IFRS® Accounting

Staff paper

Agenda reference: 3

Emerging Economies Group meeting

Date	**10 May 2023**
Project	**Amendments to the Classification and Measurement of Financial Instruments**
Topic	**Exposure Draft *Amendments to the Classification and Measurement of Financial Instruments***
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Purpose of this session

- Provide EEG members with an overview of the Exposure Draft (ED) *Amendments to the Classification and Measurement of Financial Instruments*
- Seek views from EEG members on the proposals in the ED

Questions for EEG members

- See questions on slide 5

Information for EEG members:

- Slides 7–14 provide an overview of the ED

Contents

Questions for EEG members

Questions for EEG members

- What are your preliminary views on the proposals in the ED?
- Are there any areas in the proposals where you think further application guidance/explanations would be needed?

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Overview of proposals

Overview

The IASB's objectives

To respond to feedback on the PIR of the classification and measurement requirements in IFRS 9 *Financial Instruments* by improving:

- the understandability of some of these requirements; and
- the usefulness of related information disclosed by an entity applying the requirements in IFRS 7 *Financial Instruments: Disclosures*

What is the IASB proposing?

The IASB proposes amendments relating to:

- derecognition of financial liabilities settled through electronic transfer;
- solely payments of principal and interest on the principal amount outstanding (SPPI) assessment in classifying financial assets; and
- disclosure of information about some financial instruments

Derecognition of financial liabilities

When can an entity derecognise a financial liability?

- IFRS 9 usually requires ***settlement date*** accounting for financial assets and financial liabilities
- An entity is permitted to deem a financial liability that is settled using an electronic payment system to be discharged ***before the settlement date*** if, and only, if the entity has initiated the payment instruction and there is:
  - no ability to withdraw, stop or cancel the payment instruction;
  - no practical ability to access the cash; and
  - insignificant settlement risk

Financial assets with ESG-linked features

When can an entity measure a financial asset with ESG-linked features at amortised cost?

- An entity applies guidance on assessing whether contractual cash flows are ***SPPI***, including considering:
  - elements of interest in a basic lending arrangement
  - contractual terms that change the amount or timing of contractual cash flows
- No exemption from SPPI requirements for ESG-linked features

Basic lending arrangements

When are contractual cash flows inconsistent with a basic lending arrangement?

- compensation for risks or market factors not typically considered basic lending risks or costs, even if such terms are common in the market
- cash flows change in a way that is not aligned with the direction and magnitude of changes in lending risks or costs.

*The assessment of interest focuses on **what** an entity is being compensated for, rather than **how much** compensation an entity receives*

Example

The interest rate on a loan is periodically adjusted when a market-determined carbon price index reaches a contractually defined threshold

The contractual cash flows are not SPPI
The contractual cash flows change in response to a market factor which is not a basic lending risk or cost

Contingent events that change contractual cash flows

When are changes in contractual cash flows consistent with a basic lending arrangement?

- contractual cash flows are SPPI in all circumstances, irrespective of the probability of the contingent event occurring
- the occurrence of the contingent event is specific to the debtor
- the resulting contractual cash flows represent neither an investment in the debtor nor an exposure to the performance of specified assets

Example

The interest rate on a loan is periodically adjusted by a specified number of basis points if the debtor achieves a contractually specified reduction in greenhouse gas emissions

The cash flows are SPPI
The occurrence of the contingent event is specific to the debtor and the cash flows are SPPI in all circumstances

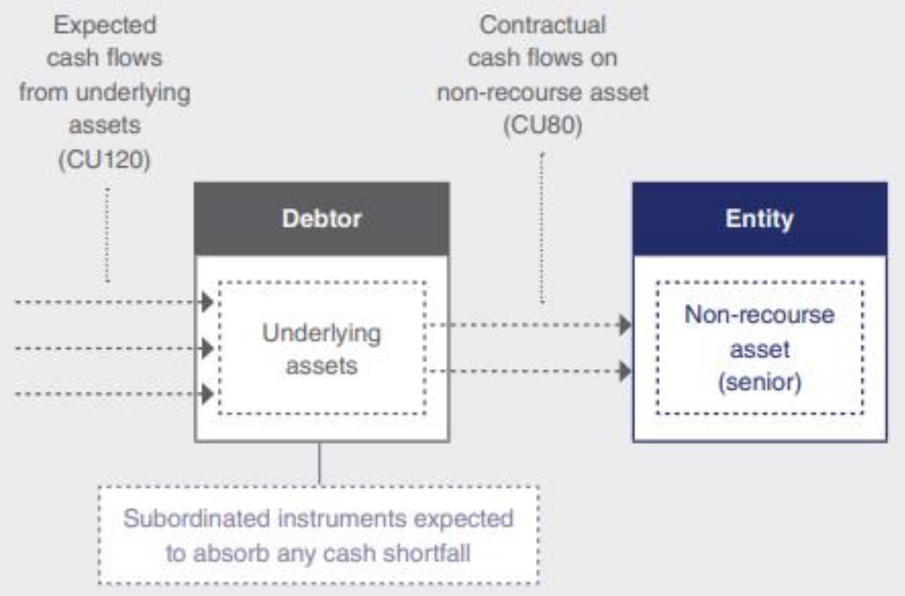
Non-recourse features

When does a financial asset have non-recourse features?

- the right to receive cash flows is limited to the cash flows from specified assets both over the life of the financial asset and in default

What should the entity consider in 'looking through to' the underlying assets?

- the legal and capital structure of the debtor, including extent to which cash flows from underlying assets are expected to exceed the contractual cash flows on the financial asset being classified

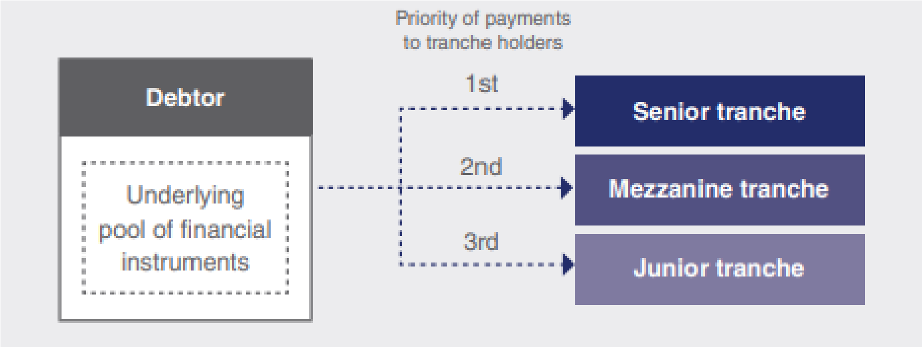


Example of structure in which (a) cash flows from the underlying assets are expected to exceed those of the financial asset; and (b) any cash shortfall is expected to be absorbed by subordinated instruments issued by the debtor.

Contractually linked instruments (CLIs)

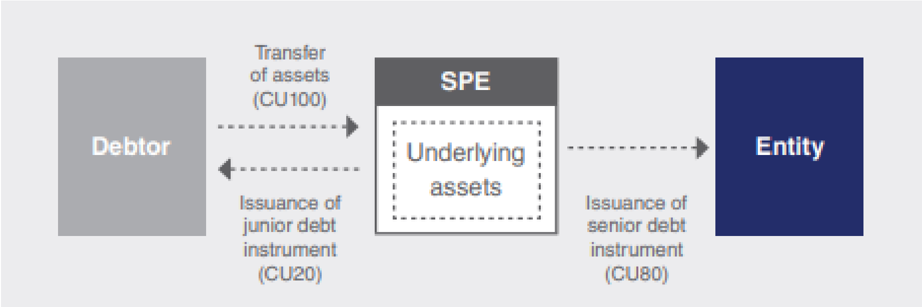
What is in scope of the CLI requirements?

- multiple CLIs creating concentrations of credit risk that result in the disproportionate allocation of losses



What is not in scope of the CLI requirements?

- Secured lending arrangements in which the sponsor/debtor holds the junior instrument in the special purpose entity(SPE)



The underlying pool in a CLI transaction may include financial instruments that are not in scope of the classification criteria of IFRS 9, if their cash flows are SPPI equivalent

Disclosures

Equity investments with gains and losses presented in OCI

- the FV change during the reporting period, showing separately the FV change related to investments derecognised during the period
- the aggregate FV of investments in equity instruments at the end of the reporting period (rather than for each investment)

Contractual terms that could change the timing or amount of contractual cash flows based on a contingent event

- a qualitative description of the nature of the contingent event
- quantitative information about the range of changes to contractual cash flows that could result
- the gross carrying amount of financial assets and the amortised cost of financial liabilities subject to those terms

Next step

Next step

- The IASB will consider the comments it receives on the Exposure Draft and will decide whether to proceed with the proposed amendments
- The comment letter deadline is ***19 July 2023***
- The ED and supporting material is available on the project website

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