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Project	TLTRO III transactions (IFRS 9 and IAS 20)		
Paper topic	Initial consideration		

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Introduction

1. The IFRS Interpretations Committee (Committee) received a submission asking how banks account for the European Central Bank (ECB)'s Targeted Longer-Term Refinancing Operations (TLTRO). The submitter has identified diversity in the application of the requirements in IFRS 9 *Financial Instruments* and IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance* in relation to the accounting for TLTRO transactions by banks.

2. The objective of this paper is to:

   (a) provide the Committee with a summary of the matter;

   (b) present our research and analysis; and

   (c) ask the Committee whether it agrees with our recommendation not to add a standard-setting project to the work plan.

Structure of the paper

3. This paper includes:

   (a) background information (paragraphs 1 to 15);

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(b) staff's analysis (paragraphs 16 to 45);

(c) staff's assessment against the Committee's agenda criteria (paragraphs 46 to 47); and

(d) staff's recommendation (paragraph 48).

4. There are two appendices to the paper:

(a) Appendix A—Proposed wording of the tentative agenda decision; and

(b) Appendix B—Submission.

Background information

TLTRO programmes

5. The TLTROs are ECB operations that provide financing to credit institutions[1] such as banks with the objective of stimulating lending to the bank's customers. The amount that banks can borrow through the programme is linked to the volume and amount of loans made to non-financial corporations and households.

6. The third TLTRO programme (TLTRO III) consists of ten quarterly refinancing operations or tranches starting from September 2019, each with a maturity of three years.[2] During 2020 and 2021, some of the TLTRO III transaction parameters were favourably modified to support the continued access of businesses and households to bank credit in the face of disruptions and temporary funding shortages associated with the covid-19 pandemic. For example, in April 2020 and January 2021, the TLTRO III transaction parameters were modified to reduce the applicable interest rate during the special interest rate period from 24 June 2020 to 23 June 2022 by 50 basis points.

7. Banks are required to settle interest in arrears on each TLTRO III tranche on the maturity or early repayment of the tranche. The interest rate applicable to each

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[1] According to Regulation (EU) No 575/2013, credit institution means an undertaking the business of which is to take deposits or other repayable funds from the public and to grant credits for its own account.

[2] Please refer to [Indicative calendar for the third series of targeted longer-term refinancing operations (TLTROs-III) (europa.eu)]

TLTRO III tranche is subject to the bank achieving predefined lending threshold(s) in the specified reference period(s).

8. For banks that do not achieve any of the lending thresholds during the reference periods, the interest rate for each tranche (ie the unconditional interest rate) is the average ECB interest rate on the main refinancing operations (MRO rate) over the life of the respective tranche. [3] However, during the period from 24 June 2020 to 23 June 2022, the unconditional interest rate is reduced to 50 basis points below the average MRO rate over the respective period.

9. For banks that achieve all of the lending thresholds during the reference periods, the interest rate is the average interest rate of the ECB's deposit facility (DFR) over the life of the respective tranche. Similarly, during the period from 24 June 2020 to 23 June 2022, this interest rate is reduced to 50 basis points below the average DFR rate over the respective period.

10. The MRO rate is the interest rate banks pay when they borrow money from the ECB for one week. Using this refinancing facility, banks have to provide collateral to guarantee that the money will be repaid. The MRO rate is one of the three interest rates the ECB sets every six weeks as part of its work to keep prices stable in the euro area. The DFR defines the interest banks receive (or have to pay in times of negative interest rates) for depositing money with the ECB overnight.

The question in the submission

11. The submission asks the following questions in relation to the accounting for TLTRO III transactions:

    (a) whether the TLTRO III tranches are loans at a below-market interest rate and, if so, whether the borrowing bank is required to apply IFRS 9 or IAS 20 to account for the benefit of the below-market interest rate;

    (b) if the bank is required to apply IAS 20 to account for the benefit of the below-market interest rate:

[3] For the special interest rate periods different calculations of the average MRO rate or average DFR may apply.

(i) how it assesses the period(s) in which it recognises the benefit of the TLTRO III transactions; and

(ii) whether, for the purpose of presentation, the bank adds the amount of the benefit to the carrying amount of the TLTRO III liability;

(c) how the bank calculates the applicable effective interest rate;

(d) whether the bank applies paragraph B5.4.6 of IFRS 9 to account for changes in estimated cash flows due to the revised assessment of meeting the conditions attached to the liability; and

(e) how the bank accounts for changes in cash flows related to the prior period that result from the bank's lending behaviour or from changes in the TLTRO III conditions determined by the ECB.

12. The submission asks these questions from the perspective of the borrowers receiving the TLTRO III re-financing operations (ie the banks); this paper therefore considers the application of the accounting requirements only to financial liabilities and tailors its analysis to the applicable requirements in IFRS 9 and IAS 20. This paper does not consider the accounting by the provider of the TLTRO III financing (ie the accounting for the financial assets the ECB holds).

13. The submitter provides alternative views for the main issues raised in the submission, which are reproduced in Appendix B to this paper.

Outreach

14. The purpose of any outreach we perform is to understand:

(a) the prevalence of the transaction or fact pattern submitted; and

(b) the accounting applied to that transaction or fact pattern.

15. We decided not to perform outreach on this submission for the following reasons:

(a) we are aware that the TLTRO programmes are prevalent in Europe since the first series of TLTROs was announced in 2014. Our research indicated that more than 720 European banks borrowed in excess of €1.3 billion during the first drawdown period of the TLTRO III; and

(b) we are already aware of diversity in accounting for TLTRO transactions without undertaking further research. Although the questions asked in the submission about calculating the effective interest rate are specifically in the context of TLTRO III financing, these questions are equally relevant in the context of other fact patterns (including TLTRO I and TLTRO II financing). We are aware of differing views about how to calculate the effective interest rate at initial recognition when the interest rate is subject to conditions as well as the interaction between effective interest rate and modifications. The Committee has previously responded to questions related to determining effective interest rates. The staff have also received questions related to determining effective interest rates, and how it relates to changes in expected cash flows (including modifications), in the context of the first phase of the post-implementation review (PIR) of the classification and measurement requirements in IFRS 9. The Board expects to publish the Request for Information on this PIR in Q3 2021. Diversity in practice was also confirmed from the staff's research, which included a high-level desktop review of the financial statements of some European banks to understand the accounting treatment of TLTRO III transactions.

Staff's Analysis

Application of the requirements in IFRS Standards

16. For the purpose of the analysis of the applicable accounting requirements, the staff think it is important to identify the appropriate starting point for the analysis and the order in which a bank applies the requirements in IFRS 9 and, to the extent applicable, IAS 20.

17. From the borrowing bank's perspective, IFRS 9 must be the starting point of for the borrowing bank to determine its accounting for TLTRO III transactions because the

financial liability arising from the bank's participation in the TLTRO III programme is in the scope of IFRS 9[4]. The bank:

(a) determines whether it bifurcates any embedded derivatives from the host contract as required by paragraph 4.3.3 of IFRS 9;

(b) recognises and measures the financial liability. This includes determining the fair value of the financial liability, accounting for any difference between the fair value and the transaction price and calculating the effective interest rate; and

(c) subsequently measures the financial liability, including accounting for changes in estimates of expected (future) cash flows.

18. The submitter explains that because the interest rate in a TLTRO III transaction is linked to the borrower's lending activity (ie the lending threshold is entity-specific), the variability in the interest rate described in paragraph 7 of this paper is not an embedded derivative as defined in paragraph 4.3.1 of IFRS 9[5]. This is because the submitter considers the lending threshold to be a non-financial variable that is specific to a party to the contract (ie the bank). Because the questions the submission asks are unrelated to the existence of an embedded derivative, we have not performed analysis of the requirements in IFRS 9 for the separation of embedded derivatives.

Initial recognition and measurement of the financial liability

19. Applying paragraph 5.1.1 of IFRS 9, an entity measures a financial liability at initial recognition at fair value plus or minus transaction costs, if the financial liability is not measured at fair value through profit or loss. If the fair value of the financial liability at initial recognition differs from the transaction price, an entity applies paragraphs B5.1.1 and B5.1.2A[6] of IFRS 9 to account for the difference between the fair value and the transaction price.

[4] These financial liabilities represent contractual obligations to deliver cash to another entity as described in paragraph 11 of IAS 32 *Financial Instruments: Presentation.*

[5] Paragraph 4.3.3 of IFRS 9 requires an embedded derivative to be separated from the host contract and accounted for as a derivative under IFRS 9 if (among other criteria) its economic characteristics and risks are not closely related to the economic characteristics and risks of the host and a separate instrument with the same terms would meet the definition of a derivative.

[6] As required by paragraph 5.1.1A of IFRS 9.

20. Paragraphs B5.1.1 and B5.1.2A of IFRS 9 state that the fair value of a financial instrument at initial recognition is normally the transaction price (ie the fair value of the consideration given or received). Applying IFRS 9, an entity would therefore need to determine the fair value of the liability using the assumptions that market participants would use when pricing the financial liability as required by IFRS 13 *Fair Value Measurement*.

21. When the fair value of the financial liability is different from the transaction price, paragraph B.5.1.1 requires an entity to determine the fair value and whether a part of the consideration given or received is for something other than the financial liability. For example, an entity can measure the fair value of a long-term loan that carries no interest at the present value of all future cash flows discounted using the prevailing market interest rate(s) for a similar instrument (similar with respect to currency, term, type of interest rate and other factors) with a similar credit rating. Any additional amount lent is an expense or a reduction of income unless it qualifies for recognition as some other type of asset.[7]

22. Determining whether an interest rate is a below-market interest rate is not an accounting question. However, a difference between the fair value and the transaction price of a financial liability might indicate that the interest rate on the financial liability (ie for each TLTRO III tranche) is a below-market rate. If the TLTRO III transactions are regarded as bearing below-market interest rates, a bank may need to consider whether it applies IAS 20 in accounting for the difference between the fair value of the liability and its transaction price (see paragraphs 24–33 of this paper). However, IAS 20 (<u>if applicable</u>) would apply *only* to the difference between the fair value of the financial liability at initial recognition and its transaction price. Paragraph 10A of IAS 20 confirms that an entity accounts for the financial liability itself as required by IFRS 9.

23. If an entity determines that the fair value at initial recognition is different from the transaction price but the consideration is only for the financial instrument (ie that IAS

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[7] Although paragraph B5.1.1 refers to the recognition of another type of asset, the requirements in that paragraph apply equally to financial assets and financial liabilities.

20 does not apply to the difference), paragraph B5.1.2A of IFRS 9 requires an entity to account for that difference as follows:

(a) if the fair value is evidenced by a quoted price in an active market for an identical asset or liability (ie a Level 1 input as described in IFRS 13) or based on a valuation technique that uses only data from observable markets, the entity recognises the difference as a gain or loss in profit or loss;

(b) in all other cases, the entity defers the difference and recognises it as a gain or loss only to the extent that it arises from a change in a factor (including time) that market participants would take into account when pricing the liability. Paragraph 28 of IFRS 7 *Financial Instruments: Disclosures* requires disclosure of the entity's accounting policy for recognising such differences in profit or loss.

Do TLTRO III tranches contain a government grant within the scope of IAS 20?

24. IAS 20 defines government grants as 'assistance by government in the form of transfers of resources to an entity in return for past or future compliance with certain conditions relating to the operating activities of the entity. They exclude those forms of government assistance which cannot reasonably have a value placed upon them and transactions with government which cannot be distinguished from the normal trading transactions of the entity'. IAS 20 defines government as referring to 'government, government agencies and similar bodies whether local, national or international'.

25. Applying paragraph 7 of IAS 20, an entity recognises a government grant only when there is reasonable assurance that (a) the entity will comply with the conditions attaching to it, and (b) the grant will be received.

26. Paragraph 10A of IAS 20 requires an entity to treat as a government grant the benefit of a government loan at a below-market rate of interest, and account for it in accordance with IAS 20. The entity is required to measure the benefit of the below-market interest rate as the difference between the initial carrying value of the loan determined in accordance with IFRS 9 and the proceeds received.

27. Paragraph 12 of IAS 20 requires an entity to recognise government grants in profit or loss on a systematic basis over the periods in which the entity recognises as expenses the related costs for which the grants are intended to compensate—the entity

considers the conditions and obligations that have been, or must be, met when identifying the costs for which the benefit of the loan is intended to compensate (paragraph 10A of IAS 20). Paragraph 20 of IAS 20 deals with government grants that becomes receivable as compensation for expenses or losses already incurred or for the purpose of giving immediate financial support to the entity with no future related costs—it requires an entity to recognise such government grants in profit or loss of the period in which it becomes receivable.

28. Paragraph 35 of IAS 20 gives an example of assistance that cannot be distinguished from the normal trading transactions of an entity and, thus, is not accounted for as a government grant – a government procurement policy that is responsible for a portion of the entity's sales. In that example, there might be an unquestioned benefit to the entity but any attempt to segregate the trading activities from government assistance could well be arbitrary.

29. A bank would therefore need to determine whether IAS 20 is applicable to the TLTRO III tranches. As discussed in paragraph 22 of this paper, if applicable, IAS 20 would apply only to the difference between the initial carrying amount of the financial liability (as required by paragraph 5.1.1 of IFRS 9) and the consideration received. The staff are of the view that, for the TLTRO III tranches to contain a government grant within the scope of IAS 20, the following would need to apply:

    (a) it would need to be determined that the ECB meets the definition of government in IAS 20;

    (b) the interest rate charged on the TLTRO III tranches would need to be determined to be a below-market interest rate; and

    (c) TLTRO III transactions with the ECB would need to be distinguishable from the normal trading transactions of the bank.

30. Determining whether the ECB meets the definition of government and whether the interest rate charged on the TLTRO III tranches is a below-market interest rate are not accounting questions and would require an entity to exercise judgement.

31. Banks routinely obtain financing from the ECB as part of their 'normal trading transactions'. To be accounted for as a government grant, the TLTRO III programme

must be distinguishable from the other financing provided by the ECB that is part of the bank's normal trading transactions.

32. Based on the fact pattern in the submission, it is unclear which costs any government grant would be intended to compensate the banks for, because the provision of TLTRO III funding does not appear to restrict the interest rates banks can charge their customers.

33. However, the staff are of the view that if an entity concludes there is a government grant, the requirements in IAS 20 are clear about how to account for a government grant and over which period to recognise the grant. Judgement is required regarding the non-accounting questions noted above – based on the specific facts and circumstances pertaining to the TLTRO III tranches – to determine whether the tranches contain a government grant within the scope of IAS 20. Therefore, the staff think the Committee is not in a position to opine on whether the TLTRO III tranches contain a government grant within the scope of IAS 20.

Calculation of the effective interest rate on initial recognition of the financial liability

34. For the purpose of financial liabilities, Appendix A to IFRS 9 defines the amortised cost of a financial liability as the amount at which the financial liability is measured at initial recognition minus the principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between that initial amount and the maturity amount.

35. Appendix A to IFRS 9 also defines the effective interest rate (in the context of financial liabilities) as the rate that exactly discounts estimated future cash flows through the expected life of the financial liability to the amortised cost at initial recognition. When calculating the effective interest rate, an entity estimates the expected cash flows by considering all the contractual terms of the financial instrument (for example, prepayment, extension, call and similar options). The calculation includes all fees and points paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs, and all other premiums or discounts.

36. It is clear from the definition of the amortised cost of a financial liability that the amortised cost at initial recognition is the fair value on initial recognition plus or minus any transaction costs as required by paragraph 5.1.1 of IFRS 9.

37. In the context of the submission, the question arises as to what to consider in estimating the ‘expected future cash flows’ and, specifically, whether the expected future cash flows reflect an assessment of whether the bank will satisfy the conditions attached to the liability. The question of what to consider in estimating the expected future cash flows for the purpose of calculating the effective interest rate is relevant not only in the fact pattern described in the request. Similar questions arise in many other circumstances and we are aware of diversity in practice in this regard. The staff think the fact pattern described in the submission is part of a broader practice matter and therefore should not be analysed in isolation. Analysing this specific example in isolation could have unintended consequences for fact patterns that raise similar questions about the application of IFRS Standards. Therefore, the staff believes this matter should be considered as part of the PIR on the classification and measurement requirements in IFRS 9, together with similar matters already identified by the staff in the first phase of the PIR.

Subsequent measurement of the financial liability at amortised cost

38. As per the contractual terms of the TLTRO III tranches, interest is settled in arrears on maturity or early repayment of these financial instruments. Therefore, there is only one cash flow on the instrument, which is determined by the ECB several days before maturity.

39. The original effective interest rate is based on estimated future cash flows at inception as set out in paragraphs 34–37 of this paper. Whether a bank updates the effective interest rate over the life of a tranche depends on the applicable requirements in IFRS 9. Paragraphs B5.4.5 and B5.4.6 of IFRS 9 set out how to account for changes in estimated (future) cash flows.

40. Paragraph B5.4.5 of IFRS 9 applies to floating-rate financial assets and financial liabilities for which estimated (future) cash flows are revised to reflect movements in markets rates of interest. Periodic re-estimations of those cash flows to reflect such movements alter the effective interest rate. IFRS 9 does not elaborate on what is

meant by *floating rate*. However, it is clear that a financial instrument with variable contractual cash flows – which can periodically be adjusted to reflect movements in market rates – is a floating rate financial instrument.

41. As previously discussed by the Board in October 2008, there are several possible views on how wide or narrow to interpret the term 'market rates'.[8] It is generally accepted that market rates refer to the variable element of the interest rate that changes in response to changes in market rates (for example, benchmark interest rates or other rates that an entity deems market rates). However, specified fixed elements such as a credit spread – which are not adjusted or do not change when market rates change – are not seen as reflecting movements in market rates.

42. When considering changes in cash flow estimates, paragraph B5.4.5 of IFRS 9 applies only to the variable interest rate element of a floating-rate instrument. This is because the requirements focus on the treatment of a floating interest rate element that resets to market rates. Those requirements do not refer to the fixed interest rate element of an instrument, which is typically not reset to market rates (for example, a credit or other spread or a stepped interest margin).[9] Therefore, a floating-rate instrument can have both a floating interest element to the interest rate (for example, the element in a TLTRO III tranche relating to the MRO rate or the DFR) and a fixed interest rate element (for example, the fixed 50 basis points reduction in the interest rate for a special interest period of the TLTRO III tranches).

43. Paragraph B.5.4.6 of IFRS 9 applies to changes in estimated (future) cash flows of financial liabilities other than those addressed in paragraph B5.4.5, irrespective of whether the change arises from a modification or another change in expectations. Periodic re-estimation of cash flows adjusts the amortised cost of a financial liability to the present value of these re-estimated cash flows by discounting the estimated future cash flows at the financial liability's original effective interest rate. The adjustment is recognised in profit or loss.

44. If the terms of the TLTRO III tranches have been modified (for example, the introduction of an early repayment option or a 50 basis points interest rate reduction

[8] See October 2008 Board meeting Agenda Paper 6.

[9] As illustrated in paragraph B27 of the Implementation Guidance to IFRS 9

in a special interest rate period), a bank first needs to consider if the changes constitute a modification of terms affecting the particular tranche of the TLTRO III programme, because each tranche would be a separate unit of account. If the change represents a modification to the contractual terms of a tranche, the bank first applies the requirements in paragraphs 3.3.2 and B3.3.6 of IFRS 9 to determine whether the modification results in the derecognition of a tranche. If the bank has concluded that the changes are not modifications or that the modification does not result in derecognition, the bank adjusts the amortised cost of the financial liability to reflect the modified contractual cash flows discounted at the original effective interest rate. The bank recognises the adjustment to the amortised cost of the financial liability immediately in profit or loss as required by paragraph B5.4.6 of IFRS 9.[10]

45. This means, if, as a result of the modification or change in expected cash flows, the bank estimates the final repayment cash flow to be different from that used in determining the original amortised cost, the adjustment to the carrying amount reflects this change in line with the contractual terms of the TLTRO tranche. Therefore, the bank makes no adjustments to interest recognised in profit or loss in prior periods as contemplated by the submission because this change in expected cash flows does not constitute the correction of an error in the prior period. For changes in future expected cash flows other than modifications the application of paragraph B5.4.6 of IFRS 9 depends on the bank's estimate of the expected future cash flows when determining the effective interest rate at initial recognition. As discussed in paragraph 37 the questions that arise in that context are part broader practice matter and therefore should not be analysed in isolation, but should be considered as part of the PIR on the classification and measurement requirements in IFRS 9, together with similar matters already identified by the staff in the first phase of the PIR.

[10] The Board intended that modification of financial liabilities should be treated in the same way as modifications of financial asset as per paragraph BC4.252 and BC 4.253 of IFRS 9.

Should the Committee add a standard-setting project to the work plan?

Accounting for any government grant in the scope of IAS 20

Is it necessary to add to or change IFRS Standards to improve financial reporting?[11]

46. Based on our analysis in paragraphs 24-33 of this paper, in our view if an entity determines that there is a government grant within the scope of IAS 20 in the fact pattern described in the request, the requirements in IAS 20 provide an adequate basis for the entity to determine how to account for the government grant and over which period to recognise the grant.

Accounting for the financial liability in the scope of IFRS 9

Is the matter sufficiently narrow in scope that the Board or the Committee can address it in an efficient manner, but not so narrow that it is not cost-effective for the Board or the Committee and stakeholders to undertake the due process required to change a Standard? [12]

47. In our view, the fact pattern described in the submission is part of a broader practice matter relating to calculating the effective interest rate when the amount of future estimated cash flows are conditional on future events. As described in paragraphs 15(b) and 37 of this paper, similar questions arise in other circumstances. We would suggest that the fact pattern described in the submission form part of a more comprehensive analysis of how current expectations of future cash flows affect the effective interest rate calculation and the amortised cost or gross carrying amount of a financial instrument. Analysing this single type of transaction in isolation could have unintended consequences for fact patterns that involve similar questions about the application of IFRS Standards. The staff therefore conclude that the matter submitted is, in isolation, too narrow for the Board or the Committee to address in a cost-effective manner.

[11] Paragraph 5.16(b) of the *Due Process Handbook*.

[12] Paragraph 5.16(d) of the *Due Process Handbook*.

Staff recommendation

48. Based on our assessment of the work plan criteria in paragraph 5.16 of the *Due Process Handbook* (discussed in paragraphs 46 to 47 of this paper), we recommend that the Committee does not add a standard-setting project to the work plan. Instead, we recommend publishing a tentative agenda decision that explains that:

    (a) the Committee is not in a position to provide a view on whether the TLTRO III tranches contains a government grant within the scope of IAS 20 because the relevant questions that need to be answered are not accounting questions. Nonetheless, if an entity determines that there is a government grant within the scope of IAS 20, the requirements in IAS 20 provide an adequate basis for the entity to determine how to account for the government grant and over which period to recognise the grant.

    (b) the matters related to calculating the effective interest rate are too narrow for the Committee to consider in isolation. In our view, those matters are better addressed as part of the Board's PIR of the classification and measurement requirements in IFRS 9, together with other questions on the application of the requirements for modifications of financial instruments and the calculation of the effective interest rate. We note that such a decision would be consistent with previous decisions of the Committee when the Board is considering a matter as part of an existing project.

49. Appendix A to this paper sets out the proposed wording of the tentative agenda decision. In our view, the proposed tentative agenda decision (including the explanatory material contained within it) would not add or change requirements in IFRS Standards.[13]

[13] Paragraph 8.4 of the *Due Process Handbook* states: 'Agenda decisions (including any explanatory material contained within them) cannot add or change requirements in IFRS Standards. Instead, explanatory material explains how the applicable principles and requirements in IFRS Standards apply to the transactions or fact pattern described in the agenda decision.'

Questions for the Committee

1. Does the Committee agree with our analysis of the requirements in IFRS Standards, outlined in paragraphs 16–45 of this paper?
2. Does the Committee agree with our recommendation not to add a standard-setting project to the work plan?
3. Does the Committee have any comments on the proposed wording of the tentative agenda decision set out in Appendix A to this paper?

Appendix A—Proposed wording of the tentative agenda decision

TLTRO III transactions (IFRS 9 *Financial Instruments* and IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance*)

The Committee received a request about how to account for the targeted longer-term refinancing operations (TLTROs) of the European Central Bank (ECB). The TLTROs are targeted programmes for which the amount a participating bank can borrow and the interest rate it pays on each tranche within the programme is linked to the volume and amount of loans it makes to non-financial corporations and households.

The request asks:

(a) whether the TLTRO III tranches involve loans at a below-market interest rate and, if so, whether the borrowing bank is required to apply IFRS 9 or IAS 20 to account for the benefit of the below-market interest rate;

(b) if the bank is required to apply IAS 20 to account for the benefit of the below-market interest rate:

    (i) how it assesses the period(s) in which it recognises the benefit of the TLTRO III transactions; and

    (ii) whether, for the purposes of presentation, the bank adds the amount of the benefit to the carrying amount of the TLTRO III liability;

(c) how the bank calculates the applicable effective interest rate;

(d) whether the bank applies paragraph B5.4.6 of IFRS 9 to account for changes in estimated cash flows due to the revised assessment of meeting the conditions attached to the liability; and

(e) how the bank accounts for changes in cash flows related to the prior period that result from the bank's lending behaviour or from changes in TLTRO III conditions determined by the ECB.

Application of the requirements in IFRS Standards

The Committee observed that IFRS 9 is the starting point for the borrowing bank to determine its accounting for TLTRO III transactions because the financial liability

arising from the bank's participation in the TLTRO III programme is in the scope of IFRS 9. The bank:

(a) determines whether it bifurcates any embedded derivatives from the host contract as required by paragraph 4.3.3 of IFRS 9;

(b) recognises and measures the financial liability. This includes determining the fair value of the financial liability, accounting for any difference between the fair value and the transaction price and calculating the effective interest rate; and

(c) subsequently measures the financial liability, including accounting for changes in the estimates of expected cash flows.

Because the questions the request asks are unrelated to the existence of an embedded derivative, this agenda decision does not discuss the requirements in IFRS 9 regarding the separation of embedded derivatives.

Initial recognition and measurement of the financial liability

Applying paragraph 5.1.1 of IFRS 9, at initial recognition the bank measures a TLTRO III liability at fair value plus or minus transaction costs, if the financial liability is not measured at fair value through profit or loss. The fair value of a financial instrument at initial recognition is normally the transaction price (ie the fair value of the consideration given or received) (paragraphs B5.1.1 and B5.1.2A of IFRS 9).

If the fair value of the financial liability at initial recognition differs from the transaction price, the bank applies paragraphs B5.1.1 and B5.1.2A of IFRS 9 to account for that difference. In that case, paragraph B.5.1.1 requires the bank to determine the fair value and whether part of the consideration given or received is for something other than the financial liability. Applying IFRS 9, an entity therefore determines the fair value of the liability using the assumptions that market participants would use when pricing the financial liability as required by IFRS 13 *Fair Value Measurement.*

The Committee observed that determining whether an interest rate is a below-market rate is not an accounting question. Nonetheless, a difference between the fair value

of a financial liability at initial recognition and the transaction price might indicate that the interest rate on the financial liability (ie for each TLTRO III tranche) is a below-market rate.

If the bank determines that the fair value of a TLTRO III liability at initial recognition differs from the transaction price but the consideration is not only for the financial liability, the bank considers whether that difference represents a government grant (as defined in IAS 20), and if so, applies IAS 20 to account for the difference. In this case, IAS 20 applies *only* to the difference between the fair value of the financial liability at initial recognition and the transaction price. Paragraph 10A of IAS 20 specifies that the bank accounts for the financial liability itself as required by IFRS 9.

If the bank determines that the fair value of a TLTRO III liability at initial recognition differs from the transaction price but the consideration is only for the financial liability, the bank applies paragraph B5.1.2A of IFRS 9 to account for that difference.

Do TLTRO III tranches contain a government grant in the scope of IAS 20?

IAS 20 defines government grants as 'assistance by government in the form of transfers of resources to an entity in return for past or future compliance with certain conditions relating to the operating activities of the entity. They exclude those forms of government assistance which cannot reasonably have a value placed upon them and transactions with government which cannot be distinguished from the normal trading transactions of the entity'. IAS 20 defines government as referring to 'government, government agencies and similar bodies whether local, national or international'.

Paragraph 10A of IAS 20 requires an entity to treat as a government grant the benefit of a government loan at a below-market rate of interest and apply IAS 20 to account for that benefit. The benefit of a below-market interest rate is the difference between the initial carrying amount of the loan determined applying IFRS 9 and the proceeds received. Paragraphs 12 and 20 of IAS 20 specify requirements for the recognition of government grants in profit or loss.

The Committee observed that TLTRO III tranches would contain a government grant in the scope of IAS 20 only if it were determined that:

(a) the ECB meets the definition of government in IAS 20;

(b) the interest rate charged on the TLTRO III tranches is a below-market interest rate; and

(c) the TLTRO III transactions with the ECB are distinguishable from the borrowing bank's normal trading transactions.

The Committee observed that determining whether the ECB meets the definition of government and whether the interest rate charged on the TLTRO III tranches is a below-market rate are not accounting questions and would require the use of judgement. The Committee noted therefore that it is not in a position to conclude on whether the TLTRO III tranches contain a government grant in the scope of IAS 20.

The Committee nonetheless concluded that if the TLTRO III tranches contain a government grant in the scope of IAS 20, the requirements in IAS 20 provide an adequate basis for the bank to determine how to account for that government grant.

Calculation of the effective interest rate on initial recognition of the financial liability

For the purpose of measuring financial liabilities, Appendix A to IFRS 9 defines the amortised cost of a financial liability and also the effective interest rate. The calculation of the effective interest rate requires an entity to estimate the expected cash flows through the expected life of the financial liability.

In calculating the effective interest rate for a TLTRO III liability on initial recognition, the question arises as to what to consider in estimating the expected future cash flows and, specifically, whether the expected future cash flows reflect an assessment of whether the bank will satisfy the conditions attached to the liability. The Committee noted that the question of what to consider in estimating the expected future cash flows for the purpose of calculating the effective interest rate is relevant not only in the fact pattern described in the request. Similar questions arise in many other circumstances. The Committee therefore concluded that calculating the effective interest rate is a broader matter, which it should not analyse in isolation

for TLTRO III liabilities. Analysing this matter for TLTRO III liabilities in isolation could have unintended consequences for other financial instruments, the measurement of which involves similar questions about the application of IFRS Standards. The Committee is therefore of the view that this matter should be considered as part of the Post-implementation Review (PIR) of the classification and measurement requirements in IFRS 9, together with similar matters already identified in the first phase of the PIR.

Subsequent measurement of the financial liability at amortised cost

Paragraphs B5.4.5 and B5.4.6 of IFRS 9 specify requirements for how an entity accounts for changes in estimated future cash flows.

Paragraph B5.4.5 applies to floating-rate financial liabilities, the estimated future cash flows of which are revised to reflect movements in market rates of interest. Periodic re-estimations of those cash flows to reflect such movements alter the effective interest rate. IFRS 9 does not elaborate on what is meant by floating rate. However, the Committee observed that a financial instrument with variable contractual cash flows – which can periodically be adjusted to reflect movements in market rates – is a floating-rate financial instrument.

The Committee also observed that a floating-rate financial instrument may consist of a floating interest rate element (which is reset to market rates) plus or minus other elements (which are not reset to market rates).

When considering changes in cash flow estimates, the Committee noted that paragraph B5.4.5 applies only to the variable interest rate element of a floating-rate instrument. This is because the requirements deal with the treatment of a floating-rate interest rate element, which resets to market rates. Paragraph B5.4.5 does not refer to the other interest rate elements of an instrument, which are typically not reset to market rates (for example, a credit or other spread, or a stepped interest margin).

Paragraph B.5.4.6 applies to changes in estimated future cash flows of financial liabilities other than those addressed in paragraph B5.4.5, irrespective of whether the change arises from a modification or another change in expectations.

The Committee noted that, if – as a result of a modification or change in expected cash flows – the bank estimates the final repayment cash flow in the TLTRO III liability to be different from that used in determining the original amortised cost, the adjustment to the carrying amount reflects this change in line with the contractual terms of the TLTRO liability. The bank therefore makes no adjustments to interest recognised in profit or loss in prior periods because the change in expected cash flows does not constitute the correction of a prior period error.

The Committee also noted that the application of paragraph B5.4.6 of IFRS 9 relates to the bank's estimates of future expected cash flows when determining the effective interest rate on initial recognition of the financial liability and that the question is part of a broader matter, which it should not analyse in isolation for TLTRO III liabilities. The Committee is therefore of the view that this matter should also be considered together with similar matters already identified in the first phase of the PIR on the IFRS 9 classification and measurement requirements.

Conclusion

The Committee concluded that if the bank determines that the TLTRO tranches contain a government grant in the scope of IAS 20, the requirements in IAS 20 provide an adequate basis for an entity to determine how to account for that government grant.

With respect to the calculation of the effective interest rate for a TLTRO III liability, the Committee concluded that the matter described in the request is, in isolation, too narrow for the Board or the Committee to address in a cost-effective manner. Instead, the Board should consider this matter as part of the PIR of the classification and measurement requirements in IFRS 9.

For these reasons, the Committee [decided] not to add a standard-setting project to the work plan.

Appendix B—Submission

B1. We have reproduced the submission below.

…

Agenda Item Request: Accounting for the TLTRO III transactions (IFRS 9, IAS 20)

…

In the context of ESMA's supervisory convergence work in the area of financial reporting, I would like to raise with you an issue related to the application of IFRS 9 *Financial Instruments* and IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance.* ESMA has identified diversity in the application of the requirements of IFRS 9 and IAS 20 in relation to the accounting treatment of the European Central Bank's Targeted Longer-Term Refinancing Operations (TLTRO III) by banks.

Accordingly, ESMA kindly suggests that the IFRS Interpretations Committee (IFRS IC) considers clarifying the relevant accounting requirements. A detailed description of the case is set out in the appendix to this letter.

…

APPENDIX – DETAILED DESCRIPTION OF THE ISSUE

Description of fact pattern

1. The targeted longer-term refinancing operations (TLTROs) are operations of the European Central Bank (ECB) that provide financing to credit institutions. The TLTROs are targeted operations, as the amount that banks can borrow is linked to their loans to non-financial corporations and households. By offering banks long-term funding at attractive conditions they stimulate bank lending to the real economy.
2. The third TLTRO programme (TLTRO III) consists of ten refinancing operations, each with a maturity of three years, starting in September 2019 with a quarterly frequency. During 2020, some of the transaction parameters were modified to support the continued access of businesses and households to bank credit in the face of disruptions and temporary funding shortages associated with the COVID-19 pandemic.
3. The borrowing rate applicable to the TLTRO III loans is linked to the lending patterns of the participating banks. The reduced interest rates are subject to the achievement of predefined lending performance thresholds based on the eligible net lending of the bank in the specified periods.
4. The borrowing rate in these operations for banks which do not achieve lending performance thresholds is the average ECB interest rate on the main refinancing operations (MRO rate) over the life of the respective refinancing operation. However, during the periods from 24 June 2020 to 23 June 2021 and from 24 June 2021 to 23 June 2022, the borrowing rate is 50 basis points below the average MRO rate over the respective period.

5. For banks that reach the lending performance threshold during the predefined reference periods the borrowing rates can be as low as 50 basis points below the average interest rate on the deposit facility (DFR) during the periods from 24 June 2020 to 23 June 2021 and from 24 June 2021 to 23 June 2022, and as low as the average interest rate on the deposit facility during the rest of the life of the respective TLTRO III transaction.[14]
6. Interest will be settled in arrears on the maturity of each TLTRO III operation or on early repayment.
7. The modifications of the TLTRO III transaction parameters related to the introduction of a lower borrowing rate during the special interest rate periods from 24 June 2020 to 23 June 2021 and from 24 June 2021 to 23 June 2022 were made on 30 April 2020 and on 10 December 2020[15] respectively.

Rationale for submission

a) Accounting for the transactions according to requirements of IFRS 9 or IAS 20.

8. As part of their monitoring and supervisory activities, ESMA and national enforcers have identified diversity as to whether IAS 20 requirements are applied to the TLTRO III transactions.
9. Generally, financial instruments are accounted for according to the requirements of IFRS 9. However, the benefit of a loan at a below-market rate of interest is accounted for in accordance with IAS 20 provided that the loan is received from a party qualified as "government, government agencies and similar bodies" as defined by the standard. More specifically, according to IAS 20, the benefit of the below-market rate of interest (measured as the difference between the initial carrying value of the loan determined in accordance with IFRS 9 and the proceeds received) shall be recognised in profit or loss on a systematic basis over the periods in which the entity recognises as expenses the related costs for which the grant is intended to compensate.

b) Use of discrete or "blended" effective interest rates to calculate the interest expense

10. As the borrowing rate for banks which do not achieve lending performance thresholds during the special interest rate periods is 50 basis points lower than the borrowing rate applicable for the remaining term of the loan, there are different views on how to calculate the applicable effective interest rate. In particular, it is questionable whether it is necessary to use discrete interest rates for the calculation of the interest expense on the loans in each individual accounting period or whether an average ("blended") effective interest rate should be applied for the entire term of the loan. Another view is that there is an accounting

[14] For details on the terms of the TLTRO III operations see information published on the ECB's website: https://www.ecb.europa.eu/mopo/implement/omo/tltro/html/index.en.html.

[15] The decision of the ECB's Governing Council to extend the period of favourable interest rates to June 2022 took effect on 3 February 2021, when the corresponding amendments to the TLTRO III conditions were published in the Official Journal of the European Union.

policy choice with regard to these two methods. This question arises regardless of whether IAS 20 is eligible.

c) **Accounting treatment of the changes in estimates of payments due to revised assessment of meeting the eligibility criteria upon application of IFRS 9**

11. There are different approaches to the accounting treatment of changes in estimates of payments due to a change in the assessment of whether the lending performance thresholds will be reached. The change in the assessment may also result from the ECB's modifications of the TLTRO III transaction parameters (see paragraph 7) with a retrospective effect on the interest rate applied. The issue in question is whether recalculation of the amortised cost of the financial liability in accordance with the paragraph B5.4.6 of IFRS 9 is required as result of those changes.

Current practice

a) **Accounting for the transactions according to requirements of IFRS 9 or IAS 20.**

View 1: TLTRO III transactions are loans at a below-market interest rate and include benefits which are treated as government grants according to IAS 20

12. Proponents of view 1 note that TLTRO III transactions allow banks to refinance at potentially very favourable conditions. In particular, depending on the time period and achievement of the lending performance thresholds the borrowing rate might be significantly under MRO rate. Moreover, during the special interest rate periods which were introduced later on in the context of the COVID-19 pandemic, the borrowing rate can even be as low as the average DFR minus 50 basis points. Bank refinancing at these interest rates is quite low compared to the current refinancing costs of many banks. Therefore, proponents of view 1 believe that TLTRO III transactions are loans at a below-market interest rate. In their view, the favourable rate is compensation for the banks' financing cost over the related period.

13. IFRS 9 provides for the basis of accounting for financial instruments, whether at market rate or at below-market interest rate. However, IAS 20 deals with the accounting for any benefit of a government loan at below-market rate of interest. Proponents of view 1 note that the TLTRO III are provided by the ECB, which is the central bank of the 19 European Union countries and, as such, not a government. However, paragraph 3 of IAS 20 defines government as governments, government agencies and similar bodies whether local, national or international. There is no specific guidance in IAS 20 on which institutions can be considered similar bodies. Since the ECB is a supra-national public institution, one of the institutions of the European Union, proponents of view 1 believe that the ECB shall be considered a similar body under this definition. Moreover, considering the explanations on the TLTRO III transactions and changes to its conditions by the ECB[16] ("preserve the very attractive funding conditions", "support banks' efforts to keep credit flowing to the real

[16] https://www.ecb.europa.eu/press/pr/date/2020/html/ecb.pr201210_1~e8e95af01c.en.html

economy in a time of high stress", "provides for further incentives for banks", "ensure that counterparties can flexibly benefit from the prolonged support"), proponents of view 1 consider that the benefit of a below-market rate of interest from ECB corresponds to a government grant, as defined in paragraph 3 of IAS 20 ("assistance by government in the form of transfers of resources to an entity in return for past of future compliance with certain conditions relating to the operating activities of the entity").

14. In result, under view 1, the TLTRO III transactions are loans at a below-market interest rate which benefits shall be treated as government grants according to IAS 20.
15. IAS 20 provides guidance on the recognition of government grants in profit or loss. According to paragraph 8, a government grant is recognised only when there is reasonable assurance that the conditions attached to it are met. Paragraph 10A explains the measurement of the benefit of the below-market rate of interest and paragraph 12 requires the recognition of that benefit in profit or loss on a systematic basis over the periods in which the entity recognises as expense the related costs that the grant is intended to compensate.
16. However, with regards to TLTRO III transactions, it is not clear which costs are intended to be compensated by the benefit of these transactions and in which period the corresponding expenses are recognised by the banks. According to one view, once the relevant conditions are met, the benefit will be spread over the remaining time of the transaction. Proponents of another view argue that the period is determined by timing of bank's lending to non-financial corporations and households, to which the TLTRO III interest rate is linked.
17. In addition, it is not clear whether the requirements of IAS 20 regarding the presentation of grants related to assets can be applied to the TLTRO III transactions. According to paragraph 24, two methods of presentation of grants are regarded as acceptable, recognising grant as deferred income or deducting grant when calculating the carrying amount of the asset. According to one view, the second method could be applied to the TLTRO III transactions by analogy. Proponents of this view consider it permissible to add the amount of the benefit of the TLRTO III loan when calculating the carrying amount of the TLTRO III liability. According to another view, this analogy is unacceptable.

View 2: TLTRO III transactions are accounted for as loans at a market interest rate according to IFRS 9

18. The fair value of the loan is determined in accordance with IFRS 13 *Fair Value Measurement* as an "exit price". A fair value measurement of a liability assumes thereby that the liability is transferred to a market participant at the measurement date. The relevant market is the principal market or, in absence of a principal market, the most advantageous market which the borrower has access to. Even when there is no observable market to provide pricing information about the transfer of a liability at the measurement date, a fair value measurement shall assume that a transaction takes place at that date using the assumptions that market participants would use when pricing the liability. Since there is no secondary market for the TLTRO III loans, the borrowers need to develop those

assumptions considering factors specific to the liability, the relevant market and the market participants as required by paragraph 23 of IFRS 13.

19. Proponents of view 2 argue that, when developing the measurement assumptions, it should be taken into account that the TLTRO III transactions, where the borrowing rate is linked to the lending behaviour of banks, have unique conditions. Different interest rates may apply to banks participating in TLTRO III transactions, and even for a given bank, different interest rates will apply over the life of the loan. These conditions make them hardly comparable to other bank refinancing instruments, so that there are no suitable benchmarks for TLTRO III loans. Taking into account these observations, proponents of view 2 consider that it is reasonable to assume that TLTRO III transactions are not at below-market interest rates but rather at market.

20. Moreover, proponents of view 2 argue that even if the TLTRO III transactions were at a below-market interest rate, they still would not meet the definition of government grants under IAS 20. First of all, the definition of government or similar bodies is not consistent with the status of central banks given their independence. Moreover, the ECB's very specific tasks and responsibilities, which focus on defining and implementing the monetary policy in the Euro area, make this institution substantially different from governments or governmental agencies which typically provide economic benefits to businesses as part of their fiscally oriented measures. The character of the ECB's targeted longer-term refinancing operations, which declared objective is to support the accommodative stance of monetary policy, confirms this view.

21. Apart from that, proponents of view 2 point out that the purpose of the TLTRO-operations is to free up resources in the banking system for non-financial corporations and households, so that the main beneficiaries of the TLTRO III-loans are not the specific banks but rather those entities to which banks might now lend, or even the banking system.

22. Furthermore, proponents of this view note that the accounting treatment of a grant according to IAS 20 assumes that there is an expense which the grant compensates for. It is not clear how this would apply to a lending facility from a central bank to a financial institute which does not bind banks to any specific limitations on the interest rate applied to their customers.

23. For loans at below-market interest rate which do not meet the definition of a government grant in IAS 20, the difference between the transaction price and the lower fair value shall be treated according to paragraph B.5.1.2A(b) of IFRS 9. Assuming that unobservable inputs will be used in calculating the fair value of loans, this would result in recognition of that difference in profit or loss over the remaining life of the loan.

b) Use of discrete or "blended" effective interest rates to calculate the interest expense (regardless of whether IAS 20 is eligible)

View 1: Discrete interest rates shall be used

24. According to paragraphs 5.3.1 and 4.2.1 of IFRS 9, the TLTRO III loans are subsequently measured at amortised cost.[17] Interest expense on these loans shall be calculated by using the effective interest method, applying the effective interest rate (EIR) (paragraph 5.4.1 and Appendix A of IFRS 9). As the interest paid on the loans is linked to the DFR and/or MRO rate, the interest payments will vary with changes in those rates. However, even with an unchanged MRO rate, banks which do not achieve lending performance thresholds will apply different borrowing rates in different time periods to calculate the interest payments on the loans. The borrowing rate applied by those banks during the special interest rate periods is 50 basis points below the borrowing rate applied for the rest of the loan term.[18] Proponents of view 1 note that the borrowing rate applicable during the special interest rate periods was reduced by the ECB after the launch of the first TLTRO transactions in light of disruptions and temporary funding shortages associated with the COVID-19 pandemic. Therefore, according to view 1, it is reasonable to apply a lower EIR for the calculation of the interest expense on the loans during the period when banks' lending behaviour was affected by the COVID-19, i.e. during the special interest rate periods.

View 2: A "blended" interest rate shall be used

25. Proponents of view 2 believe that a constant "blended" interest rate should be used over the entire life of the loan to calculate the interest expense on the loans for the TLTRO III refinancing operations launched after the loan terms were amended to introduce a lower borrowing rate during the special interest rate period (subject to the changes in the MRO rate[19] and potential EIR adjustments related to the achievement of the lending performance thresholds). In their argumentation, proponents of view 2 refer to Example B.27 in the Guidance on Implementing IFRS 9, which explains the calculation of the EIR for instruments with a predetermined rate of interest that increases or decreases progressively.

View 3: The use of a discrete or "blended" interest rate is an accounting policy choice

26. Proponents of view 3 point out that in contrast to the loans in Example B.27 the rate of interest of the TLTRO III is not predetermined. They consider TLTRO III instruments to be variable rate loans, as their interest rate is linked to the DFR and/or MRO rate and to the lending patterns of the participating banks. Proponents of view 3 acknowledge that entities normally account for periodic floating-rate payments on an accrual basis in the period they

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[17] The fact that the interest rate is linked to the bank's lending activity does not imply the existence of an embedded derivate as defined in paragraph 4.3.1 of IFRS 9 because the non-financial variable is specific to the party to the contract.

[18] For example, the borrowing rate applied during the special interest rate period is -1,0% if the borrowing rate applied for the rest of the loan term is -0,5%.

[19] Current MOR rate of 0 % was set by the ECB on 16 March 2016.

are earned. However, they believe that for reasons of practicability a constant "blended" interest rate may also be used as an accounting policy choice.

c) Accounting treatment of the changes in estimates of payments due to revised assessment of meeting the eligibility criteria upon application of IFRS 9

View 1: Immediate recognition of amortised cost adjustment in profit or loss

27. Proponents of view 1 believe that any changes in the estimates of payments resulting from the revised assessment of reaching the lending performance thresholds should be accounted for according to paragraph B5.4.6 of IFRS 9 as this paragraph is applied when an entity revises its estimates of payments or receipts (excluding modifications in accordance with paragraph 5.4.3 and changes in estimates of expected credit losses). Under this view, the bank shall recalculate the amortised cost of the financial liability, discounting the re-estimated future cash flows with the original EIR, and recognise the adjustment to amortised cost in profit or loss. It is, however, not clear how the changes in cash flows that relate to the period before the change in the assessment of reaching the thresholds should be treated when calculating the new amortised cost under this view. To answer this question, it might be necessary to distinguish between the changes resulting from the bank's lending behaviour and those due to modifications of TLTRO III conditions by the ECB.

View 2: Adjustment of the EIR due to the changes in estimates of payments

28. Proponents of view 2 note that the TLTRO III loans are floating-rate financial liabilities because the interest payed on the loans is linked to the DFR and/or MOR rate. In accordance with the specific requirements for floating-rate instruments under paragraph B5.4.5 of IFRS 9, no catch-up adjustment to profit or loss is recognised when the re-estimation of cash flows reflects movements in the market interest rates. Proponents of view 2 consider the application of the requirements of paragraph B5.4.5 to the TLTRO III loans to be appropriate. However, since the changes in the estimates might result bank's behaviour and from the modifications of loans conditions by the ECB, it is questionable, whether the changes in the estimates of payments can be considered the result of changes of market interest rates.

Request

29. ESMA seeks clarification on

- How to assess whether the TLTRO III transactions involve loans at a below-market interest rate and, if so, whether the advantage of the below-market rate of interest needs to be accounted for according to the requirements of IFRS 9 or IAS 20 (see details under (a) in section 3 of this Appendix);
- how to assess in which period the benefit of the TLTRO III transactions needs to be recognised, if the advantage of the below-market interest rate needs to be accounted for according to IAS 20 (see details under (a) in section 3 of this Appendix);

- whether it is acceptable, in terms of presentation, to add the amount of the benefit of the TLRTO III loan when calculating the carrying amount of the TLTRO III liability (see details under (a) in section 3 of this Appendix);
- how to calculate the applicable effective interest rate (see details under (b) in section 3);
- whether the changes in estimates of payments due to revised assessment of meeting the eligibility criteria (i.e. achievement of predefined lending performance thresholds) should be accounted for in accordance with paragraph B5.4.6 of IFRS 9 requiring recalculation of the amortised cost of the financial liability or not (see details under (c) in section 3); and
- how to account for changes in cash flows related to the prior period resulting from the bank's lending behaviour or from changes in TLTRO III conditions by the ECB (see details under (c) in section 3).

30. ESMA is of the view that the lack of clarity of the wording of IFRS 9 and IAS 20 leads to divergent practices of the European banks. Given the overall volume of the TLTRO III operations, ESMA considers that this matter is relevant across the EU with a material effect on the financial statements of the affected banks.[20]

31. Consequently, ESMA invites the IFRS IC to clarify the applicable requirements.

[20] Please refer to ESMA Public Statement on the accounting for TLTRO III.