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## IFRS<sup>®</sup> Interpretations Committee meeting

Date	<b>November 2022</b>
Project	<b>Potential annual improvements—IFRS 7—implementation guidance</b>
Topic	<b>Initial consideration</b>
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## Introduction

1. We have been informed about a potential lack of clarity in paragraph IG20C of IFRS 7 *Financial Instruments: Disclosures* because that paragraph fails to state that the example does not illustrate all the requirements in paragraph 35M of IFRS 7.
2. This paper:
  - (a) provides the Interpretations Committee (Committee) with a summary of the matter;
  - (b) presents our research and analysis; and
  - (c) asks the Committee whether it agrees with our preliminary views to include a proposed amendment to paragraph IG20C of IFRS 7 in the next *Annual Improvements to IFRS Accounting Standards Cycle* (annual improvements).

## Structure of this paper

3. This paper includes:
  - (a) background information (paragraphs 4–7);
  - (b) staff analysis and preliminary views (paragraphs 8–17);
  - (c) question for the Committee;
  - (d) Appendix A—recommended proposed amendment to paragraph IG20C of IFRS 7; and
  - (e) Appendix B—illustrative tables in paragraph IG20C of IFRS 7.

## Background information

4. Paragraph 35M of IFRS 7 sets out disclosure requirements relating to credit risk exposure and states:

To enable users of financial statements to assess an entity's credit risk exposure and understand its significant credit risk concentrations, an entity

shall disclose, by *credit risk rating grades*, the gross carrying amount of financial assets and the exposure to credit risk on loan commitments and financial guarantee contracts. This information shall be provided separately for financial instruments:

- (a) for which the loss allowance is measured at an amount equal to 12-month expected credit losses;
- (b) for which the loss allowance is measured at an amount equal to lifetime expected credit losses and that are:
  - (i) financial instruments for which credit risk has increased significantly since initial recognition but that are not credit-impaired financial assets;
  - (ii) financial assets that are credit-impaired at the reporting date (but that are not purchased or originated credit-impaired); and
  - (iii) trade receivables, contract assets or lease receivables for which the loss allowances are measured in accordance with paragraph 5.5.15 of IFRS 9.
- (c) that are purchased or originated credit-impaired financial assets.

5. Paragraph IG20C of IFRS 7 illustrates application of paragraph 35M of IFRS 7 and includes illustrative tables that are reproduced in Appendix B to this paper. Above the illustrative tables, paragraph IG20C states:

The following example illustrates some ways of providing information about an entity's credit risk exposure and significant credit risk concentrations in accordance with paragraph 35M of IFRS 7. The number of grades used to disclose the information in accordance with paragraph 35M of IFRS 7 shall be consistent with the number that the entity uses to report internally to key management personnel for internal credit risk management purposes. However, if information about credit risk rating grades is not available without undue cost or effort and an entity uses past due information to assess whether credit risk has increased significantly since initial recognition in accordance with paragraph 5.5.11 of IFRS 9, the entity shall provide an analysis by past due status for those financial assets.

6. The tables in paragraph IG20C of IFRS 7 do not illustrate all the disclosure requirements in paragraph 35M of IFRS 7—and the paragraph does not state that it omits illustration of particular requirements.

For example, the tables illustrate neither an entity's exposure to credit risk on loan commitments and financial guarantee contracts nor the requirements in paragraph 35M(b)(i)–(ii) or 35M(c).<sup>1</sup>

### Question raised

7. The question raised is whether paragraph IG20C of IFRS 7 should be updated to state that it does not illustrate all the requirements in paragraph 35M of IFRS 7.

### Staff analysis and preliminary views

8. As reproduced in paragraph 4, paragraph 35M of IFRS 7 requires an entity to disclose, by credit risk rating grades, the gross carrying amount of financial assets and the exposure to credit risk on loan commitments and financial guarantee contracts. The paragraph requires an entity to provide the information separately for financial instruments in several categories: (a) those with a loss allowance equal to 12-month expected credit losses; (b) those with a loss allowance equal to lifetime expected credit losses; and (c) those that are purchased or originated credit-impaired financial assets.
9. For financial instruments with a loss allowance equal to lifetime expected credit losses (category (b) as described in paragraph 8), paragraph 35M(b)(i)–(ii) requires an entity to disclose separately credit risk information for '(i) financial instruments for which credit risk has increased significantly since initial recognition but that are not credit-impaired financial assets'; and '(ii) financial assets that are credit-impaired at the reporting date (but that are not purchased or originated credit-impaired)'.
10. Paragraph IG20C of IFRS 7 illustrates 'some ways' of providing the information required by paragraph 35M of IFRS 7 and includes illustrative tables as reproduced in Appendix B to this paper. However, paragraph IG20C does not illustrate all the requirements in paragraph 35M; for example, it does not provide illustrative disclosures of: exposure to credit risk on loan commitments and financial guarantee contracts; information required by paragraph 35M(b)(i)–(ii) as described in paragraph 9; or information about purchased or originated credit-impaired financial assets as required by paragraph 35M(c).
11. As a general matter, in our view it is not necessary for implementation guidance (or illustrative examples) to state in every case whether all requirements are illustrated for a particular referenced paragraph in an IFRS Accounting Standard. We think doing so would result in additional disclaimer language that would add unnecessary length to implementation guidance and illustrative examples.
12. However, we note that paragraph IG20B of IFRS 7—which illustrates application of requirements in paragraphs 35H–35I of IFRS 7—states: "[t]his example does not illustrate the requirements for financial assets that are purchased or originated credit-impaired". We think this statement in paragraph IG20B may set an expectation for readers that paragraph IG20C—which appears directly after paragraph IG20B—would also state, if applicable, that it does not illustrate particular requirements in paragraph

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<sup>1</sup> Paragraph IG20D of IFRS 7 illustrates one way to apply the requirements in paragraphs 35M(b)(iii) and 35N for trade receivables.

35M of IFRS 7. Therefore, for consistency between paragraphs IG20B and IG20C, we recommend updating paragraph IG20C.

13. In our view, this matter can be efficiently resolved by adding a statement to paragraph IG20C of IFRS 7 that it does not illustrate all the requirements in paragraph 35M of IFRS 7 (see Appendix A to this paper). We think this is a minor correction that will remove a potential inconsistency between paragraphs IG20B and IG20C and will improve understandability and application of the implementation guidance accompanying IFRS 7.

### Does this matter meet the annual improvements criteria?

14. Paragraphs 6.10–6.13 of the *Due Process Handbook* include the criteria for annual improvements. To meet these criteria, the proposed solution would need to be limited to:
  - (a) clarifying the wording in an Accounting Standard, which involves either replacing unclear wording in existing Accounting Standards or providing requirements where an absence of requirements is causing concern; or
  - (b) correcting relatively minor unintended consequences, oversights or conflicts between existing requirements.
15. In our view, our proposed solution to amend paragraph IG20C of IFRS 7 (see Appendix A to this paper) meets these criteria as explained in paragraph 13. Our recommended amendment would maintain consistency with the principles and requirements in IFRS 7 and would not propose a new (or change an existing) principle or requirement.
16. Although strictly speaking an amendment to the implementation guidance accompanying IFRS 7 may not be required—because implementation guidance accompanies, but is not part of, an IFRS Accounting Standard—we see benefit in removing the potential for confusion related to paragraph IG20C as described in this paper. We note that the IASB previously amended illustrative examples through annual improvements; Illustrative Example 13 accompanying IFRS 16 *Leases* was amended through [Annual Improvements to IFRS Standards 2018–2020](#).

### Summary of staff preliminary views

17. Based on our analysis in paragraphs 8–16, our preliminary views are to:
  - (a) propose that the IASB amend paragraph IG20C of IFRS 7 to add a statement that the example does not illustrate all the requirements in paragraph 35M of IFRS 7 (see Appendix A to this paper); and
  - (b) include this proposed amendment in the next annual improvements cycle.

**Question for the Committee****Question for the Committee**

Do Committee members agree with our preliminary views as summarised in paragraph 17 of this paper? If 'no', do you have any other suggestions?

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## Appendix A—recommended proposed amendment to paragraph IG20C of IFRS 7

- A1. Our proposed amendment to paragraph IG20C of IFRS 7 would add a statement that the example does not illustrate all the requirements in paragraph 35M of IFRS 7.
- A2. New text is underlined.

IG20C The following example illustrates some ways of providing information about an entity's credit risk exposure and significant credit risk concentrations in accordance with paragraph 35M of IFRS 7; this example does not illustrate all the requirements in paragraph 35M of IFRS 7. The number of grades used to disclose the information in accordance with paragraph 35M of IFRS 7 shall be consistent with the number that the entity uses to report internally to key management personnel for internal credit risk management purposes. However, if information about credit risk rating grades is not available without undue cost or effort and an entity uses past due information to assess whether credit risk has increased significantly since initial recognition in accordance with paragraph 5.5.11 of IFRS 9, the entity shall provide an analysis by past due status for those financial assets.

## Appendix B—Illustrative tables in paragraph IG20C of IFRS 7

B1. The following illustrative tables are included in paragraph IG20C of IFRS 7:

<b>Consumer loan credit risk exposure by internal rating grades</b>				
20XX	<b>Consumer—credit card</b>		<b>Consumer—automotive</b>	
CU'000	<b>Gross carrying amount</b>		<b>Gross carrying amount</b>	
	<b>Lifetime</b>	<b>12-month</b>	<b>Lifetime</b>	<b>12-month</b>
Internal Grade 1–2	X	X	X	X
Internal Grade 3–4	X	X	X	X
Internal Grade 5–6	X	X	X	X
Internal Grade 7	X	X	X	X
<b>Total</b>	<b>X</b>	<b>X</b>	<b>X</b>	<b>X</b>

<b>Corporate loan credit risk profile by external rating grades</b>				
20XX	<b>Corporate—equipment</b>		<b>Corporate—construction</b>	
CU'000	<b>Gross carrying amount</b>		<b>Gross carrying amount</b>	
	<b>Lifetime</b>	<b>12-month</b>	<b>Lifetime</b>	<b>12-month</b>
AAA-AA	X	X	X	X
A	X	X	X	X
BBB-BB	X	X	X	X
B	X	X	X	X
CCC-CC	X	X	X	X
C	X	X	X	X
D	X	X	X	X
<b>Total</b>	<b>X</b>	<b>X</b>	<b>X</b>	<b>X</b>

<b>Corporate loan risk profile by probability of default</b>				
20XX	<b>Corporate—unsecured</b>		<b>Corporate—secured</b>	
CU'000	<b>Gross carrying amount</b>		<b>Gross carrying amount</b>	
	<b>Lifetime</b>	<b>12-month</b>	<b>Lifetime</b>	<b>12-month</b>
0.00 – 0.10	X	X	X	X
0.11 – 0.40	X	X	X	X
0.41 – 1.00	X	X	X	X
1.01 – 3.00	X	X	X	X
3.01 – 6.00	X	X	X	X
6.01 – 11.00	X	X	X	X
11.01 – 17.00	X	X	X	X
17.01 – 25.00	X	X	X	X
25.01 – 50.00	X	X	X	X
50.01+	X	X	X	X
<b>Total</b>	<b>X</b>	<b>X</b>	<b>X</b>	<b>X</b>