IFRS

# STAFF PAPER

March 2018

## IFRS Interpretations Committee Meeting

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| **Project** | **IFRS 9 and IAS 1 –– Presentation of interest revenue for particular financial instruments** | | |
| Paper topic | Agenda decision to finalise | | |
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## Objective

1. This paper considers feedback on the IFRS Interpretations Committee's (Committee) tentative agenda decision on IFRS 9 *Financial Instruments* and IAS 1 *Presentation of Financial Statements*—Presentation of interest revenue for particular financial instruments. The paper:

   (a) analyses comments received on the tentative agenda decision, and

   (b) asks the Committee if it agrees with the staff recommendation to finalise the agenda decision.

## Introduction

2. The Committee received a request about the effect of the consequential amendment that IFRS 9 made to paragraph 82(a) of IAS 1. That consequential amendment requires an entity to present separately, in the profit or loss section of the statement of comprehensive income or in the statement of profit or loss, interest revenue calculated using the effective interest method (EIM). The request asked whether that requirement affects the presentation of fair value gains and losses on derivative instruments that are not part of a designated and effective hedging relationship

(applying the hedge accounting requirements in IFRS 9 or IAS 39 *Financial Instruments: Recognition and Measurement*).

3. Appendix A to IFRS 9 defines the term 'effective interest method' and other related terms. Those interrelated terms pertain to the requirements in IFRS 9 for amortised cost measurement and the expected credit loss impairment model. In relation to financial assets, the Committee observed that the effective interest method is a measurement technique whose purpose is to calculate amortised cost and allocate interest revenue over the relevant time period. The Committee also observed that the expected credit loss impairment model in IFRS 9 is part of, and interlinked with, amortised cost accounting.

4. The Committee noted that amortised cost accounting, including interest revenue calculated using the EIM and credit losses calculated using the expected credit loss impairment model, is applied only to financial assets that are subsequently measured at amortised cost or fair value through other comprehensive income (FVOCI). In contrast, amortised cost accounting is not applied to financial assets that are subsequently measured at fair value through profit or loss (FVPL).

5. Consequently, the Committee concluded that the requirement in paragraph 82(a) of IAS 1 to present separately an interest revenue line item calculated using the EIM applies only to those assets that are subsequently measured at amortised cost or FVOCI (subject to any effect of a qualifying hedging relationship applying the hedge accounting requirements in IFRS 9 or IAS 39).

6. The Committee did not consider any other presentation requirements in IAS 1 or broader matters related to the presentation of other 'interest' amounts in the statement of comprehensive income. This is because the consequential amendment that IFRS 9 made to paragraph 82(a) of IAS 1 did not affect those matters. More specifically, the Committee did not consider whether an entity could present other interest amounts in the statement of comprehensive income, in addition to presenting the interest revenue line item required by paragraph 82(a) of IAS 1.

7. The Committee concluded that the principles and requirements in IFRS Standards provide an adequate basis for an entity to apply paragraph 82(a) of IAS 1 and present separately, in the profit or loss section of the statement of comprehensive income or in

the statement of profit or loss, interest revenue calculated using the EIM. Consequently, the Committee tentatively decided not to add this matter to its standard-setting agenda.

## Comment letter analysis

8. We received seven comment letters on the tentative agenda decision, reproduced in Appendix B to this paper (attached in a separate document).

9. The Accounting Standards Committee of Germany (ASCG), the Association of National Accountants of Nigeria (ANAN) and Deloitte agree with the Committee's decision not to add the matter to its standard-setting agenda for the reasons outlined in the tentative agenda decision.

10. The Autorité des Normes Comptables (ANC), the French Banking Federation (FBF), KMPG and Mazars either express concerns on, or disagree with, particular aspects of the Committee's technical analysis and conclusion.

11. Respondents' comments, together with our analysis, are presented below.

### *The scope of the tentative agenda decision*

12. As explained above, the Committee received a request about whether the consequential amendment that IFRS 9 made to paragraph 82(a) of IAS 1 affects the presentation of fair value gains and losses on 'trading derivatives'—ie derivative instruments that are not part of a designated and effective hedging relationship (applying the hedge accounting requirements in IFRS 9 or IAS 39). The request noted that such derivative instruments are measured at FVPL and asked whether the consequential amendment that IFRS 9 made to paragraph 82(a) of IAS 1 has the effect that entities are prohibited from presenting particular cash flows on the derivatives (for example, the accrued and realised cash flows on an interest rate swap) as 'interest revenue' in profit or loss, separately from other movements in their fair value.

13. KMPG says the tentative agenda decision (summarised in paragraphs 2 to 7 of this paper) does not effectively address the submitter's question because it does not address whether 'interest' income and expense from 'trading derivatives' can be

presented separately from other fair value gains and losses. The respondent says there is diversity in practice regarding the presentation of such amounts and recommends that the Committee address this question by either revising the tentative agenda decision or adding a narrow-scope project to the Committee's standard-setting agenda.

14. Mazars says the Committee went beyond the scope of the request by addressing how the requirement in paragraph 82(a) of IAS 1 applies to instruments *other than* 'trading derivatives'.

### *Staff analysis*

15. Agenda Paper 3 for the November 2017 Committee meeting explained the scope of the staff analysis and recommendation, and we highlighted that scope during the meeting. Specifically, we acknowledged that the agenda paper intentionally addressed only the consequential amendment that IFRS 9 made to paragraph 82(a) of IAS 1. That is because the request focussed on that change. In addition, the consequential amendment is effective for annual periods beginning on or after 1 January 2018 and, therefore, we considered the matter to be urgent in nature. The analysis confirmed that 'interest' amounts on 'trading derivatives' are not within the scope of this new presentation requirement.

16. However, we noted that we did not analyse, or present a staff view on, other presentation requirements in IAS 1 or broader matters related to the presentation of other 'interest' amounts in the statement of comprehensive income. That is because the consequential amendment that IFRS 9 made to IAS 1 did not affect those matters.

17. At its November 2017 meeting, the Committee discussed, and agreed with, the scope of the staff analysis.

18. We continue to think that the agenda decision should address only the consequential amendment that IFRS 9 made to paragraph 82(a) of IAS 1. We think it is important to address any uncertainty in practice about the scope of this new presentation requirement in a timely manner, which includes but is not limited to confirming that the requirement does not apply to 'interest' amounts on 'trading derivatives'. However, we think it would be inappropriate at this point in time to consider broader matters related to the presentation of interest amounts that were not affected by

IFRS 9. In addition, respondents have not provided any new information beyond that considered by the Committee when reaching its tentative agenda decision. Consequently, we recommend the Committee does not make any changes to the tentative agenda decision in response to comments received on the scope of the analysis.

### *Applying the presentation requirement in paragraph 82(a) of IAS 1 to financial assets that are subsequently measured at amortised cost or FVOCI*

19. As explained above, the Committee concluded that the requirement in paragraph 82(a) of IAS 1 to present separately an interest revenue line item calculated using the EIM applies only to those financial assets that are subsequently measured at amortised cost or FVOCI.

20. KPMG disagrees with the Committee's conclusion. In the respondent's view, an entity is not precluded from presenting interest on non-derivative financial assets measured at FVPL as 'interest revenue calculated using the effective interest method' if:

    (a) the entity computes such interest using the EIM, and

    (b) either the financial asset meets the 'solely payments of principal and interest on the principal amount outstanding' condition (SPPI condition) set out in paragraphs 4.1.2(b) and 4.1.2A(b) of IFRS 9 or, if not, the calculation and presentation of interest is appropriate in the context of the economic characteristics of the asset.

21. The respondent provides several reasons for its view. It says that the disclosure requirement in paragraph B5(e) of IFRS 7 *Financial Instruments: Disclosures*, which requires an entity to disclose whether net gains or net losses on financial instruments measured at FVPL include interest or dividend income, suggests that it is acceptable to present interest revenue for financial assets measured at FVPL. In addition, the respondent says that, while an entity is required to apply the EIM to financial assets measured at amortised cost and FVOCI, neither IFRS 9 nor IAS 1 precludes the entity from using that methodology to calculate and present interest on particular non-derivative financial assets measured at FVPL. The respondent says that while

paragraph 82(a) of IAS 1 refers to 'interest revenue calculated using the EIM', that paragraph does not state that such a calculation must have been *required* by IFRS 9. Finally, the respondent expresses the view that the definition of 'effective interest method' and related definitions are set out in Appendix A of IFRS 9, rather than in the chapters of IFRS 9 on amortised cost and FVOCI, which suggests that those definitions could be applied in other cases.

22. The ANC and the FBF also note paragraph B5(e) of IFRS 7. The ANC says that there is no conceptual reason to prohibit entities from presenting interest amounts on particular financial assets measured at FVPL (such as 'simple' financial assets that do not meet the SPPI condition) as 'interest revenue calculated using the effective interest method' as long as those interest amounts can be calculated. That respondent says that the requirement in paragraph B5(e) of IFRS 7 indicates that an entity can isolate such interest amounts even when they arise on financial assets measured at FVPL. The FBF also says that paragraph B5(e) of IFRS 7 implies that an entity can present interest amounts on financial assets measured at FVPL separately as a line item such as 'interest income', instead of being included with other gains and losses on those assets.

### *Staff analysis*

23. At its November 2017 meeting, the Committee observed that the EIM is an integral part of amortised cost accounting. That is, with regards to financial assets, the EIM is a measurement technique whose purpose is to calculate amortised cost and allocate interest over the relevant time period. IFRS 9 prescribes which financial assets are subject to amortised cost accounting. Specifically, amortised cost accounting, including interest revenue calculated using the effective interest method and credit losses calculated using the expected credit loss impairment model, is applied *only* to financial assets that are subsequently measured at amortised cost or FVOCI. In contrast, amortised cost accounting is not applied to financial assets that are subsequently measured at FVPL.

24. Consequently, the Committee concluded that the requirement to present separately an interest revenue line item calculated using the EIM, which was added to paragraph 82(a) of IAS 1 as part of the Board's deliberations on amortised cost

measurement and impairment methodology, applies only to those assets that are subsequently measured at amortised cost or FVOCI.

25. We continue to agree with the Committee's conclusion. We note that the Committee considered many of the points summarised in paragraphs 20-22 of this paper during its discussion of this matter at its meeting in November 2017.

26. We acknowledge that the definition of 'effective interest method' and related definitions are set out in Appendix A of IFRS 9. The structure of IFRS 9 is such that all defined terms are set out in that appendix. However, the requirements for applying the effective interest method, and calculating interest revenue, are set out in Section 5.4 'Amortised cost measurement'. That section of IFRS 9 is relevant only to financial assets that are subsequently measured at amortised cost or FVOCI.

27. The comments raised about paragraph B5(e) of IFRS 7 imply a disconnect between what is presented as interest revenue applying paragraph 82(a) of IAS 1 and what is disclosed or presented applying IFRS 7. However, we think those paragraphs address different matters—paragraph B5(e) of IFRS 7 applies to 'interest income' on financial assets that are subsequently measured at FVPL whereas the presentation requirement added to paragraph 82(a) of IAS 1 applies to 'interest revenue calculated using the effective interest method'. As discussed earlier in this paper, we highlight that the Committee did not consider whether an entity could present other interest amounts—such as those discussed in paragraph B5(e) of IFRS 7—in the statement of comprehensive income, in addition to presenting the interest revenue line item required by paragraph 82(a) of IAS 1. In addition, the Committee did not consider how those other interest amounts might be calculated. Therefore, we think the tentative agenda decision does not affect the presentation, or calculation, of those amounts except for concluding that they cannot be included in the interest revenue line item required by paragraph 82(a) of IAS 1.

28. Therefore, we recommend the Committee does not make any changes to the wording of the tentative agenda decision in response to the comments received on its conclusion that the requirement in paragraph 82(a) of IAS 1 to present separately an interest revenue line item calculated using the EIM applies only to those financial assets that are subsequently measured at amortised cost or FVOCI.

### *The interaction between the new presentation requirement in IAS 1 and the requirement in paragraph 20(b) of IFRS 7*

29. Paragraph 20(b) of IFRS 7 sets out a disclosure requirement related to the statement of comprehensive income. This paragraph states (emphasis added):

> An entity shall disclose the following items of income, expense, gains or losses **either in the statement of comprehensive income or in the notes**:
>
> …
>
> (b) **total interest revenue** and total interest expense **(calculated using the effective interest method) for financial assets that are measured at amortised cost or that are measured at fair value through other comprehensive income** in accordance with paragraph 4.1.2A of IFRS 9 **(showing these amounts separately)**.
>
> …

30. The ANC and the FBF suggest there might be an inconsistency between the requirement in paragraph 20(b) of IFRS 7 and the requirement in paragraph 82(a) of IAS 1. This is because paragraph 20(b) of IFRS 7 requires an entity to present interest revenue calculated using the EIM *either* in the statement of comprehensive income *or* in the notes, whereas paragraph 82(a) of IAS 1 requires an entity to present such amounts in the statement of comprehensive income. Those respondents think that the requirement in IFRS 7 should take precedence over the requirement in IAS 1 so that entities have the choice to present that information either in the statement of comprehensive income or in the notes.

31. In addition, Mazars observes that paragraph 20(b) of IFRS 7 uses more precise wording because that paragraph states explicitly that the requirement applies to financial assets that are measured at amortised cost or at FVOCI, whereas IAS 1 does not explicitly name those measurement categories. As a result of that wording difference, Mazars says that the Committee's conclusion set out in the tentative agenda decision may not be the only acceptable interpretation of the requirement that IFRS 9 added to paragraph 82(a) of IAS 1.

### *Staff analysis*

32. We think the requirements in paragraph 82(a) of IAS 1 and paragraph 20(b) of IFRS 7 are complementary, rather than inconsistent. Specifically, IFRS 7 requires further disaggregation of the interest revenue information required by IAS 1.

33. We think that the phrase ‘showing these amounts separately’ in paragraph 20(b) of IFRS 7 is important in understanding how those requirements in IAS 1 and IFRS 7 interact:

    (a) Paragraph 82(a) of IAS 1 requires an entity to present separately, in the profit or loss section of the statement of comprehensive income or in the statement of profit or loss, interest revenue calculated using the EIM. In other words, at a minimum an entity must present a *single amount* comprising interest revenue on assets that are measured at amortised cost and assets that are measured at FVOCI.

    (b) Paragraph 20(b) of IFRS 7 requires an entity to present or disclose interest revenue (calculated using the EIM) on assets that are measured at amortised cost and assets that are measured at FVOCI, showing those amounts *separately*. In other words, an entity must show *two amounts* (assuming the entity holds financial assets in both measurement categories). This disaggregation can either be disclosed in the notes or presented in the statement of comprehensive income.

34. We think the wording in paragraph 20(b) of IFRS 7 is necessarily more precise (ie it ‘names’ the relevant measurement categories) than the wording in paragraph 82(a) of IAS 1. This is because paragraph 20(b) of IFRS 7 requires an entity to show interest revenue on those two categories separately—it would be difficult to describe that required disaggregation without specifying the relevant measurement categories.

35. Consequently, we recommend the Committee does not make any changes to the wording of the tentative agenda decision in response to the comments received on the interaction with the requirement in paragraph 20(b) of IFRS 7.

### *The relevance and cost of the new presentation requirement in paragraph 82(a) of IAS 1*

36. The ANC, the FBF and Mazars question whether requiring entities to present separately an interest revenue line item calculated using the EIM for assets that are subsequently measured at amortised cost or FVOCI would provide relevant information. In those respondents' view, entities should have flexibility to apply judgement in order to present interest revenue in a manner that is consistent with how they manage their financial assets.

37. The ANC and the FBF suggest that the debate about the presentation of interest amounts, including the relevance of presenting separately an interest line item calculated using the EIM, should be reconsidered in the context of a broader project such as the Board's project on Primary Financial Statements.

38. In addition, the ANC says that the Committee's conclusion that entities must present separately an interest revenue line item calculated using the EIM for assets that are subsequently measured at amortised cost or FVOCI would result in significant costs. This is because some preparers have already used a broader interpretation of 'interest revenue' for the purposes of applying that presentation requirement.

*Staff analysis*

39. The Board exposed the proposal to present separately interest revenue calculated using the effective interest method in both the Supplementary Document *Financial Instruments: Impairment* (2011) and the Exposure Draft *Financial Instruments: Expected Credit Losses* (2013), before it finalised that new requirement in the completed version of IFRS 9 in 2014. We think the Board fully considered the usefulness and relevance of the information provided when it developed that requirement.

40. The request asked the Committee about the effect of that new presentation requirement and the Committee has responded to that request. In this situation, we think the Committee's role is not to reconsider the relevance or usefulness of the information provided.

41. In addition, we think that presentation requirement indeed results in relevant information. This is because it provides a 'link' between the statement of financial

position and statement of comprehensive income for the financial assets to which amortised cost accounting applies. Specifically, as discussed at the Committee's November 2017 meeting, users of financial statements have said that it is useful to see this particular interest revenue line item in the statement of comprehensive income and understand how it relates to particular financial assets in the statement of financial position.

42. We note the concern about the implementation costs related to the requirement to present separately interest revenue calculated using the effective interest method. However, in its comment letter, the respondent acknowledges the requirement to determine this amount for the purposes of applying paragraph 20(b) of IFRS 7 (reproduced in paragraph 29 and discussed in paragraphs 32-34 of this paper). Therefore, we are unconvinced that the application of this presentation requirement would result in significant additional costs (ie compared to applying the requirement in paragraph 20(b) of IFRS 7).

43. Consequently, we recommend the Committee does not make any changes to the wording of the tentative agenda decision in response to the comments received on the relevance of the information provided or the related implementation costs.

### *Wording of the tentative agenda decision*

#### *Clarification of the effect of hedge accounting*

44. As set out in paragraph 5 of this paper, the Committee concluded that the requirement in paragraph 82(a) of IAS 1 to present separately an interest revenue line item calculated using the EIM for assets that are subsequently measured at amortised cost or FVOCI is 'subject to any effect of a qualifying hedging relationship applying the hedge accounting requirements in IFRS 9 or IAS 39'. The FBF and Mazars ask the Committee to clarify this wording. The FBF does not provide further information on the clarification requested, but Mazars suggests the Committee replace the phrase

'*subject to* any effect…' that was used in the tentative agenda decision with the phrase '*including* any effect…'.

*Presentation of interest revenue as a separate line item*

45. KPMG says that while the consequential amendment made by IFRS 9 to paragraph 82(a) of IAS 1 requires an entity to present separately interest revenue calculated using the EIM, that amendment does not require a separate line item for that amount. In the respondent's view, separate presentation of such interest revenue may be achieved in other ways (such as parenthetically to a broader revenue line item). Consequently, the respondent recommends amending the wording in the tentative agenda decision so that it does not imply that a separate line item is required.

*Staff analysis*

46. In relation to the first drafting suggestion, we think the wording in the tentative agenda decision sufficiently acknowledges, consistent with the Committee's intention, that an entity can adjust the interest revenue line item required by paragraph 82(a) of IAS 1 for any effect of a qualifying hedging relationship applying the hedge accounting requirements in IFRS 9 or IAS 39.

47. In relation to the second drafting suggestion, we note that paragraph 82 of IAS 1 states (emphasis added):

> In addition to items required by other IFRSs, the profit or loss section or the statement of profit or loss shall include **line items** that present the following amounts for the period:
>
> (a) revenue, presenting separately:
>
> > (i) interest revenue calculated using the effective interest method; and
> >
> > (ii) …

48. When read together with the lead-in sentence in paragraph 82 of IAS 1, we think it is clear that the requirement to separately present interest revenue calculated using the EIM entails presenting a separate line item for that amount.

49. Consequently, we recommend the Committee does not make any changes to the wording of the tentative agenda decision in response to respondents' drafting suggestions.

## Staff recommendation

50. On the basis of our analysis, we recommend that the Committee finalise the tentative agenda decision as published in the November 2017 IFRIC Update. Appendix A to this paper outlines the proposed wording for the final agenda decision.

| **Question for the Committee** |
| --- |
| Does the Committee agree with the staff recommendation to finalise the agenda decision set out in Appendix A to this paper? |

## Appendix A

A1. We propose the following wording for the final agenda decision (deleted text is struck through)—there is no change to the wording of the tentative agenda decision:

**IFRS 9 *Financial Instruments* and IAS 1 *Presentation of Financial Statements*—Presentation of Interest Revenue for Particular Financial Instruments**

The Committee received a request about the effect of the consequential amendment that IFRS 9 made to paragraph 82(a) of IAS 1. That consequential amendment requires an entity to present separately, in the profit or loss section of the statement of comprehensive income or in the statement of profit or loss, interest revenue calculated using the effective interest method. The request asked whether that requirement affects the presentation of fair value gains and losses on derivative instruments that are not part of a designated and effective hedging relationship (applying the hedge accounting requirements in IFRS 9 or IAS 39 *Financial Instruments: Recognition and Measurement*).

Appendix A to IFRS 9 defines the term 'effective interest method' and other related terms. Those interrelated terms pertain to the requirements in IFRS 9 for amortised cost measurement and the expected credit loss impairment model. In relation to financial assets, the Committee observed that the effective interest method is a measurement technique whose purpose is to calculate amortised cost and allocate interest revenue over the relevant time period. The Committee also observed that the expected credit loss impairment model in IFRS 9 is part of, and interlinked with, amortised cost accounting.

The Committee noted that amortised cost accounting, including interest revenue calculated using the effective interest method and credit losses calculated using the expected credit loss impairment model, is applied only to financial assets that are subsequently measured at amortised cost or fair value through other comprehensive income. In contrast, amortised cost accounting is not applied to financial assets that are subsequently measured at fair value through profit or loss.

Consequently, the Committee concluded that the requirement in paragraph 82(a) of IAS 1 to present separately an interest revenue line item calculated using the effective interest method applies only to those assets that are subsequently measured at amortised cost or fair value through other comprehensive income (subject to any effect of a qualifying hedging relationship applying the hedge accounting requirements in IFRS 9 or IAS 39).

The Committee did not consider any other presentation requirements in IAS 1 or broader matters related to the presentation of other 'interest' amounts in the statement of comprehensive income. This is because the consequential amendment that IFRS 9 made to paragraph 82(a) of IAS 1 did not affect those matters. More specifically, the Committee did not consider whether an entity could present other interest amounts in the statement of comprehensive income, in addition to presenting the interest revenue line item required by paragraph 82(a) of IAS 1.

The Committee concluded that the principles and requirements in IFRS Standards provide an adequate basis for an entity to apply paragraph 82(a) of IAS 1 and present separately, in the profit or loss section of the statement of comprehensive income or in the statement of profit or loss, interest revenue calculated using the effective interest method. Consequently, the Committee ~~[~~decided~~]~~ not to add this matter to its standard-setting agenda.