
IASB[®] meeting

Date	November 2023
Project	Amendments to the Classification and Measurement of Financial Instruments
Topic	Feedback analysis – Derecognition of financial liabilities through electronic transfer
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Purpose of this paper

1. Question 1 of the Exposure Draft *Amendments to the Classification and Measurement of Financial Instruments* (ED) asked for feedback on the proposed requirements regarding the derecognition of a financial liability through electronic transfer.
2. This paper analyses the feedback on these proposed requirements and asks whether the IASB agree with the staff recommendations for responding to this feedback.
3. This paper is structured as follows:
 - (a) [summary of staff recommendations and questions to the IASB](#);
 - (b) [proposals in the ED](#);
 - (c) [feedback on proposals](#); and
 - (d) [staff analysis and recommendations](#).

Summary of staff recommendations and question to the IASB

4. The staff recommend to finalise the proposed amendments in the ED, subject to:

- (a) deleting the reference to settlement date accounting and instead replacing this with a reference to settlement date in a revised version of paragraph B3.1.2A of the ED along with an explanation that settlement date refers to the date on which the right to receive or obligation to pay cash (or another financial asset) is established or extinguished, see paragraph 48; and
- (b) aligning the requirement in paragraph B3.3.8(a) with that of paragraph B3.3.8(b) of the ED so that both refer to ‘practical ability’, see paragraph 75.

Question for the IASB

Does the IASB agree with our recommendations in paragraph 4 of this paper?

Proposals in the ED

5. The ED proposed in paragraph 3.1.2A to clarify that an entity is required to apply settlement date accounting when derecognising a financial asset or a financial liability. In addition, when meeting the proposed requirements in paragraphs 3.3.8–3.3.10 of the ED, an entity is permitted to deem a financial liability that is settled using an electronic payment system to be discharged before the settlement date.

Feedback on proposals

Date of initial recognition or derecognition

6. Most respondents generally agreed with the proposal in paragraph B3.1.2A of the ED to clarify the settlement date principle when recognising or derecognising financial assets and financial liabilities.
7. However, many respondents said that further clarifications are needed to the proposed wording of the requirements to limit the risk of unintended consequences.

Respondents were concerned that reference to the application of settlement date

accounting (as described in paragraph B3.1.6 of IFRS 9) when read in combination with the general principle in paragraph 3.1.1 of IFRS 9, may have unintended consequences that could lead to further diversity in practice developing. The main reasons given can be grouped into the following categories:

- (a) applying the proposed requirements to derivatives; and
- (b) the interaction between the requirements for settlement date accounting as described in paragraph B3.1.6 and section B32 of the Implementation Guidance to IFRS 9.

Applying the proposed requirements to derivatives

8. Many respondents said that it is unclear whether or how the proposed requirements would apply to derivatives. They were concerned that the new proposals are inconsistent with the general recognition principle in paragraph 3.1.1 and the related application guidance in paragraphs B3.1.1–B3.1.2 of IFRS 9.
9. In particular, these respondents cited paragraphs B3.1.2(c) and B3.1.2(d) as examples where the reference to the settlement date is often not relevant as there will be no delivery of cash or another financial asset at inception. Instead, in these examples, financial assets or liabilities are recognised on the commitment date which is in line with their contractual status.
10. Similar to the concerns about derivatives, a few respondents also noted the potential impact of paragraph B3.1.2A on their accounting treatment for short sale transactions.

Interaction between settlement date accounting and Implementation Guidance

11. Commenting on the wording of paragraph B3.1.2A, many respondents observed that settlement date accounting as described in paragraph B3.1.6 of IFRS 9 refers only to financial assets and not to financial liabilities. These respondents said that settlement date accounting in paragraph B3.1.6 is explained as applying to the recognition of an asset on the day it is received by the entity and the derecognition of an asset and

recognition of any gain or loss on disposal. This paragraph also explains the accounting of the asset to be received in case of a purchase of an asset in the intervening period between trade and settlement date.

12. However, in the absence of a reference to financial liabilities many respondents queried how to apply the requirements regarding settlement date accounting to the recognition and derecognition of financial liabilities. In particular, some respondents were concerned about potential unintended consequences of the proposed requirements when derecognising financial liabilities because, in their view, the requirements in paragraphs 3.3.1 and B3.3.1 of IFRS 9 are based on legal extinguishment rather than on settlement date accounting.
13. Some other respondents pointed out that section B32 of the Implementation Guidance to IFRS 9 states that there are no specific requirements on applying settlement date accounting to financial liabilities. In their opinion the proposed requirements therefore cannot reference to paragraph B3.1.6 of IFRS 9 which only describes settlement date accounting for financial assets. They therefore said that paragraph B3.1.2A of the ED should be removed as, in their opinion, it constitutes a new requirement rather than a clarification of existing requirements.

Derecognition of financial liabilities

14. Feedback on paragraphs B3.3.8–B3.3.10 of the ED which establish the criteria for derecognising a financial liability before the settlement date can be divided into comments regarding:
 - (a) the scope of the proposed requirements;
 - (b) the proposed criteria for derecognising a financial liability before the settlement date; and
 - (c) the operational effects on entities' information technology and analysis of electronic payment systems.

Scope of the proposed requirements

15. Regarding the scope of the proposed requirements some respondents focussed on the limitation of these requirements:
- (a) to electronic payments systems; and
 - (b) to financial liabilities.

Limited to electronic payment systems

16. The proposed requirements in paragraphs B3.3.8 and B3.3.9 of the ED only apply if a financial liability is settled with cash through electronic transfer using an electronic payment system. Some respondents suggested that the proposed requirements should also include other means of payment, such as cheques or similar transactions and should therefore not be limited to transfers using an electronic payment system.
17. In their view, not considering such means of payment would significantly change current accounting outcomes which are long-standing established industry practice. A few respondents stated that excluding cheques from the scope of the proposed requirements would implicitly create a new requirement whereby entities will need to confirm with a counterparty if cash for the settlement of a financial liability has been received before it could be derecognised. They therefore suggested that the proposed requirements should be applied to cheques as well.

Limited to financial liabilities

18. Some respondents said that similar requirements for the derecognition of financial assets are needed as this was the fact pattern originally submitted to the IFRS Interpretations Committee. These respondents said that not permitting the derecognition of a trade receivable before the settlement date will require a change in industry practice, particularly when considering payment methods such as cheques and credit card receivables. In addition, they are of the view that it would lead to inconsistencies in accounting for intercompany balances. This is because of the potential timing differences when derecognising trade receivables and trade payables

which are settled through electronic cash transfer applying the proposed requirements. For example, a situation could arise whereby a subsidiary applies the proposed exception in paragraph B3.3.8 of IFRS 9 and derecognises its intercompany payable to a fellow subsidiary before settlement date. However, the other subsidiary derecognises the corresponding intercompany receivable on settlement date once the cash payment is received. According to these respondents this would lead to operational complexities when consolidating group entities.

19. Furthermore, a few respondents said that the IASB has not provided a sufficiently convincing case in its Basis of Conclusions on the ED for not extending the proposed requirements for financial liabilities to some financial assets. In their opinion this would result in changes to current practice of accounting for so-called ‘cash in transit’ items because it is not clear whether these would meet the definition of a cash equivalent (feedback suggests that current practice is to reclassify trade receivables to cash in transit receivable once they’ve been notified that the counterparty has made a payment instruction), another financial asset, or something else.
20. They further noted it is equally unclear where these balances should be presented in the cash flow statement. In their view, cash in transit is often much more liquid and less risky than some other instruments which usually qualify as cash equivalents. Therefore, if entities were obliged to present these very highly liquid assets outside the cash and cash equivalents category, the resulting information would not be useful or relevant. Consequently, these respondents recommended that the IASB should either delay the amendment to consider these issues or should add them to another broader project that considers issues in relation to IAS 7 *Statement of Cash Flows* (for example the Statement of Cash Flows and Related Matters project).

Proposed criteria for derecognising a financial liability before the settlement date.

21. While most respondents agreed with the proposed criteria in paragraph B3.3.8 of the ED, some respondents stated that the proposed criteria set too high a threshold to overcome in practice, resulting in the proposals being of little practical benefit.

No ability to withdraw, stop or cancel the payment instruction (paragraph B3.3.8(a))

22. Many respondents commented that the proposed requirement for an entity to have no ability to withdraw, stop or cancel a payment instruction, would in effect mean that nearly all electronic payment systems would not satisfy the requirement because of the protective rights inherent in an electronic payment system such as an ability to recall the payment in the case of fraud or technical error. In their view, ‘ability’ appears to be an absolute requirement (with possible legal implications) and determining the point where there is no absolute ability to cancel a payment instruction is operationally complex, particularly for cross-border transactions and may vary by instructing bank or electronic payment system(s) used.
23. Respondents therefore suggested to either remove that requirement or to align it to the requirement in paragraph B3.3.8(b) to refer to practical ability, for example by requiring an entity to have no practical ability to withdraw, stop or cancel the payment instruction.

No practical ability to access the cash used for settlement (paragraph B3.3.8(b))

24. A few respondents commented that it is not clear whether and how the exception to derecognising a financial liability would apply if a payment instruction would be settled by way of an overdraft or other similar facility with a negative balance and if this refers to the broader definition of cash in paragraph 8 of IAS 7. They noted that paragraph 8 of IAS 7 acknowledges that ‘in some countries, bank overdrafts which are repayable on demand form an integral part of an entity’s cash management’ and ‘are included as a component of cash and cash equivalents’. They are therefore of the view that such facilities should also be in scope of the proposed requirements.

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25. A few respondents were concerned that the proposed clarification in paragraph B3.1.2A of the ED and the requirements in paragraph B3.3.8 of the ED could result in situations where users of financial statements could be misled about the amount of cash at the reporting date if an entity initiates many payment instructions before the reporting date but do not apply the requirements in proposed paragraph B3.3.8. In such a case, the entity would show a large cash balance at the reporting date that could be depleted shortly after the reporting date when the payment instructions are settled. These respondents noted that paragraph 48 of IAS 7 requires an entity to disclose significant cash balance held by the entity that are not available for use by the group and questioned whether this requirement would apply to such a situation.
26. A few respondents also said payment systems typically allow a customer to prepare a transaction in advance and normally there is not a requirement that funds are available before the payment is actually initiated. They were unclear whether the proposed requirement in paragraph B3.3.8(b) of the ED implicitly would not permit such an approach as it refers to the entity's practical ability to access the cash.

Settlement risk

27. While most respondents generally agreed that the settlement risk with the electronic payment system should be insignificant, some respondents asked for more guidance on what is meant by 'settlement risk', for example by defining settlement risk.
28. These respondents also said that the terms 'short' and 'standard administrative process' in the proposed paragraph B3.3.9 of the ED require further explanation on how to interpret these terms in the context of the electronic payment systems used. They are of the view that, due to the numerous electronic payments using different processes and timescales, these terms might be applied inconsistently, for example if a payment is created for a future date.
29. A few other respondents were of the view that the requirement for settlement risk to be insignificant might not be needed. This is because the other requirements related to the entity not having the practical ability to access the cash or to withdraw the

payment instruction already require the completion of the payment instruction not to be subject to the entity's ability to deliver the cash on the settlement date. In contrast, a few other respondents specifically said that this criterion is needed to ensure that the proposed exception is applied only in the appropriate circumstances and not, for example, in situations where payment instructions are scheduled for a future date and subject to the entity having sufficient funds on that future date to honour the payment instruction.

Optional adoption on a system-by-system basis

30. A few respondents suggested that, instead of allowing the proposed requirements to be applied on a system-by-system basis, they should be applied on an 'all-or-nothing' basis to all electronic payment systems that meet the criteria to avoid the potential for abuse. Specifically, they were concerned that such a practice may result in similar transactions being treated differently by an entity that uses similar (but different) payment systems.
31. On the other hand, a few respondents said that one electronic payment system may offer different types of payment transactions where the timing and the terms and conditions between payment initiation and settlement date could vary. As a result, the application of the proposed requirements could also vary by type of payment transaction within the same electronic payment system which in their opinion would not be appropriate and not result in useful financial information.
32. Lastly, a few respondents stated that it is not clear whether an assessment is required to be performed at payment initiation only or continuously to determine when the liability could be derecognised.

Operational effects on information technology

33. A few respondents commented that unintended consequences could also arise when considering the proposals in paragraphs B3.1.2A and B3.3.8 of the ED. These respondents said that significant time may be required to establish an understanding of

the systems and payments that may fall under the scope of the amendments and how this will impact the organisation, which may include legal review of the relevant electronic payment systems. For example, an analysis may incorporate numerous payment systems across multiple jurisdictions including both domestic and cross-border payments. The application of paragraph B3.3.8 may also create inconsistencies in how electronic payments are treated as opposed to non-electronic payments.

34. As a consequence, they therefore suggested separating finalisation of the proposed amendments in relation to electronic cash transfers from the rest of the ED to allow time for the necessary work to be completed.

Other observations

35. Other comments made by respondents included:
- (a) specifying that when a financial liability is derecognised before the settlement date, the corresponding cash amount is also derecognised and that this also extends to the presentation of cash in accordance with IAS 7 (see also paragraph 19); and
 - (b) defining ‘electronic payment system’, including whether the assessment is based on the contractual rights and obligations only or also considers any statutory rights and obligations that might apply.

Staff analysis and recommendations

Date of initial recognition or derecognition

General requirements for recognising or derecognising a financial asset or a financial liability

36. Paragraph 3.1.1 of IFRS 9 sets out the general initial recognition requirements for financial assets and financial liabilities, stating:

An entity shall recognise a financial asset or a financial liability in its statement of financial position when, and only when, the entity becomes party to the contractual provisions of the instrument (see paragraphs B3.1.1 and B3.1.2) ...

37. Paragraph 3.2.3 of IFRS 9 sets out the general principle for derecognition of financial assets, stating:

An entity shall derecognise a financial asset when, and only when:

(a) the contractual rights to the cash flows from the financial asset expire, or

(b) it transfers the financial asset as set out in paragraphs 3.2.4 and 3.2.5 and the transfer qualifies for derecognition in accordance with paragraph 3.2.6.

(See paragraph 3.1.2 for regular way sales of financial assets.)

38. Paragraph 3.3.1 sets out the general principle for derecognition of financial liabilities, stating:

An entity shall remove a financial liability (or a part of a financial liability) from its statement of financial position when, and only when, it is extinguished—ie when the obligation specified in the contract is discharged or cancelled or expires.

39. Paragraph 3.1.2 of IFRS 9 provides an exception from the general requirements for transactions that meet the definition of a regular way purchase or sale of a financial asset. That paragraph states:

A regular way purchase or sale of financial assets shall be recognised and derecognised, as applicable, using trade date accounting or settlement date accounting (see paragraphs B3.1.3–B3.1.6).

Application of the general requirements

40. As stated in paragraph 6 of this paper, most respondents agreed with the proposed clarification with regards to the settlement date principle, ie the date on which a financial asset and financial liability is recognised or derecognised. However, respondents did not necessarily agree with applying settlement date accounting as referred to in paragraph B3.1.6 of IFRS 9.
41. The staff acknowledged stakeholder feedback that references to settlement date accounting might appear to be inconsistent with other requirements in IFRS 9 and therefore risks having unintended consequences. We think these concerns could be resolved by refining the wording of the proposed amendments, rather than requiring a fundamental change from what was proposed in the ED.
42. Although paragraph 3.1.1 of IFRS 9 states that a financial asset or financial liability is recognised when an entity becomes a party to the contractual provisions, this does not mean the mere signing of a contract is sufficient to recognise or derecognise a financial asset or a financial liability. As is explained in paragraph B3.1.2 and section B32 of the Implementation Guidance to IFRS 9, an entity becomes a party to the contract when at least one of the parties has performed under the contract and as a result a legal right to receive or obligation to pay has been established (see for example subparagraphs B3.1.2(a) and (b) of IFRS 9).
43. In our view, this is consistent with what is described in paragraph B3.1.6 of IFRS 9 in the context of regular way transactions as the settlement date, ie one of the parties to the contract has performed by delivering the financial asset and therefore the other party has a right to receive or an obligation to pay cash.
44. Similarly, paragraphs 3.2.3 and 3.3.1 of IFRS 9 require a financial asset or financial liability to be derecognised when the right to receive cash expires or the obligation to pay cash is extinguished. For financial liabilities, this is illustrated in paragraph B3.3.1(a) which states that a financial liability is extinguished when an entity

discharges the liability by paying the counterparty either in cash or another financial asset or by delivering goods and services.

45. Therefore, in this context, ‘settlement date’ refers to the date on which an entity’s right to receive or obligation to pay cash is established or extinguished. In other words, a financial asset is derecognised when the entity no longer has the right to receive cash (or another financial asset) either because it has received the cash (or another financial asset) and therefore the right has expired or the right to receive cash has been transferred. Equally, a financial liability is derecognised when the obligation is extinguished either because the entity has delivered the cash (or another financial asset) or the obligation has been cancelled.
46. With regards to derivatives, the right to receive and obligation to pay cash are typically established when the parties commit to the contract, ie the commitment date. This is illustrated in subparagraphs B3.1.2(c) and (d) of IFRS 9. Therefore, for derivatives the commitment date (also sometimes called trade date) and the settlement date is the same date. This is because both parties have fulfilled their obligations under the contract on the commitment date and no part of the contract remains executory.

Staff recommendation

47. We acknowledge that paragraph B3.1.6 and the reference to settlement date accounting only apply in the context of a purchase or sale of a financial asset in a regular way purchase. We also acknowledge that section B32 of the Implementation Guidance to IFRS 9 states that IFRS 9 does not include any specific requirements about trade date accounting and settlement date accounting in the case of transactions in financial instruments that are classified as financial liabilities. However, we note that this section refers back to the general recognition or derecognition requirements in IFRS 9 as described in paragraphs 36–39, which is what is referred to as the settlement date with reference to regular way transactions.

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48. To avoid any unintended consequences that could result from referring to settlement date accounting, we recommend replacing this with a reference to settlement date along with an explanation that it refers to the date on which the right to receive or obligation to pay cash (or another financial asset) is established or extinguished.

Derecognition of financial liabilities

49. The staff analysis is based on the comments received and considers:
- (a) the scope of the proposed requirements;
 - (b) the proposed criteria for derecognising a financial liability before the settlement date and
 - (c) operational considerations.

Scope of the proposed requirements

Limited to electronic payment systems

50. The staff acknowledge feedback about other means of payments such as cheques or similar transactions that do not rely on an electronic environment to execute the initiation and transfer of the payment. However, as noted in BC37 of the Basis for Conclusions on the ED, the question asked to the IFRS Interpretations Committee and the practical challenges that led to the proposed requirements, arose from the nature of the payment method being used, ie electronic cash transfers.
51. The staff note that the proposed requirements in paragraph B3.3.8 of the ED is an exception to the general requirements in IFRS 9 as discussed in paragraphs 36–46 of this paper. By nature, any exception needs to apply to only a narrow scope of transactions or instruments otherwise the principles in the Standard would be eroded. In addition, when developing the proposed requirements in the ED, the IASB considered and rejected an approach to make broader scope amendments to the derecognition requirements in IFRS 9 (as explained in paragraph BC12 of the Basis for Conclusions on the ED).

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52. The underlying rationale for the proposed criteria in paragraph B3.3.8 of the ED is that, after a payment instruction has been initiated and the entity has no [practical] ability to withdraw the instruction, the completion of the payment (ie delivering the cash) is subject only to a standardised administrative process and not to settlement risk.¹ Electronic payment systems establish a controlled environment for cash transfers so that the risk of the cash not being delivered to the creditor is minimal (or *de minimis*). This is because these electronic payment systems follow a standard administrative process to complete these transactions.
53. For other payment methods, such as cheques, completion of the payment remains subject to settlement risk that is more than insignificant until the cash is delivered (ie transferred from the payer's account). The staff therefore continue to be of the view that the only circumstances in which it would be appropriate for a financial liability to be derecognised before the settlement date are those proposed in paragraph B3.3.8 of the ED.

Limited to financial liabilities

54. The staff also acknowledge feedback that the scope of the proposed exception should be extended to the derecognition of financial assets (for example trade receivables) and the recognition of a 'cash-in-transit' financial asset once payment has been advised.
55. When developing the proposed requirements in paragraph B3.3.8 of the ED, the IASB considered whether a similar exception to the general derecognition criteria for financial assets could be developed. However, as explained in Agenda Paper [16B](#) for the November 2022 IASB meeting, this would not be appropriate. This is because for financial assets, there is no equivalent notion of having no [practical] ability to withdraw or cancel a payment instruction. Equally, the criteria cannot be based on requiring an entity to know when a counterparty has no [practical] ability to withdraw

¹ The term 'practical' is in square brackets as we suggest inserting it in paragraph 3.3.8(a) of the ED as part of our recommendation.

a payment instruction as the recognition of a financial asset is based on the entity's contractual right to receive cash (or another financial asset) and derecognition is based on the expiry of the right to receive and not that of the counterparty. Therefore, a confirmation from the creditor that a payment instruction has been initiated, does not lead to the expiry of the right to receive cash. It is only once the cash is received that such a right expires.

56. When an entity is initiating a payment instruction through an electronic payment system (and the entity has no [practical] ability to withdraw the instruction), there is a time before the cash is delivered, that the entity loses the practical ability to access (ie use) the cash. However, when an entity has received notification that a creditor has submitted a payment instruction, the entity still does not have the practical ability to access the cash; that only happens when the cash is delivered to the entity's account. Therefore, such a criterion could also not lead to the derecognition of a financial asset before the settlement date.
57. The staff therefore continue to be of the view that a similar exception could not apply to financial assets.

Proposed criteria for derecognising a financial liability before the settlement date.

No ability to withdraw, stop or cancel the payment instruction (paragraph B3.3.8(a))

58. When proposing the criteria to deem a financial liability to be discharged before the settlement date, the IASB considered that if an entity has the ability to withdraw, stop or cancel a payment instruction, the entity could still prevent the payment from completing and, in those circumstances, it could not be said that the entity has discharged the liability, as currently required by paragraph B3.3.1(a) of IFRS 9. In other words, the entity's obligation to pay cash has not been extinguished.
59. However, we acknowledge respondents' concerns about the practicality of this particular criterion. As noted in paragraph BC28 of the Basis for Conclusions on the

ED, an assessment of whether an entity has the (absolute) ability to withdraw, stop or cancel a payment instruction, or at which point that is no longer the case, depends on the electronic payment system in question and could require, amongst other things, an analysis of the relevant features of the system. However, as observed by respondents, most, if not all, electronic payment systems have protective rights that means an entity legally as the ability to stop or cancel a payment instruction for example to prevent fraud or can withdraw the instruction subject to severe financial penalties.

60. Although the proposed requirements are an exception to the general requirements in IFRS 9, we agree with respondents that the proposed criteria set too high a threshold and would likely result in the proposed exception having no practical effect as the criteria might never be met. We therefore recommend aligning this requirement with the requirement in paragraph B3.3.8(b) with regards to the practical ability to access the cash. We are, however, of the opinion that the term ‘practical’ does not need further explanation as it is already used in the relevant section of IFRS 9 (see for example paragraph 3.2.9 of IFRS 9).

No practical ability to access the cash used for settlement (paragraph B3.3.8(b))

61. Referring to respondents’ comments that it is not clear whether and how the exception to derecognising a financial liability would apply if a payment instruction would be settled by way of an overdraft or other similar facility with a negative balance and if paragraph B3.3.8(b) refers to the broader definition of cash in paragraph 8 of IAS 7, we are of the opinion that ‘cash’ in the proposed requirements has the same meaning as used throughout IFRS 9 and IAS 32. We therefore think that further explanations are neither necessary nor would it be helpful as this could have the potential for unintended consequences. In our view, this is consistent with the explanation in paragraph BC37 of the Basis for Conclusions on the ED that the practical challenges that lead to the development of the proposed exception, did not relate to the nature of the account from which a payment is made. We think this equally includes the nature of the cash being used.

62. With regards to questions raised about payment instructions being prepared in advance for future payments to be made, we think that the proposed requirements are clear. A financial liability can only be derecognised before the settlement date if the proposed criteria are met. However, a payment instruction that is prepared for a future payment that will be made, will most likely not meet the requirements for the financial liability to be deemed to be discharged because such instructions can usually still be withdrawn, cancelled or amended and the entity does not lose the practical ability to access the cash. Therefore, we are of the view that no further refinements to the proposed requirements are necessary.

Settlement risk

63. Paragraphs B3.3.8(c) and B3.3.9 of the ED require the settlement risk of any electronic payment system to be insignificant for a financial liability settled through an electronic payment to be eligible for the proposed exception. Settlement risk is described in paragraph BC33 of the Basis for Conclusions on the ED:

‘Settlement risk’ generally refers to the risk that a transaction will not be settled (or completed) and therefore that the debtor will not deliver cash to the creditor on the settlement date. For the purposes of the requirements in paragraphs B3.1.6 and B3.3.1 of IFRS 9, when a financial liability has been discharged by paying cash to a creditor, the creditor is no longer exposed to any settlement risk associated with the transaction.

64. We continue to be of the view that, for a financial liability to be derecognised before the settlement date, the counterparty must no longer be exposed to risk of non-payment by the debtor. Paragraph B3.3.9 of the ED proposes application guidance when that is the case using the terms ‘short’ and ‘standard administrative process’ both of which support the notion of eliminating settlement risk.
65. We believe that the principle would not be further clarified by providing additional application guidance as it might involve setting an arbitrary threshold with regards to

the number of days. As a result, we do not recommend any amendments to the current wording of paragraph B3.3.9 of the ED.

Operational considerations

Definition of an electronic payment systems

66. While there is no definition of an electronic payment system in the ED, we are not convinced that there can be a consistent definition considering the multiple electronic payment systems in use around the globe. However, as pointed out in paragraph BC37 of the Basis for Conclusions on the ED, it was the nature of the payment method being used (ie electronic cash payments) that gave rise to the practical challenges the IASB intended to address in the ED. Therefore, it is the nature of the payment method rather than an exact definition of the system used which is important when applying judgement.
67. We acknowledge respondents' questions with regards to whether the proposed requirements require a continuous assessment of the proposed criteria in paragraph B3.3.8 of the ED. While it is true that the characteristics of an electronic payment system need to enable the criteria to be met until the payment is completed by delivering the cash, we do not consider this to require specific consideration. This is because the assessment of whether an electronic payment system is consistent with those criteria are based on the terms and conditions that governs the system. If there are any changes in those terms and conditions, an entity would need to reassess whether that system still meets the criteria. However, this does not mean an entity needs to continuously reassess between the payment initiation date and the settlement date whether the criteria are met.
68. We acknowledge respondents' suggestions to apply the proposed requirements on an 'all-or-nothing' basis rather than on a system-by-system basis, however we fail to see the potential for abuse of the proposed requirements. This is because the comments imply that the proposed requirements could be used to manipulate the payment date when settling financial liabilities. However, to derecognise a financial liability before

settlement date (when the relevant requirements are met), is an exception that is intended to provide a practical approach in very specific circumstances. Making the application of the exception subject to an assessment of all payment systems to identify which meet the requirements could be quite onerous on entities because each system needs to be assessed individually. In addition, this will also require additional requirements to be developed for when an entity starts to use a new electronic payment system or when one payment system ceases to satisfy the criteria.

69. We therefore recommend not making any changes to the proposed requirements in this regard.

The corresponding 'credit'

70. We acknowledge respondents' questions, as described in paragraphs 19 and 35 of this paper, about the credit entry when a financial liability is derecognised before the settlement date and how to account for the cash to be used for settlement when an entity elects to apply the proposed requirements.
71. In our view, the corresponding derecognition of the cash when the proposed criteria in paragraph 3.3.8 of the ED are met is consistent with the IASB's intention behind the proposed exception. This is because, when the proposed requirements are met, the entity concludes that it has no practical ability to access the cash to be used for settlement. By deeming the liability as discharged through such electronic transfer, an entity also deems the right to the cash flows of the financial asset to be expired once it loses its practical ability to access it.
72. Furthermore, we think that recognising another financial liability (such as a payable for the cash to be delivered) rather than derecognising the cash would raise the same questions about the current practice of accounting for so-called 'cash in transit' items as discussed by respondents in paragraphs 19–20, which we do not think is an appropriate way of reflecting the rights and obligation of these items (see paragraphs 54–57).

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73. With regards to comments made by respondents about the potential for users of financial statements to be misled about the amount of cash at the reporting date if an entity initiates many payment instructions before the reporting date but do not apply the requirements in proposed paragraph B3.3.8 (see paragraph 25), we acknowledge that paragraph 48 of IAS 7 require disclosure of the amount of encumbered cash at the reporting date. There are also other requirements in IFRS 7 and IAS 1 that require an entity to disclose information that is needed for users of financial statements to understand the nature, amount and timing of future cash flows.

Effects on information technology

74. We acknowledge the concerns that respondents expressed about potentially requiring a long transition period to apply the proposed requirements in paragraphs B3.3.8 and B3.3.9 of the ED, compared to the other proposed amendments. This is something we will take it into consideration when we consider feedback on the proposed effective date and transition requirements for the proposals in the ED.

Staff recommendation

75. Based on our analysis in paragraphs 49–74 we recommend aligning the requirement in paragraph B3.3.8 (a) with that of paragraph B3.3.8(b) of the ED so that both refer to ‘practical ability’. We do not recommend any other changes to the wording in the ED.