Staff paper

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IASB® meeting

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Project	**Amortised Cost Measurement**
Topic	**Application of the 10 per cent test**
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Objective and structure of the paper

1. At its June 2026 meeting, the IASB tentatively decided to propose amending IFRS 9 *Financial Instruments* to provide application guidance about how to determine whether a modification of a financial instrument is substantial and therefore results in derecognition. The proposed application guidance will include the '10 per cent test' described in paragraph B3.3.6 of IFRS 9.

2. The objective of this paper is to consider application questions raised by stakeholders about applying the 10 per cent test to specific financial instruments. The paper also discusses potential clarifications to address those questions and asks the IASB whether it agrees with the staff recommendations.

3. This paper is structured as follows:

   (a) summary of staff recommendations and questions for the IASB;

   (b) applicable requirements and issues;

   (c) reminder of the IASB's discussion in June 2026;

   (d) financial instruments with options or contingent terms; and

   (e) revolving credit facilities.

Summary of staff recommendations and questions for the IASB

4. We recommend that the IASB proposes amending IFRS 9 to clarify that, for purposes of applying the 10 per cent test:
   (a) an entity considers all contractual terms of the financial instrument; and
   (b) if the contractual terms include an option or a contingent term, the entity determines the contractual cash flows for purpose of the test on the basis that the option is exercised, or the contingent event occurs, at the earliest possible date specified in the contract. The probability or estimated timing of the option being exercised, or the contingent event occurring, has no effect on determining those contractual cash flows.

5. We also recommend that the IASB clarify that, for purposes of applying the 10 per cent test to a financial asset or financial liability that is a revolving credit facility, the contractual cash flows are determined based on the terms of the facility in its entirety. In particular, the entity would determine the contractual cash flows based on the maximum credit capacity over the remaining term of the facility, under the new and original terms.

Questions for the IASB
1. Does the IASB agree with the staff recommendation in paragraph 4 of this paper?
2. Does the IASB agree with the staff recommendation in paragraph 5 of this paper?

Applicable requirements and issues

Key applicable requirements

6. Paragraph B3.3.6 of IFRS 9 describes the 10 per cent test as:

> …the terms are substantially different if the discounted present value of the cash flows under the new terms, including any fees paid net of any fees received and discounted using the original effective interest rate, is at least 10 per cent different from the discounted present value of the remaining cash flows of the original financial liability. In determining those fees paid net of fees received, a borrower includes only fees paid or received between the borrower and the lender, including fees paid or received by either the borrower or lender on the other's behalf.

Application questions

7. During the post-implementation reviews of IFRS 9, some stakeholders asked for application guidance on how to apply the 10 per cent test for two types of financial instruments:

   (a) financial assets and financial liabilities with options (callable or puttable) or contingent terms (terms triggered by the occurrence of a specified event); and

   (b) revolving credit facilities, such as credit cards or overdraft facilities.

8. **For financial instruments with options or contingent terms**, stakeholders said IFRS 9 does not specify how an entity should reflect those terms when applying the 10 per cent test. They asked whether the test is applied:

   (a) assuming that options are exercised or the contingent events occur;

   (b) using a probability-weighted approach; or

   (c) by disregarding such contractual terms.

9. Stakeholders also said that each of these approaches is applied in practice, and therefore there is diversity in application.

10. **For revolving credit facilities**, stakeholders said that applying the 10 per cent test is challenging, particularly when a facility is undrawn at the assessment date. Paragraph B3.3.6 of IFRS 9 requires an entity to compare the discounted present value of the original contractual cash flows with that of the modified contractual cash flows. However, if the facility has not yet been drawn, it's carrying amount would be nil, making it difficult to apply the test.

11. Consequently, they said that in practice, entities assess whether a modification of a revolving credit facility is substantial by qualitatively analysing changes in contractual cash flows, rather than applying a quantitative test.

12. Stakeholders, including financial institutions and auditors, raised this question mainly in the context of revolving credit facilities that are financial assets. A few also referred to revolving credit facilities that are financial liabilities, because paragraph B3.3.6 of IFRS 9 specifically refers to financial liabilities.

13. Stakeholders also noted that, even when the carrying amount of a revolving credit facility is nil at the reporting date, determining whether a modification results in derecognition is important because it affects several aspects of the accounting for the facility, including expected credit losses (ECL) for financial assets and any related costs or fees for financial assets and financial liabilities.

Reminder of the IASB's discussion in June 2026

14. At its June 2026 meeting, the IASB discussed:

    (a) the objective of assessing whether a modification of a financial asset or a financial liability is substantial. That objective is to determine whether the nature, timing, amounts, or uncertainty of the cash flows under the original contractual terms are substantially different from those under the modified terms; and

(b) the approach for assessing whether a modification of a financial asset or a financial liability is substantial and therefore results in derecognition (general approach).

15. With regards to the general approach, the IASB tentatively decided to propose that:

(a) an entity would determine whether a modification of a financial instrument is substantial based on a holistic analysis of the changes in the contractual cash flows. The entity would consider qualitative and quantitative factors as part of this analysis. The '10 per cent test' could supplement the analysis but would not be the decisive factor in isolation.

(b) the factors an entity considers in determining whether a modification is substantial include, but are not limited to:

(i) a change in the currency in which principal or interest is denominated, which would suggest the modification is substantial.

(ii) a change in cash flow characteristics that alters the assessment of whether the cash flows are solely payments of principal and interest for a financial asset; or whether an embedded derivative is separated from the host contract for a financial liability. Such a change would suggest the modification is substantial.

(iii) a change in borrower counterparty, which would suggest the modification is substantial, unless the change is between entities under common control.

(iv) the reason for the modification. A commercial renegotiation to reset the financial instrument to current market terms would suggest the modification is substantial. Conversely, a modification attributable to the borrower's financial difficulty would suggest the modification is not substantial.

(c) the relevance and weighting of each factor would depend on the type and characteristics of the financial instrument and economic conditions. An entity would consider reasonable and supportable information that is available without undue cost or effort and relevant to the instrument being assessed.

Financial instruments with options or contingent terms

Staff analysis

16. The feedback in paragraph 8 of this paper raises two questions about financial instruments with options or contingent terms:

(a) whether those terms must be considered in the 10 per cent test; and

(b) if so, how to reflect them when comparing the discounted present value of the modified and original contractual cash flows.

17. In our view, disregarding contractual terms such as options or contingent terms would be inconsistent with the 10 per cent test. Paragraph B3.3.6 of IFRS 9 requires an analysis of the cash flows under the new contractual terms compared with those under the original terms to determine whether the terms are substantially different. It does not limit that analysis to particular terms only.

18. However, we acknowledge that IFRS 9 does not specify how to reflect those terms in the 10 per cent test.

19. In our view, the starting point for analysing this matter is the objective of the 10 per cent test. The IASB noted in paragraph BC3.34 of the Basis for Conclusions on IFRS 9 that the objective of the 10 per cent test is to 'quantitatively assess the **significance of any difference between the old and new <u>contractual terms</u>** on the basis of the changes in the contractual cash flows between the borrower and lender'.

20. This description suggests that the 10 per cent test compares the contractual cash flows under the original and modified terms, without incorporating expectations about whether, or when, those cash flows might arise. For example, if a modification introduces a new prepayment option, the entity would perform the test on the basis that the option is exercised in accordance with the contractual terms, rather than estimating the probability or estimated timing of the option being exercised.

21. However, it could be argued that such an approach would be inconsistent with other requirements in IFRS 9 which require an entity to estimate future cash payments or receipts through the expected life of the financial asset or financial liability.

22. In particular, Appendix A of IFRS 9 requires an entity, when calculating the Effective Interest Rate (EIR), to estimate expected cash flows by considering all contractual terms of the financial instrument (including prepayment, extension, call and similar options) but shall not consider the expected credit losses. There is a presumption that the cash flows and the expected life of a group of similar financial instruments can be estimated reliably. However, in those rare cases when it is not possible to reliably estimate the cash flows or the expected life of a financial instrument (or group of financial instruments), the entity shall use the contractual cash flows over the full contractual term of the financial instrument (or group of financial instruments).

23. These principles indicate that, when considering all contractual terms of a financial instrument (including prepayment, extension, call and similar options), an entity estimates the cash flows or expected life of the financial instrument, or group of financial instruments, unless it cannot do so reliably.

24. Based on this analysis, we identified two approaches for reflecting options and contingent terms in the 10 per cent test:

   (a) **an expected cash-flows approach**—an entity would apply the test using estimated cash flows over the expected life of the financial instrument. This would be consistent with the principles used to calculate the EIR of a financial instrument on initial recognition. The cash flows under this approach would reflect the entity's expectations about an option being exercised or a contingent event occurring; and

(b) **a contractual-terms approach**—an entity would apply the test on the basis that an option is exercised, or a contingent event occurs, at the earliest possible date specified in the contract.

25. We also identified a third approach, which is applied in some jurisdictions. Under that approach, an entity applies the 10 per cent test under both scenarios—assuming exercise or occurrence, and assuming non-exercise or non-occurrence—and use the outcome that produces the smaller quantitative difference. However, we did not analyse this approach further because we think it would make the 10 per cent test operationally complex, and therefore not proportionate to the supplementary role of this test in assessing whether a modification is substantial.

26. As noted in paragraphs 15 of this paper, the IASB tentatively decided that the 10 per cent test supplements the qualitative assessment, instead of being used to determine the outcome on its own. Given that supplementary role, we think that any approach the IASB proposes for reflecting options or other contingent terms in this test should be proportionate and avoid undue complexity or costs for preparers.

Expected cash-flows approach

27. This approach would require an entity to apply the 10 per cent test by estimating the cash flows applying the same principles used to calculate the EIR (see paragraph 22 of this paper). The cash flows under this approach would be estimated over the expected life of the financial instrument. However, if the cash flows or expected life of the instrument cannot be estimated reliably, the entity would use the contractual cash flows over the instrument's full contractual term.

28. The main advantages of this approach are that it would:

(a) reflect expected behaviour by incorporating the entity's expectations about how options and contingent terms would affect contractual cash flows instead of assuming a contractual scenario that may not occur. If those effects can be estimated reliably, this approach could provide a more faithful representation of the significance of the modification and avoid outcomes driven by contractual dates that do not reflect how the instrument is expected to behave; and

(b) better align with the existing principles in IFRS 9 for estimating cash flows for purposes of determining the EIR on initial recognition.

29. However, in analysing this approach, we think the IASB should also consider the known practice issues that arise when estimating cash flows for the purposes of calculating the EIR. As discussed in September 2025, stakeholders reported application questions and diversity in two areas:

(a) **which conditional terms to include in the estimate**—many entities include only some conditional terms when calculating the EIR on initial recognition. They generally do so because they determine that the effects from the omitted terms are immaterial or because they do not have sufficient information to estimate their effects reliably.

(b) **how conditional terms are reflected in the estimate**—entities apply judgement in selecting an estimation method based on the relevant facts and circumstances. Methods used in practice include a most-likely-outcome approach, which reflects a binary estimate of whether or not a contingent event is expected to occur, and a probability-weighted approach, which reflects a range of possible outcomes.

30. At the time, the IASB tentatively decided to take no further action on these matters. It noted that IFRS 9 already requires entities to consider **all** contractual terms in calculating the EIR, unless it is not possible to make a reliable estimate.

31. The IASB also noted that IFRS 9 does not prescribe a specific estimation method; entities use judgement to select an appropriate approach based on the facts and circumstances, sometimes by analogy to other IFRS Accounting Standards. Standard-setting in this area was therefore unlikely to significantly improve financial reporting.

32. Given these practice issues in applying the EIR principles, we think applying those same principles to the 10 per cent test could carry similar challenges—and related diversity—into that test. As a result, the IASB might not effectively resolve the matter described in paragraphs 8–9 of this paper.

Contractual-terms approach

33. This approach would require an entity to apply the 10 per cent test on the basis that an option is exercised, or a contingent event occurs, at the earliest possible date specified in the contract. Under this approach, the entity would not take into account its own expectations about whether the option will be exercised or the contingent event will occur.

34. The main advantages of this approach are that:

    (a) it would be consistent with the objective of a modification assessment which is to determine whether the nature, timing, amounts, or uncertainty of the cash flows under the original contractual terms are substantially different from those under the modified terms (see paragraph 15 of this paper);

    (b) it would align with the objective of the 10 per cent test, which focuses on the significance of any difference between the old and new contractual terms (see paragraph 19 of this paper). It would also align with other IFRS 9 assessments that focus on contractual terms—such as solely payments of principal and interest for financial assets and embedded derivative assessment for financial liabilities. In these assessments, the focus is on whether the instrument includes contractual terms that could affect the cash flows, rather than on expectations about if, or when, those terms may occur.

(c) it would be operationally simpler to apply by avoiding the need for entities to estimate contractual cash flows and expected term, including applying judgement about whether options are expected to be exercised, or contingent events are expected to occur, and the related probability and timing; and

(d) it could improve comparability in practice by establishing a clear, consistent basis for applying the 10 per cent test. It would also be expected to improve comparability between lender and borrower accounting outcomes for the same financial instrument, because, unlike the expected cash-flows approach, this approach does not require estimation of cash flows and the application of judgement.

Staff recommendation

35. Based on our analysis, we think that the contractual-terms approach provides a better basis for clarifying the application of the 10 per cent test. Given the supplementary role of the test, this simpler approach would also be more proportionate.

36. We therefore recommend the IASB clarify that, in applying the 10 per cent test:

(a) an entity considers all contractual terms of the financial instrument; and

(b) if the contractual terms include an option or a contingent term, the entity determines the contractual cash flows for purpose of the test on the basis that the option is exercised, or the contingent event occurs, at the earliest possible date specified in the contract. The probability or estimated timing of the option being exercised, or the contingent event occurring, has no effect on determining those contractual cash flows.

Revolving credit facilities

Staff analysis

37. We acknowledge that applying the 10 per cent test as required by paragraph B3.3.6 of IFRS 9 to revolving credit facilities raises specific application challenges for both financial assets and financial liabilities. As stakeholders noted, these facilities often have no fixed repayment structure and may be undrawn at the modification date, making it difficult to identify the cash flows to compare.

38. In the context of financial assets, we note that IFRS 9 already acknowledges the distinctive characteristics of revolving credit facilities and includes specific requirements for recognising ECL on them. In particular, paragraph 5.5.20 of IFRS 9 states that some financial instruments include both a loan and an undrawn commitment component, and that an entity's contractual ability to demand repayment and cancel the undrawn commitment does not limit its exposure to credit losses to the contractual notice period. For such financial instruments, the entity shall measure ECL over the period that the entity is exposed to credit risk and ECL would not be mitigated by credit risk management actions, even if that period extends beyond the maximum contractual period.

39. Paragraph B5.5.39 of IFRS 9 states that revolving credit facilities generally have the following characteristics:

    (a) the financial instruments do not have a fixed term or repayment structure and usually have a short contractual cancellation period (for example, one day);

    (b) the contractual ability to cancel the contract is not enforced in the normal day-to-day management of the financial instrument and the contract may only be cancelled when the entity becomes aware of an increase in credit risk at the facility level; and

    (c) the financial instruments are managed on a collective basis.

40. Considering stakeholders' application questions and the distinctive characteristics of revolving credit facilities, we think the IASB should explore whether to provide specific application guidance on the quantitative assessment of modifications for these facilities. That guidance would apply to revolving credit facilities that are financial assets and financial liabilities. It could clarify whether—and, if so, how—an entity assesses the significance of differences between the original and new contractual terms.

41. As discussed at the IASB's February 2025 meeting, the IASB could consider two possible approaches for revolving credit facilities:

    (a) remove the quantitative assessment for these facilities, so that an entity would assess the significance of a modification using qualitative factors only; or

    (b) tailor the 10 per cent test to the characteristics of such instruments to require an entity to analyse changes in the contractual cash flows of the facility in its entirety rather than changes in the carrying amount.

Qualitative assessment only approach

42. Under this approach, an entity would assess whether a modification of a revolving credit facility is substantial using qualitative factors only, without supplementing the assessment with a quantitative 10 per cent test.

43. The main advantages of this approach are that it would:

    (a) be simpler to apply, particularly when a facility is undrawn, has no fixed repayment structure or has a short contractual cancellation period. However, if the most relevant qualitative factors do not clearly indicate whether or not a modification is substantial, the entity may need to perform a more exhaustive qualitative analysis.

    (b) avoid the need to make additional assumptions about future drawdowns, utilisation patterns or repayment behaviour for use in a quantitative test; and

(c) align with the current practice of many entities that assess modifications of such facilities using qualitative factors only (see paragraph 11 of this paper).

Facility-level approach

44. Under this approach, an entity would apply the 10 per cent test by reference to the difference in the contractual terms of the overall facility including the overall credit limit. The cash flows used in the test would be based on the maximum available credit over the remaining term of the facility under the original and modified terms. The assessment would therefore not depend only on the amount drawn at the modification date but on the overall credit limit of the facility.

45. The main advantages of this approach are that it would:

(a) retain a quantitative test as a supplement to the qualitative analysis, consistent with the general approach tentatively decided by the IASB in June 2026. This would avoid creating a separate approach for one subset of financial instruments, namely, revolving credit facilities;

(b) make the 10 per cent test operational to revolving credit facilities even when a facility is undrawn or only partly drawn. This would help an entity assess whether a modification is substantial when qualitative factors alone do not provide a clear conclusion;

(c) better reflect the contractual economics of a revolving credit facility. The parties' rights and obligations relate to the facility's credit limit, not only to amounts drawn at a particular date. Using credit capacity as the basis for the 10 per cent test would therefore reflect the broader rights and obligations arising from these facilities; and

(d) improve comparability among financial instruments because it retains the quantitative 10 per cent test. As a result, it provides entities with a common basis for applying the quantitative test for all relevant financial instruments.

Staff recommendation

46. In our view, the facility-level approach provides a more appropriate basis for clarifying the application of the 10 per cent test to revolving credit facilities. It is more consistent with the general approach tentatively decided by the IASB in June 2026 and avoids excluding these facilities from quantitative analysis solely because they have revolving features.

47. We therefore recommend that the IASB clarify that, for the purposes of applying the 10 per cent test to a financial asset or financial liability that is a revolving credit facility, the contractual cash flows are determined based on the terms of the facility in its entirety. In particular, the entity would determine the cash flows based on the maximum available credit over the remaining term of the facility, under the new and original terms.