpretation Committee
30 Cannon Street
London EC4M 6XH

United Kingdom

Paris, July 10, 2012

RE: IFRS Interpretation Committee tentative agenda decision, May 2012: IAS 39 - ***Accounting for different aspects of restructuring Greek Government Bonds***

Dear Sir,

MAZARS is pleased to comment on the IFRS Interpretation Committee tentative decision not to add to its agenda the issue related to the *Accounting for different aspects of restructuring Greek Government Bonds.*

We support the view of the IFRS Interpretation Committee that, given the specific characteristics of the Greek Government Bonds' (GGB) restructuring, the old GGBs should be derecognized. We also agree that no significant diversity in practice is expected regarding the derecognition of old GGBs. We therefore agree with the proposed decision not to add this issue to the agenda of the IFRS Interpretation Committee.

We also agree with the Interpretation Committee that several approaches can be applied to financial asset restructuring as IAS 39 does not specifically address these situations. Although we do agree that in the specific case of GGBs restructured in March 2012, each approach identified leads to the same conclusion (i.e. derecognition of old GGBs), we consider that a different fact pattern could have resulted in different conclusions (i.e. derecognition vs. no derecognition) depending on the approach applied.

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MAZARS

In the context of current economic environment, financial asset restructuring is becoming a frequent and significant issue. We therefore encourage the IFRS Interpretation Committee to recommend the IASB to clarify the accounting treatment of financial assets' modifications/restructuring either through a limited amendment to IAS 39 or as part of the finalization of IFRS 9 *Financial instruments*.

Should you have any questions regarding the above comments, please do not hesitate to contact Michel Barbet-Massin (+33 1 49 97 62 27) or Edouard Fossat (+33 1 49 97 65 92).

Best regards,

Michel Barbet-Massin
Head of Financial Reporting Technical Support

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24 July 2012

Re: Tentative agenda decision on IAS 39 Financial Instruments: Recognition and Measurement — Accounting for different aspects of restructuring Greek government bonds

Dear Sir/Madame,

We are pleased to have the opportunity to comment on the tentative agenda decision taken by the IFRS Interpretation Committee (IFRS IC) on the *Accounting for different aspects of restructuring Greek government bonds.*

We substantially agree with the IFRS IC's conclusion that the old Greek government bonds should be derecognised in their entirety and therefore the issue should not be added to the agenda of IFRS IC. However, we would like to point out the following aspects.

- The IFRS IC argues that the derecognition occurs in this case in accordance with the paragraph 17(a), i.e. due to the fact that the cash flows are to be considered expired, and not for the paragraph 17(b) providing the transfers of the contractual rights to receive the cash flows of the financial asset.
  We do not believe correct the argument used by IFRS IC which moves from the fact that the transfer of the contractual rights to receive the cash flows under IAS 39.17(b) is possible only when the debtor (i.e. the subject who has to pay those cash flows) is different from the transferee.
  This assumption is not always verified: indeed, it is a common situation that an entity buys back its own debt securities/shares. This transaction qualifies – for both parties, the seller and the

buyer – as a transfer for purposes of, respectively, de-recognition and recognition, even if one party is also the issuer of the instrument being traded.

- The IFRS IC argues that it can be concluded for derecognition also by analogy with the requirements for the derecognition of financial liabilities. We agree with the conclusion from a substantive point of view, when the subject of renegotiation is not an impaired financial asset (see the following bullet point). However, it seems legitimate to ask why, if the application by analogy to financial assets is correct, this provision has not been explicitly provided in the IAS 39. Therefore, we suggest to consider carefully the consequences of the tentative decision, that should result, through the annual improvements, in a clear requirement in IAS 39;

- The transaction, considered as a whole, is a restructuring of creditors' exposure to the Greece. In fact, IAS 39.59(c) specifies that granting to a borrower, for economic or legal reasons relating to his financial difficulty, a concession that the lender would not otherwise considered is an indicator of impairment. This means that, according to this approach, the post-restructuring exposure should be classified as "impaired" (in a sort of continuity between old and new) and that the loss should be classified as an "impairment loss".
  However it has to be recognized that, when the restructuring involves the transformation of the original exposure in a different legal form (e.g. conversion of a mortgage in a borrower's shares), it is inevitable to register the derecognition of the old exposure (loan) and the recognition of the new exposure (equity).
  In addition, in this case it is very likely that *before* the restructuring, the creditors would hold the Government Greek Bonds in different portfolios (some valued at cost, others at fair value) and *after* the restructuring they could have made a different allocation of new securities issued. Therefore, for simplicity and considering that the application of the provision in IAS 39.59(c) is relevant only when both *before and after* the restructuring the securities are allocated to a portfolio valued at amortized cost, we believe that in most cases the outcome of the IFRS IC approach does not substantially differ – in term of measurement – from that achievable when considering that renegotiation as a restructuring.
  However, in order to avoid unintended consequences, we urge that the IFRS IC final decision clarifies that the approach followed in this case (consisting in breaking the initial exposure into more tranches and therefore reasoning separately on each one as it was a stand-alone exposure) is due to the peculiarities of the specific case considered (sovereign debt, support from the international community, etc..) and cannot be applied by analogy to other situations (e.g. restructuring of a corporate exposure).

With reference to the other issue regarding the accounting for the GDP-linked security granted as part of the renegotiation of Greek Government Bonds, in our opinion the statement that the GDP is not a "non-financial variable" is highly questionable. In fact, both the IFRS 9.IG.B.8 and the IFRS 9.B4.3.8 (f) (ii) clearly indicate that revenues and sales specific to one party of the derivative are considered as "financial" variables. This interpretation is confirmed by the fact that in the IFRS 9 the reference to "non-financial variables" has been introduced merely to distinguish derivative instruments from insurance contracts.

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

Yours sincerely,

Angelo Casò
(Chairman)

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Mr Wayne Upton
Chairman
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Our ref MV/288

Contact Mark Vaessen

25 July 2012

Dear Mr Upton

Tentative agenda decision: IAS 39 *Financial Instruments: Recognition and Measurement – Accounting for different aspects of restructuring Greek Government Bonds*

We are writing to express our support for the conclusion in the tentative agenda decision, IAS 39 *Financial Instruments: Recognition and Measurement – Accounting for different aspects of restructuring Greek Government Bonds*, that the bonds should be de-recognised.

However, in terms of the technical analysis set out in the tentative agenda decision there is one aspect with which we do not agree. The seventh paragraph of that section states: "...the relevant facts led the Committee to conclude that, in determining whether the transaction results in the de-recognition of the financial asset, both approaches (i.e. extinguishment under paragraph 17(a) of IAS 39 or substantial change of the terms of the asset) would result in de-recognition."

We believe that this indication that there are two approaches is inappropriate and inconsistent with the preceding text, particularly that set out in the fourth paragraph. The lead-in to that paragraph reads "In applying paragraph 17a of IAS 39.....". We believe that this preceding text appropriately expresses only one approach (i.e. a requirement to assess whether there is an expiry under IAS 39.17(a)) and that consideration as to whether there is a substantial change of the terms of the asset is an element of that overall approach rather than a separate or different approach. Accordingly, we suggest amending the words of that paragraph along the following lines:

"In the fact pattern submitted the relevant facts led the Committee to conclude that the transaction results in the de-recognition of the bonds under paragraph 17a of IAS 39 because the old bonds have as a matter of fact been extinguished and, in the context of the discussion above on the application by analogy of paragraph 40 of IAS 39, there has been a substantial change in the terms of the assets".

Please contact Mark Vaessen on +44 (0) 20 7694 8589 or Chris Spall on +44 (0) 20 7694 8445 if you wish to discuss any of the issues raised in this letter.

Yours sincerely

KPMG IFRG Limited

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Email: ifric@ifrs.org

18 July 2012

Dear Mr Upton,

Tentative agenda decision: IAS 39 Financial Instruments: Recognition and Measurement—Accounting for different aspects of restructuring Greek Government Bonds

Deloitte Touche Tohmatsu Limited is pleased to respond to the IFRS Interpretation Committee's publication in the May 2012 *IFRIC Update* of the tentative decision not to take onto the IFRIC's agenda a request for guidance on application of the requirements of IAS 39 to the restructuring of Greek Government Bonds (GGBs), in particular whether the restructuring should result in derecognition of the whole asset, or only part of it, and the appropriate accounting for the GDP linked security that was offered as part of the restructuring.

We agree with the IFRS Interpretations Committee's decision not to add this item onto its agenda and with the analysis set out in the tentative agenda decision, other than in the following respect.

We believe that the draft wording that the assumption that "the part of the principal amount of the old GGBs that was exchanged for new GGBs could be separately assessed for derecognition [is] more favourable for achieving partial derecognition" could be misinterpreted. We would, therefore, suggest that the paragraph of the section on derecognition be amended to note that the submission recognised that, according to paragraph 16(a) of IAS 39, specifically identifiable or fully proportionate cash flows are a pre-requisite for partial recognition.

In addition, we recommend that the Committee note in the agenda decision that, although the submitter requested an interpretation of IAS 39, the conclusions reached by the Committee would apply equally under IFRS 9 as the two Standards are equivalent in respect of the derecognition requirements considered by the Committee.

Finally, we note that the Committee does not believe it will be able to interpret on a timely basis what is meant by a 'non-financial variable specific to a party to the contract' and regards this as an open question. Although we agree this may not be resolved in a short time frame to provide immediate clarity for those reporters that hold the GDP-linked security, we are concerned this is an issue of wider relevance that was (per the October 2008 *IASB Update*) to be considered for inclusion in a future project following the Board’s decision not to proceed with an amendment to the definition of a derivative proposed in October 2007 but is not currently being addressed as part of the project to replace IAS 39. This question will continue to be relevant in applying IFRS 9 as the definition of a derivative is important in classifying financial liabilities and assessing embedded derivatives in all contractual arrangements other than financial assets under that Standard. We therefore urge the Committee to request that the Board consider what is meant by a ‘non-financial variable specific to a party to the contract’ as part of the classification and measurement element of the IFRS 9 project.

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
Technical