IFRS™

STAFF PAPER

February 2021

IASB® meeting

Project	**Financial Instruments with Characteristics of Equity (FICE)**		
Paper topic	Disclosures: Outreach feedback and research findings		
CONTACT(S)	Angie Ah Kun	aahkun@ifrs.org	+44 (0) 20 7246 6418
	Uni Choi	uchoi@ifrs.org	+44 (0) 20 7246 6933
	Hyejin Lee	hlee@ifrs.org	+44 (0) 20 7246 6453
	Riana Wiesner	rwiesner@ifrs.org	+44 (0) 20 7246 6412

Purpose of this paper

1. The purpose of Agenda Papers 5A-5D of this meeting is to set out potential disclosures that can be developed as part of the FICE project, using the disclosure proposals in the 2018 Discussion Paper *Financial Instruments with Characteristics of Equity* (2018 DP) as a starting point. In this paper the staff provide background information on the disclosures part of the FICE project, summarise the additional outreach conducted with stakeholders and present the findings from the staff's research on regulatory disclosures provided by banks and insurers.

2. In this meeting, the Board is not asked to make any decisions but any comments or questions on the potential disclosure refinements are welcomed. The staff will then consider whether further refinements are necessary based on the feedback from this meeting and present proposed disclosures for the Board's tentative decisions at a future meeting.

3. In addition, once the Board completes its discussion on the classification requirements, the staff plan to assess whether any additional disclosures are

necessary in light of the classification decisions made. The staff are of the view that the Board can start its discussion on the disclosures set out in Agenda Papers 5B-5D of this meeting now rather than towards the end of this project given the general support from stakeholders as explained in paragraph 7 below. Also, these disclosures can be developed relatively independently of the specific topics being considered in the classification part of the project.

4. This paper is structured as follows:

(a) background (paragraphs 5–8);

(b) summary of additional outreach with stakeholders (paragraphs 9–10);

(c) summary of research on regulatory disclosures (paragraphs 11–17); and

(d) question for the Board (paragraph 18).

Background

5. At the October 2019 Board meeting (Agenda Paper 5), the Board discussed the FICE project plan and noted that the starting point for developing additional disclosures should be the proposals in the 2018 DP. Those proposals should be further developed or modified taking into account the feedback.

6. At the July 2019 Board meeting, the Board discussed the detailed feedback received from various stakeholders (including users of financial statements) in comment letters and outreach on the section of the 2018 DP dealing with the Board's preferred approach to disclosures (Agenda Paper 5B and Agenda Paper 5D).

7. That detailed feedback revealed that there was general support for the disclosure proposals, particularly amongst users of financial statements. Stakeholders generally agreed that the proposed disclosures could capture features of claims that are not presented by the binary distinction between financial liabilities and equity and could improve disclosures for equity instruments, which are currently lacking.

8. However, various stakeholders identified a number of potential challenges that may arise in preparing and using the proposed disclosures. The staff developed

potential refinements to mitigate these challenges based on the 2018 DP feedback received (see Agenda Paper 5B-5D of this meeting). The staff also performed outreach with users of financial statements and other stakeholders during the course of 2020 to obtain their views on the potential refinements developed by the staff. In addition, the staff performed research on regulatory disclosure requirements to determine if there were any overlapping disclosures. Based on the feedback from the additional outreach, research findings and considering the need to balance the requests from users of financial statements with the concerns of preparers of financial statements, the staff developed potential approaches on the way forward for discussion by the Board.

Summary of additional outreach with stakeholders

9. Over the course of 2020, the staff conducted outreach on potential refinements to the disclosures proposed in the 2018 DP with users of financial statements (both equity and debt analysts), preparers and accounting standard setters. Meetings were conducted with 5 groups and 4 individuals. Some meetings were conducted in public including:

    (a) March 2020 Capital Markets Advisory Committee (CMAC) meeting; and

    (b) December 2020 Accounting Standards Advisory Forum (ASAF) meeting.

10. Users of financial statements generally supported the potential disclosure refinements, acknowledging that they improve the disclosures proposed in the 2018 DP and take into account feedback from stakeholders. Preparers of financial statements generally expressed support for some of the potential disclosure refinements and raised some concerns with others. Detailed feedback on the potential refinements is discussed in Agenda Papers 5B-5D of this meeting.

Summary of research findings on regulatory disclosures

11. Many stakeholders asked the Board to consider the information that is already required to be disclosed when developing new disclosure requirements. Many of them referred to the disclosures financial institutions are required to provide under regulatory requirements such as BASEL III and Solvency II. These regulatory disclosures are not part of the financial statements and may not be subject to the same financial reporting processes and controls as the information reported in the financial statements.

12. The staff performed research on regulatory disclosure requirements to determine if there are any existing regulatory disclosure requirements for priority on liquidation, potential dilution and terms and conditions of capital instruments. A summary of the findings is set out below.

13. Regulatory capital consists of high-quality capital that is classified based on their loss absorbing capacity, ie how readily the capital is available to be used to absorb losses. There are multiple tiers of capital, which are based on the order or the circumstances in which they absorb losses. For more information see Agenda Paper 5E of this meeting.

14. Pillar 3 of the Basel framework seeks to promote market discipline through regulatory disclosure requirements. The staff understand that banks are required to disclose information relating to a bank's regulatory capital and risk exposures including:

    (a) 'Composition of regulatory capital' separately for each tier, which shows the hierarchy in absorbing losses.

    (b) 'Main features of regulatory capital instruments and of other TLAC[1]-eligible instruments' which provides information on 37 items including

[1] TLAC (Total loss-absorbing capacity) is an international standard, finalised by the Financial Stability Board (FSB) in November 2015, intended to ensure that G-SIBs have enough equity and bail-in debt to pass losses to investors and minimise the risk of a government bailout. It aims to (1) reduce the probability of failure of G-SIBs by increasing their loss-absorbency (addressed in the Basel framework); and (2) reduce the extent or impact of failure of G-SIBs, by improving global recovery and resolution measures (where work is led by the FSB). TLAC instruments are composed of regulatory capital and other eligible financial instruments with some adjustments.

maturity (perpetual or dated), accounting classification, issuer call, coupons/dividends, convertibility (with conversion rate), write down feature, type of subordination and position in subordination hierarchy in liquidation (specifying the instrument type immediately senior in the insolvency creditor hierarchy).

(c) 'Creditor ranking at legal entity level' which provides creditors with information regarding their ranking in the liability structure of each resolution entity upon resolution[2]. This disclosure is only required for the global systematically important banks (G-SIBs) under TLAC.

15. The requirements differ among countries with regards to the level of detail required in publicly disclosed information. In Europe, the regulatory capital base is reported in great detail using a template given by the European Banking Authority. With regards to MREL[3] and TLAC less information has so far been given since the requirements have not yet been fully implemented.

16. As for insurers, International Capital Standard (ICS)[4] includes Insurance Core Principles on public disclosures, which will be used to inform how specific ICS disclosure rules for capital adequacy will be developed. Those principles state that disclosures about the insurer's capital adequacy include information on:

(a) its objectives, policies and processes for managing capital and assessing capital adequacy;

[2] Resolution occurs at the point where the authorities determine that a bank is failing or likely to fail, that there is no other supervisory or private sector intervention that can restore the institution to viability within a short timeframe and that normal insolvency proceedings would cause financial instability while having an impact on the public interest.

[3] MREL (Minimum Requirement for own funds and Eligible Liabilities) is similar standard to TLAC for European banks, which is included in Bank Recovery and Resolution–Directive 2014/59/EU (BRRD).

[4] The Insurance Capital Standard (ICS) is a consolidated group-wide capital standard that applies to internationally active insurance groups (IAIGs). It is a part of a package of reforms completed by the International Association of Insurance Supervisors (IAIS) in response to the Financial Crisis of 2007–2009. Currently, large, global insurance groups are subjected to different capital standards that make it difficult to compare their solvency positions. The ultimate goal of the ICS is to establish a single ICS that includes a common methodology that achieves comparable outcomes across jurisdictions. The current ICS version 2.0 is not a finalised standard and is tested in a 5 year monitoring period. In the monitoring period of 2020–2024, the IAIS will annually review the participation of IAIGs and the feedback received from supervisors and industry stakeholders during the monitoring period will be used to further improve the ICS.

(b) the solvency requirements of the jurisdiction(s) in which the insurer operates; and

(c) the capital available to cover regulatory capital requirements. If the insurer uses an internal model to determine capital resources and requirements, information about that model is disclosed.

At this stage, ICS version 2.0 does not include specific public disclosure requirements.

17. In Europe, insurers under Solvency II are required to disclose the description of the capital management including the structure and amount of own funds and their quality in the Solvency and Financial Condition Report (SFCR). In the European Insurance and Occupational Pensions Authority's Guidelines on Reporting and Public Disclosure, Guideline 12 requires a description, for each material own fund item, of the extent to which it is available, subordinated, as well as its duration and any other features that are relevant for assessing its quality. We understand that in meeting this requirement, insurers would be disclosing key terms and conditions of financial instruments used in their capital management with the extent of disclosure being dependent on each entity's specific circumstances. Insurers are also required to publish quantitative information in the public Quantitative Reporting Templates included within the SFCRs, which does not include any information on the priority on liquidation nor dilution effect of financial instruments.

Question for the Board

18. The staff would like to ask the Board the following question.

Questions for the Board
Do Board members have any comments or questions on the staff's outreach and research set out in this paper?