IFRS® Accounting

Staff paper

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IASB® meeting

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Project	**Gain or loss on derecognition (IFRS 7)**
Topic	**Potential annual improvement**
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Introduction

1. We have been informed about a potential lack of clarity in paragraph B38 of IFRS 7 *Financial Instruments: Disclosures* that arises because it refers to another paragraph in IFRS 7 that no longer exists.

2. The IFRS Interpretations Committee (Committee) discussed this matter at its meeting in November 2022—see Agenda Paper 3E for that meeting.

3. The objective of this paper is:

    (a) to provide the International Accounting Standards Board (IASB) with background on the matter and staff analysis, including consideration of the Committee's discussion; and

    (b) to ask the IASB whether it agrees with our recommendation to include a proposed amendment to paragraph B38 of IFRS 7 in its next *Annual Improvements to IFRS Accounting Standards Cycle* (annual improvements).

Structure of this paper

4. This paper includes:

   (a) Background information;

   (b) Staff analysis, including consideration of the Committee's discussion and transition requirements;

   (c) Staff recommendations and question for the IASB; and

   (d) Appendix A—recommended proposed amendment to paragraph B38 of IFRS 7.

Summary of staff recommendations

5. We recommend that the IASB:

   (a) propose an amendment to paragraph B38 of IFRS 7 to replace the reference to paragraph 27A of IFRS 7 with a reference to paragraphs 72–73 of IFRS 13 *Fair Value Measurement*;

   (b) develop no specific transition requirements for this proposed amendment; and

   (c) include this proposed amendment in its next annual improvements cycle.

Background information

6. Paragraph B38 of IFRS 7 includes a reference to paragraph 27A of IFRS 7 which no longer exists; the paragraph states [emphasis added]:

> Paragraph 42G(a) requires an entity to disclose the gain or loss on derecognition relating to financial assets in which the entity has continuing involvement. The entity shall disclose if a gain or loss on derecognition arose because the fair values of the components of the previously recognised asset (ie the interest in the asset derecognised and the interest retained by the entity) were different from the fair value of the previously recognised asset as

> a whole. In that situation, the entity shall disclose whether the fair value measurements included significant inputs that were not based on observable market data, as described in **paragraph 27A**.

7. Prior to their deletion, paragraphs 27–27B of IFRS 7 set out disclosure requirements relating to fair value. In particular, paragraph 27A of IFRS 7 described a fair value hierarchy and how an entity would classify fair value measurements within each level of the hierarchy:

> To make the disclosures required by paragraph 27B an entity shall classify fair value measurements using a fair value hierarchy that reflects the significance of the inputs used in making the measurements. The fair value hierarchy shall have the following levels:
>
> (a) quoted prices (unadjusted) in active markets for identical assets or liabilities (Level 1);
>
> (b) inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (ie as prices) or indirectly (ie derived from prices) (Level 2); and
>
> (c) inputs for the asset or liability that are not based on observable market data (unobservable inputs) (Level 3).
>
> The level in the fair value hierarchy within which the fair value measurement is categorised in its entirety shall be determined on the basis of the lowest level input that is significant to the fair value measurement in its entirety. For this purpose, the significance of an input is assessed against the fair value measurement in its entirety. If a fair value measurement uses observable inputs that require significant adjustment based on unobservable inputs, that measurement is a Level 3 measurement. Assessing the significance of a particular input to the fair value measurement in

> its entirety requires judgement, considering factors specific to the asset or liability.

8. In May 2011, the IASB issued IFRS 13. As part of that issuance, the IASB made consequential amendments[1] to several IFRS Accounting Standards, including deleting paragraphs 27–27B of IFRS 7. However, paragraph B38 of IFRS 7 was not updated to reflect this deletion. Consequently, it now includes a reference to a paragraph that no longer exists.

Question raised

9. The question raised is whether paragraph B38 of IFRS 7 should be updated to remove or replace the reference to paragraph 27A of IFRS 7, which no longer exists.

Staff analysis

10. We agree there is a need to update paragraph B38 of IFRS 7. We think the current reference to paragraph 27A results from an oversight when IFRS 13 was issued; the reference to paragraph 27A would normally have been updated through a consequential amendment.

11. The requirements in paragraphs 72–75 of IFRS 13 effectively replaced those previously set out in paragraphs 27–27B of IFRS 7. In particular, the requirements in paragraphs 72–73 of IFRS 13 replaced those previously set out in paragraph 27A of IFRS 7.

12. Paragraph 72 of IFRS 13 states:

> To increase consistency and comparability in fair value measurements and related disclosures, this IFRS establishes a fair value hierarchy that categorises into three levels (see

[1] Paragraph 6.31 of the IFRS Foundation's *Due Process Handbook* states that '[w]hen a new IFRS Standard, or amendment to a Standard, is issued, it is also accompanied by amendments to other Standards that are a consequence of the new requirements—these are called 'consequential amendments'.'

> paragraphs 76–90) the inputs to valuation techniques used to measure fair value. The fair value hierarchy gives the highest priority to quoted prices (unadjusted) in active markets for identical assets or liabilities (Level 1 inputs) and the lowest priority to unobservable inputs (*Level 3 inputs*).

13. Paragraph 73 of IFRS 13 states:

> In some cases, the inputs used to measure the fair value of an asset or a liability might be categorised within different levels of the fair value hierarchy. In those cases, the fair value measurement is categorised in its entirety in the same level of the fair value hierarchy as the lowest level input that is significant to the entire measurement. Assessing the significance of a particular input to the entire measurement requires judgement, taking into account factors specific to the asset or liability. Adjustments to arrive at measurements based on fair value, such as costs to sell when measuring fair value less costs to sell, shall not be taken into account when determining the level of the fair value hierarchy within which a fair value measurement is categorised.

14. In our view, this matter can be efficiently resolved by replacing the reference in paragraph B38 of IFRS 7 to paragraph 27A with a reference to paragraphs 72–73 of IFRS 13.

Does this matter meet the annual improvements criteria?

15. Paragraphs 6.10–6.13 of the *Due Process Handbook* include the criteria for annual improvements. To meet these criteria, the proposed solution would need to be limited to:

    (a) clarifying the wording in an Accounting Standard, which involves either replacing unclear wording in existing Accounting Standards or providing requirements where an absence of requirements is causing concern; or

(b) correcting relatively minor unintended consequences, oversights or conflicts between existing requirements.

16. In our view, our proposed solution to amend paragraph B38 of IFRS 7 (see Appendix A to this agenda paper) meets these criteria. As we explained earlier, replacing the reference to paragraph 27A of IFRS 7 with a reference to paragraphs 72–73 of IFRS 13 would efficiently resolve the matter. Such an amendment would maintain consistency with the principles and requirements in IFRS 7 and IFRS 13 and would not propose a new (or change an existing) principle or requirement.

The Committee's discussion

17. The Committee discussed this potential annual improvement at its November 2022 meeting. All Committee members agreed, or did not disagree, with our analysis and preliminary views. Committee members provided no further comments.

Transition requirements

18. Our proposed amendment to paragraph B38 of IFRS would improve clarity in that paragraph, without changing or adding new requirements. We do not expect any change in practice arising from this proposed amendment. Therefore, in our view, there is no need to develop any specific transition requirements.

19. In the absence of any specific transition requirements, an entity would apply the proposed amendment retrospectively in accordance with paragraph 19(b) of IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*.

Staff recommendations and question for the IASB

20. Based on our analysis in paragraphs 6–17 of this agenda paper, we recommend the IASB, as part of its next annual improvements cycle, amend paragraph B38 of IFRS 7

to replace the reference to paragraph 27A of IFRS 7 with a reference to paragraphs 72–73 of IFRS 13 (see Appendix A to this agenda paper).

21. Based on our analysis in paragraphs 18–19 of this agenda paper, we recommend the IASB develop no specific transition requirements.

Question for the IASB
Does the IASB agree with our recommendations: a. to propose an amendment to paragraph B38 of IFRS 7 to replace the reference to paragraph 27A of IFRS 7 with a reference to paragraphs 72–73 of IFRS 13; b. to develop no specific transition requirements for this proposed amendment; and c. to include this proposed amendment in its next annual improvements cycle?

Appendix A—recommended proposed amendment to paragraph B38 of IFRS 7

A1. Our proposed amendment to paragraph B38 of IFRS 7 would replace the reference to paragraph 27A of IFRS 7 with a reference to paragraphs 72–73 of IFRS 13. New text is underlined and deleted text is struck through.

> B38 Paragraph 42G(a) requires an entity to disclose the gain or loss on derecognition relating to financial assets in which the entity has continuing involvement. The entity shall disclose if a gain or loss on derecognition arose because the fair values of the components of the previously recognised asset (ie the interest in the asset derecognised and the interest retained by the entity) were different from the fair value of the previously recognised asset as a whole. In that situation, the entity shall disclose whether the fair value measurements included significant inputs that were not based on observable market data, as described in ~~paragraph 27A~~ <u>paragraphs 72–73 of IFRS 13</u>.