STAFF PAPER

November 2021

IFRS® Interpretations Committee meeting

Project	**TLTRO III Transactions (IFRS 9 and IAS 20)**
Paper topic	Comment letters

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Introduction

1. This paper reproduces comment letters on the IFRS Interpretations Committee's tentative agenda decision 'TLTRO III Transactions (IFRS 9 and IAS 20)' published in June 2021.

The Interim Chair
20 July 2021
ESMA32-339-183

Sue Lloyd
Chair
IFRS Interpretation Committee
Columbus Building
7 Westferry Circus
Canary Wharf
London E14 4HD
United Kingdom

The IFRS Interpretations Committee's tentative agenda decision on TLTRO III Transactions (IFRS 9 and IAS 20)

Dear Ms Lloyd,

The European Securities and Markets Authority (ESMA) thanks the IFRS Interpretations Committee's (IFRS IC) for the extensive discussion of ESMA's Agenda Item Request on accounting for the TLTRO III transactions (IFRS 9, IAS 20). We also appreciate the opportunity to respond to the IFRS IC's publication of the tentative agenda decision related to this issue.

ESMA believes that in order to reduce the existing diversity in the application of the requirements of IFRS 9 and IAS 20, it would be helpful if the IFRS IC provided more clarity regarding the applicability of IAS 20 on the TLTRO III transactions, in particular giving further guidance on determining whether a central bank or other similar body meets the broad definition of government under IAS 20. It would also be useful if the IFRS IC could provide guidance on whether and how conditions attached to the interest rate should be reflected in the estimates and revisions of expected future cash flows when determining the effective interest rate. We consider that the IFRS 9 Post Implementation Review progress will not allow a timely response for TLTRO III or other refinancing programs in the future.

Moreover, ESMA notes that both the interest rate on the main refinancing operations (MRO) and the borrowing rate in TLTRO III operations are instruments of the ECB's monetary policy operations and, as such, can be unilaterally changed by the ECB anytime. The ECB could have defined the TLTRO interest rate without any reference to the MRO rate. Against this background, ESMA finds it difficult to understand why, according to the tentative agenda decision, the TLTRO III interest rate is considered to be a combination of a fixed and a variable interest rate element, while the MRO rate is referred to as an example of a variable interest rate.

Therefore, ESMA kindly suggests that the IFRS Interpretations Committee (IFRS IC) considers removing the reference to the fixed 50 basis points discount given by the ECB on particular

TLTRO III tranches for a fixed period as an example of interest rate elements that are fixed and therefore not reset to reflect movements in the market rates of interest.

In case you have any questions or comments regarding this letter, I suggest you contact Evert van Walsum, Head of the Investors and Issuers Department (Evert.vanWalsum@esma.europa.eu).

Yours sincerely,

Tuominen Anneli 912372492

Anneli Tuominen

FÉDÉRATION
BANCAIRE
FRANÇAISE

Banking supervision
And Accounting issues Unit

The Director

Paris, July 28th, 2021

FBF comments on TLTRO III Transactions (IFRS9 Financial Instruments and IAS 20 Accounting for Government Grants and Disclosure of Government Assistance)

Dear Mrs Lloyd,

The French Banking Federation (FBF) is pleased to provide the IFRS IC comments on its tentative agenda decision regarding a submission asking about how banks account for the European Central Bank's (ECB's) Targeted Longer-Term Refinancing Operations Programme (TLTRO) III transactions.

We generally agree with the Committee's analysis and tentative agenda decision on this topic. However, we disagree with one point in the analysis regarding the subsequent measurement of financial liabilities at amortized cost.

In its tentative agenda decision on whether to apply paragraphs B5.4.5 or B5.4.6 of IFRS 9 to the re-estimation of the TLTRO III cash flows, the Committee considered i) that IFRS 9 B5.4.5 applies only to the variable interest rate component of liabilities, ii) that IFRS 9 does not elaborate on what is meant by floating rate and iii) that a financial instrument with variable contractual cash flows – which can periodically be adjusted to reflect movements in the market rates of interest – is a floating-rate financial instrument.

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Applied to TLTRO III operations, the Committee considered that the floating rate element was relative to the banks' rate on the main refinancing operations (MRO) or to the deposit facility rate (DFR). Accordingly, the Committee considered that the fixed 50 basis points discount given by the ECB on TLTRO III tranches for a fixed period was a fixed component not reset to reflect movements in market interest rates and to which paragraph B5.4.6 applies.

We disagree on this last point.

In our view, it is not possible to consider that the interest rate of the targeted lending operations (the average rate applied in the Eurosystem's main refinancing operations and the 50 basis points below the main refinancing operations or the deposit facility depending on whether the bank's lending threshold is met) is a combination of variable rate and a fixed component.

The TLTRO interest rate must be considered in its entirety as it is part of the set of ECB interest rates that remains the primary monetary policy instrument with the ECB as market maker. Even though, the interest rate for the TLTRO III operations is not a new rate as such but is derived from the rate applied to the main refinancing operations (MROs), with adjustments for some specified periods as from June 24, 2020, to June 23, 2022, it shall be considered as a specific rate that the ECB adjusts from time to time to achieve its monetary policy as would be the case for MRO or DFR. It should also be noted that the ECB, unlike a traditional counterparty, has the possibility to unilaterally modify the TLTRO rate and this brings the TLTRO rate closer to a traditional variable rate.

When recalibrating targeted lending operations, the aims of the ECB are to further support real economy and to maintain favourable credit conditions, i.e., loans to households excluding real estate loans and loans to non-financial companies, by easing the refinancing conditions for banks in a context of high economic uncertainty and challenging credit environment resulting from the pandemic situation.

The TLTRO interest rate is a market interest rate because the new refinancing conditions are available to all EU banks if they are eligible to targeted lending operations. Moreover, the changes to TLTRO III apply to all TLTRO III operations that occur during a specified period without discriminating conditions, for example, related to the characteristics of the credit or to the risk quality of the credit.

The last ECB's refinancing operations show that TLTRO III is a specific instrument to which banks have largely subscribed by turning away from the ECB's usual DFR or MRO refinancing operations, given the interest rate conditions of the targeted lending operations offered.

In addition, we do not believe it would be appropriate that the Committee determines whether an interest rate is a fixed rate or a variable rate as this is a matter of facts and circumstances beyond the scope of a standards interpretation.

For all the reasons mentioned above, we advocate that the example in brackets mentioning the fixed 50 basis points as a fixed rate should be deleted from the tentative agenda decision, as follows.

> *The Committee also observed that a floating-rate financial instrument may consist of a variable interest rate element, which is reset to reflect movements in the market rates of interest (for example, the ECB rate on the main refinancing operations) plus or minus other elements, which are fixed and therefore not reset to reflect movements in the market rates of interest ~~(for example, the fixed 50 basis points discount given by the ECB on particular TLTRO III tranches for a fixed period)~~.*

Besides, about the question whether TLTRO III transactions should be accounted for under IFRS 9 or IAS 20, we support the Committee's position in its tentative agenda decision. More specifically, we share the view that judgment is required based on the specific facts and circumstances to determine whether TLTRO III tranches contain a government grant in the scope of IAS 20 and the requirements in IAS 20 are clear about how to account for the grant if it is concluded that there is a government grant.

Accordingly, we believe that any changes to the tentative agenda decision on this issue would require further analysis and appropriate consultation with stakeholders.

We hope you find these comments useful and would be pleased to provide any further information you might require.

Yours sincerely,

Bertrand Lussigny

POSITION PAPER

Tentative Agenda Decision TDA TLTRO III Transactions (IFRS 9 and IAS 20)

WSBI (World Savings and Retail Banking Group)
ESBG (European Savings and Retail Banking Group)
Rue Marie-Thérèse, 11 - B-1000 Brussels

ESBG Transparency Register ID 8765978796-80

July 2021

WSBI

ESBG

Thank you for giving us an opportunity to comment on the tentative agenda decisions of the IFRS Interpretation Committee published in June 2021. Our comments and concerns on the accounting treatment on TLTRO III tranches are provided below and we hope you will find those useful and relevant. The IFRIC Interpretation Committee is requested to consider our concerns appropriately to depict a true and fair view and economic substance of the transactions/events.

1. Regarding whether TLTRO III tranches contain a government grant in the scope of IAS 20

Assessing whether the ECB meets the definition of government in IAS 20 requires judgement. However, this judgement should not be based on entities' specific facts and circumstances. These facts and circumstances are common to all eurozone financial institutions, and hence the consideration or not as a government shall be applied consistently. We also agree that the Interpretations Committee is not in the position to conclude whether the ECB meets the definition of government under IAS 20. To this end, a public statement from the ECB /ESMA with the conclusions of this assessment would provide further clarity on this issue.

On this regard, WSBI - ESBG believes that there are not any components of TLTRO III credit facilities within the scope of IAS 20 based on the following aspects:

- ECB's independence from the EU institutions or bodies, from any government of an EU Member State or from any other body, preclude it to be considered as a government under IAS 20 definition. This independence is laid down in the institutional framework for the single monetary policy (Treaty and Statute).
-
- Interest rate cannot be deemed as below-market, as it is available to a broad range of market participants (eurozone banks).
-
- IAS 20 assumes that there is an expense which the grant compensates for. In the context of TLTRO III facilities, it is not clear what expense the grant is compensating given the fact that there are no binding restrictions to financial institutions in the application of interest rates to their customers.

Before assessing whether TLTRO III tranches contain a government grant in the scope of IAS 20, financial institutions must assess any difference between the transaction price and the consideration received under IFRS 9 if it is received for only the financial liability. WSBI - ESBG believe the IFRIC Committee should further discuss the nature of such difference as such point is not developed in the TAD and could lead to inconsistency among financial entities.

2. Calculating the effective interest rate on initial recognition of the financial liability

In ESBG's view, TLTRO III tranches are variable rate instruments considering that interest rate is linked to DRF (deposit facility rate) and / or MRO (main refinancing operations) rate and to the lending patterns of the participating banks. As such, on initial recognition the effective interest rate is calculated based on the expected future cash flows stemming from the entity's assessment of its lending behaviour over the life of the loan to meet the thresholds.

We note that the TAD does not conclude whether the expected future cash flows should reflect an assessment of whether the bank will satisfy the conditions attached to the liability. We believe that further clarification is needed on how to reflect uncertain conditions in calculating the effective interest rate before the IFRS 9 Post-implementation review.

3. Subsequent measurement of the financial liability at amortised cost

In its tentative decision on the analysis of the application of paragraphs B5.4.5 and B5.4.6 of IFRS 9, which define the accounting for changes in estimated cash flows, the Committee considered that IFRS 9 B5.4.5 applies only to the variable interest rate component of liabilities, that IFRS 9 does not elaborate on what is meant by floating rate and that a financial instrument with variable contractual cash flows – which can periodically be adjusted to reflect movements in the market rates of interest – is a floating-rate financial instrument.

The Committee also observed that '…*a floating-rate financial instrument may consist of a variable interest rate element, which is reset to reflect movements in the market rates of interest (for example, the ECB rate on the main refinancing operations) plus or minus other elements, which are fixed and therefore not reset to reflect movements in the market rates of interest* *<u>(for example, the fixed 50 basis points discount given by the ECB on particular TLTRO III tranches for a fixed period</u>*). *When considering how to account for changes in cash flow estimates, the Committee noted that paragraph B5.4.5 of IFRS 9 applies only to the variable interest rate element of a floating-rate instrument (as far as it reflects movements in the market rates of interest) and not to other interest rate elements of the instrument (which are typically not reset to reflect movements in the market rates of interest)*' (emphasis added).

In other words, the TAD specifies that the fixed 50 basis points discount given by the ECB on particular TLTRO III tranches for a fixed period is a fixed element and accordingly, that paragraph B5.4.6 of IFRS 9 applies when accounting for any change in the instrument's estimated future cash flows resulting from a change in that element—in particular when the ECB decided that the borrowing rate applying to some refinancing operations would be 50 basis points below the MRO rate over a specified fixed period. <u>WSBI - ESBG disagrees with this observation</u>.

We agree there are many circumstances in which a borrowing rate that includes a benchmark interest rate and a fixed component must be analysed as including both:

- a variable interest rate element—to which paragraph B5.4.5 of IFRS 9 applies—and,
- another fixed element—to which paragraph B5.4.6 of IFRS 9 applies,

however, <u>we think the TAD addresses very specific circumstances that could justify applying paragraph B5.4.5 of IFRS 9 to any change in the fixed 50 basis points element</u>. We think (i) the Committee's observation is a possible view of how to analyse the interest rate that applies to TLTRO III tranches and (ii) reaching any conclusion in this respect requires the use of judgement. We also observe the TAD deals with other matters that requires the use of judgement.

The TLTRO interest rate must be considered in its entirety as it is part of the set of ECB interest rates that remains the primary monetary policy instrument:

- the ECB is the 'market maker'. Accordingly, it would be contradictory to conclude that change in an interest rate introduced by a market maker is not a change in the market rate.
- the ECB is able to reset unilaterally the rate at any point in time—i.e. it has the right to amend the rate at any time. The fact that the ECB's initial decision published 22 July 2019, was subsequently superseded by a decision on 30 April 2020, which was subsequently superseded by a decision on 29 January 2021 provides evidence of the ECB's 'market maker' capacity. Furthermore, the banks can voluntarily repay early (either partly or fully) as of September 2021 (refer to Q32 in the linked ECB site) with no penalty. This would support the view that the reduction in the 50bp fixed rate can be considered to reflect movements in market rates of interest.

-

When recalibrating targeted lending operations, the aims of the ECB are to further support real economy and to maintain favourable credit conditions, i.e., loans to households excluding real estate loans and loans to non-financial companies, by easing the refinancing conditions for banks in a context of high economic uncertainty and challenging credit environment resulting from the pandemic situation.

The TLTRO interest rate is a market interest rate because the new refinancing conditions are available to all EU banks if they are eligible to targeted lending operations.

We think that the specific facts and circumstances relating to TLTRO III transactions require an entity to apply its judgment when assessing whether the 50 basis points reduction is a fixed or variable element. The Committee's observation as currently drafted in the TAD is only a possible view.

For all the reasons mentioned above, we advocate that the example in brackets mentioning the fixed 50 basis points as a fixed rate should be deleted from the tentative decision, as follows:

> *The Committee also observed that a floating-rate financial instrument may consist of a variable interest rate element, which is reset to reflect movements in the market rates of interest (for example, the ECB rate on the main refinancing operations) plus or minus other elements, which are fixed and therefore not reset to reflect movements in the market rates of interest ~~(for example, the fixed 50 basis points discount given by the ECB on particular TLTRO III tranches for a fixed period).~~*

About WSBI (World Savings and Retail Banking Institute)

WSBI represents the interests of 6,760 savings and retail banks around the world. WSBI focuses on international regulatory issues that affect the savings and retail banking industry. It supports the aims of the G20 in achieving sustainable, inclusive, and balanced growth, and job creation, whether in industrialised or less developed countries. Supporting a diversified range of financial services to meet customer need, WSBI favours an inclusive form of globalisation that is just and fair. It supports international efforts to advance financial access and financial usage for everyone. WSBI members have total assets of $16 trillion and serving some 1.7 billion customers in nearly 80 countries who seek retail banking services. WSBI members are committed to further unleash the promise of sustainable, responsible 21st century banking.

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About ESBG (European Savings and Retail Banking Group)

ESBG represents the locally focused European banking sector, helping savings and retail banks in 21 European countries strengthen their unique approach that focuses on providing service to local comunities and boosting SMEs. An advocate for a proportionate approach to banking rules, ESBG unites at EU level some 900 banks, which together employ more than 650,000 people driven to innovate at roughly 50,000 outlets. ESBG members have total assets of €5.3 trillion, provide €1 trillion in corporate loans (including to SMEs), and serve 150 million Europeans seeking retail banking services. ESBG members are committed to further unleash the promise of sustainable, responsible 21st century banking. Our transparency ID is 8765978796-80.

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FRANÇAISE
Liberté
Égalité
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AUTORITÉ
DES NORMES COMPTABLES

Paris, 20 July 2021

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PDC n°38

Mrs Sue Llyod
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June 2021 IFRIC *Update*—Feedback on the Tentative Agenda Decision TLTRO III Transactions *(IFRS 9 and IAS 20)*

Dear Sue,

I am writing to you on behalf of the Autorité des Normes Comptables (ANC) to express our views on the above-mentioned IFRS Interpretations Committee's (Committee) Tentative Agenda Decision (TAD) published in June 2021.

- **Committee's overall technical analysis included in the TAD**

We agree with the Committee's technical analysis and tentative conclusion as set out in the TAD except for one aspect of the analysis that relates to the subsequent measurement of the financial liability (see below).

- **Subsequent measurement of the financial liability at amortised cost**
    - ***The Committee expressed only a possible view in the TAD on how to analyse the interest rate that applies to TLTRO III tranches***

The Committee noted in the TAD that paragraphs B5.4.5 and B5.4.6 of IFRS 9 *Financial Instruments* specify requirements for how an entity accounts for changes in the estimated future cash flows of a financial liability. In particular, the Committee observed that (i) paragraph B5.4.5[1] applies to floating-rate financial liabilities, (ii) IFRS 9 does not elaborate on what is meant by floating rate and (iii) a financial instrument with variable contractual cash flows—which can periodically be adjusted to reflect movements in the market rates of interest—is a floating-rate financial instrument.

We agree with those observations.

The Committee went on and observed that '*...a floating-rate financial instrument may consist of a variable interest rate element, which is reset to reflect movements in the market rates of interest (for example, the ECB rate on the main refinancing operations) plus or minus other elements, which are fixed and therefore not reset to reflect movements in the market rates of interest* (*for example, the fixed 50 basis points discount given by the ECB on*

[1] Paragraph B5.4.5 of IFRS 9 states that '*...period re-estimation of cash flows to reflect the movements in the market rates of interest alters alter the effective interest rate (EIR)...*' of a financial instrument subsequently measured at amortised cost (emphasis added).

particular TLTRO III tranches for a fixed period). When considering how to account for changes in cash flow estimates, the Committee noted that paragraph B5.4.5 of IFRS 9 applies only to the variable interest rate element of a floating-rate instrument (as far as it reflects movements in the market rates of interest) and not to other interest rate elements of the instrument (which are typically not reset to reflect movements in the market rates of interest)' (emphasis added).

In other words, the TAD specifies that the fixed 50bp discount given by the ECB on particular TLTRO III tranches for a fixed period is a fixed element and accordingly, that paragraph B5.4.6 of IFRS 9 applies when accounting for any change in the instrument's estimated future cash flows resulting from a change in that element—in particular when the ECB decided that the borrowing rate applying to some refinancing operations would be 50bp below the MRO rate over a specified fixed period.

We disagree with this observation.

We agree there are many circumstances in which an entity analyses a borrowing rate that includes a benchmark interest rate and a fixed component as including both:
- a variable interest rate element—to which paragraph B5.4.5 of IFRS 9 applies—and,
- another fixed element—to which paragraph B5.4.6 of IFRS 9 applies.

However, we think the TAD addresses very specific circumstances that could justify applying paragraph B5.4.5 of IFRS 9 to any change in the fixed 50bp element. We also think the Committee cannot express any view on this specific matter. This is because:
- the Committee's observation is a possible view of how to analyse the interest rate that applies to TLTRO III tranches. Reaching any conclusion in this respect requires the use of judgement (see below for an alternative view).
- the TAD deals with other matters which also require the use of judgement. The Committee only outlined the analysis an entity has to perform in relation to those matters—the Committee did not express any view on the conclusion an entity should reach for such matters.
- the TAD does not, itself, include any evidence that would substantiate the Committee's observation.

- ***An alternative view on the matter***

As mentioned above, we think the Committee's observation whereby the 50bp reduction is a fixed element—ie a fixed spread that is not a movement in the market rates of interest—is only a possible view on to analyse the interest rate that applies to TLTRO III tranches.

We also note that the TAD does not include any technical analysis that would support the Committee's view. That being said, on the basis of the public discussions which took place at the June 2021 Committee's meeting, we understand the Committee tentatively reached this conclusion considering that:
- the 50 bp element was 'locked in' and therefore, was not subject to movements. In contrast, the MRO and DFR rates were subject to movements and were, in the Committee's view, the market rates; and
- the fact that an interest rate element may change does not automatically result in the rate being a floating rate.

We think those arguments could be valid in many circumstances. However, they ignore the very specific facts and circumstances applying to TLTRO III transactions. We think an alternative view exists and a technical analysis supports this view.

The analysis below focuses solely on the changes that the ECB made in January 2021 to the borrowing rate of TLTRO III operations. We acknowledge that the ECB made other changes to the borrowing rate before that date. However, the outstanding amount of the TLTRO III program really gained momentum in June 2020, moving from €0.21 to €1.6 trillion. The only change the ECB has made to the borrowing rate cince June 2020 occurred in January 2021.

We distinguished below the case of entities that applied their judgement and concluded that (i) TLTRO III tranches include a government grant in the scope of IAS 20 *Accounting for Government Grants and Disclosure of Government assistance* and (ii) IFRS 9 applies to TLTO III tranches in their entirety—ie the tranches include no government grant.

- *Entities that concluded that TLTRO III tranches contained a government grant in the scope of IAS 20*

Those entities generally considered that the MRO rate was not the market interest rate. This is because there were few transactions to which this interest rate applied between June 2021 and June 2022. The statistics available on the ECB's website and shown in Appendix 1 to this letter provide evidence the MRO rate applied to relatively few transactions (€0.2 billion).

This contrasts with the number of the transactions which occurred in the context of the TLTRO III program whose outstanding amount is €2.2 trillion. A maximum [MRO–50bp] interest rate has applied to those transactions since June 2020—this maximum interest applies if banks do not achieve predefined lending performance thresholds.

Accordingly, those entities assessed that the rate at which banks could borrow from the ECB under the TLTRO III program without achieving the predefined lending performance was the market rate of interest.

Those entities also considered the following aspects when making their assessment:

- the ECB is the 'market maker'. Accordingly, it would be contradictory to conclude that change in an interest rate introduced by a market maker is not a change in the market rate.
- the rate of main refinancing operations is one of the three key ECB rates. As such, the MRO rate is a monetary decision from the Governing Council of the ECB. The reset of MRO rate is discrete over time (last reset to 0 per cent occurred on 18 September 2019). Absent any significant transactions at the current MRO rate, it is equivalent from the borrower perspective to get new refinancing operations from ECB at [MRO–50bp] or at a new MRO rate reset to -0.50 per cent.
- the ECB is able to reset unilaterally the rate at any point in time—ie it has the right to amend the rate at any time. The fact that the ECB's initial decision published 22 July 2019, was subsequently superseded by a decision on 30 April 2020, which was subsequently superseded by a decision on 29 January 2021 provides evidence of the ECB's 'market maker' capacity. Furthermore, the banks can voluntarily repay early (either partly or fully) as of September 2021 (refer to Q32 in the linked ECB site) with no penalty. This would support the view that the reduction in the 50bp fixed rate can be considered to reflect movements in market rates of interest.
- [MRO–50 bp] which now corresponds to [-50 bp] is consistent with the rates observed on the interbank market—see Ester and Euribor 1 Year in Appendix 2 to this letter.

In the light of the arguments set out above, we think that determining whether the 50bp reduction is a movement in market rate of interest requires the use of judgement based on the specific facts and circumstances. This is similar to the judgment required to determine whether an interest rate is a below-market rate on initial recognition. We also note in this regard that it would be contradictory to permit an entity to apply its judgement to assess whether a rate is a market rate on initial recognition of a TLTRO III tranche, and meanwhile, not permit that entity to apply its judgment on whether the reduction in that rate is a change that reflects a movement in the market rate.

- *Entities that concluded that IFRS 9 applies to TLTRO III tranches in their entirety*

Those entities generally considered that the ECB had defined as many market rates as there are permutations of different lending targets.

Appendix 3A to this letter presents the market rate that applied to TLTRO III transactions before the change the ECB made in January 2021. Appendix 3B to this letter presents the market rate after that date. The change resulted in the ECB defining a new lending target ASRP. If banks met this additional lending target, together with the three preexisting lending targets, the interest rate applied to their refinancing TLTRO III transactions moved from DFR to [DFR–50bp] with a floor at -1 per cent. Accordingly, those entities held the view that the ECB had defined a new interest rate that is linked to the new ASRP lending target.

For reasons similar to those described above—ie the ECB is (i) the 'market maker' and (ii) able to reset unilaterally the rate at any point in time—those entities considered that the change introduced in January 2021 change should lead them to assess that [DFR–50 bp] was the new market rate for the banks that met the new lending target (before that date, banks could borrow from the ECB at DFR rate if they met the three lending targets).

The same rationales would apply to the changes that the ECB made to any different permutation of the three first lending targets.

Here again, we think that determining whether the 50bp reduction is a movement in market rate of interest requires the use of judgement based on the specific facts and circumstances.

- ***Proposed way forward***

We think that the specific facts and circumstances relating to TLTRO III transactions require an entity to apply its judgment when assessing whether the 50bp reduction is a fixed or variable element. The Committee's observation as currently drafted in the ED is only a possible view.

Accordingly, we recommend the Committee delete the brackets '(*for example, the ECB rate on the main refinancing operations)*' and '*…(for example, the fixed 50 basis points discount given by the ECB on particular TLTRO III tranches for a fixed period)…*' in any final agenda decision. The agenda decision would read as follows:

> *… The Committee also observed that a floating-rate financial instrument may consist of a variable interest rate element, which is reset to reflect movements in the market rates of interest ~~(for example, the ECB rate on the main refinancing operations)~~ plus or minus other elements, which are fixed and therefore not reset to reflect movements in the market rates of interest ~~(for example, the fixed 50 basis points discount given by the ECB on particular TLTRO III tranches for a fixed period)~~…*

- **Interaction between IAS 20 and IFRS 9**

IAS 20 and IFRS 9 are two IFRS Standards which were developed at very different times—IAS 20 was originally issued in April 1983 whereas the completed version of IFRS 9 was published in July 2014. The joint application of these IFRS Standards gives rise to practical difficulties and seems to show that their interaction has never been thoroughly thought.

In particular, we note that their ongoing interaction is not entirely clear, most notably after an entity has initially recognised a government loan at a below-market rate applying paragraph 10A of IAS 20. We understand the TAD does not include any analysis on this matter and, if so, we agree with the Committee's approach in this respect.

We recommend the Committee not modify the scope of any final agenda decision to consider some aspects of the above-mentioned ongoing interaction—we think any analysis in this respect would go beyond the request received and would warrant specific (i) analysis from the Committee and (ii) proper exposure for comments.

Should you need any further information, please do not hesitate to contact me.

Yours sincerely,

Patrick de Cambourg

Patrick de Cambourg

Appendix 1—Data from Banque de France on MRO versus TLTRO III transactions

Opérations de refinancement en euro 2020				
Référence de l'opération	Date de valeur	Type d'opération	Montant alloué (en millions d'euros)	Date d'échéance
20210089	07/07/2021	MRO	72	14/07/2021
20210086	01/07/2021	LTRO	3	30/09/2021
20210085	30/06/2021	MRO	85	07/07/2021
20210081	24/06/2021	PELTRO	520	30/06/2022
20210078	24/06/2021	TLTRO III	109 829	26/06/2024
20210082	23/06/2021	MRO	91	30/06/2021
20210077	16/06/2021	MRO	124	23/06/2021
20210074	09/06/2021	MRO	185	16/06/2021
20210071	02/06/2021	MRO	197	09/06/2021
20210068	27/05/2021	LTRO	40	26/08/2021
20210067	26/05/2021	MRO	376	02/06/2021
20210064	19/05/2021	MRO	117	26/05/2021
20210061	12/05/2021	MRO	111	19/05/2021
20210058	05/05/2021	MRO	72	12/05/2021
20210055	29/04/2021	LTRO	25	29/07/2021
20210054	28/04/2021	MRO	252	05/05/2021
20210051	21/04/2021	MRO	126	28/04/2021
20210048	14/04/2021	MRO	137	21/04/2021
20210045	07/04/2021	MRO	190	14/04/2021
20210042	01/04/2021	LTRO	93	01/07/2021
20210041	31/03/2021	MRO	461	07/04/2021
20210038	25/03/2021	PELTRO	421	31/03/2022
20210034	24/03/2021	TLTRO III	330 501	27/03/2024
20210037	24/03/2021	MRO	271	31/03/2021
20210033	17/03/2021	MRO	609	24/03/2021
20210030	10/03/2021	MRO	22/11/1901	17/03/2021
20210027	03/03/2021	MRO	502	10/03/2021
20210024	25/02/2021	LTRO	30	27/05/2021
20210023	24/02/2021	MRO	622	03/03/2021
20210020	17/02/2021	MRO	459	24/02/2021
20210017	10/02/2021	MRO	427	17/02/2021
20210014	03/02/2021	MRO	157	10/02/2021
20210011	28/01/2021	LTRO	6	29/04/2021
20210010	27/01/2021	MRO	236	03/02/2021
20210007	20/01/2021	MRO	234	27/01/2021
20210004	13/01/2021	MRO	521	20/01/2021
20210001	06/01/2021	MRO	180	13/01/2021
20200248	16/12/2020	TLTRO III	50414	20/12/2023
20200244	03/12/2020	PELTRO	1681	29/07/2021
20200229	05/11/2020	PELTRO	747	29/07/2021
20200215	08/10/2020	PELTRO	1008	26/08/2021
20200207	30/09/2020	TLTRO III	174464	27/09/2023
20200195	03/09/2020	PELTRO	794	26/08/2021
20200174	06/08/2020	PELTRO	5684	30/09/2021
20200136	24/06/2020	PELTRO	15611	30/09/2021
20200131	24/06/2020	TLTRO III	1308433	28/06/2023
20200098	21/05/2020	PELTRO	851	30/09/2021
20200029	25/03/2020	TLTRO III	114979	29/03/2023
20190129	18/12/2019	TLTRO III	97718	21/12/2022
20190097	25/09/2019	TLTRO III	3396	28/09/2022

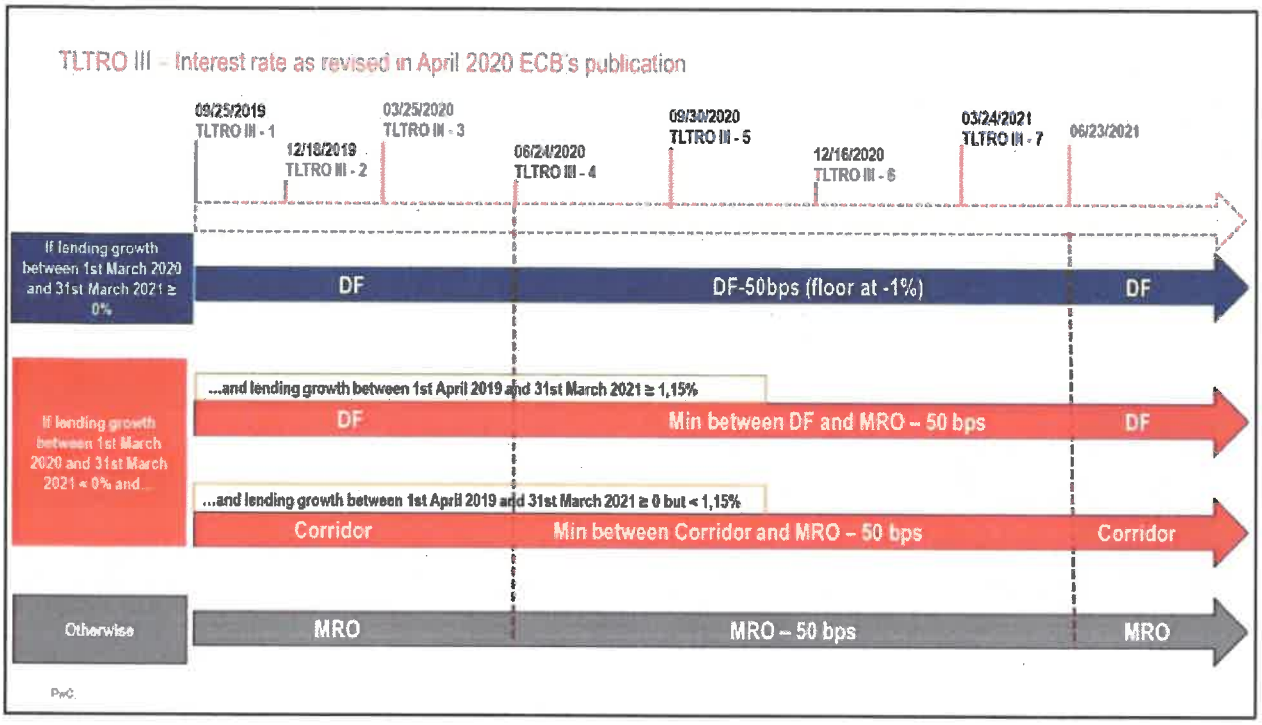
Somme de Montant				
Type d'opération	Années	Trimestres	Date de valeur	Total
⊟LTRO	⊞2021			197
Total LTRO				197
⊟MRO	⊞2021			7 506
Total MRO				7 506
⊟PELTRO	⊞2020			26 576
	⊞2021			941
Total PELTRO				27 517
⊟TLTRO III	⊞2019			101 114
	⊞2020			1 648 290
	⊞2021			440 330
Total TLTRO III				2 189 734
Total général				2 224 954

Average outstanding amount 200,16

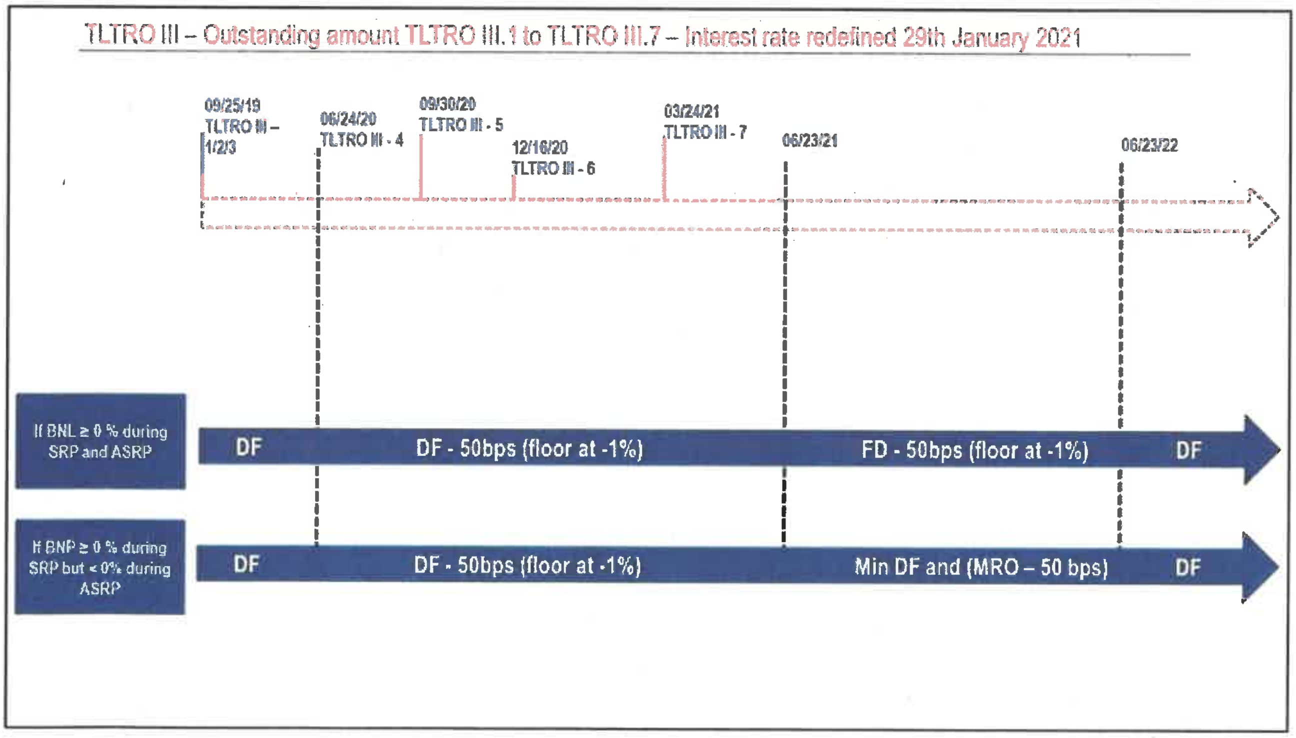
Appendix 2—Statistics of Ester and Euribor 12 months

DATE	EURIBOR 12M (%)	DATE	ESTER (%)
02/11/2020	-0,486	02/11/2020	-0,555
03/11/2020	-0,486	03/11/2020	-0,553
04/11/2020	-0,486	04/11/2020	-0,558
05/11/2020	-0,483	05/11/2020	-0,556
06/11/2020	-0,483	06/11/2020	-0,558
09/11/2020	-0,483	09/11/2020	-0,558
10/11/2020	-0,472	10/11/2020	-0,557
11/11/2020	-0,473	11/11/2020	-0,558
12/11/2020	-0,468	12/11/2020	-0,548
13/11/2020	-0,469	13/11/2020	-0,556
16/11/2020	-0,476	16/11/2020	-0,558
17/11/2020	-0,474	17/11/2020	-0,557
18/11/2020	-0,483	18/11/2020	-0,557
19/11/2020	-0,483	19/11/2020	-0,557
20/11/2020	-0,483	20/11/2020	-0,557
23/11/2020	-0,484	23/11/2020	-0,557
24/11/2020	-0,482	24/11/2020	-0,556
25/11/2020	-0,482	25/11/2020	-0,554
26/11/2020	-0,483	26/11/2020	-0,556
27/11/2020	-0,487	27/11/2020	-0,557
30/11/2020	-0,487	30/11/2020	-0,56
01/12/2020	-0,487	01/12/2020	-0,557
02/12/2020	-0,486	02/12/2020	-0,556
03/12/2020	-0,488	03/12/2020	-0,556
04/12/2020	-0,49	04/12/2020	-0,555
07/12/2020	-0,499	07/12/2020	-0,555
08/12/2020	-0,504	08/12/2020	-0,559
09/12/2020	-0,507	09/12/2020	-0,556
10/12/2020	-0,504	10/12/2020	-0,556
11/12/2020	-0,499	11/12/2020	-0,557
14/12/2020	-0,505	14/12/2020	-0,558
15/12/2020	-0,503	15/12/2020	-0,551
16/12/2020	-0,499	16/12/2020	-0,557
17/12/2020	-0,495	17/12/2020	-0,556
18/12/2020	-0,498	18/12/2020	-0,558
21/12/2020	-0,492	21/12/2020	-0,557
22/12/2020	-0,493	22/12/2020	-0,558
23/12/2020	-0,495	23/12/2020	-0,559
24/12/2020	-0,494	24/12/2020	-0,555
28/12/2020	-0,495	28/12/2020	-0,553
29/12/2020	-0,495	29/12/2020	-0,557
30/12/2020	-0,499	30/12/2020	-0,555
31/12/2020	-0,499	31/12/2020	-0,583
04/01/2021	-0,502	04/01/2021	-0,566
05/01/2021	-0,503	05/01/2021	-0,563
06/01/2021	-0,509	06/01/2021	-0,566
07/01/2021	-0,509	07/01/2021	-0,565
08/01/2021	-0,51	08/01/2021	-0,562
11/01/2021	-0,503	11/01/2021	-0,564
12/01/2021	-0,506	12/01/2021	-0,563
13/01/2021	-0,498	13/01/2021	-0,562
14/01/2021	-0,505	14/01/2021	-0,564
15/01/2021	-0,508	15/01/2021	-0,566
18/01/2021	-0,503	18/01/2021	-0,565
19/01/2021	-0,502	19/01/2021	-0,564
20/01/2021	-0,506	20/01/2021	-0,564
21/01/2021	-0,505	21/01/2021	-0,562
22/01/2021	-0,498	22/01/2021	-0,561
25/01/2021	-0,493	25/01/2021	-0,564
26/01/2021	-0,504	26/01/2021	-0,558
27/01/2021	-0,505	27/01/2021	-0,563
28/01/2021	-0,513	28/01/2021	-0,561
29/01/2021	-0,512	29/01/2021	-0,564
01/02/2021	-0,511	01/02/2021	-0,566
02/02/2021	-0,515	02/02/2021	-0,564
03/02/2021	-0,507	03/02/2021	-0,559
04/02/2021	-0,508	04/02/2021	-0,564
05/02/2021	-0,504	05/02/2021	-0,565
08/02/2021	-0,503	08/02/2021	-0,563
09/02/2021	-0,503	09/02/2021	-0,564
10/02/2021	-0,503	10/02/2021	-0,564
11/02/2021	-0,502	11/02/2021	-0,565
12/02/2021	-0,502	12/02/2021	-0,564
15/02/2021	-0,505	15/02/2021	-0,563
16/02/2021	-0,5	16/02/2021	-0,564
17/02/2021	-0,498	17/02/2021	-0,563
18/02/2021	-0,498	18/02/2021	-0,562
19/02/2021	-0,494	19/02/2021	-0,563
22/02/2021	-0,494	22/02/2021	-0,564
23/02/2021	-0,496	23/02/2021	-0,565
24/02/2021	-0,494	24/02/2021	-0,564
25/02/2021	-0,497	25/02/2021	-0,564
26/02/2021	-0,483	26/02/2021	-0,566

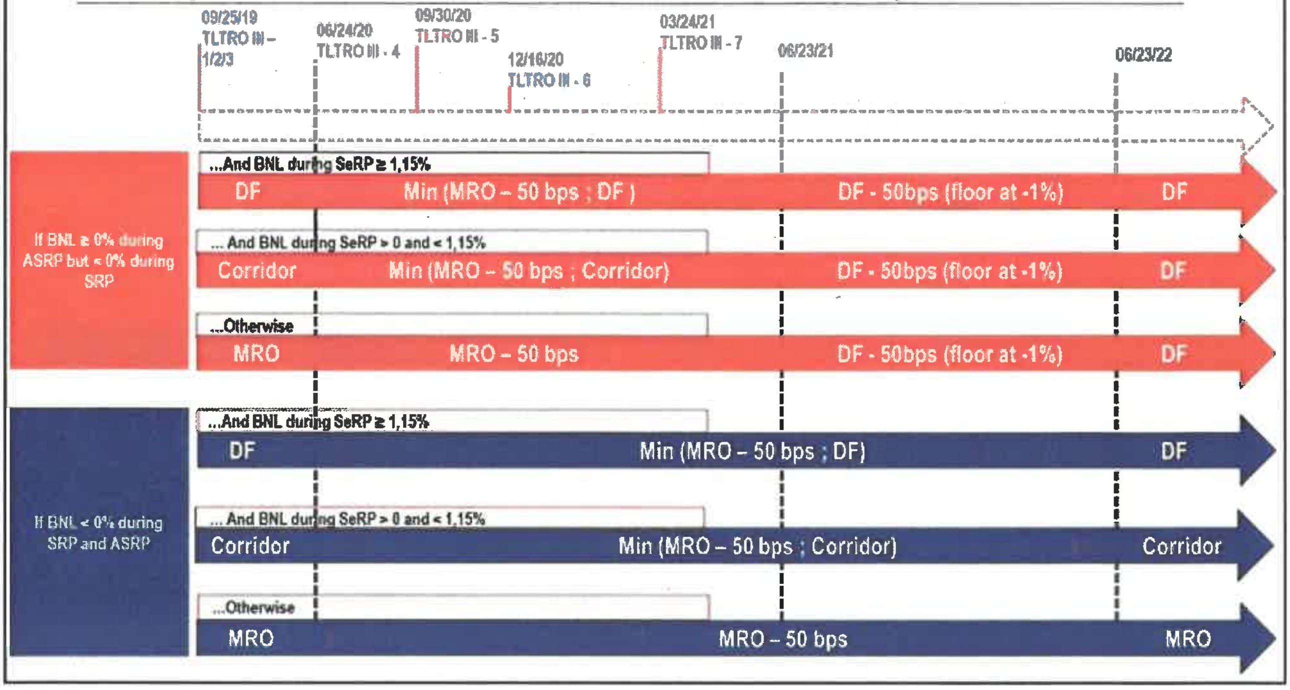
Appendix 3A—Interest rate applying to TLTRO III operations before January 2021



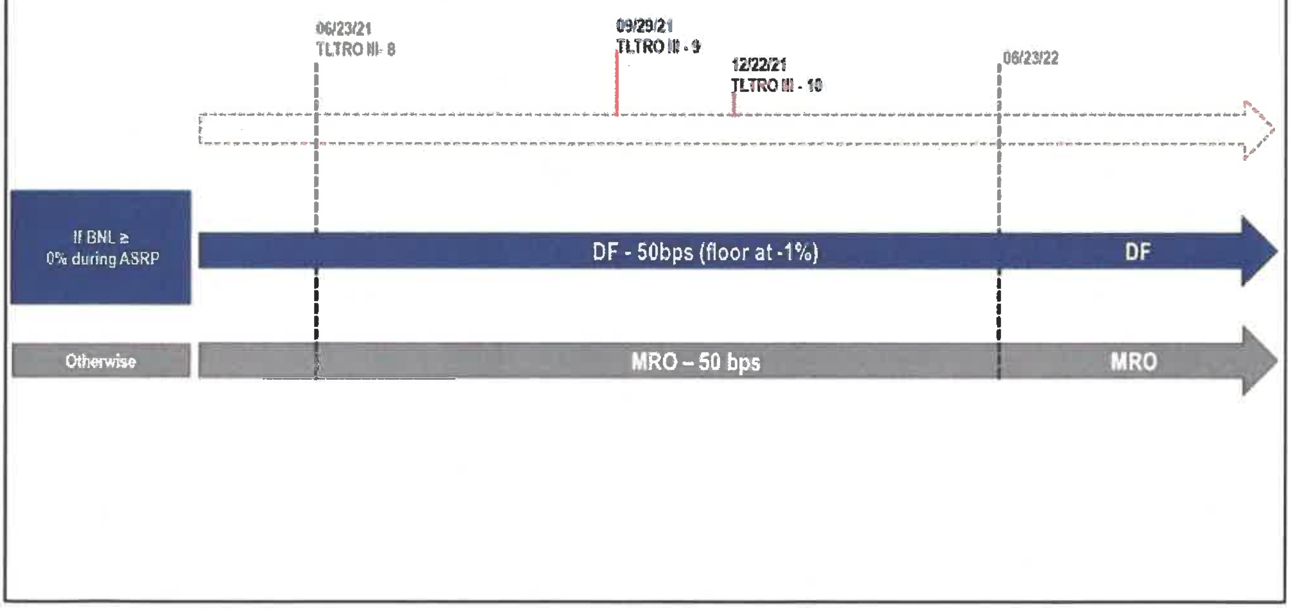
Appendix 3B—Interest rate applying to TLTRO III operations from January 2021 onwards



Outstanding amount TLTRO III.1 to TLTRO III.7 – Interest rate redefined 29th January 2021



Outstanding amount TLTRO III.8 to TLTRO III.10 – Interest rate defined 29th January 2021



BNP PARIBAS

Deputy Chief Financial Officer

Paris, August 4th, 2021

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June 2021 IFRIC Update—Feedback on the Tentative Agenda Decision TLTRO III Transactions (IFRS 9 and IAS 20)

We are pleased to provide BNP Paribas's views on the IFRS Interpretation Committee's (Committee) Tentative Agenda Decision (TAD), published in June 2021 on TLTRO III Transactions (IFRS 9 and IAS 20).

We generally agree with the Committee's tentative conclusion with the exception of the interpretation that the 50 basis points discount given by the ECB on particular TLTRO III tranches for a fixed period is not part of a market rate of interest. We think that the TAD should be modified to remove such interpretation as we think that there is an alternative valid interpretation. This is that the ECB as a central bank is not comparable to a standard market participant. As a central bank, the ECB is able to unilaterally set and amend the terms of its central bank lending facilities with no exception for TLTRO III. Accordingly, the rate set by the ECB for the TLTRO III tranche for a particular period is de facto a market rate of interest (similar to how the rate on the main refinancing operations is acknowledged as a market rate) even though expressed on the basis of other existing rates (MRO or DFR).

The TLTRO III scheme is specific and we don't think all relevant facts have been presented and considered in this analysis. In addition, as outlined in paragraph 41 of the agenda paper and discussed previously by the International Accounting Standards Board in October 2008, there is some judgement in determining how to interpret the term 'market rate' in this context. This certainly seems to be the case for rates that are set by central banks in their lending operations. Given the level of judgement required to determine whether the TLTRO III rate is a market rate or not, it would make sense that no decision be taken by the committee on this matter in the same manner as no decision is taken on whether TLTRO III tranches contain a grant.

We think the TAD should be amended to remove this part. Specifically, this could entail the following amendments:

"… The Committee also observed that a floating-rate financial instrument may consist of a variable interest rate element, which is reset to reflect movements in the market rates of interest ~~(for example, the ECB rate on the main refinancing operations)~~ plus or minus other elements, which are fixed and therefore not reset to reflect movements in the market rates of interest ~~(for example, the fixed 50 basis points discount given by the ECB on particular TLTRO III tranches for a fixed period)~~…"

We thank IFRIC for taking our views into consideration and remain available for any question regarding our comments.

Yours sincerely,

V Cott

Véronique Cotten

6 August 2021

Ms Sue Lloyd
Chair
IFRS Interpretations Committee
Columbus Building
7 Westferry Circus
Canary Wharf
London E14 4HD
United Kingdom

Dear Sue,

RE: Tentative agenda decision | TLTRO III Transactions (IFRS 9 Financial Instruments and IAS 20 Accounting for Government Grants and Disclosure of Government Assistance)

We are responding to your invitation to comment on the Tentative Agenda Decision (TAD) – TLTRO III Transactions (IFRS 9 Financial Instruments and IAS 20 Accounting for Government Grants and Disclosure of Government Assistance) published June 2021, on behalf of PricewaterhouseCoopers.

Following consultation with members of the PricewaterhouseCoopers network of firms, this response summarises the views of member firms who commented on the tentative agenda decision (TAD). "PricewaterhouseCoopers" refers to the network of member firms of PricewaterhouseCoopers International Limited, each of which is a separate and independent legal entity.

We understand that the Committee was asked to respond to a very specific fact pattern in the submission and that the analysis in the TAD is restricted to the questions the Committee was asked. We are concerned that there are multiple elements to the TLTRO III programme that require careful analysis and judgement, and we certainly appreciate the difficulty in addressing such a complex fact pattern in the context of an Agenda Decision. Overall, we do not believe the Committee should be addressing such complex individual transactions; and we agree that the questions of principle described in the request are part of a broader matter that IFRIC is not in a position to address, in isolation, in a cost-effective manner.

Furthermore, since the TAD is not conclusive on whether this transaction falls within the scope of IAS 20 versus IFRS 9, diversity in practice will not be resolved. Finally, we are concerned that the analysis in the TAD provides definitive guidance in certain specific areas while leaving other matters

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open to judgement, while at the same time also deferring other matters to the Post-Implementation review of IFRS 9. Given the potential for unintended consequences and the interconnected nature of the accounting issues, we believe it is better to remove the detailed analysis and defer resolution on matters of principles to the Board as part of the PIR of IFRS 9.

If IFRIC decides nonetheless to proceed with the more detailed Agenda Decision, our key concerns fall under the following headings: (1) Application of IFRS 9, (2) Matters for consideration in the PIR of IFRS 9, (3) Application of IAS 20 if IFRIC determines that IAS 20 is applicable.

1) Application of IFRS 9

We believe the TAD should more clearly separate the analysis of the changes to the terms of the TLTRO III between unconditional and conditional changes in interest rates.

Unconditional changes (i.e. the changes in interest rates introduced by the ECB that are not dependent on lending targets)

We agree in principle that a floating rate instrument may consist of both variable and fixed interest rate elements. However, we believe it is important to determine first whether the interest rate as a whole is a market floating rate, before considering whether the rate should be split into component parts.

We consider that determining whether the 50 basis point reduction of interest rate (i.e. the unconditional change) is a movement in the market rate in the very specific context of the ECB's TLTRO III programme is an area of judgement that should be based on the facts and circumstances. When considering whether the 50bp is a movement in the market rate, we believe that the analysis should have regard to:

> (1) the ECB's role as a market maker that has the ability to unilaterally reset the rates at any point in time, per the existing contractual terms. As stated on the ECB's website, the ECB uses a range of monetary policy tools to keep prices stable. The tools used by the ECB include setting key interest rates for the economy, lending to banks to support the flow of credit to households and businesses, and buying assets to help funding conditions in all parts of the economy; and
>
> (2) the absence of lending targets for market participants to be able to avail themselves of the rate.

Additionally, we note that the TAD acknowledges, in the context of initial recognition, that whether a rate is a market rate or not is a matter of judgement. Similarly, we believe that whether subsequent changes in the cash flows that are not linked to lending targets (i.e. that are unconditional) reflect changes in a market rate or not is also a matter of judgement. This judgement should also consider the analysis above, particularly the existing contractual terms under which the ECB has the ability to unilaterally reset the rates at any point in time. It would be inconsistent, in our mind, to allow judgement at initial recognition but not for subsequent measurement. Consequently, if the exercise of judgement leads to the conclusion that the changes in interest rates are changes in market rates, these changes should be recognised by applying B5.4.5.

Consequently, we suggest that the TAD be revised to remove the text in bold below:

> "The Committee also observed that a floating-rate financial instrument may consist of a variable interest rate element, which is reset to reflect movements in the market rates of interest **(for example, the ECB rate on the main refinancing operations)** plus or minus other elements, which are **fixed and therefore** not reset to reflect movements in the market rates of interest **(for example, the fixed 50 basis points discount given by the ECB on particular TLTRO III tranches for a fixed period)**.

Conditional changes (i.e. the changes in rates that will depend on lending targets)

We agree that paragraph B5.4.6 of IFRS 9 applies to changes in estimated future cash flows (that is, changes that are driven by whether or not a lending threshold is met).

2) Matters for consideration in the PIR of IFRS 9

We are concerned that the words in the TAD are inconsistent between the guidance given on the application of B5.4.6 and the matters for consideration in the PIR of IFRS 9. The following paragraphs appear to conflict with each other:

Specific guidance provided on IFRS 9 paragraph B5.4.6

> "Paragraph B5.4.6 of IFRS 9 applies to changes in estimated future cash flows of financial liabilities other than those dealt with in paragraph B5.4.5, irrespective of whether the change arises from a modification or another change in expectations."

Matters for consideration in the PIR of IFRS 9

> "The Committee observed that the question of whether conditions attached to the interest rate should be reflected in the estimates **and revisions of expected future cash flows** when determining the effective interest rate is part of a broader matter, which it should not analyse solely in the context of TLTRO III tranches. The Committee is therefore of the view that this matter should be considered as part of the post-implementation review of the classification and measurement requirements in IFRS 9, together with similar matters already identified in the first phase of that review."

The inconsistency arises from the paragraphs reproduced above (under the header 'specific guidance provided on IFRS 9 paragraph B5.4.6') which provide specific guidance that B5.4.6 applies to changes in estimated future cash flows, while the other paragraphs (under the header 'matters for consideration in the PIR of IFRS 9') suggest that the existing guidance does not address how revisions should be accounted for and that this should therefore be considered as part of the post-implementation review of IFRS 9.

The proposed wording may imply that there is judgement in determining how changes in expected future cash flows should be accounted for, rather than following the guidance in B5.4.6.

Also, we note some inconsistencies between the wording in the TAD and the guidance in IFRS 9 paragraph B 5.4.6, primarily the use of the words 'revisions' versus 'changes' and 'estimated future' versus ‘expected future’ cash flows.

Consequently, we suggest that the TAD be revised to remove the text highlighted in bold above, and also update the wording in the conclusion paragraph that refers to revisions rather than changes.

3) Application of IAS 20 if IFRIC determines that IAS 20 is applicable

If IFRIC determines that IAS 20 is the applicable standard, we agree that paragraph 10A of IAS 20 provides guidance on the accounting at initial recognition for a grant component embedded in a government loan that carries a below-market interest rate.

However, we are concerned with the application of paragraph 10A in isolation when there is conditionality associated with the grant component (i.e. conditions have to be met for an entity to be eligible for the below market rate of interest). The proposed drafting may be read to imply that any government grant component that is subsequently identified (for example, when the reasonable assurance threshold was not met at initial recognition, but is met at a later date) cannot be accounted for under IAS 20.

We disagree with a reading of IAS 20 that implies that a government grant associated with a loan at a below market rate can only be recognised at the initial recognition of the loan, for the following reasons:

- Paragraph 10A may be read to apply only to those loans when on initial recognition there is certainty that the interest rate will be at a below market rate of interest (i.e. an unconditional rate), and that loans where there is conditionality associated with the rate (and hence the grant) should be accounted for using the general requirements of IAS 20 in paragraphs 7, 9, 12, 20 and 32 both for initial recognition and for subsequent measurement of the `grant’ component.
- The overarching principle in paragraph 9 of IAS 20 which states that the manner in which a grant is provided should not affect the accounting thereof also needs to be considered.

Consequently, we believe that the TAD should be clarified to state that judgement should be applied in determining the applicable paragraphs in IAS 20, and that the principles highlighted in paragraphs 7, 9, 12, 20 and 32 also need to be considered.

If you have any questions in relation to this letter please do not hesitate to contact Henry Daubeney PwC Head of Reporting and Chief Accountant (henry.daubeney@pwc.com) or Marie Kling (marie.kling@pwc.com), Global IFRS Leader for Financial Instruments.

Yours faithfully

PricewaterhouseCoopers

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10 August 2021

Sue Lloyd
Chair
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United Kingdom

Dear Ms Lloyd

Tentative agenda decision – TLTRO III Transactions (IFRS 9 and IAS 20)

Deloitte Touche Tohmatsu Limited is pleased to respond to the IFRS Interpretations Committee's publication in the June 2021 Update of the tentative decision not to take onto the Committee's agenda the request for clarification on how to account for the third programme of the targeted longer-term refinancing operations (TLTROs) of the European Central Bank (ECB).

We generally agree with the analyses presented in the tentative agenda decision, except as noted below.

The tentative agenda decision states that:

"…floating-rate financial instrument may consist of a variable interest rate element, which is reset to reflect movements in the market rates of interest (for example, the ECB rate on the main refinancing operations) plus or minus other elements, which are fixed and therefore not reset to reflect movements in the market rates of interest (for example, the fixed 50 basis points discount given by the ECB on particular TLTRO III tranches for a fixed period)."

The fact that the fixed 50 basis point discount given by the ECB is presented as an example of a fixed element that does not reflect movements in market rates of interest may be read to imply that the overall interest rate on the TLTRO III is necessarily not a market rate of interest. Determining whether a change in estimated cash flows reflects movements in market rates of interest for the purposes of assessing whether IFRS 9:B5.4.5 or IFRS 9:B5.4.6 applies can be a challenging judgement in many circumstances (as it was also under the equivalent requirements in IAS 39, paragraphs AG7 and AG8 respectively). This judgement is particularly challenging when assessing interest rates on funding by a central bank, given that one of the roles of central banks is to set market rates of interest. In the case of the TLTRO III, the rate is not set as a result of a negotiation between the ECB and the borrowers. Instead, the ECB has a unilateral right to change the rate of interest. We suggest that the difficulties inherent in the assessment of whether an interest rate is a market rate, including but not only in the case of funding provided by central banks, may be an area to be considered as part of the post-implementation review of the classification and measurement requirements in IFRS 9. In the meantime, we believe that it would be preferable if the agenda decision did not include a conclusion on the effect of the 50-basis point discount given by the ECB on TLTRO III tranches.

Deloitte.

Additionally, the tentative agenda decision addresses the application of IAS 20:10A (on the benefit of a government loan at a below-market rate of interest) only in the context of initial recognition of the loan. It does not address whether a grant may be recognised in the case of:

a) a bank that, at initial recognition, had no reasonable assurance that it will be eligible for receiving the grant, but subsequently obtains reasonable assurance, e.g. because the relevant thresholds have been met; or

b) a change in terms and conditions applicable to the TLTRO III tranches that does not lead to derecognition of drawn TLTRO III tranches.

Whilst IAS 20:10A addresses measurement of the grant by reference to the initial carrying amount of the loan, it can be argued that this paragraph applies at the date when the requirements for initial recognition of a grant in IAS 20:7 are met (i.e. when reasonable assurance exists that the entity will meet the conditions attached to the grant and that the grant will be received). This may be at a date that is not the date of initial recognition of the loan. Indeed, in the case of the TLTRO III tranches, the conditions in IAS 20:7 may not be met until there is reasonable assurance on whether the relevant thresholds are met or the TLTRO terms and conditions have changed which may be at a date after the loan is initially recognised. We believe the agenda decision would benefit from clarifying whether IAS 20:10A would permit a grant being recognised at that later date.

If you have any questions concerning our comments, please contact Andrew Spooner in London at +44 (0) 20 7007 0204.

Yours sincerely

Veronica Poole
Global IFRS Leader

ING

To
Ms Sue Lloyd
Chair
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Date	**Contact**	**Page**
12 August 2021	Tina Farington (Tina.Farington@ing.com)	1 of 3

Subject
Tentative Agenda Decision: TLTRO III Transactions (IFRS 9 and IAS 20)

Dear Ms Lloyd,

We appreciate the opportunity to comment on the tentative agenda decision (TAD) of the IFRS Interpretation Committee (IFRIC) published in June 2021 regarding TLTRO III Transactions.

TLTRO III is a unique and complex instrument. To account for it under IFRS requires a detailed analysis of the economic conditions (and the context) of the TLTRO III funding when making complex judgments such as:

- what constitutes a market rate (especially in the context of TLTRO when the rate is set by the ECB as a market maker within its monetary policy mandate);
- definition of government, government agencies and similar bodies;
- definitions of floating and fixed rates in IFRS, including the lack of clarity of the scope of IFRS 9.B5.4.5; and
- incorporation of expectations of meeting conditions into the effective interest rate (EIR) at initial recognition.

We appreciate the IFRIC's attention to this material topic and efforts to reduce diversity in this area – it is a challenging request. However, for the reasons described below, we would propose to delete the new application guidance included in section '*subsequent measurement of the financial liability at amortised cost*' of the TAD as detailed in the Appendix. Such suggestion would keep the IFRS 9 related wording neutral (i.e. without introducing definitions not already included in IFRS 9), in line with the rest of the TAD. We also believe that the application of the EIR for instruments where the interest rate is conditional/variable, defining floating rate instruments (or the concept of a hybrid instrument) and setting the scope of IFRS 9.B5.4.5 is better suited for a post-implementation review (PIR) of IFRS 9. Our recommendation is supported by the following:

a. Our particular concern is around the fact that the TAD introduces terms not currently defined in IFRS 9, such as 'variable interest rate element of a floating-rate' and 'a fixed element of a floating rate' and provides a prescriptive interpretation of those new terms for TLTRO III instrument by concluding that the 50bps discount given by the ECB on particular TLTRO III tranches for a fixed period is a fixed element as well as that the MRO rate is the market rate of interest (while at the same time not concluding on the market rate of interest for this instrument). To date, IFRS 9 has not been prescriptive in what is meant by floating rate (IFRIC - July 2008 agenda decision) and, the IASB has not issued further guidance to clarify it. When applying the guidance in IFRS 9, in our view, the ECB is the market maker in the TLTRO funding within its monetary policy mandate and different approaches to set the TLTRO rate could have been implemented with the same economic effects (e.g. an all-in-one interest rate). The interest mechanism set by the ECB behaves differently and is structured with a different purpose than a traditional benchmark rate plus a spread (for instance, the unconditional 50bps discount is given to all banks participating in the TLTRO, irrespective of the credit quality of the banks). With the current principles in IFRS 9.B5.4.5 on what constitutes a floating rate and a market rate we believe, this is a judgment where different views may be supported in practice (and better reflect the substance that users can understand) and should be accompanied by transparent disclosures. Following the above, we believe, it would not be unreasonable for financial institutions to conclude that the conditional and unconditional ECB interest rates as a whole are market floating interest rates, and that changes in these floating rates should therefore be recognised by applying IFRS 9.B5.4.5.

b. We question whether this is the right setting to conclude on such a fundamental aspect of IFRS 9 (interpretation of what is a floating rate and application of EIR) without comprehensive and focused deliberation. Issuing a prescriptive rules based guidance for one of the most complex interest rate mechanisms in practice creates a risk of unintended consequences to other instruments. This is another reason we encourage the IFRIC and the IASB to either consider this topic in the PIR of IFRS 9 or refresh the previous submission on this topic to the IFRIC where it was not previously concluded.

c. Current diversity in practice suggests that there is more than one way of looking at the above complexities whether in IAS 20 or IFRS 9. However, we believe that the TAD, as currently drafted, will not eliminate such diversity in practice. To the contrary, we believe it may lead to a wider gap in the outcomes in the same reporting periods between financial institutions. We note the risk of a neutral interpretation of IAS 20 where multiple views have been taken combined with the prescriptive guidance that introduces new concepts currently not defined in IFRS 9 could further exacerbate the issue.

   For example, a narrow application of the modification guidance to a fixed element under IFRS 9 (for instance, modification of the terms by the ECB in January/February 2021) would lead you to a large one off recognition of income (as changes in cash flows are unlikely to be a substantial modification). However, this measurement impact may not be visible in IAS 20 if one takes the view that this is a substantial modification (i.e. qualitatively, due to a new government grant). This would lead to inconsistent accounting treatment with significantly different accounting results (given the size of such borrowings) for identical economic facts. This would reduce the ability to compare results between financial institutions. While we do not propose to add further interpretation guidance for IAS 20, this example highlights the challenge we see of being prescriptive in IFRS 9.

If you have any questions regarding our comment letter, please contact Tina Farington (Tina.Farington@ing.com), Head of Policies and Procedures, or Irina Lukicheva (Irina.Lukicheva@ing.com), Head of IFRS Policies. We would be pleased to provide further insight into our comments.

Yours sincerely,

Tina Farington
Head of Policies and Procedures ING Group

Appendix

"Subsequent measurement of the financial liability at amortised cost
The contractual terms of the TLTRO III tranches require interest to be settled in arrears on maturity or on early repayment of each tranche. There is therefore only one cash flow on settlement of the instrument.
The original effective interest rate is calculated based on estimated future cash flows at initial recognition as required by IFRS 9. The Committee noted that whether a bank adjusts the effective interest rate over the life of a tranche depends on the contractual terms of the financial liability and the applicable requirements in IFRS 9. 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 the 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 the market rates of interest—is a floating-rate financial instrument.

~~The Committee also observed that a floating-rate financial instrument may consist of a variable interest rate element, which is reset to reflect movements in the market rates of interest (for example, the ECB rate on the main refinancing operations) plus or minus other elements, which are fixed and therefore not reset to reflect movements in the market rates of interest (for example, the fixed 50 basis points discount given by the ECB on particular TLTRO III tranches for a fixed period).~~

~~When considering how to account for changes in cash flow estimates, the Committee noted that paragraph B5.4.5 of IFRS 9 applies only to the variable interest rate element of a floating-rate instrument (as far as it reflects movements in the market rates of interest) and not to other interest rate elements of the instrument (which are typically not reset to reflect movements in the market rates of interest).~~

Paragraph B5.4.6 of IFRS 9 applies to changes in estimated future cash flows of financial liabilities other than those dealt with in paragraph B5.4.5, irrespective of whether the change arises from a modification or another change in expectations. However, when changes in contractual cash flows arise from a modification, an entity assesses whether those changes result in the derecognition of the financial liability and the initial recognition of a new financial liability by applying paragraphs 3.3.2 and B3.3.6 of IFRS 9.

The Committee considered a situation in which, as a result of a modification that does not result in derecognition or other changes in expected future cash flows, a bank estimates the final repayment cash flow relating to a TLTRO III tranche to be different from that used in determining the carrying amount. In such a situation, the bank adjusts the carrying amount to reflect the modification or other change in expected future cash flows and recognises the difference immediately in profit or loss. The bank therefore makes no adjustment to interest recognised in prior periods.

The Committee also noted that application of paragraph B5.4.6 of IFRS 9 relates to a bank's estimates of expected future cash flows in calculating the effective interest rate on initial recognition of the financial liability. This is because, applying B5.4.6, the original effective interest rate is used to discount the revised cash flows.
The Committee observed that the question of whether conditions attached to the interest rate should be reflected in the estimates and revisions of expected future cash flows when determining the effective interest rate is part of a broader matter, which it should not analyse solely in the context of TLTRO III tranches. The Committee is therefore of the view that this matter should be considered as part of the post-implementation review of the classification and measurement requirements in IFRS 9, together with similar matters already identified in the first phase of that review".

16 August 2021

Ms. Sue Lloyd
Chair
IFRS Interpretations Committee
Columbus Building
7 Westferry Circus
Canary Wharf
London E14 4HD
United Kingdom

Dear Ms. Lloyd,

IFRS Interpretations Committee Tentative Agenda Decisions

The Malaysian Accounting Standards Board (MASB) welcomes the opportunity to provide comments on the following Tentative Agenda Decisions:

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

(b) Economic Benefits from Use of a Windfarm (IFRS 16 *Leases*)

We agree with the Interpretations Committee's reasons set out in the respective Tentative Agenda Decisions for not adding these items onto to the work plan.

If you need further clarification, please contact the undersigned by email at beeleng@masb.org.my or at +603 2273 3100.

Thank you.

Yours sincerely,

TAN BEE LENG
Executive Director

afme/ Finance for Europe

Submitted electronically via **www.ifrs.org** website

16 August 2021

Dear Sir / Madam,

The IFRS Interpretations Committee's Tentative Agenda Decision: *TLTRO III Transactions (IFRS 9 and IAS 20)*

The Association for Financial Markets in Europe (AFME) welcomes the opportunity to comment on the Tentative Agenda Decision: *TLTRO III Transactions (IFRS 9 and IAS 20)*[1] ("Tentative Agenda Decision" or "TAD") by the IFRS Interpretations Committee ("IFRIC" or "Committee").

TLTRO III funding is a complex and unique instrument which raises many accounting questions. To name a few, they include what constitutes a 'market rate', a 'floating rate' and a 'fixed rate'; how expectations regarding conditional interest should be incorporated into the application of the effective interest rate. For all of these items, a detailed analysis of the TLTRO III program as well as judgement are required.

We appreciate the analysis undertaken by IFRIC to help address this issue, however, we are concerned with the statement in the TAD that *the fixed 50 basis points discount given by the ECB on particular TLTRO III tranches for a fixed period represent a fixed element of a floating rate*, rather than being viewed as a variable interest rate element of a floating rate. We note that the terms of TLTRO III were modified by the ECB at its sole discretion already four times, including interest rates. Such modifications introduced unconditional interest, changed its size (from 25bps to 50bps) and increased the period in which it applies. Following this, our members consider it should be a matter of judgment as to whether this discount is viewed as a variable interest element of the floating rate on the basis that this is different than a standard benchmark rate with a fixed spread. For example, the ECB, in their capacity as a market maker and as part of its monetary policy mandate, could have chosen to create an 'all-in-one-rate' (new 'TLTRO rate') or can create it in the future, and change it over time to reflect the same economics instead of using the existing MRO rate as a starting point and adding 50 bps to it in certain periods. Such all-in-one rate would have been seen as a floating rate. Therefore, we believe, there are different supportable views on this matter, and we propose that the relevant sentence in the TAD should be removed, ie the sentence which concludes with the words *"for example, the fixed 50 basis points discount given by the ECB on particular TLTRO III tranches for a fixed period".*

Based on the above, we would appreciate if the TAD remained more neutral on the application of IFRS 9. We would propose removing the explicit conclusion on unconditional 50bps being a fixed element and leaving it up to the judgement of preparers. We would like to note that IFRS is not prescriptive in what is meant by a floating rate and IFRIC did not conclude on this wider matter in the past (July 2008). Given the broader nature and potential wide-spread implications of such matters as what constitutes market, floating and fixed rates

[1] https://www.ifrs.org/projects/work-plan/tltro-iii-transactions-ifrs-9-and-ias-20/tentative-agenda-decision-and-comment-letters/

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as well as the application of the effective interest rate when future cash flows are conditional, we believe that these topics are better suited for a post implementation review of IFRS 9.

We thank IFRIC for taking our views into consideration and we remain available to discuss the content of this letter or to provide any further clarity with regard to the statements made.

Yours faithfully,

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About AFME

AFME (Association for Financial Markets in Europe) advocates for deep and integrated European capital markets which serve the needs of companies and investors, supporting economic growth and benefiting society. AFME is the voice of all Europe's wholesale financial markets, providing expertise across a broad range of regulatory and capital markets issues. AFME aims to act as a bridge between market participants and policy makers across Europe, drawing on its strong and long-standing relationships, its technical knowledge and fact-based work. Its members comprise pan-EU and global banks as well as key regional banks, brokers, law firms, investors and other financial market participants. AFME participates in a global alliance with the Securities Industry and Financial Markets Association (SIFMA) in the US, and the Asia Securities Industry and Financial Markets Association (ASIFMA) through the GFMA (Global Financial Markets Association). For more information please visit the AFME website: www.afme.eu. Follow us on Twitter @AFME_EU

International Organization of Securities Commissions
Organisation internationale des commissions de valeurs
Organização Internacional das Comissões de Valores
Organización Internacional de Comisiones de Valores
المنظمة الدولية لهيئات الأوراق المالية

16 August 2021

Ms. Sue Lloyd
Chair of the IFRS Interpretations Committee
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Our REF: 2021/O/C1/IFRIC/MS/56

RE: Tentative Agenda Decision – TLTRO III Transactions (IFRS 9 and IAS 20)

Dear Ms. Lloyd,

The International Organization of Securities Commissions (IOSCO) Committee on Issuer Accounting, Auditing and Disclosure (Committee 1) thanks you for the opportunity to provide our comments on the IFRS Interpretations Committee (IFRS IC) tentative agenda decision, *TLTRO III Transactions* (TAD).

IOSCO is committed to promoting the integrity of the international markets through promotion of high quality accounting standards, including rigorous application and enforcement. Members of Committee 1 seek to further IOSCO's mission through thoughtful consideration of accounting and disclosure concerns and pursuit of improved transparency of global financial reporting. The comments we have provided herein reflect the general consensus among the members of Committee 1 and are not intended to include all of the comments that might be provided by individual securities regulator members on behalf of their respective jurisdictions.

We appreciate the IFRS IC addressing this topic to support preparers in their application of International Financial Reporting Standard (IFRS) 9, *Financial Instruments* (IFRS 9) and International Accounting Standard (IAS) 20, *Accounting for Government Grants and Disclosure of Government Assistance* (IAS 20) to the fact pattern submitted. We do not disagree with the explanations provided in the TAD with regard to the application of IFRS 9 to the fact pattern in the submission, however, some members of Committee 1 believe that the IFRS IC should provide further guidance regarding whether the conditions attached to the interest rate should be reflected in the estimates and revisions of expected future cash flows when determining the effective interest rate. Those members do not believe that waiting to address the issue as part of the IFRS 9 post-implementation review will provide a timely response for entities participating in the TLTRO III or other refinancing programs in the near future.

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With regard to the applicability of IAS 20, we acknowledge that this determination requires judgment. However, given the specificity of the facts and circumstances presented in the submission, we believe the IFRS IC has the ability to make the necessary judgments to reach conclusions regarding the applicability of IAS 20 and could include those conclusions in a final agenda decision. Further, given the broad applicability of the issue, we believe it is important to reduce the accounting diversity that currently exists amongst issuers that receive TLTRO III loans.

Specifically, we believe the IFRS IC can conclude on whether the interest rates on the TLTRO III loans represent a below-market rate. Some Committee 1 members believe that the European Central Bank (ECB) uses the TLTRO program as part of its monetary policy objectives to set market rates and makes the same arrangements available to all qualifying institutions. Thus, because the ECB is the market-maker with respect to these arrangements, they do not believe that the arrangements represent below-market rates of interest as per IAS 20. Meanwhile, other Committee 1 members believe that the interest rate on the loans, when considering the adjustments for meeting various lending thresholds and the basis points reduction in response to the Covid-19 pandemic, do represent a below-market rate of interest. Further, we believe the IFRS IC could conclude on whether the ECB represents an international government, governmental agency or similar body, as defined in IAS 20. Members believe that these are questions where the IFRS IC could provide guidance on how to evaluate whether central bank programs constitute below market rates and whether an international central bank constitutes an international government, governmental agency or similar body and in doing so, the IFRS IC could reduce diversity in practice.

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We appreciate your thoughtful consideration of the views provided in this letter.

If you have any questions or need additional information, please do not hesitate to contact Cameron McInnis, Chair of the Accounting Subcommittee of Committee 1 at +1 416-593-3675 or myself. In case of any written communication, please mark a copy to me.

Yours sincerely,

Makoto Sonoda
Chair
Committee on Issuer, Accounting, Audit and Disclosure
International Organization of Securities Commissions

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16 August 2021

Dear IFRS Interpretations Committee members,

Invitation to comment – Tentative Agenda Decision (TAD): TLTRO III Transactions (IFRS 9 *Financial Instruments* and IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance*)

Ernst & Young Global Limited, the central coordinating entity of the global EY organisation, welcomes the opportunity to offer its views on the above tentative agenda decision of the IFRS Interpretations Committee (the Committee or IFRS IC) published in the June 2021 *IFRIC Update*.

The Committee discussed how to account for the third programme of the targeted longer-term refinancing operations (TLTROs) of the European Central Bank (ECB). The tentative agenda decision (TAD) proposes that such finance would primarily fall within the scope of IFRS 9 *Financial Instruments*. If there is an off-market component at inception, there might be a difference to account for as a government grant within the scope of IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance*. It is only if that component was provided by government in a transaction that can be distinguished from the borrowing bank's normal trading operations that it would represent a government grant within the scope of IAS 20.

We have highlighted four key areas below in which we believe the tentative agenda decision can be enhanced.

<u>The interpretation of 'similar bodies' as contemplated in the definition of 'government' in IAS 20</u>

The TAD states that determining whether TLTRO III tranches contain a government grant requires judgement based on the specific facts and circumstances. The Committee observes 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.

One of the considerations is whether the ECB meets the definition of government in IAS 20. Paragraph 3 of IAS 20 defines government as 'government, government agencies and similar bodies whether local, national or international'. The latter part of the definition, 'similar bodies whether local, national or international' is not defined further in the standard. Determining whether organisations such as the ECB meet the definition of government is a critical element of the fact pattern to interpret.

We find ourselves at a time when there are widespread efforts to provide economic and fiscal support internationally and locally, whether to combat the effect of the COVID-19 pandemic or for other reasons. In many cases, these efforts are co-ordinated by public agencies that act on behalf of the government in distributing funding (e.g., international agencies that are not politically controlled by a single government but are involved in the funding of vaccine development against COVID-19 or malaria), rather than directly by central governments. Therefore, if resources received from such entities are to be consistently accounted for and presented in the financial statements of recipients, the interpretation of 'similar bodies' is of great importance, not just within the context of TLTRO III.

By leaving the assessment of 'similar bodies' open to judgement and not providing further guidance on what should be considered, the TAD may inadvertently lead to increased diversity in practice amongst recipients of such resources.

Therefore, we recommend that the Committee expands the TAD to provide guidance on what factors would be relevant in determining whether such 'similar bodies' could be regarded as government for these purposes. If the Committee does not believe they can address this, we recommend that it be addressed by the Board. Given the current volume of support measures, it would be helpful if the Committee could provide additional guidance sooner rather than deferring the matter to a potential standard setting project.

<u>The interaction between IAS 20 and IFRS 9</u>

The TAD states that "if a bank determines that the fair value of a TLTRO III tranche at initial recognition differs from the transaction price and that the consideration received is for more than just the financial liability, the bank assesses whether that difference represents a government grant as defined in IAS 20. The Committee noted that if the difference represents a government grant, paragraph 10A of IAS 20 applies only to that difference."

This wording suggests that the measurement of any grant is constrained to the amount determined on initial recognition of the liability unless an event occurs that leads to the derecognition of the original liabilities and recognition of new obligations. This would mean that the grant measurement cannot be reassessed subsequently should either the scheme itself, or expectations about meeting the scheme's criteria, change in a manner that does not constitute a derecognition event. This seems to contradict the definition of a government grant in paragraph 3 of IAS 20, which refers to "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". The definition in paragraph 3 does not limit a government grant to amounts identified at initial recognition of a transaction.

During the July IFRS IC meeting, the staff explained that this wording in the TAD was meant to clarify that the entire loan is not in the scope of IAS 20; only the grant portion is in scope of IAS 20. We believe that this point can still be made without suggesting that an additional grant component cannot be identified after initial recognition. The current wording may have unintended consequences.

For example, in measuring the fair value of the loan at initial recognition, market participants would probability-weight the likelihood of the bank meeting its lending targets and, therefore, receiving the more favourable rate. Unless it is either 0% or 100% likely that the bank will meet the targets (both when the tranche is drawn and in the final outcome), the difference between the fair value of the liability and the transaction price will not be the same as the ultimate amount of benefit that the bank receives from the ECB. Even if there is reasonable assurance and the full benefit is subsequently received, the amount of the grant as measured under paragraph 10A on initial recognition will not be equal to the benefit that is ultimately received. It seems inconsistent with the definition of a government grant in paragraph 3 of IAS 20 not to update the measurement of the government grant to include the full transfer of resources to the entity, especially as the definition considers that the transfer of resources may be in return for past or future compliance with certain conditions (which an entity may not be certain of meeting at inception).

Additionally, consider an on-market loan that is issued by government and the interest or principal obligations are subsequently reduced. Unless this modification results in derecognition of the original loan, the wording in the TAD suggests that paragraph 10A, being only applicable at initial recognition of the loan, would not apply. Judgement would then need to be exercised in determining whether the reduction is within the scope of IAS 20 or IFRS 9, using other paragraphs and the general definition of a government grant in IAS 20. We provide an example of how this judgement could be made by using the guidance in paragraph 10 of IAS 20 below. We see little reason to have different treatment for subsequent reductions based on whether the initial loan did, or did not, contain a government grant. Therefore, we believe that the TAD is too restrictive in not allowing for judgement to be exercised for events that occur after initial recognition of government loans.

The reference in the TAD to the application of paragraph 10A of IAS 20 indicates that the guidance on forgivable loans in paragraph 10 of IAS 20 is not applicable. The TLTRO III fact pattern is very similar to a forgivable loan because the potential benefit provided to a bank, should it meet the conditions, is akin to waiving interest cash payments[1] that the bank would otherwise be obliged to make. While the definition of a forgivable loan refers to waiving repayment under certain prescribed conditions, we do not believe this has to be read as referring to waivers of the principal amount only.

Paragraph 9 of IAS 20 sets out a clear principle that the manner in which a grant is received does not affect the accounting method to be adopted in regard to the grant. As an example, it

[1] The daily facility rate (DFR) is the rate offered to banks on their deposits with the ECB. The main refinancing operations (MRO) rate is the rate charged by the ECB to banks to borrow money. The ECB's monetary policy guidance explains that the DFR and MRO rates act as a floor and a cap to the overnight money market respectively, thereby setting a corridor within which overnight money market rates can fluctuate. Therefore, the potential switch from the higher MRO rate to the lower DFR as contemplated in the contingent pricing of TLTRO III is akin to forgiving interest charges that would have arisen under the higher MRO rate even if the quantum of this potential waiver is not known at initial recognition of the loan.

states that a grant is accounted for in the same manner whether it is received in cash or as a reduction of a liability to the government. Interest accrued is a liability to the central bank. Therefore, if accrued interest is revised downwards due to the entity meeting the prescribed conditions, this is a reduction in a liability.

Paragraph 10A aims to clarify that the loan which 'hosts' the grant is in the scope of IFRS 9 and should, therefore, give rise to imputation of interest. This is confirmed by paragraph BC3 to IAS 20. However, paragraph 10A does not address situations in which contingent rates indexed to specific performance targets result in a variable amount of grant. This is why we believe it is reasonable to refer to the principles in paragraphs 3 and 9 of IAS 20, as well as the more specific guidance on forgivable loans (i.e., subject to prescribed conditions) in order to reflect the contingent feature of the TLTRO III rate.

In light of the above, we recommend revising the TAD to clarify that the identification of a government grant is not limited to initial recognition. This could be done by stating that the example in the TAD regarding the application of paragraph 10A illustrates a possible approach at initial recognition for a below-market loan, but does not consider the accounting for additional benefits subsequently granted by government through further decreases in the rate or for a change in a contingent rate indexed on the entity's ability to meet defined conditions.

Application of B5.4.6 to subsequent changes in rate announced by the ECB

The TAD states that,

> "The Committee also observed that a floating rate financial instrument may consist of a variable interest rate element, which is reset to reflect movements in the market rates of interest (for example, the ECB rate on the main refinancing operations) plus or minus other elements, which are fixed and, therefore, not reset to reflect movements in the market rates of interest (for example, the fixed 50 basis points discount given by the ECB on particular TLTRO III tranches for a fixed period).
>
> When considering how to account for changes in cash flow estimates, the Committee noted that paragraph B5.4.5 of IFRS 9 applies only to the variable interest rate element of a floating rate instrument (as far as it reflects movements in the market rates of interest) and not to other interest rate elements of the instrument (which are typically not reset to reflect movements in the market rates of interest).
>
> Paragraph B5.4.6 of IFRS 9 applies to changes in estimated future cash flows of financial liabilities other than those dealt with in paragraph B5.4.5, irrespective of whether the change arises from a modification or another change in expectations".

This guidance appears contradictory to the earlier guidance in the TAD that judgement needs to be applied when determining whether the TLTRO III tranches contain a government grant. By saying that changes to the 50 basis points (bps) spread are not in scope of paragraph B5.4.5, the Committee seems to indicate that the overall rate is not a market rate despite this being a question that the Committee sought not to answer in the first place.

In addition, we believe there is an argument to allow judgement to support that the TLTRO III rate is a market rate and that paragraph B5.4.5 would, therefore, be applicable to changes in the 50bps spread, rather than requiring the application of paragraph B5.4.6. The ECB's monetary policy guidance[2] describes the TLTRO III programme as being an additional tool for the ECB to set rates and drive liquidity. The guidance makes it clear that the ECB is setting the TLTRO III rate just as it sets the MRO rate and the DFR. The TLTRO III rate and related performance targets have been unilaterally amended four times since July 2019, illustrating how the ECB uses this rate to drive liquidity within the Eurozone.

Therefore, we believe the wording used in the TAD is too strict in requiring these changes to be accounted for using paragraph B5.4.6. We believe it also makes sense to see them as grants or as changes to a market rate, or at least to allow entities to apply judgement. We recommend that the Committee reconsiders the wording in the TAD accordingly.

Whether conditions attached to the interest rate should be reflected in the estimates and revisions of expected future cash flows when determining the effective interest rate

In the TAD, the Committee observes that this is part of a broader matter and should be covered in the Post-implementation Review (PIR) of IFRS 9.

If the TLTRO III loans are judged not to contain an element of government grant, we understand IFRS 9 to be clear that, in most cases, changes in estimates of contingent rates (where those changes are neither due to separable embedded derivatives nor changes in market rates) would give rise to an adjustment under paragraph B5.4.6.
Our concern is that by stating that this question needs to be deferred to the PIR, it may lead entities to believe that there is room not to apply paragraph B5.4.6 in such cases. This could lead to renewed diversity in practice.

Where IFRS 9 is not clear is how (not if) such expectations should be taken into consideration when determining the effective interest rate. For example, should a most likely amount or probability-weighted approach be applied? If this is what the Committee had intended to refer to, then we recommend clarifying this in the final agenda decision.

Closing remarks

We recently conducted a benchmarking exercise to understand the approaches that are currently being applied in practice; we have noted that there is diversity in practice. In our sample, we observed that half of the banks have identified an element of grant in the TLTRO III financing conditions and have applied IAS 20, in which case, the benefit of the below-market rate has been recognised over the entire three-year financing period assuming they had reasonable assurance to meet the required conditions (most often without blending

[2] The Monetary Policy of the ECB, 2011, section 4 – Monetary Policy Implementation. Extracts included in Appendix A.

the rate). The rest of the banks have applied IFRS 9, in which case, they have applied B5.4.6. to any revision in estimates regarding their performance targets but they have applied B5.4.5. to changes decided by the ECB (in particular, the addition of a -50bp discount for the period from June 2020 to June 2022). Interestingly, we also observed that some of the guidance proposed in the TAD, notably the application of paragraph B5.4.6 to subsequent changes in the TLTRO III scheme (e.g., changes in the 50bps and the period for which it applies) would represent a change from current practice for all of the market participants surveyed.

Should you wish to discuss the contents of this letter with us or the results of our benchmarking exercise, please contact Leo van der Tas at the above address or on +44 (0) 20 7951 3152.

Yours faithfully

Ernst & Young Global Limited

Appendix A - Extracts from ECB monetary policy[3]

The following extracts explain key details of the ECB's monetary policy that are relevant to TLTRO III as follows.

Page 93 – Highlights how the Eurosystem's deposit facility is a critical element of the monetary base of the euro area
Page 94 – Highlights the role the ECB plays in managing liquidity
Page 95-96 – Explain the role of the main refinancing operation and deposit facility
Page 99 – 100 – Explain the interaction between the DFR and MRO rate
Page 106 – Explains the difference between the MRO and other rates such as LTRO rates
Page 108 – Further explains how the ECB uses the DFR and MRO rates to form a corridor within which market rates can fluctuate without necessarily needing to transact on those extreme ends of the corridor

[3] The Monetary Policy of the ECB, 2011, section 4 – Monetary Policy Implementation.

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4 MONETARY POLICY IMPLEMENTATION

This chapter explains how the Eurosystem implements monetary policy decisions using its monetary policy instruments. The first section gives an overview of the objectives and general principles that govern the functioning of the Eurosystem's operational framework. The second section briefly describes the main monetary policy instruments (open market operations, the minimum reserve system and the standing facilities), while the subsequent sections examine these in greater detail and present the interaction between the monetary policy instruments and the banks' liquidity needs in the context of a central bank balance sheet. The final section provides a brief assessment of the operational framework's performance in the first 12 years of the single monetary policy.

4.1 OBJECTIVES AND GENERAL PRINCIPLES BEHIND THE DESIGN OF THE OPERATIONAL FRAMEWORK

The money market and the transmission of monetary policy

As discussed in Chapter 3, short-term money market rates play a pivotal role in the transmission of monetary policy. By steering such rates, monetary policy exerts significant influence over short-term nominal market interest rates and, through various channels, over the spending decisions of companies and households, monetary and financial developments and, ultimately, the price level.

The operational framework...

In order to achieve its primary objective of maintaining price stability for the euro area as a whole, the Eurosystem uses a set of monetary policy instruments and procedures. These provide the operational framework for the implementation of monetary policy decisions in practice.

...and the monetary policy strategy

The operational framework and the monetary policy strategy each have a specific role in the implementation of monetary policy. The strategy determines which level of money market interest rates is required to maintain price stability over the medium term, whereas the operational framework determines how to achieve this interest rate level using the available monetary policy instruments and procedures.

The functions of the operational framework include steering short-term interest rates and managing liquidity, ...

A central bank steers short-term money market rates by signalling its monetary policy stance through its decisions on key interest rates and by managing the liquidity situation in the money market. The central bank, as the sole issuer of banknotes and bank reserves, is the monopoly supplier of the monetary base. The monetary base of the euro area consists of currency (banknotes and coins) in circulation, the reserves held by counterparties with the Eurosystem and recourse by credit institutions to the Eurosystem's deposit facility. These items are liabilities on the Eurosystem's balance sheet. Reserves can be broken down further into required and excess reserves. In the Eurosystem's minimum reserve system, counterparties are obliged to hold reserves with the national central banks (NCBs) (see Section 4.3). In addition to these required reserves, credit institutions usually hold only a small amount of voluntary excess reserves with the Eurosystem. This may, however, be different in periods

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of acute financial market tensions. By virtue of its monopoly, a central bank is able to manage the liquidity situation in the money market and influence money market interest rates. Broadly speaking, the Eurosystem allocates an amount of liquidity that allows euro area credit institutions to fulfil their liquidity needs at a price that is in line with its signalled policy intentions, as reflected in the key interest rates set by the ECB.

...signalling the monetary policy stance, ...

In addition to steering interest rates by managing liquidity, a central bank can also signal its monetary policy stance to the money market. To signal a change in the monetary policy stance, a central bank usually changes the conditions under which it is willing to enter into transactions with credit institutions. The most obvious of these are the key interest rates set by the central bank.

...and ensuring an orderly functioning of the money market

In its operations, a central bank also aims to ensure an orderly functioning of the money market and to help credit institutions to meet their liquidity needs in a smooth manner. This is achieved by providing regular refinancing to credit institutions, as well as facilities that allow them to deal with end-of-day imbalances and transitory liquidity fluctuations.

The key principles of the operational framework are operational efficiency, ...

The operational framework of the Eurosystem is based on a number of guiding principles. These principles act in a complementary and mutually reinforcing manner. The overriding principle is operational efficiency. This can be defined as the capacity of the operational framework to enable monetary policy decisions to feed through as precisely and as quickly as possible to short-term money market rates. These in turn affect the price level through the various channels of the monetary policy transmission mechanism. In other words, operational efficiency ensures the signalling and transmission of monetary policy.

...separation between monetary policy formulation and implementation, ...

As regards effective signalling, the operational framework needs to allow the determination of the monetary policy stance to be kept separate from liquidity management. Specifically, this implies a strict distinction between, on the one hand, monetary policy decisions that are geared towards the maintenance of price stability and, on the other hand, liquidity operations intended to keep market interest rates close to the level determined by the monetary policy stance.

...and market orientation

To ensure the efficient transmission of monetary policy, the operational framework has to be consistent with the principles of a market-oriented economy in which competition is key to ensuring the efficient allocation of resources. This principle is enshrined in the Treaty on the Functioning of the European Union. Article 127 of the Treaty states that, in pursuing its objectives, the Eurosystem "... shall act in accordance with the principle of an open market economy with free competition, favouring an efficient allocation of resources ...". The proper functioning of the interbank market is vital to the transmission of monetary policy from the very short end of the money market to the real economy and prices.

Other guiding principles are equal treatment, harmonisation, ...

Other important principles are equal treatment of financial institutions and the harmonisation of rules and procedures throughout the euro area. Given the area-wide focus, credit institutions must be treated equally across the euro area, irrespective of their size or location. This harmonisation of rules and procedures aims to ensure equal treatment by providing identical

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conditions for all credit institutions in the euro area in connection with transactions with the Eurosystem.

...simplicity, transparency, continuity, safety and cost efficiency...

The operational framework also needs to be consistent with the principles of simplicity, transparency, continuity, safety and cost efficiency. Simplicity and transparency ensure that financial market participants understand the intentions behind monetary policy operations. The principle of continuity requires the avoidance of frequent and major adjustments in instruments and procedures, so that central banks and their counterparties can rely on past experience when participating in monetary policy operations. The principle of safety requires the Eurosystem's financial and operational risks to be kept to a minimum, while cost efficiency should ensure low operational costs for both the Eurosystem and its counterparties arising from the operational framework.

Table 4.1 Eurosystem monetary policy operations

Monetary policy operations	Type of transaction [1]		Maturity	Frequency
	Liquidity-providing	Liquidity-absorbing		
Open market operations				
Main refinancing operations	• Reverse transactions	–	• One week [2]	• Weekly
Longer-term refinancing operations	• Reverse transactions	–	• Three months	• Monthly
Fine-tuning operations	• Reverse transactions • Foreign exchange swaps	• Reverse transactions • Collection of fixed-term deposits • Foreign exchange swaps	• Non-standardised	• Non-regular
Structural operations	• Reverse transactions	• Issuance of ECB debt certificates	• Standardised/ non-standardised	• Regular and non-regular
	• Outright purchases	• Outright sales	–	• Non-regular
Standing facilities				
Marginal lending facility	• Reverse transactions	–	• Overnight	• Access at the discretion of counterparties
Deposit facility	–	• Deposits	• Overnight	• Access at the discretion of counterparties

1) See Box 4.3 for descriptions of the various types of open market transaction.
2) The maturity has been one week since 10 March 2004. Prior to that date it was two weeks (see Box 4.2).

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...as well as decentralised implementation

Finally, one principle that is specific to the Eurosystem is the decentralisation of the implementation of monetary policy. In accordance with this principle, the Eurosystem's monetary policy operations are normally implemented through the NCBs, which means that the ECB coordinates the operations, while the transactions are carried out by the NCBs.

4.2 OVERVIEW OF THE EUROSYSTEM'S OPERATIONAL FRAMEWORK

The Eurosystem's operational framework is described in greater detail in the ECB publication entitled "The implementation of monetary policy in the euro area – General documentation on Eurosystem monetary policy instruments and procedures".

Open market operations

The Eurosystem uses two types of operation: open market operations and standing facilities. Table 4.1 provides an overview of the essential features of these operations. The most important operations are open market operations. This is the term used for operations that are conducted on the initiative of the ECB, usually in the money market. As described in Section 2.6, "money market" refers to the market in which the maturity of transactions is generally less than one year. Open market operations include main refinancing operations (MROs), longer-term refinancing operations (LTROs), fine-tuning operations (FTOs) and structural operations. These operations play an important role in steering interest rates, signalling the stance of monetary policy and managing the liquidity conditions for the euro area banking sector.

Main refinancing operations

MROs are the most important open market operations and represent the key monetary policy instrument of the Eurosystem. Through MROs, the Eurosystem lends funds to its counterparties. In order to protect the Eurosystem against financial risks, lending is always against adequate collateral. For more detailed information on the Eurosystem's counterparties and on the collateral required in its liquidity-providing operations, see Box 4.1.

Box 4.1 Counterparties and collateral

1. Counterparties

The Eurosystem's monetary policy framework is formulated with a view to ensuring the participation of a broad range of counterparties. Counterparties to Eurosystem monetary policy operations must fulfil certain eligibility criteria. These criteria are defined in such a way as to ensure equal treatment for institutions across the euro area and that counterparties fulfil certain operational and prudential requirements. The general eligibility criteria are uniform throughout the euro area.

To be an eligible counterparty, a credit institution must be subject to the Eurosystem's minimum reserve system and at least one form of harmonised European Union/ European Economic Area (EU/EEA) supervision by national authorities, as well as being financially sound. Financially sound institutions operating in the euro area and subject to non-harmonised supervision by competent national authorities of a standard comparable to harmonised EU/EEA supervision may also be accepted as counterparties (e.g. branches

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Reverse transactions

Lending through open market operations normally takes place in the form of reverse transactions. In these reverse transactions, the central bank buys assets under a repurchase agreement or grants a loan against assets pledged as collateral (see Box 4.3). Reverse transactions are therefore temporary open market operations which provide funds for a limited, pre-specified period only.

Standing facilities

For the purpose of controlling short-term interest rates in the money market and, in particular, restricting their volatility, the Eurosystem also offers two standing facilities to its counterparties: the marginal lending facility and the deposit facility. Both facilities have an overnight maturity and are available to counterparties on their own initiative. The interest rate on the marginal lending facility is normally substantially higher than the corresponding money market rate, and the interest rate on the deposit facility is normally substantially lower than the money market rate. As a result, credit institutions normally only use the standing facilities in the absence of other alternatives. As there are no limits on access to these facilities (except for the collateral requirements of the marginal lending facility), the rate on the marginal lending facility and the rate on the deposit facility normally provide a ceiling and a floor, respectively, for the overnight rate in the money market. These instruments are examined in more detail in Section 4.5.

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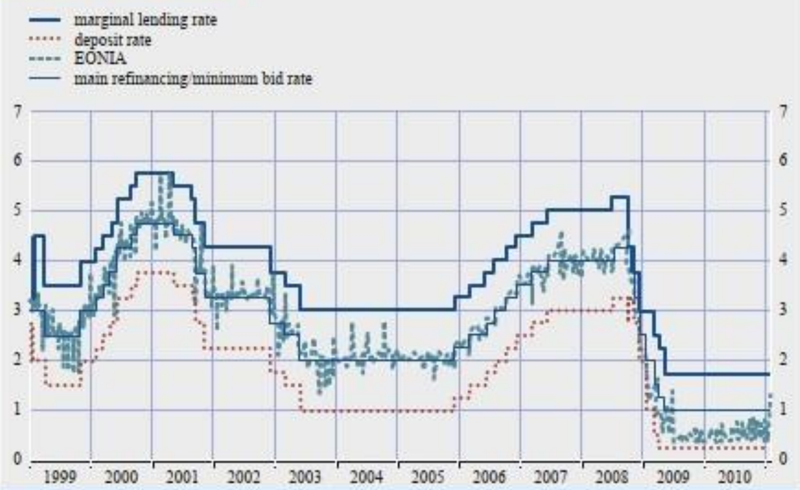
Chart 4.2 Key ECB interest rates and the EONIA since 1999

(percentages per annum; daily data)



Source: ECB.

1) Before 28 June 2000 MROs were conducted as fixed rate tenders. Starting with the operation settled on 28 June 2000, and until the operation settled on 15 October 2008, MROs were conducted as variable rate tenders with a pre-announced minimum bid rate. Since the operation settled on 15 October 2008, MROs have been conducted as fixed rate tenders with full allotment. This procedure is scheduled to remain in place at least until the maintenance period ending on 12 July 2011. The minimum bid rate refers to the minimum interest rate at which counterparties may place their bids (see Section 4.4).

Corridor of standing facility interest rates

By setting the rates on the standing facilities, the Governing Council effectively determines the corridor within which the overnight money market rate can fluctuate. Chart 4.2 shows the development of key ECB interest rates since January 1999 and how the interest rates on the standing facilities have provided a ceiling and a floor for the overnight market interest rate, measured by the euro overnight index average (EONIA).

EONIA, key ECB interest rates and the minimum reserve system

Chart 4.2 shows that, in normal times, the EONIA has generally remained close to the rate on the MROs, thus demonstrating the importance of these operations as the main monetary policy instrument of the Eurosystem. This behaviour changed in October 2008, when the Eurosystem adopted non-standard measures to counter the negative effects of the intensification of the financial crisis (see Box 5.1 and Chapter 5). Chart 4.2 also shows that the EONIA exhibits a pattern of occasional spikes. This pattern is related to the Eurosystem's minimum reserve system, as explained further in Section 4.3.

Finally, Chart 4.2 shows that the differences between the standing facility interest rates and the rate on the MROs were kept unchanged between April 1999 and October 2008 at ±1 percentage point. The width of the corridor was then temporarily narrowed to ±0.5 percentage point, before being widened again to ±0.75 percentage point in May 2009, when the Governing Council decided to set the rate for the MROs at 1.0%.

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higher price if they wanted to obtain more liquidity.

However, a different problem arose with variable rate tenders with a minimum bid rate. In a few cases, the aggregate of all bids submitted in the tender was lower than the amount needed for the smooth fulfilment of reserve requirements ("underbidding"). As these episodes also stemmed from significant interest rate speculation, the Governing Council decided to adjust its operational framework as of March 2004 (see Box 4.2). In October 2008 a fixed rate full allotment procedure was introduced for all refinancing operations for a certain period (see Box 5.1). This was intended to mitigate the adverse effects that dysfunctional money markets were having on the liquidity situation of solvent banks in the euro area and to support the flow of credit to firms and households.

Publication of liquidity needs

When it switched to variable rate tenders, the Eurosystem also started to announce, each week, the estimated liquidity needs of the banking system for the period until the day before the settlement of the next MRO. The publication of this estimate assists counterparties in preparing their bids for the forthcoming MRO. Section 4.6 describes the factors which determine the liquidity needs of the banking system.

Longer-term refinancing operations

LTROs

In addition to the weekly MROs, the Eurosystem also executes regular monthly LTROs with a three-month maturity. The Eurosystem may also conduct additional LTROs which can have other maturities (e.g. one maintenance period, six months or twelve months) (see Box 5.1). These operations are aimed at providing longer-term liquidity to the banking system. This is deemed useful in order to prevent all the liquidity in the money market from having to be rolled over each week and to give counterparties access to longer-term refinancing. Like the MROs, these LTROs are conducted as standard tenders in a decentralised manner, and all counterparties fulfilling general eligibility criteria may participate (see Box 4.1).

Eurosystem as a "rate taker"

Since it was not considered desirable for the Eurosystem to influence money market rates at more than one point along the maturity spectrum, the LTROs have been designed to ensure that the Eurosystem acts as a "rate taker" in these operations. In order not to blur the signal arising from the Eurosystem's MROs, LTROs are normally executed in the form of pure variable rate tenders with pre-announced allotment volumes. The Governing Council normally indicates in advance the volume to be allotted in forthcoming tenders. Under exceptional circumstances, the Eurosystem may also execute LTROs through fixed rate tenders and may decide to accommodate all bids in the operations (full allotment procedure) (see Box 5.1).

Fine-tuning operations

FTOs

The Eurosystem may also carry out open market operations on an ad hoc basis, i.e. FTOs. The frequency and maturity of such operations are not standardised. FTOs can be liquidity-absorbing or liquidity-providing. They are aimed at managing the liquidity situation in the money market and steering interest rates, in particular in order to smooth the effects on interest rates of unexpected liquidity fluctuations in the market. FTOs may be conducted on the last day

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High degree of flexibility

The potential need for rapid action in the event of unexpected market developments makes it desirable for the Eurosystem to retain a high degree of flexibility in the specification of FTOs. They are normally executed in a decentralised manner by the NCBs, but the Governing Council can decide, under exceptional circumstances, to have bilateral FTOs executed by the ECB. For operational reasons, only a limited number of selected counterparties may participate in FTOs. In order to facilitate access during the financial crisis, the list of counterparties eligible for FTOs was extended, increasing from around 140 to around 2,000 eligible counterparties.

Structural operations

Structural operations

The operational framework also provides the Eurosystem with the possibility of conducting "structural operations". These operations are executed at the initiative of the ECB to adjust the structural liquidity position of the Eurosystem vis-à-vis the financial sector, i.e. the amount of liquidity in the market over the longer term. These operations can be conducted using reverse transactions, outright operations or the issuance of ECB debt certificates (see Box 4.3).

In principle, structural operations can be liquidity-providing or liquidity-absorbing and their frequency can be regular or non-regular. Structural operations in the form of reverse transactions and the issuance of debt instruments are normally carried out through standard tenders. Structural operations in the form of outright transactions are normally executed through bilateral procedures.

4.5 STANDING FACILITIES

Marginal lending and deposit facilities are…

As mentioned above, the Eurosystem also implements monetary policy by setting the interest rates on its standing facilities. Standing facilities provide or absorb liquidity with an overnight maturity on the initiative of counterparties. Two standing facilities are available to eligible counterparties: the marginal lending facility and the deposit facility. In normal circumstances, there is little incentive for banks to use standing facilities, as the interest rates applied to them are normally unfavourable when compared with market rates.

…important in exceptional circumstances…

Chart 4.4(a) shows the average daily use of the standing facilities from January 1999 to August 2008. Their use largely remained below €1 billion before the onset of the financial turmoil in August 2007, demonstrating that the facilities serve mainly to provide and absorb liquidity in exceptional circumstances. Chart 4.4(b) illustrates that the use of the standing facilities increased abruptly during the financial crisis as a number of banks preferred to keep more central bank reserves than required and to deposit the additional reserves in the deposit facility instead of lending them out to other banks. The reasons for this included uncertainty and perceived counterparty risk. Under the full allotment procedure introduced by the Eurosystem in October 2008, the total amount of liquidity provided by the Eurosystem is the sum of the amounts of liquidity requested by individual banks. As the overall amounts requested by banks were higher than the liquidity needs of the banking system during this period, the excess liquidity was deposited in the deposit facility. This points both to precautionary liquidity hoarding and to market segmentation (as the banks requesting liquidity may not be the same as those depositing excess liquidity with the Eurosystem).

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16 August 2021

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Online submission: https://www.ifrs.org/projects/work-plan/tltro-iii-transactions-ifrs-9-and-ias-20/

Dear Sue

Tentative agenda decision - TLTRO III Transactions (IFRS 9 and IAS 20)

I am pleased to make this submission on the above Tentative Agenda Decision (TAD) relating to European Central Bank's (ECB) targeted longer-term refinancing operations (TLTROs) -TLTRO III Transactions (IFRS 9 and IAS 20).

I have extensive experience in accounting advice on International Financial Reporting Standards across a wide range of clients, industries and issues in the for-profit, not-for-profit, private and public sectors.

My clients have included listed companies, unlisted and private companies, charitable and not-for-profit organisations, federal, state and local government departments and agencies in the public sector, and government owned corporations (government business enterprises). I also have some commercial, standard setting and academic experience.

Overall

I do not agree with the Committee's decisions in the TAD:

- not to conclude on whether the ECB meets the definition of a government agency (or similar body) under IAS 20
- the TAD conclusions on splitting the floating rate loan into two components (with the50 basis point being a fixed component).

I do not offer any comments on the other aspects of the TAD.

Government Grant issue

The Committee needs to pursue this issue as it is a clear area of diversity in practice. There seems to be an interpretation issue, rather than a judgement issue. The Committee has recently issued interpretations on similar issues on the application of accounting standards including:

- Deposits relating to taxes other than income tax

- Cryptocurrencies
- Customer's right to receive access to the supplier's software hosted on the cloud that /

Extract from IAS 20

> *Government* refers to government, government agencies and similar bodies whether local, national or international.

The underlying areas of diversity should be identified. For example:

- Whether the European Parliament is a government (it has its own members of parliament)?
- Whether the European Central Bank is part of the European Parliament (that the ECB is accountable to)?
- Are government agencies (or similar bodies) limited to controlled entities of a government?
- If not, whether an entity jointly owned by government agencies (e.g. National Central Banks) is itself a government agency (or similar body)?

In Australia, the Reserve Bank of Australia is considered independent[1]. However, despite its independence, it is considered a controlled entity of the Commonwealth of Australia[2] (based on the Australian equivalent to IFRS 10).

The reasons why some preparers believe that the European Central Bank is not a government agency (or similar body) under IAS 20 may have implications for how grants (which are wider than subsidised financing arrangements) are recognised in Australia by private sector entities. In particular, whether they fall under the Australian equivalent of IAS 20 or not.

Grants received by private sector entities in Australia can include:

- Grants from government controlled entities.
- Grants from entities that are not government controlled entities, but the entities are established under the law of the respective parliament (protective rights for appointment of boards are often involved). These entities may be regarded as 'public sector entities' and subject to the jurisdiction of the respective government auditor.
- Grants from entities that are jointly owned by a combination of governments or government agencies (for example a group of local governments, or a combination of state and local government entities).

Splitting the floating rate into two components

I do not agree with the Committee's decision on splitting a floating rate into components. There is no mention of doing that in IFRS 9 paragraph 5.4.5 referred to by the TAD:

> B5.4.5 For floating-rate financial assets and floating-rate financial liabilities, periodic re-estimation of cash flows to reflect the movements in the market rates of

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[1] https://www.rba.gov.au/education/resources/explainers/origins-of-the-reserve-bank-of-australia.html, viewed 16 August 2021

[2] Controlled entity – Note 14, Consolidated Financial Statements for the year ended 30 June 2020, viewed 16 August 2021 https://www.finance.gov.au/sites/default/files/2020-12/consolidated-financial-statements-201920.pdf

> interest alters the effective interest rate. If a floating-rate financial asset or a floating-rate financial liability is recognised initially at an amount equal to the principal receivable or payable on maturity, re-estimating the future interest payments normally has no significant effect on the carrying amount of the asset or the liability.

Negotiating a discount to the loan reference rate is common in Australia for home loans. That discount is often a nominated amount (fixed), but may be linked to other conditions, and therefore may change. Discounts may be given by the bank if they do not have to pay for mortgage broker commission (i.e. direct application to the bank), and the discount may have conditions such as number of other accounts or other bank products.

The Committee should remove the conclusions on separating the adjustments for a fixed component on a floating rate loan. If the Committee wishes, then it should refer the matter to the Board for review in the post-implementation review – like other issues the Committee has not concluded on.

Yours sincerely,

David Hardidge
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Date: August 16, 2021

Ms Sue Lloyd,
Chair, IFRS Interpretations Committee,
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Dear Ms Sue,

Subject: Comments of the Institute of Chartered Accountants of India on Tentative Agenda Decision (TAD) issued by IFRS Interpretations Committee (IFRS IC) on TLTRO III transactions (IFRS 9 and IAS 20)

The Accounting Standards Board (ASB) of the Institute of Chartered Accountants of India (the ICAI) welcomes the opportunity to comment on above referred Tentative Agenda Decision of IFRS Interpretations Committee.

In this regard, we are of the view that an explanation should be added to the agenda decision as to how the applicable principles and requirements in IFRS Standards apply to the transaction or fact pattern described in the agenda decision, beyond the acknowledgement of diversity in accounting in the related staff paper of IFRS IC June 2021. The TAD does not provide a clear conclusion as to how the applicable principles and requirements in IFRS 9 and IAS 20 will apply to the TLTRO III transactions. To reduce the diversity, this TAD should provide guidance to clarify the applicability of IAS 20 on the TLTRO III transactions.

With regard to the subsequent measurement of TLTRO III liability, it needs to be assessed that whether the change in interest rate is covered by paragraph B5.4.5 or paragraph B5.4.6 of IFRS 9. We are of the view that whether the interest rate is variable (i.e., paragraph B5.4.5 is applicable) or fixed (i.e., paragraph B5.4.6 is applicable) is based on specific facts and circumstances of each case. Accordingly, language of TAD may be revised in this regard.

With kind regards,

CA. Parminder Kaur
Secretary,
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Our ref RD/288

16 August 2021

Dear Ms Lloyd

Tentative Agenda Decision: *TLTRO III Transactions (IFRS 9 and IAS 20)*

We appreciate the opportunity to comment on the IFRS Interpretations Committee's ('the Committee') tentative agenda decision "TLTRO III Transactions (IFRS 9 and IAS 20)" ('TAD'). We have consulted with, and this letter represents the views of, the KPMG network.

Overall, we support the Committee's tentative decision not to add a standard setting project to the work plan. We support the reasons for not doing so, and we agree that certain matters are best addressed through the post-implementation review ('PIR') of the classification and measurement requirements in IFRS 9 *Financial Instruments*.

In particular, we note that aspects of the questions raised such as what constitutes a market interest rate, what are the defining characteristics of a floating interest rate instrument and how to account for the modification of floating interest rate financial liabilities are well known and complex areas of practice. For this reason, we therefore recommend that the sections of the TAD addressing IFRS 9 are reviewed to ensure that they do not inadvertently introduce changes to current interpretations of the standards in advance of the conclusion of those projects and to avoid the introduction of potentially new practice issues that could impact a wide variety of fact patterns. At the same time, we believe that the section of the TAD addressing IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance* could be enhanced to promote greater consistency in application.

In that context, we have set out below areas where we believe that the TAD could be made clearer without affecting the Committee's overall recommendation not to add a standard setting project to the workplan.

What constitutes a floating rate instrument?

It is acknowledged in the TAD that IFRS 9 does not define what is meant by a floating rate instrument. We agree and it has been an area of practice interpretation for many years. Consistent with this conclusion, we believe that the Committee does not need to further elaborate on the issue by characterising the ECB's Deposit Facility Rate (and subsequent 50bp reduction) available to TLTRO III borrowers as (i) a variable interest rate element which is reset to reflect movements in the market rates of interest and (ii) another element which is fixed and therefore not reset to reflect movements in the market rates of interest. By providing this detailed analysis, the TAD inadvertently provides guidance on what constitutes a floating rate. We believe that defining a floating rate (and as a result the appropriate treatment following the modification of such a rate) is a subject that should be debated in full during the PIR of IFRS 9.

We also note that the ECB is capable of adjusting the borrowing rate in TLTRO III operations unilaterally at any time (as confirmed by ESMA) as instruments of the ECB's monetary policy operations. It is not clear how a change in such a rate, no matter if the change is made up in terms of fixed and/or floating components can be determined to be made up of one part that resets to reflect movements in market rates of interest and one part that does not.

Modification of financial liability that is prepayable without penalty

Determining whether a modification has taken place and applying the appropriate accounting for modifications is an area of some diversity in practice. One area of debate relates to the derecognition of a liability when it matures in accordance with the original contractual terms of the instrument and whether that also extends to cover the contractual acceleration of maturity that occurs through the exercise of a prepayment option. We do not believe that the requirements of modifications and exchanges of debt instruments extend to the usual repayment of a loan at maturity and its replacement by a new loan on arm's length terms even if the new loan is with the same lender. However, if the original terms of the liability include a prepayment option exercisable without significant penalty, then it is possible to view a replacement of old debt with new debt on arm's length terms as contractual maturity of the original instrument in accordance with its original terms. If an entity views the replacement of prepayable old debt with arm's length new debt in such a way, it may conclude that it has derecognised its old debt without performing any analysis in respect of substantive or non-substantive modification. The new debt would be subject to normal IFRS 9 accounting including determining a new original effective interest rate for the new debt.

It is our understanding that TLTRO III loans are prepayable without significant penalty.

Alternatively, it may also be possible to view a loan that is prepayable without significant penalty wholly as a floating rate. In such circumstances the borrower would be free to refinance with the same or other lenders at the new market rate as opposed to modifying the contract.

The TAD implies that approaches such as the ones noted above are not permitted by being too prescriptive as to when B.5.4.6 is applied without considering the prepayable nature of the instruments. We believe that the nature of the loans (being prepayable without significant penalty) is an important part of the analysis that is not discussed in the TAD. We believe that the TAD could be made more concise without changing its conclusion by not detailing the mechanics of modifications for these exposures. We further believe that issues arising (including a detailed consideration of the effects of prepayment features without significant penalty on the analysis) should be addressed in the comprehensive PIR of IFRS 9 as the implications of forming a view in these particular circumstances could have wide ranging repercussions for many other situations.

Whether or not the ECB meets the definition of government in IAS 20

We note that the TAD observes that making the determination of whether the ECB meets the definition of government in IAS 20 is a judgement based on specific facts and circumstances. The implication is that entities could come to different conclusions as to whether the ECB is, or is not, a government per the definition in IAS 20. We do not believe that consistent application is best served by such a response. There is a single set of facts available to all in order to make that assessment and we believe that there should be a single answer to that question. By not forming a view on that specific question, we believe that the Committee is permitting practice diversity to persist in an area where it could easily rectify the situation. This would not affect the other judgements that would need to be made before an entity could conclude on whether TLTRO III tranches contain a government grant within scope of IAS 20.

The recognition of a government grant subsequent to initial recognition of a loan

The TAD discusses the impact of subsequent changes in cash flow estimates under IFRS 9 but not whether, and if so how, subsequent changes in cash flow estimates affect the identification and accounting for a government grant under IAS 20. This omission could be read to imply that it is not necessary to consider IAS 20 after initial recognition of the loan. While IAS 20.10A describes how to measure the benefit arising from a loan at initial recognition, the general requirements of IAS 20 may, depending on the facts and circumstances, require recognition of a government grant subsequently.

For example, IAS 20.7(a) and IAS 20.8 require that no grant is recognised until there is reasonable assurance that the entity will comply with the conditions attached to the grant. Should an entity be granted a below market rate loan by a government conditional on meeting certain conditions, and the entity does not initially have reasonable assurance that it will comply with the conditions, it is not clear how the difference, between fair value[1] and the cash received for the loan should be treated on day 1 and subsequently.

We also believe that it may be appropriate to recognise a government grant in respect of a loan subsequent to initial recognition when the entity gains reasonable assurance that it will meet the conditions (i.e. its assessment changes) – as required by IAS 20.7(a) and IAS 20.8.

We further believe that when a government changes the terms and conditions of loan that was issued at a market rate to an instrument that will bear interest at a below market rate contingent upon the borrower meeting specified conditions, that government is providing assistance *"…in the form of [a] transfer of resources to an entity in return for past or future compliance with certain conditions relating to the operating activities of the entity…"* (IAS 20.3 definitions of a government grant). The assessment under IFRS 9 as to whether the modification is substantial does not affect whether the definition in IAS 20 is met.

We therefore recommend that the section of the TAD addressing IAS 20 should address subsequent changes in cash flow estimates. We also recommend that the section of the TAD headed "Subsequent measurement of the financial liability at amortised cost" be reviewed to ensure it does not conflict with IAS 20.

Please contact Reinhard Dotzlaw at rdotzlaw@kpmg.ca, Brian O'Donovan at brian.odonovan@kpmgifrg.com or Colin Martin at colin.martin@kpmgifrg.com if you wish to discuss any of the issues raised in this letter.

Yours sincerely

KPMG IFRG Limited

[1] While we agree that what to consider in estimating the expected future cash flows for the purpose of calculating the effective interest rate in IFRS 9 is a wider issue and should not be considered by the Committee solely in the context of TLTRO III transactions, the fair value of the liability considers the same set of cash flows. That is, the probability of whether an institution will meet or will not meet the lending criteria of the TLTRO III scheme is an integral part of the fair value calculation. An entity that market participants assume has a 100% chance of meeting the criteria would have a different fair value to an entity that market participants assume has a 0% chance of meeting the criteria because each would use a different set of cash flows. The implication is that there will be a difference between fair value and cash advanced for a least a portion, if not the majority, of borrowers.