UKEB
UK Endorsement Board

IASB Exposure Draft *Amendments to the Classification and Measurement of Financial Instruments: Proposed amendments to IFRS 9 and IFRS 7* - Final Comment Letter

Executive Summary

Project Type	Influencing
Project Scope	Moderate
Purpose of the paper	
The purpose of this paper is to obtain: a) Board approval for the issue of a Final Comment Letter (FCL) on the International Accounting Standards Board (IASB)'s Exposure Draft (ED) *Amendments to the Classification and Measurement of Financial Instruments: Proposed amendments to IFRS 9 and IFRS 7*; b) Board approval for the publication of the Feedback Statement (FS); and c) Board feedback on the draft Due Process Compliance Statement (DPCS).	
Summary of the Issue	
The IASB's ED addresses concerns raised during the IASB's *Post-implementation Review of IFRS 9 – Classification and Measurement* (PIR) project. It proposes amendments to IFRS 9 *Financial Instruments* and IFRS 7 *Financial Instruments: Disclosures*. The UKEB's Draft Comment Letter (DCL) was issued on 26 May 2023, welcoming the ED as addressing many of the concerns the UKEB raised in its response to the PIR Request for Information. The DCL also identified some concerns regarding the clarity and practicality of the proposed requirements, suggesting potential enhancements to address those concerns. Additional outreach since publication of the DCL has provided additional information and examples of the practical challenges arising from the ED proposals.	

Decisions for the Board
Subject to any amendments arising at this meeting, does the Board approve: • The FCL for issue to the IASB and publication on the UKEB website? • The FS for publication on the UKEB website? In addition, the Board is asked whether it has any comments on the draft DPCS for the project?
Recommendation
The Secretariat recommends that, subject to any amendments agreed at this meeting, the Board approves the FCL and FS for issue and publication.
Appendices
Appendix A (Draft) Final Comment Letter Appendix B (Draft) Feedback Statement Appendix C Draft DPCS

Background

1. In March 2023 the IASB issued the Amendments. The IASB comment period ends on 19 July 2023.

2. The Amendments form part of the IASB's response to feedback received as part of its IFRS 9 *Post-implementation Review (PIR) of IFRS 9 – Classification and Measurement* project. It is summarised on the UKEB project page.

3. An education session on the proposals was provided to the Board during its private meeting in April 2023. The Secretariat conducted desk-based research and discussed the IASB's proposals with the Financial Instruments Working Group (FIWG) in April 2023 to inform the Draft Comment Letter (DCL). At its May 2023 meeting the Board decided that the UKEB comment letter should take a pragmatic approach, focussing on a small number of critical changes sufficient to allow stakeholders to arrive at a common interpretation of requirements ("Option 1" as described in those board papers), rather than recommend a more fundamental redraft ("Option 2").The Board specified the letter should highlight that this approach may require the IASB to make subsequent amendments for future market developments.

4. The DCL was approved at the May 2023 board meeting and published on the UKEB website on 26 May 2023. The DCL noted that the UKEB welcomed the ED as it addressed many of the concerns raised by the UKEB in its response to the IFRS 9 PIR Request for Information. The DCL welcomed the proposal to create an option when derecognising financial liabilities settled with cash using an electronic payment system, the proposals to address financial assets with ESG-linked features and the efforts to clarify the distinction between non-recourse finance and contractually linked instruments. The DCL also identified concerns regarding the clarity and practicality of certain requirements, and suggested potential enhancements to those proposals.

5. UKEB news alerts and LinkedIn posts were used to raise awareness of the publication of the DCL. An educational video on the derecognition of financial liabilities proposals was posted on the UKEB website to further alert stakeholders to the potential changes.

Further outreach and feedback on the DCL

6. The Secretariat conducted further outreach activities to inform the FCL. The proposals were discussed with the FIWG, the Preparer Advisory Group (PAG), the Investor Advisory Group (IAG) and the Accounting Firms and Institutes Advisory Group (AFIAG) in June 2023. The UKEB also hosted roundtable events with UK Finance and with preparers. One written response to the DCL was also

received. A summary of the key feedback from stakeholders is presented in paragraphs 8-18 below.

7. Stakeholder discussion was wide ranging. The key themes are summarised below. Further detail can be seen in the April and June FIWG minutes, and in the June PAG, IAG and AFIAG minutes[1].

Derecognition of financial liabilities

8. Preparers and accounting firms considered that, as currently drafted, the alternative to settlement date accounting would not be widely used. There would be cost incurred in assessing whether payment systems met the criteria, and in the necessary system changes (which may encompass treasury, ledger and payment systems which one preparer noted was a "non-trivial" change). This was considered disproportionate for any benefit to preparers interested in using the expedient. It was noted use of the option would increase diversity in recognition policy both within entities (some systems may qualify, some may not) and between different entities.

9. The AFIAG and the FIWG reported that many businesses derecognise financial liabilities at the point of payment instruction. It was considered derecognition at that point underpinned good financial control. The PAG observed that their businesses were either already using settlement date accounting or could do so through a "true-up" mechanism, which would not be onerous, while other preparers we spoke to noted they derecognised at the point of payment instruction. Another stakeholder disagreed with the statement at BC10 that IFRS 9 already requires the use of settlement date accounting, and the related assumption that this amendment is only a clarification.

10. Regarding electronic payment systems currently used, the PAG, the AFIAG and UK Finance roundtable participants confirmed that BACS payments were widely used in the UK, alongside Faster Payments and credit cards. FIWG members and UK Finance roundtable participants thought that businesses would have to make global enquiries into current payment methods used, and whether they met the various criteria. It was thought that as BACS had a cancellation window of at least 24 hours, and as funds could be withdrawn prior to settlement commencing, it was unlikely to meet the criteria for use of the option.

11. Some stakeholders considered that a holistic assessment of the recognition/derecognition criteria for financial assets/liabilities may be more beneficial than making narrow changes in isolation for electronic payments. This would minimise unintended consequences. Stakeholders also noted the clarification that settlement date accounting applies to financial liabilities is more complex than presented. For example they noted that settlement date accounting is currently described in the standard in the context of financial assets, and may

[1] Minutes for the June PAG, IAG and AFIAG meetings are due to be published on 12, 13 and 14 July respectively.

not simply read across to financial liabilities due to the different timing or asymmetry of available information about cash movements for assets and liabilities.

12. A small number of stakeholders suggested the proposals should apply more broadly than to only those settled using electronic payment systems, and that any payment that met the criteria should qualify for use of the option.

Classification of financial assets

13. All stakeholder groups considered that the amendments relating to ESG-linked features were required urgently. This could be achieved by decoupling these requirements from the other proposals and having an earlier effective date, or by permitting early adoption of these proposals.

14. All stakeholder groups agreed that the proposals lacked sufficient clarity to ensure consistent application, and that the examples were overly simplistic and failed to show sufficient analytical detail.

15. The proposals related to the “direction and magnitude” of cash flow changes were noted by many as contradictory to the requirement to assess “what an entity is being compensated for rather than how much compensation an entity receives”, and potentially challenging to implement. It was acknowledged that the link between a change in contractual cash flows and a change in the basic lending risk/cost can be unclear, or difficult to evidence. The FIWG discussed ideas to improve the clarity of the new proposals, including those related to “direction and magnitude”, but no clear consensus was reached. Some suggestions inspired by that discussion have been incorporated into the FCL, either as marked-up changes to IASB text or as narrative suggestions.

16. The FIWG, the AFIAG and the UK Finance roundtable agreed the criteria for “*the occurrence (or non-occurrence) of the contingent event must be specific to the debtor*” would be problematic for transactions that contained ESG-linked features with targets elsewhere in the corporate group, and that the use of targets elsewhere in the group/at consolidated level should be permitted. One stakeholder did not support widening the scope to groups or other group entities, and suggested that using “party to the contract” may avoid needing to define “specific to the debtor” as this term is already understood from the IFRS 9 derivative definition.

17. Paragraph BC67 of the Amendments states that changes in contractual cash flows that are due to contingent events “*specific to the creditor or another party would be inconsistent with a basic lending arrangement*”. The FIWG and UK Finance roundtable participants expressed concern that this paragraph may have unintended consequences for loans with other features, including protective cost/tax clauses that are widespread in the UK market. This could result in many amortised cost loans needing to be reclassified to fair value through profit and loss.

Contractually Linked Instruments (CLIs) and non-recourse finance

18. The UK Finance roundtable and the April 2023 FIWG meeting suggested that elements of the IASB September board paper explanation of residual value risk within finance leases should be included within the Amendments.

Key changes

19. The table below summarises the key changes between the DCL and FCL.

Key changes Draft to Final Comment Letter	
Draft Comment Letter	**Final Comment Letter**
Derecognition of Financial Liabilities	
The option may be impractical as the timing for derecognition falls somewhere between time of instruction and settlement, resulting in system and operational costs disproportionate with benefit gained.	The fundamental point remains but language around this is strengthened. Further examples of practical difficulties are included in the text. The likely inconsistency in the timing of derecognition both within entities and between entities is highlighted.
Recommends the option allows derecognition at point of payment instruction instead.	Our recommendation remains unchanged, and has been supported by stakeholders.
This recommendation avoids the need for short term accounting entries (receivables/ cash in transit) which may give rise to further accounting diversity.	Standalone point removed from letter and merged with paragraph 10. Point remains at A10 of Appendix A..
Recommended the final sentence in B3.3.9 be deleted to streamline the multiple requirements re settlement risk.	Some stakeholders thought this sentence was necessary, while others disagreed. Streamlining the settlement risk language is a low priority compared to other more fundamental points raised in the letter, so this recommendation has been deleted.

n/a	New point added to suggest there may be benefit in the IASB conducting a holistic review of recognition/derecognition requirements instead of an isolated approach for electronic cash payments.
Classification of Financial Assets	
Notes that the UKEB deliberated whether it would be better for the IASB to take additional time to create a clearer set of principles, and that if this approach is not taken the IASB may need to revisit the proposals at a future date.	Expanded the point to emphasise that the IASB should consider whether instruments with contingencies qualifying for amortised cost accounting could impact other aspects of IFRS 9, and to highlight the importance of the pipeline project *Amortised Cost Measurement.*
The changes are unclear and do not adequately explain how the ESG-linked feature meets the basic lending criteria.	The fundamental point remains, but tone of the letter is strengthened and we highlight the IASB may be unable to comply with their stated objective of "clarifying the application guidance of…ESG linked features" if guidance is not improved.
Examples do not have sufficient complexity and analysis to mitigate for the above.	Point is expanded to specifically request three changes to examples – include more examples, show clearer analysis against the requirements, and make examples more complex.
Greater clarity is required regarding the "direction and magnitude test". Suggested wording to achieve this is provided.	Separated to stand alone section. Text expanded to acknowledge the link between cash flow and lending risk/cost may not always be clear or easy to evidence with this relatively new product set. Examples provided. Suggested wording modified to introduce the term "directionally consistent" rather than "direction and magnitude".
We note we are not convinced that "cashflows due to contingent event that is specific to the creditor or another party would be inconsistent with basic lending"	Following further feedback from stakeholders this point has been expanded to specifically reference protective cost/tax clauses, and note that as these are common in the UK market this may result in many existing

holds true in all cases. Recommended wording to address this provided.	amortised cost instruments being reclassified to fair value through profit and loss.
Use of ESG targets set elsewhere in the corporate group/consolidated level should not be a barrier to being considered basic lending.	No material change.
The ED proposals are likely to lead to a greater number of instruments qualifying for amortised cost accounting and encourage the IASB to commence the pipeline project *Amortised Cost Measurement* as soon as possible.	Standalone point removed and combined with the discussion of future IASB work at paragraph 13..

Final Comment Letter (FCL)

20. The FCL is attached for consideration and, subject to amendments agreed by the Board, approval for issue to the IASB and publication on the UKEB website.

Feedback Statement

21. The draft Feedback Statement relating to the FCL is attached for consideration and approval.

Due Process Compliance Statement (DPCS)

22. The draft DPCS for the project is attached for consideration. A final version will be brought back to the September 2023 meeting for noting once the final project steps are complete.

Questions for the Board
1. Subject to any amendments agreed at this meeting, does the Board approve: • The FCL for issue to the IASB and publication on the UKEB website? • The FS for publication on the UKEB website? 2. Does the Board have any comments on the draft DPCS for the project?

Next steps

23. The FCL will be submitted to the IASB on 19 July. The FCL together with the Feedback Statement will be published on the UKEB website. The DPCS will be updated to reflect the final project steps and presented at the September meeting for noting.

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IFRS 9: Classification & Measurement Exposure Draft Timeline

Date	**Milestone**	
Influencing phase		
24 April 2023	Outreach with the UKEB FIWG	Complete
27 April 2023	**Board:** Education session	Complete
27 April 2023	**Board:** Considers the PIP **Secretariat:** Revises PIP for any Board comments	Complete
18 May 2023	**Board:** Considers Draft Comment Letter **Secretariat:** Revises DCL for any Board comments	Complete
May 2023	**Secretariat:** Publishes Draft Comment Letter, comment period 30 days.	Complete
May-June 2023	Further outreach as described in the Project Initiation Plan.	Complete
13 July 2023	**Board:** Considers Final Comment Letter, Feedback Statement, draft Due Process Compliance Statement **Secretariat:** Revises documents for any Board comments.	To be completed
19 July 2023	IASB comment period ends **Secretariat:** submits Final Comment Letter **Secretariat:** Final Comment Letter and Feedback Statement published on website	To be completed
21 September 2023	**Board:** Approves final Due Process Compliance Statement	To be completed

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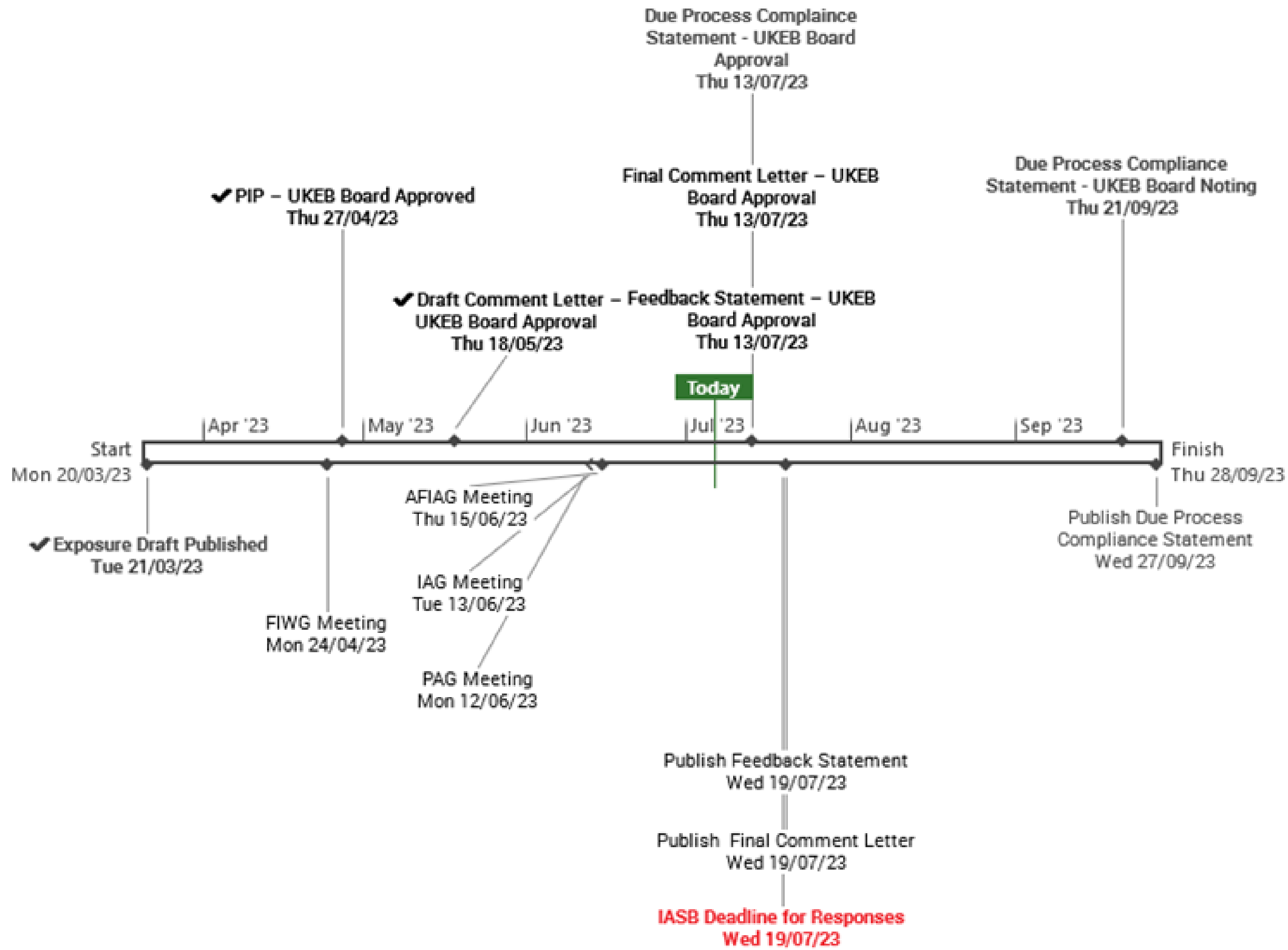
Timeline



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Dr Andreas Barckow
Chairman
International Accounting Standards Board`
Columbus Building
7 Westferry Circus
Canary Wharf
London
E14 4HD

XX July 2023

Dear Dr Barckow

Exposure Draft ED/2023/2 Amendments to the Classification and Measurement of Financial Instruments – Proposed amendments to IFRS 9 and IFRS 7

1. The UK Endorsement Board (UKEB) is responsible for endorsement and adoption of IFRS Accounting Standards for use in the UK and therefore is the UK's National Standard Setter for IFRS Accounting Standards. The UKEB also leads the UK's engagement with the IFRS Foundation on the development of new standards, amendments and interpretations. This letter is intended to contribute to the Foundation's due process. The views expressed by the UKEB in this letter are separate from, and will not necessarily affect the conclusions in, any endorsement and adoption assessment on new or amended international accounting standards undertaken by the UKEB.

2. There are currently approximately 1,500 entities with equity listed on the London Stock Exchange that prepare their financial statements in accordance with IFRS.[1] In addition, UK law allows unlisted companies the option to use IFRS and approximately 14,000 such companies currently take up this option.[2]

3. We welcome the opportunity to provide comment on the International Accounting Standards Board (IASB) Exposure Draft (ED) *Amendments to the Classification and Measurement of Financial Instruments: Proposed amendments to IFRS 9 and IFRS 7* (the Amendments). In developing this letter, we have consulted with stakeholders in the UK, including users of accounts, preparers of accounts, and accounting firms and institutes.

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1 UKEB calculation based on LSEG and Eikon data, May 2023. This calculation includes companies listed on the Main market as well as on the Alternative Investment Market (AIM).

2 UKEB estimate based on FAME, Companies Watch and other proprietary data.

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4. We welcome the IASB's responsiveness to the concerns raised by stakeholders, including those in our response[3], on the request for information on the *Post-implementation Review of IFRS 9 – Classification and Measurement.* The UKEB highlighted the following concerns:

    a) The potential unintended consequences for the derecognition of financial liabilities arising from the IFRS Interpretations Committee tentative agenda decision *Cash Received via Electronic Transfer as Settlement for a Financial Asset*.

    b) The importance of making it easier for financial instruments with ESG-linked features to achieve amortised cost accounting in circumstances where they are, in substance, basic lending transactions.

    c) The need for further guidance on the application of the effective interest method, particularly in relation to the application of IFRS 9 paragraphs B5.4.5 and B5.4.6.

    d) The need for increased clarity in distinguishing between non-recourse finance and contractually linked instruments when applying the cash flow characteristics test.

5. We note and welcome that the ED addresses most of these matters, with the remaining item addressed in the IASB pipeline project *Amortised Cost Measurement*. Our main observations and recommendations are set out in the paragraphs that follow. Responses to the IASB's specific questions about the ED are included in the Appendix to this letter.

Derecognition of financial liabilities

6. We welcome the IASB's proposal to create an option when derecognising financial liabilities settled with cash using an electronic payment system. This acknowledges that such payment methods have different characteristics to historic forms of payment, including greater speed and certainty of settlement. Without this option, the clarification that settlement date accounting is required may be disruptive and costly for those using other derecognition approaches. However, we are concerned that the proposals, in their current form, may only have limited success in addressing stakeholder concerns. It is important that any option granted is sufficiently cost-effective to enable its application.

7. We consider that the successful implementation of the proposals depends on whether the criteria for use of the option can be applied to common electronic

[3] Comment letter to the IASB on the Post-implementation Review of IFRS 9 – Classification and Measurement, 28 January 2022 , link to document here.

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payment systems, without imposing disproportionate operational cost on entities. Our analysis has identified significant doubts as to whether the application of the new requirements to some of the major UK payment systems, such as BACS, could achieve the proposed accounting without incurring disproportionate disruption and costs. No stakeholders consulted in our outreach for this project expressed interest in using this option.

8. A strict interpretation of the criteria for applying the option would indicate that derecognition of the liability would be required to take place sometime between the date of instruction to the electronic payment system and settlement date. The exact timing of this derecognition would vary by payment system and banking provider. This is further explained in ED paragraphs A6 - A7 and A11- A12 of Appendix A. The system and operational costs to identify and account for the different timings of these events would be likely to be disproportionate to the benefit gained, leading to limited take up. As many entities use more than one payment system this option will also increase inconsistency in derecognition practices. Some payment systems will qualify for the option and some will not (or will not have been subject to an assessment process against the criteria), leading to multiple derecognition practices both within a single entity and between different entities.

9. Instead, we recommend that the accounting should aim to provide a simple and practical method of managing and recording transactions that have only a short duration. Electronic payments have a short settlement period and a cancellation window which is even shorter. Further, we are informed by preparers and accounting firms that the cancellation of such payments is rare. The date of instruction is easily identifiable, and, as it does not vary by settlement system or banking provider, would allow for consistent application by all entities. This suggests that for many electronic payment systems the most appropriate alternative to settlement date accounting is one that allows derecognition of the liability at the point the instruction for payment is made. We think such an approach will be readily understood by users and will avoid disruption and improve consistency amongst preparers.

10. Finally, we question whether sufficient time has been spent on assessment of the broader consequences of clarifying the derecognition requirements for financial assets and liabilities. The exposure draft specifically refers to IFRS 9 paragraph B3.1.6 which discusses settlement date accounting in the context of assets. However, due to the asymmetry of information regarding the receipt of cash payments it should not be assumed that requirements for the settlement of assets can be directly read across to liabilities. Additionally, the proposals in the ED would create the need to record short term accounting entries (receivables or cash-in-transit) for the brief period between the payment instruction and the point at which cancellation is no longer possible. This is operationally complex and would provide little benefit to users of accounts. As this matter is not urgent, should the IASB not proceed with our recommendation above, we consider there

would be merit in the IASB withdrawing this section of the proposals and conducting a project to look more holistically at the question of trade/settlement date accounting for assets and liabilities. This would minimise the risk of unintended consequences, and also provide an opportunity to consider the issues raised regarding the derecognition of financial assets in the IFRS Interpretations Committee tentative decision *Cash Received via Electronic Transfer as Settlement for a Financial Asset*s, which this ED does not address.

Classification of financial assets

11. We welcome the IASB's work in this area, which we previously identified as one in which the requirements of IFRS 9[4] could be improved. We believed that in the absence of clear guidance inconsistent accounting practices would develop. Our stakeholders previously told us, and still assert, that many financial instruments that would be considered basic lending, but for the ESG-linked feature, should be measured at amortised cost.

12. We believe the ED proposals, in their current form, are only partially successful in addressing these concerns. We acknowledge that in drafting these proposals the IASB has attempted to make only limited changes to IFRS 9, mainly to avoid any unintended consequences. However, our outreach has indicated that this has led to a lack of clarity in the proposals that, in turn, could lead to considerable diversity in practice and, contrary to the IASB's intention, unintended consequences.

13. When considering these proposals, we deliberated whether it would be beneficial for the IASB to take additional time to create a clearer set of principles that would provide a more robust framework better able to address future events and innovations. In the absence of this, we consider there is a high risk the IASB will need to revisit these proposals at a future date. The pipeline project *Amortised Cost Measurement* will be critical to ensure that instruments with ESG-linked features (or other contingencies), which are now more likely to qualify for amortised cost accounting, can be measured consistently and on an appropriate basis. Consideration should also be given as to whether instruments with contingencies qualifying for amortised cost accounting could impact other aspects of IFRS 9. We therefore encourage the IASB to commence its pipeline project as soon as possible and to ensure the consequences of the changes in classification requirements are addressed as necessary in the wider standard.

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4 Comment letter to the IASB on the Post-implementation Review of IFRS 9 – Classification and Measurement, 28 January 2022, link to document here.

14. However, we are also cognisant that during outreach certain UK stakeholders emphasised the urgency of resolving the classification of instruments with ESG-linked features. Should the IASB conclude that this urgency requires a pragmatic solution, we identify below the critical changes necessary to allow the current proposals to work in practice. Our detailed observations and recommendations are included in paragraph A15 - A25 of Appendix A.

    a) It is not currently clear how ESG-linked features comply with the concepts of basic lending risks and costs explained in paragraphs B4.1.7A and B4.1.8A. Further detailed guidance is necessary to explain how the ESG-linked feature represents basic lending risks or cost. If these principles cannot be readily understood, they will be difficult to apply to financial instruments with ESG-linked features and other future contracts with contingent events, leading to greater diversity in practice. Unless further guidance is provided there is a risk that the IASB will not meet its objective stated at IN5b of the ED to "clarify the application guidance for assessing the contractual cash flow characteristics of financial assets including...those with ESG-linked features".

    b) The new requirement regarding the "magnitude and direction" of cash flows appears contradictory and challenging to implement. Further consideration should be given to how the statement at B4.1.8A that the assessment should focus on "what an entity is being compensated for, rather than how much compensation an entity receives" sits alongside the requirement in the same paragraph to assess the "magnitude of the change". At face value this appears contradictory. In practice identifying an appropriate cash flow magnitude for any given change in risk/cost may prove challenging as such relationships may be complex and subjective. In this relatively young market the link between the cash flow and the change in risk/cost may be unclear or difficult to quantify. This is further discussed, and suggested wording to clarify the proposals is provided, in paragraphs A17 -A20 of Appendix A.

    c) The current examples at B4.1.13 and B4.1.14 are simplistic and therefore not helpful in resolving the issues of interpretation of the basic lending and direction and magnitude requirements described above. We suggest that further clarity in the text of the standard should be accompanied by more comprehensive examples to provide clarification to stakeholders and ensure consistent application. These examples should clearly analyse the key features of the instrument and how they meet (or fail to meet) the criteria set out in the amended classification requirements at B4.1.7A – B4.1.10A. This would demonstrate how the various criteria are applied to the fact pattern to arrive at the proposed classification. Without this we anticipate significant diversity in practice when entities attempt to apply the proposals.

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15. The ED requires contingent events to be "specific to the debtor" if amortised cost accounting is to be achieved (paragraph B4.1.10A and BC67). We agree with the IASB that reference to ESG targets external to the group (for example to an industry index) is beyond the scope of basic lending and should not meet the test at B4.1.10A as "specific to the debtor". However, the current drafting appears problematic for both ESG-linked instruments and other types of contingent events.

    a) A strict interpretation of the criterion at B4.1.10A that the contingent event be "specific to the debtor" implies that only ESG-linked targets set at the level of the borrowing entity would be successful in meeting the criteria for contractual cashflows that are solely payments of principal and interest. Given emerging market practice, we consider that it may be necessary to permit classification as basic lending for loans with ESG-linked targets set at consolidated level or referencing other group companies where the incentive to change ESG-related behaviour is most relevant.

    b) One unintended consequence of the "specific to the debtor" criteria could be for other contingent events that are today considered compatible with basic lending. For example, certain protective cost clauses or tax clauses are common in contracts considered to represent basic lending, but these clauses may relate to contingent events specific to other parties (for example, to the creditor or to the government in the context of changing laws, taxes or regulation). Such clauses relate to the cost associated with extending credit to the debtor, which is one of the permitted features of basic lending. However, such clauses would not meet the "specific to the debtor test" nor the associated explanation at BC67 that in a basic lending arrangement the creditor is "compensated only for basic lending risks and the cost associated with extending credit to the debtor. Therefore, a change in cash flows due to a contingent event that is specific to the creditor or another party would be inconsistent with a basic lending arrangement". If this criterion is not corrected this could result in significant numbers of basic lending transactions currently classified at amortised cost being re-classified as fair value through profit or loss.

    Suggested wording to address the issues described at paragraph 15a and 15b is provided at paragraph A25 of Appendix A. Further ideas to address the issue described at paragraph 15a have been included at paragraph A23 of Appendix A.

16. Further detail on these topics can be found in Appendix A to this letter.

17. If you have any questions about this response, please contact the project team at UKEndorsementBoard@endorsement-board.uk.

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Yours sincerely

Pauline Wallace
Chair
UK Endorsement Board

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UK Endorsement Board

Appendix A: Questions on ED *Amendments to the Classification and Measurement of Financial Instruments*

Question 1—Derecognition of a financial liability settled through electronic transfer
Paragraph B3.3.8 of the draft amendments to IFRS 9 proposes that, when specified criteria are met, an entity would be permitted to derecognise a financial liability that is settled using an electronic payment system although cash has yet to be delivered by the entity. Paragraphs BC5–BC38 of the Basis for Conclusions explain the IASB's rationale for this proposal. Do you agree with this proposal? If you disagree, please explain what aspect of the proposal you disagree with. What would you suggest instead and why?

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Overview

A1. We welcome the IASB's proposal to create an option when derecognising financial liabilities settled with cash using an electronic payment system. This acknowledges that such payment methods have different characteristics to historic forms of payment, including greater speed and certainty of settlement. Without this option, the clarification that settlement date accounting is required may be disruptive and costly for those using other derecognition approaches. However, we are concerned that the proposals, in their current form, may only have limited success in addressing stakeholder concerns. It is important that any option granted is sufficiently cost-effective to enable its application.

A2. We consider that the successful implementation of the proposals depends on whether the criteria for use of the option reflect common electronic payment systems, without imposing disproportionate operational cost on entities. Our analysis has identified significant doubts as to whether these new requirements would allow the option to be used for some major UK payment systems, such as BACS, without entities incurring disproportionate disruption and costs. No stakeholders consulted during our outreach expressed interest in using this option should it become available.

A3. Further, as every payment system in every jurisdiction would need to be assessed to use the proposed option, it is likely that entities would find themselves using the

option for some payment systems (which passed the criteria in paragraph B3.3.8) but not others (systems which did not pass the criteria, or where the entity chose not to invest in performing the assessment). This will lead to greater inconsistency in the derecognition of financial liabilities between entities, and even within the same entity or group.

A4. The proposals clarify the use of settlement date accounting for financial liabilities. In doing so ED paragraph B3.1.2A specifically refers to IFRS 9 paragraph B3.1.6, which only discusses settlement date accounting in the context of assets. However, due to the information asymmetry regarding cash payments it cannot be assumed that requirements for the settlement of assets directly read across to the settlement of liabilities, as information on whether the recipient has received the funds is less readily available. If the IASB does not adopt the recommendation at A8 below to allow derecognition at the time of payment instruction, we consider there would be merit in the IASB withdrawing this proposal and undertaking a longer-term project to consider settlement date accounting and the recognition and derecognition of financial assets and liabilities more holistically. This would minimise the risk of unintended consequences and provide an opportunity to consider the issues on the derecognition of financial assts raised in the IFRS Interpretations Committee tentative decision *Cash Received via Electronic Transfer as Settlement for a Financial Asset*, which this ED does not address.

A5. Investors we spoke to assumed assets and liabilities were derecognised at the same time and appreciated the symmetry this provided should any timing difference be material. However we note disclosure of the accounting policy choice as to whether the option was used, and the associated timing of derecognition, under IAS 1 *Presentation of Financial Statements,* would assist investor understanding.

Ability to stop, withdraw or cancel

A6. Paragraph B3.3.8(a) specifies that "the entity has no ability to withdraw, stop or cancel the payment instruction". This seems very restrictive. For example, we question whether the fact that a system permits the cancellation of a fraudulent transaction should affect the accounting classification of all other transactions on that system. It is also operationally complex. For many UK payment systems, the point at which there is no ability to cancel a payment (Time Cancellation "TC") is subsequent to the issuance of the payment instruction (Time of Instruction "TI"). We are aware of a number of operational complexities in this context, including:

a) TC varies by type of electronic payment system.

b) For each electronic payment system TC may vary by instructing bank.

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c) TC could also be subject to individual circumstances related to factors such as what time of day both TI and TC occurred.

d) Entities are likely to use multiple electronic payment systems depending on their business needs, and may have more than one banking relationship.

A7. An example of this would be the BACS system, one of the highest volume electronic payment processing systems in the UK. Once a payment instruction is issued, BACS has an approximate three-day processing cycle but entities have an approximate one-day window for cancellation, the exact timing of which varies depending on which bank is used. This complexity is likely to make the proposed option costly to implement in operational and accounting systems. Where an option is to be provided as a practical expedient, this extra cost appears disproportionate to any benefit gained.

A8. In our view the accounting should aim to provide a simple and practical method of managing and recording transactions that have only a short duration. Electronic payments have a short settlement period and a cancellation window which is even shorter. Further, we are informed by preparers and accounting firms that it is rare for such payments to be cancelled. Cancellations are subject to financial penalty, and considerable practical barriers including the resource impact of cancelling and reperforming batch payment runs, and relationship management issues with other suppliers expecting payment in the cancelled batch. The date of instruction is easily identifiable, and, as it does not vary by settlement system or banking provider, would allow for consistent application by all entities. This suggests that for many electronic payments the most appropriate option is one that allows derecognition of the liability settled by electronic payment system at the time the instruction for the payment is made. We think such an approach will be readily understood by users and will avoid disruption and improve consistency amongst preparers.

A9. However, should the IASB proceed with the existing proposals, we recommend that the criteria regarding cancellation at paragraph B3.3.8a be removed or, failing that, modified to read "no practical ability to withdraw, stop or cancel…".

A10. The proposals in the ED would create the need to record short term accounting entries (receivables or cash-in-transit) for the brief period between the payment instruction and the point at which cancellation is no longer possible. This is operationally complex and would provide little benefit to users of accounts. Our proposed solution above avoids the need to decide whether cash moving through the settlement system represents cash-in-transit or a receivable, eliminating another potential source of diversity in practice.

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Other considerations

A11. In the absence of a definition of "electronic payment system" there appears to be confusion amongst UK stakeholders as to what is the intended scope of electronic payment systems. Discussions with stakeholders considered four main types of payment systems:

a) Those that move money from a bank account shortly after a payment instruction (for example in the UK these include BACS, Faster Payments, CHAPS and SWIFT).

b) Those that move money from a bank account on a regular basis established in advance (in the UK these include Direct Debit and Standing Orders).

c) Card based payments, including debit cards and credit cards.

d) Other digital payment methods including Apple Pay, Google Pay and PayPal (where the underlying payment mechanism may be linked to items A11a. or A11c. above).

A12. Based on our high level analysis it seems possible some systems will never meet the criteria for use of the option as currently drafted, effectively falling permanently outside its scope. It is possible the IASB did not intend some payment systems, such as those described at A11d, to be within the scope of these proposals. Our stakeholder outreach has indicated differing opinions as to whether certain types of systems were intended to be considered, and whether such payment systems can ever pass the necessary criteria. If it was IASB's intention to exclude certain common payment systems, clarification of that would be helpful in ensuring consistent practice.

Question 2—Classification of financial assets—contractual terms that are consistent with a basic lending arrangement
Paragraphs B4.1.8A and B4.1.10A of the draft amendments to IFRS 9 propose how an entity would be required to assess: a) interest for the purposes of applying paragraph B4.1.7A; and b) contractual terms that change the timing or amount of contractual cash flows for the purposes of applying paragraph B4.1.10. The draft amendments to paragraphs B4.1.13 and B4.1.14 of IFRS 9 propose additional examples of financial assets that have, or do not have, contractual cash flows that are solely payments of principal and interest on the principal amount outstanding.

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Question 2—Classification of financial assets—contractual terms that are consistent with a basic lending arrangement
Paragraphs BC39–BC72 of the Basis for Conclusions explain the IASB's rationale for these proposals. Do you agree with these proposals? Why or why not? If you disagree, please explain what aspect of the proposals you disagree with. What would you suggest instead and why?

Overview

A13. We welcome the IASB's work in this area, which we previously identified as one in which the requirements of IFRS 9[5] could be improved. We believed that in the absence of clear guidance inconsistent accounting practices would develop. Our stakeholders previously told us and still assert that financial instruments which, but for the ESG-linked feature, would be considered basic lending should be measured at amortised cost.

A14. We believe the proposals, in their current form, are only partially successful in addressing these concerns. We acknowledge that in drafting these proposals the IASB has attempted to make only limited changes to IFRS 9. However, this has led to proposals that are unclear and likely to lead to diversity in practice. To achieve the IASB's stated objective (paragraph IN5b of the ED) to "clarify the application guidance for assessing the contractual cash flow characteristics of financial assets including...those with ESG-linked features" further guidance will be required. The key issues that should be resolved to meet this objective are:

a) Further detailed guidance should be provided that explains how the ESG-linked feature represents basic lending risks or cost.

b) Further consideration should be given to how the statement at B4.1.8A that the assessment should focus on "what an entity is being compensated for, rather than how much compensation an entity receives" sits alongside the requirement in the same paragraph to assess the "magnitude of the change".

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5 Comment letter to the IASB on the Post-implementation Review of IFRS 9 – Classification and Measurement, 28 January 2022, link to document here.

c) More complex and comprehensive examples should be provided. The current examples at B4.1.13 and B4.1.14 are simplistic and therefore not helpful in resolving the issues of clarity noted above..

d) Further consideration should be given to the requirement that contingent events must be "specific to the debtor" if amortised cost accounting is to be achieved (paragraph B4.1.10A and BC67). We agree with the IASB that reference to ESG targets external to the group (for example to an industry index) is beyond the scope of basic lending and should not meet the test at B4.1.10A as "specific to the debtor". However, the current drafting appears problematic for both ESG-linked instruments and other types of contingent events.

These issues are explained further in paragraphs A15 - A25 below.

Detailed feedback

Clarity of requirements

A15. Further detailed guidance should be provided that explains how the ESG-linked feature represents basic lending risks or cost. The approach taken in paragraph B4.1.8A ,which describes characteristics which may be inconsistent with basic lending, is helpful as highlighting such "red flags" can provide a practical basis for application and interpretation. However, it remains unclear how ESG-linked features comply with the concepts of basic lending risks and costs explained in paragraphs B4.1.7A and B4.1.8A. If these principles cannot be readily understood, they will be difficult to apply to ESG-linked features and other future contracts with contingent events, leading to greater diversity in practice. Unless further guidance is provided there is risk that the IASB will not meet its objective stated at IN5b of the ED to "clarify the application guidance for assessing the contractual cash flow characteristics of financial assets including...those with ESG-linked features".

The use of examples

A16. The examples of analysis currently shown in ED paragraphs B4.1.13 and B4.1.14 are simplistic, and the analysis column arrives directly at the conclusion without any analysis demonstrating how each of the relevant criteria described at paragraph B4.1.7.A – B4.1.10A is met. We recommend:

a) The analysis column be revised to show an assessment of each fact pattern against the proposed criteria, to determine if the fact pattern is consistent with the criteria for basic lending and whether there are any "red flags" present that would raise doubt about such a conclusion.

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b) More complex examples are included. This would better illustrate the application of the criteria.

c) An increased number of examples is used to assist understanding. As the guidance in this area is not clear the use of more examples than are used elsewhere in IFRS 9 may assist in demonstrating the IASB's intent. We would be happy to assist the IASB staff in identifying or testing suitable examples.

Direction and magnitude

A17. Further consideration should be given to how the statement at B4.1.8A that the assessment should focus on "what an entity is being compensated for, rather than how much compensation an entity receives" sits alongside the requirement in the same paragraph to assess the "magnitude of the change". At face value this appears contradictory and has caused some confusion amongst stakeholders, in terms of understanding both the nature of the requirement and its application.

A18. In practice, identifying an appropriate cash flow magnitude for any given change in risk/cost may prove challenging as such relationships can be complex and subjective. The use of softer language such as "directionally consistent" rather than "direction and magnitude" may reduce such difficulties without losing the overall intent explained in paragraph BC52.

A19. Paragraph B4.1.8A states that "a change in contractual cashflows is inconsistent with a basic lending arrangement if it is not aligned with the direction and magnitude of the change in basic lending risks or costs". However, we note that at times there may be no clear link, or such a link may be difficult to demonstrate. For example, a bank may accept a lower margin if specified ESG-related targets are met by the borrower to gain business advantageous to the bank's market position and its own ESG objectives. In this case a bank may accept a lower profit margin despite the risk of lending not having decreased. As margin is an acceptable element of basic lending as described at IFRS 9 B4.1.7A, such an arrangement should still be considered basic lending, assuming the magnitude of the change is not so great as to eliminate margin altogether. In other cases, improved ESG performance may link to improved credit risk of the borrower, but this may be difficult to demonstrate and quantify for these relatively new instruments. We have suggested revised wording to accommodate this in paragraph A20 below.

Direction and magnitude – proposed text

A20. In addition, to provide clarity and reduce the risk of diversity in practice, we make the following recommendation and highlight other stakeholder feedback the IASB may wish to consider :

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a) We recommend moving the “direction and magnitude” requirement to paragraph B4.1.10A, where other changes to contractual cashflows are discussed, incorporating some of the text from BC52 and BC70, and providing further clarification as shown below.

b) Alternatively, some stakeholders have suggested the “direction and magnitude” requirements cover the same ground as the leverage requirements at B4.1.9 of IFRS 9. If that was the IASB’s intent then referring to that section of the standard rather than introducing new language may be more effective.

c) The criteria at B4.1.10A that “the resulting contractual cashflows must represent neither an investment in the debtor nor an exposure to the performance of specified assets” would benefit from further clarification. Presumably this requirement is intended to refer to the financial performance of the specified assets, not the assets’ ESG performance. For instruments with ESG-linked targets the lender is likely to be exposed to the borrower’s ESG performance, as this may vary the interest rate paid. To improve clarity we recommend amending the requirement to “the resulting contractual cashflows must represent neither an investment in the debtor nor an exposure to the financial performance of the specified assets”.

Exposure Draft text (with UKEB markup)
B4.1.10A In applying paragraph B4.1.10, an entity shall assess whether contractually specified changes in cash flows following the occurrence (or non-occurrence) of any contingent event would give rise to cash flows that are solely payments of principal and interest on the principal amount outstanding. This assessment shall be done irrespective of the probability of the contingent event occurring (except for non-genuine contractual terms as described in paragraph B4.1.18). For a change in contractual cash flows to be consistent with a basic lending arrangement, the occurrence (or non-occurrence) of the contingent event must be specific to the debtor and its impact on contractual cash flows expected to be ~~aligned with the direction and magnitude of~~ directionally consistent with the change in basic lending risks or costs. The occurrence of a contingent event is specific to the debtor if it depends on the debtor achieving a contractually specified target, even if the same target is included in other contracts for other debtors. However, the resulting contractual cash flows must represent neither an investment in the debtor (for example, contractual terms that entitle the creditor to a share of the debtor’s revenue or profits) nor an exposure to the financial performance of specified assets (see also paragraphs B4.1.15–B4.1.16). A change in contractual cash flows is directionally consistent with the

> change in basic lending risks or costs when, for example, an increase in the credit risk of a borrower is reflected in an increase, and not a decrease, in the interest rate of the financial asset.

Specific to the debtor

A21. The ED requires contingent events to be "specific to the debtor" if amortised cost accounting is to be achieved (paragraph B4.1.10A and BC67). We agree with the IASB that reference to ESG targets external to the group (for example to an industry index) is beyond the scope of basic lending and should not meet the test at B4.1.10A as "specific to the debtor". We acknowledge this may mean that ESG-linked targets referencing "Scope 3" emissions (i.e. the ESG performance of value chains) is not in scope for basic lending. However, the current drafting appears problematic for both ESG-linked instruments and other types of contingent events.

Specific to the debtor – ESG-linked features

A22. A strict interpretation of the criterion at B4.1.10A that the contingent event be "specific to the debtor" implies that only ESG-linked targets set at the level of the borrowing entity would be successful in meeting the criteria for contractual cashflows that are solely payments of principal and interest. In accordance with emerging market practice, we consider that entities should be permitted to classify as basic lending loans with ESG-linked targets set at consolidated level or referencing other group companies where the incentive to change ESG-related behaviour is most relevant.

A23. For ESG-linked contingent events there are a number of ways the IASB could make clear that consolidated, parent or other group company ESG targets are acceptable to meet the criteria at ED paragraph B4.1.10A. The most straightforward would be to define "specific to the debtor" (although we note this may give rise to unintended consequences). Alternatively modified wording such as that presented at paragraph A25 below could be used. A lighter touch approach could be to include the concept in one of the examples included in the standard to demonstrate this intent. In the example at paragraph B4.1.13 the description of Instrument EA could be modified to say "if the debtor achieves a contractually specified reduction in the group's consolidated greenhouse gas emissions". Such guidance may be sufficient for a common understanding to be established, without introducing new definitions that may lead to unintended consequences elsewhere.

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Specific to the debtor - other

A24. The "specific to the debtor" criteria could also be problematic for other contingent events that are today considered compatible with basic lending. For example, certain protective cost clauses or tax clauses are common in contracts considered to represent basic lending, but these clauses may relate to contingent events specific to other parties (for example, to the creditor or to the government in the context of changing laws, taxes or regulation). Such clauses relate to the cost associated with extending credit to the debtor, which is one of the permitted features of basic lending. However, such clauses would not meet the "specific to the debtor test" nor the associated explanation at BC67 that in a basic lending arrangement the creditor is "compensated only for basic lending risks and the cost associated with extending credit to the debtor. Therefore, a change in cashflows due to a contingent event that is specific to the creditor or another party would be inconsistent with a basic lending arrangement". If this criterion is not corrected this could result in significant numbers of basic lending transactions currently classified at amortised cost being re-classified as fair value through profit or loss.

Specific to the debtor – proposed text

A25. To acknowledge these issues, and to allow entities to better apply judgement based on individual fact patterns, we recommend the wording of these paragraphs be modified as below.

Exposure Draft text (with UKEB markup) B4.1.10A In applying paragraph B4.1.10 an entity shall assess whether contractually specified changes in cash flows following the occurrence (or non-occurrence) of any contingent event would give rise to cash flows that are solely payments of principal and interest on the principal amount outstanding. This assessment shall be done irrespective of the probability of the contingent event occurring (except for non-genuine contractual terms as described in paragraph B4.1.18). A contingent event which is specific to the debtor is consistent with a basic lending arrangement. ~~For a change in contractual cashflows to be consistent with a basic lending arrangement, the occurrence (or non-occurrence) of the contingent event must be specific to the debtor.~~ The occurrence of a contingent event is specific to the debtor if it depends on the debtor achieving a contractually specified target, even if the same target is included in other contracts for other debtors. However the resulting contractual cashflows must represent neither an investment in the debtor nor an exposure to the performance of specified assets.

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> BC67 The IASB acknowledged that requiring a contingent event to be "specific to the debtor" has similarities to the definition of a derivative in IFRS 9, which refers to a "non-financial variable" that "is not specific to a party to the contract". However, in a basic lending arrangement, the creditor is compensated only for basic lending risks and the cost associated with extending credit to the debtor. Therefore, a change in cashflows due to a contingent event that is specific to the creditor or another party would usually be inconsistent with a basic lending arrangement.

Question 3—Classification of financial assets—financial assets with non-recourse features
The draft amendments to paragraph B4.1.16 of IFRS 9 and the proposed addition of paragraph B4.1.16A enhance the description of the term 'non-recourse'. Paragraph B4.1.17A of the draft amendments to IFRS 9 provides examples of the factors that an entity may need to consider when assessing the contractual cash flow characteristics of financial assets with non-recourse features. Paragraphs BC73–BC79 of the Basis for Conclusions explain the IASB's rationale for these proposals. Do you agree with these proposals? Why or why not? If you disagree, please explain what aspect of the proposals you disagree with. What would you suggest instead and why?

Financial assets with non-recourse features

A26. The UKEB generally supports the proposals outlined in this section. However, stakeholders have told us that ED paragraph B4.1.16A describing non-recourse features could be read very narrowly, and would be likely to exclude most items other than waterfall arrangements from the non-recourse guidance. This is not how this section of IFRS 9 has been interpreted to date. The previous text at B4.1.16 referred to a creditor's claim being limited to specified assets of the debtor OR the cash flows from specified assets, whereas the proposed replacement text at B4.1.16A requires the contractual right to receive cashflows over the life of the asset AND in the case of default. So now both default (the asset) and life of the asset (cash flow) tests must be considered, whereas previously meeting either of these criteria was sufficient to qualify as a non-

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recourse feature. If this was not the IASB's intention, then further explanation to clarify this matter would be helpful.

Question 4—Classification of financial assets—contractually linked instruments
The draft amendments to paragraphs B4.1.20–B4.1.21 of IFRS 9, and the proposed addition of paragraph B4.1.20A, clarify the description of transactions containing multiple contractually linked instruments that are in the scope of paragraphs B4.1.21–B4.1.26 of IFRS 9. The draft amendments to paragraph B4.1.23 clarify that the reference to instruments in the underlying pool can include financial instruments that are not within the scope of the classification requirements of IFRS 9. Paragraphs BC80–BC93 of the Basis for Conclusions explain the IASB's rationale for these proposals. Do you agree with these proposals? Why or why not? If you disagree, please explain what aspect of the proposals you disagree with. What would you suggest instead and why?

Contractually linked instruments

A27. We welcome the IASB's efforts to clarify the distinction between non-recourse finance and contractually linked instruments. The proposals now make it clear that contractually linked instruments are considered a subset of non-recourse finance for IFRS reporting purposes. However, this clarification gives rise to potential further confusion that both the non-recourse and contractually linked instrument contractual cashflow tests may apply to contractually linked instruments, as one is a subset of the other. This could lead to diversity in practice, and we therefore recommend a further clarification that contractually linked instruments only need to be assessed using the criteria at ED paragraphs B4.1.20 – B4.1.26. This is implied at B4.1.20A but should be more explicitly stated.

A28. We welcome the fact that the text now makes clear that items which are in substance bilateral secured lending arrangements are not within the scope of the contractually linked instrument requirements.

A29. With reference to the underlying pool of assets ED paragraph B4.1.23 refers to lease receivables. The current text could be interpreted as implying that lease receivables would always meet the proposed cashflow characteristics test, which we do not believe was the IASB's intention. We note that the IASB has already considered this issue in the IASB staff paper presented to the September IASB

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meeting[6]. That paper noted that leases may have cash flow characteristics similar to solely payments of principal and interest, but may have other features such as exposure to residual value risk or to residual value guarantees that would fail to meet the characteristics of the contractual cash flows test. We recommend that this guidance is included in this section of the proposals and provide suggested wording below.

Exposure Draft text (with UKEB markup)
B4.1.23 The underlying pool must contain one or more instruments that have contractual cash flows that are solely payments of principal and interest on the principal amount outstanding. For the purpose of this assessment, the underlying pool can include financial instruments that are not within the scope of the classification requirements (see Section 4.1 of this Standard) for example, lease receivables that have contractual cash flows that are equivalent to payments of principal and interest on the principal amount outstanding. However, an entity must assess the effects of any other features of the financial instrument for compliance with the contractual cash flow requirements. For example some lease receivables may be subject to residual value risk or guarantees. Such features may not be consistent with a basic lending arrangement.

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6 AP16B Financial assets with non-recourse features and contractually linked instruments, paragraph 51-54, September 2022, https://www.ifrs.org/content/dam/ifrs/meetings/2022/september/iasb/ap16b-ccfc-financial-assets-with-non-recourse-features-and-clis.pdf

Question 5—Disclosures—investments in equity instruments designated at fair value through other comprehensive income
For investments in equity instruments for which subsequent changes in fair value are presented in other comprehensive income, the Exposure Draft proposes amendments to: a) paragraph 11A(c) of IFRS 7 to require disclosure of an aggregate fair value of equity instruments rather than the fair value of each instrument at the end of the reporting period; and b) paragraph 11A(f) of IFRS 7 to require an entity to disclose the changes in fair value presented in other comprehensive income during the period. Paragraphs BC94–BC97 of the Basis for Conclusions explain the IASB's rationale for these proposals. Do you agree with these proposals? Why or why not? If you disagree, please explain what aspect of the proposals you disagree with. What would you suggest instead and why?

Disclosure – Investments in equity instruments designated at fair value through other comprehensive income

A30. We understand the IASB has proposed these changes in relation to feedback in the previous consultation requesting the recycling to profit or loss of fair value changes previously recognised in other comprehensive income once an investment is disposed of. We do not believe this is an issue of widespread concern in the UK.

A31. The IASB's response, to provide additional disclosure on changes in the fair value of equity instruments, including for those investments derecognised in the reporting period, provides users of financial statements with additional relevant information on this topic. We agree with these proposals.

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Question 6—Disclosures—contractual terms that could change the timing or amount of contractual cash flows
Paragraph 20B of the draft amendments to IFRS 7 proposes disclosure requirements for contractual terms that could change the timing or amount of contractual cash flows on the occurrence (or non-occurrence) of a contingent event. The proposed requirements would apply to each class of financial asset measured at amortised cost or fair value through other comprehensive income and each class of financial liability measured at amortised cost (paragraph 20C). Paragraphs BC98–BC104 of the Basis for Conclusions explain the IASB's rationale for this proposal. Do you agree with this proposal? Why or why not? If you disagree, please explain what aspect of the proposal you disagree with. What would you suggest instead and why?

Disclosure – Contractual terms that could change the timing or amount of contractual cashflows.

Disclosure objectives

A32. The proposals in paragraphs 20B and 20C of the ED add requirements to disclose the nature of contingent events specific to the debtor, quantitative information about the range of changes that could result from those contractual terms and the carrying amount of instruments subject to such terms. However, they do not specify the objective of the proposed new disclosure, nor how users of financial statements are likely to use this information. In our comment letter[7] to the IASB on *Targeted standards-level Review of Disclosure* project we recommended the use of such objectives, as stakeholders find them useful when applying judgement to what should be disclosed and the best way to do so. We understand such general and specific objectives, explaining investors' information needs, are in future to be used by the IASB[8] when developing disclosure requirements. We recommend such a disclosure objective is included in these proposals.

Scope of disclosure

A33. Our stakeholders have highlighted concerns that the broad nature of the proposals at paragraphs 20B and 20C may mean that entities are required to disclose

7 Final comment letter, IASB Exposure Draft ED/2021/3, 17 December 2021, link to document here.

8 Project Summary and Feedback Statement, Disclosure Initiative – Targeted Standards-level Review of Disclosures, March 2023: https://www.ifrs.org/content/dam/ifrs/project/disclosure-initative/disclosure-initiative-principles-of-disclosure/project-summary/projectsummary-fbs-di-tsrd-march2023.pdf

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potentially irrelevant information that obscures more useful information about variations in contractual cashflows. Additionally, preparers are concerned that the quantitative information on the range of changes to contractual cashflows by class of financial asset may create a very wide range, that proves time consuming to prepare but is not useful for investor decision-making.

A34. We also note that such broad requirements increase the risk of boilerplate disclosures, and in this instance also risks duplication of, or inconsistency with, disclosure requirements that already exist elsewhere within IFRS. For example, IFRS 7 B10A already requires similar disclosures for liabilities to assist users in assessing liquidity risk, and the proposed amendments in exposure draft *Non-current Liabilities with Covenants* address disclosure related to covenants in IAS 1 *Presentation of Financial Statements*. One stakeholder suggested that the disclosure of the carrying amount of items subject to contingent events, separately identifying those measured at amortised cost and those measured at fair value, could be sufficient.

A35. We recommend that the IASB reconsiders the scope of these disclosures to improve their usefulness for users of financial statements. Duplication of existing requirements should be removed from scope, including those related to credit event contingencies, as disclosures related to breach of covenants and factors relevant to credit impaired loans are already adequately addressed in the expected credit loss requirements of this standard.

Question 7—Transition
Paragraphs 7.2.47–7.2.49 of the draft amendments to IFRS 9 would require an entity to apply the amendments retrospectively, but not to restate comparative information. The amendments also propose that an entity be required to disclose information about financial assets that changed measurement category as a result of applying these amendments. Paragraphs BC105–BC107 of the Basis for Conclusions explain the IASB's rationale for these proposals. Do you agree with these proposals? Why or why not? If you disagree, please explain what aspect of the proposals you disagree with. What would you suggest instead and why?

Transition

A36. We support the proposed transition requirements, including the requirement not to restate comparatives.

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A37. UK stakeholders continue to stress the urgency of resolving the classification and measurement requirements for financial instruments with ESG-linked features. Accordingly, we recommend that early adoption be permitted for the amendments relevant to this, including paragraphs B4.1.7A – B4.1.16. Alternatively, the ESG requirements could be de-coupled from the rest of the proposals and an earlier implementation date applied.

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UKEB FEEDBACK STATEMENT

IASB Exposure Draft
Amendments to the Classification and Measurement of Financial Instruments – Proposed amendments to IFRS 9 and IFRS 7

July 2023

UKEB

UK Endorsement Board

The UK Endorsement Board (UKEB) is responsible for endorsement and adoption of IFRS for use in the UK and therefore is the UK's National Standard Setter for IFRS. The UKEB also leads the UK's engagement with the IFRS Foundation on the development of new standards, amendments and interpretations.

The comment letter to which this feedback statement relates forms part of those influencing activities and is intended to contribute to the IFRS Foundation's due process. The views expressed by the UKEB in its comment letter are separate from, and will not necessarily affect the conclusions in, any endorsement and adoption assessment on new or amended international accounting standards undertaken by the UKEB.

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Purpose of this feedback statement

This feedback statement presents the views of UK stakeholders received during the UKEB's public consultation on its Draft Comment Letter on the IASB's Exposure Draft *Amendments to the Classification and Measurement of Financial Instruments – Proposed amendments to IFRS 9 and IFRS 7* and explains how the UKEB's Final Comment Letter addressed those views.

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The IASB's Exposure Draft

In March 2023 the IASB issued Exposure Draft (ED) IASB/ED/2023/2 *Amendments to the Classification and Measurement of Financial Instruments – Proposed amendments to IFRS 9 and IFRS 7*.

The ED is the part of the IASB's response to feedback received as part of its IFRS 9 *Post-implementation Review (PIR) of IFRS 9 – Classification and Measurement* project.

The IASB's Exposure Draft

The IASB's ED proposes amendments to IFRS 9. These amendments concern:

a) Derecognition of a financial liability settled through electronic transfer – to clarify that an entity is required to apply settlement date accounting when derecognising a financial asset or financial liability; and to permit an entity to deem a financial liability that is settled using an electronic payment system to be discharged before settlement date if specified criteria are met.

b) Classification of financial assets - to clarify the application guidance for assessing the contractual cash flow characteristics of financial assets, including:

i. financial assets with contractual terms that could change the timing or amount of contractual cash flows, for example, those with ESG-linked features;

ii. financial assets with non-recourse features; and

iii. financial assets that are contractually linked instruments.

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The IASB's Exposure Draft

The ED also proposes amendments or additions to the disclosure requirements in IFRS 7 for:

a) investments in equity instruments designated at fair value through other comprehensive income; and

b) financial instruments with contractual terms that could change the timing or amount of contractual cash flows on the occurrence (or non-occurrence) of a contingent event.

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Outreach Approach

The UKEB's outreach activities took place between January and July 2023 and were conducted to assist the UKEB in developing its Comment Letter.

Due to the project timeline, some outreach activities were performed at the outset of the project and these stakeholder views were reflected in the UKEB Draft Comment Letter.

The outreach approach was underpinned by the UKEB's guiding principles of thought leadership, transparency, independence and accountability.

As the IASB's ED related to targeted amendments to the Standards the Board took a proportionate and focused approach to outreach on the IASB proposals and the UKEB's Draft Comment Letter.

Outreach activities included:

- meetings with users, preparers, accounting firms and regulators, including discussions with the UKEB Financial Instruments Working Group;
- roundtable events with preparers;
- publication of an educational video on the UKEB website; and
- public consultation on the UKEB's Draft Comment Letter.

One written response to the UKEB's Invitation to Comment on its Draft Comment Letter was received. This is in addition to the stakeholder outreach statistics shown in the table.

All comments and views received were considered in reaching the UKEB final views on the questions raised.

Stakeholder type	Stakeholders	Organisations represented
Preparers	34	24
Auditors & Accounting firms	15	8
Regulator/ Standard setter	3	3
Users	7	7
Academics	1	1
Professional bodies / committees*	6	5

*The professional bodies/committees have multiple members, often representing a variety of stakeholder types.

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1. Derecognition of a financial liability settled through electronic transfer

IASB proposal	UKEB draft position	Stakeholders' responses to DCL	UKEB final position
• Clarifies that settlement date accounting should be applied when recognising or derecognising a financial asset or a financial liability. • Proposes an option that, when specified criteria are met, an entity would be permitted to derecognise a financial liability that is settled with cash using an electronic payment system before the settlement date.	Expressed concern about the practicalities of the accounting option. Recommended instead that such liabilities are derecognised at the time the instruction for the payment is made. Recommended streamlining the proposals related to settlement risk at B3.3.8 and B3.3.9.	• Agreed with the practical difficulties and provided examples of such challenges. • Confirmed the UKEB's understanding of commonly used payment systems in their businesses. • Expressed concerns regarding the risk of inconsistent derecognition practices developing. • Questioned whether the IASB should take a more holistic view of the settlement date accounting and recognition/derecognition issue, rather than an isolated approach for electronic payments. This matter is not urgent and a longer-term project allowing further time to consider all issues may avoid potential unintended consequences. • Some thought the settlement risk language at B3.3.8 and B3.3.9 should be retained as drafted by the IASB.	Expands on the draft position to add the following main points: • Stakeholders consulted expressed no interest in using the proposed accounting option. • Strengthens wording regarding the practical difficulties of the option based on stakeholder feedback, and provides examples. • Acknowledges the risk of inconsistent derecognition practices arising from the proposals • If the IASB does not adopt the UKEB recommendation regarding timing of derecognition, suggests the IASB undertake a more holistic review of settlement date accounting. Does not include the draft recommendation to streamline the language regarding settlement risk at B3.3.8 and B3.3.9.

UKEB

2. Contractual terms that are consistent with a basic lending arrangement

IASB proposal	UKEB draft position	Stakeholders' responses to DCL	UKEB final position
• Amends how an entity would be required to assess the classification of financial assets, particularly those with contractual terms that change the timing or amount of contractual cash flows. • Provides additional examples of financial assets that have, or do not have, contractual cash flows that are solely payments of principal and interest on the principal amount outstanding.	Welcomed the timely action to address the needs of instruments with ESG-linked features but expressed concern that: • The guidance regarding "basic lending" is not sufficiently clear. • The requirements for the new "direction and magnitude" test are not sufficiently clear. • The new "specific to the debtor" criteria creates challenges for contracts with both ESG-linked features and other types of contingent events. A number of wording changes to assist with clarity were suggested. Notes that while a pragmatic approach has been taken to this response, the IASB may need to establish a more robust framework in due course.	Emphasised that further clarity on the classification requirements is essential. Emphasised the need for enhanced examples to assist with clarity and application of the proposals. Provided further information and examples illustrating the practical and interpretation challenges arising from the new proposed requirements. Provided a range of suggestions to address these issues.	Builds upon the draft position to strengthen the language and provided further examples. The final letter: • Requests further detailed guidance on how ESG-linked features comply with the concepts of basic lending proposed in the ED. • Requests clarity on the "direction and magnitude" requirement, providing examples of practical challenges in applying this proposal. • Requests that further examples are provided, that more explicit analysis is shown, and that more complex scenarios are included in the examples. • Recommends that ESG-targets set for other entities within the same corporate group be permitted under the "specific to the debtor" requirement. • Provides examples of unintended consequences of the "specific to the debtor" requirements for other financial instruments. • Requests the IASB also consider the impact of these proposals on other areas of IFRS9, including the pipeline project *Amortised Cost Measurement*.

UKEB

3. Financial assets with non-recourse features

IASB proposal	UKEB draft position	Stakeholders' responses to DCL	UKEB final position
• Enhances the description of the term 'non-recourse'. • Provides examples of the factors that an entity may need to consider when assessing the contractual cash flow characteristics of financial assets with non-recourse features.	Supported the IASB's proposal. Highlighted to the IASB that the new definition appears narrower than existing practice, to allow the IASB to clarify if this was not its intention.	Broadly supported the draft position.	Consistent with the draft position.

UKEB

4. Contractually linked instruments

IASB proposal	UKEB draft position	Stakeholders' responses to DCL	UKEB final position
• Clarifies the description of transactions containing multiple contractually linked instruments. • Clarifies that the reference to instruments in the underlying pool can include financial instruments that are not within the scope of the classification requirements of IFRS 9, such as lease receivables.	Supported the IASB's proposed clarification on bilateral secured lending arrangements. Expressed concerns about: • Potential confusion that both the non-recourse and contractually linked instrument contractual cashflow tests may apply to contractually linked instruments, as one is now defined as a subset of the other. • The unintended consequence of implying that lease receivables would always meet the proposed cashflow characteristics test, and recommended modified wording to address this.	Broadly agreed with the UKEB position, subject to minor changes to the recommended wording on lease residuals.	Consistent with the draft position, but updates the recommended wording on lease residuals to reflect stakeholder feedback.

UKEB

5. Disclosures—investments in equity instruments designated at fair value through other comprehensive income

IASB proposal	UKEB draft position	Stakeholders' responses to DCL	UKEB final position
For investments in equity instruments for which subsequent changes in fair value are presented in other comprehensive income: • Requires disclosure of an aggregate fair value of equity instruments rather than the fair value of each instrument at the end of the reporting period. • Requires disclosure of the changes in fair value presented in other comprehensive income during the period.	Supported the IASB's proposal.	Supported this position.	Consistent with the draft position.

UKEB

6. Disclosures—contractual terms that could change the timing or amount of contractual cash flows

IASB proposal	UKEB draft position	Stakeholders' responses to DCL	UKEB final position
• Requires disclosure of contractual terms that could change the timing or amount of contractual cash flows on the occurrence (or non-occurrence) of a contingent event, separately for each class of financial assets measured at amortised cost or fair value through other comprehensive income and each class of financial liability measured at amortised cost.	Recommended the IASB provides disclosure objectives to assist stakeholders apply judgement to the disclosure requirements. Expressed concern about the broad nature of the proposals, the volume of which may obscure more relevant information. Disclosures on the range of changes to contractual cashflows by class of financial asset may be time consuming to prepare but not useful for investors' decision-making. Other requirements duplicate disclosures required elsewhere in this or other Standards. Recommended that the IASB reconsiders the scope of these disclosures.	Agreed and shared concerns about the broad scope of the proposals.	Mostly consistent with the draft position. Added a suggestion for disclosure provided by a stakeholder that additional (new) disclosure be restricted to disclosing the carrying value of items subject to contingencies, identifying those measured at amortised cost and those measured at fair value.

UKEB

7. Transition

IASB proposal	UKEB draft position	Stakeholders' responses to DCL	UKEB final position
• Requires retrospective application, but no requirement to restate comparative information. • Requires disclosure of information about financial assets that changed measurement category as a result of applying these amendments.	Generally supported the IASB's proposal. Recommended that early adoption be permitted for the amendments relevant to the classification of financial instruments with ESG-linked features.	Agreed. Confirmed that ESG-related proposals are urgent and should proceed irrespective of the timing of the other proposals.	Suggests ESG-related amendments either have the option for early adoption, or are decoupled from the rest of the proposals and have an earlier effective date.

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Disclaimer

This feedback statement has been produced in order to set out the UKEB’s response to stakeholder comments received on the IASB's Exposure Draft *Amendments to the Classification and Measurement of Financial Instruments - Proposed Amendments to IFRS 9 and IFRS 7* and should not be relied upon for any other purpose.

The views expressed in this feedback statement are those of the UK Endorsement Board at the point of publication.

Any sentiment or opinion expressed within this feedback statement will not necessarily bind the conclusions, decisions, endorsement or adoption of any new or amended IFRS by the UKEB.

UKEB
UK Endorsement Board

Contact Us

UK Endorsement Board

1st Floor | 1 Victoria Street | London |
SW1H 0ET | United Kingdom

contact@endorsement-board.uk

Web: www.endorsement-board.uk

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Appendix C: Due Process Compliance Statement: Exposure Draft: Amendments to the Classification and Measurement of Financial Instruments - Proposed amendments to IFRS 9 and IFRS 7

General UKEB requirements: The UKEB adopts international accounting standards for use within the UK, in accordance with SI 2019/685 and applies its own processes before it decides to endorse and adopt a new or amended international accounting standard.

Exposure Draft: *Amendments to the Classification and Measurement of Financial Instruments - Proposed Amendments to IFRS 9 and IFRS 7* (the Amendments) was published on 21 March 2023. The IASB comment period ends 19 July 2023.

Influencing process			
Step	**Mandatory / optional**[1]	**Metrics or evidence**	**UKEB Secretariat comments**
		Project Preparation	
Technical project added to UKEB technical work plan [Due Process Handbook (DPH) [4.29]	Mandatory	Project is included in the UKEB published technical work plan.	**Complete:** the Amendments were included in the UKEB technical work plans from July 2022 onwards.

[1] In accordance with the Due Process Handbook.

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Influencing process			
Step	**Mandatory / optional**[1]	**Metrics or evidence**	**UKEB Secretariat comments**
Project preparation (continued)			
Project Initiation Plan (PIP) [DPH 5.4 to 5.8]	Mandatory	PIP draft with project outline (background, scope, project objective) and approach for influencing (key milestones and timing) proportionate to the project	**Complete:** A PIP including purpose (project objective), background, scope, and influencing approach was prepared, taking a proportionate approach to the project.. The PIP was approved at the 27 April 2023 Board meeting.
	Mandatory	Outreach plan for stakeholders and communication approach outlined	**Complete:** this plan was outlined in the PIP. In addition the Secretariat published a project page on the UKEB website.
	Mandatory	Resources allocated	**Complete:** two Project Directors and two Project Managers worked across this project and the *Post-Implementation Review of IFRS 9* project, as described in the PIP.

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Influencing Process			
Step	**Mandatory / optional[1]**	**Metrics or evidence**	**UKEB Secretariat comments**
Project preparation (continued)			
Project Initiation Plan (PIP) [DPH 5.4 to 5.8]	Mandatory	Assessment of whether to set up an ad-hoc advisory group	**Complete:** Assessed. An ad-hoc advisory group was not considered necessary as the Financial Instruments Working Group had the relevant knowledge and experience to take this role.
PIP is approved at public meeting [DPH 5.4]	Required	UKEB Board public meeting held to approve PIP	**Complete:** the PIP was approved at the 27 April 2023 Board meeting.
Education sessions [DPH 4.10]	Optional	Board provided with education sessions on the proposals.	**Complete:** An education session on the proposals was presented at the 27 April 2023 Private Board meeting.
Desk-based research [DPH 5.9]	Optional	Review of relevant documentation	**Complete:** Desk based research was undertaken and key findings reported in the PIP.

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Influencing Process			
Step	**Mandatory/ optional**[1]	**Metrics or evidence**	**UKEB Secretariat comments**
		Communications	
Public board meetings [DPH 5.4, 5.14]	Mandatory	UKEB public meetings held to discuss technical project	**Complete:** The Board discussed the Project Initiation Plan (PIP), at its 27 April 2023 meeting and approved the draft comment letter (DCL) for issue at its 18 May meeting. ***[Pending***: *The Board discussed and approved the following documents at its 13 July 2023 meeting:* • *Final Comment Letter.* • *Feedback Statement.* • *Draft Due Process Compliance Statement.]*
Secretariat papers	Mandatory	Board meeting papers posted and publicly available on a timely basis.	**Complete:** The UKEB's April, June and July meeting papers were published on the UKEB website one week before the public meetings. Meeting minutes and recordings were made publicly available via the UKEB website. Subscribers were notified via the UKEB News Alerts.

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Influencing Process			
Step	**Mandatory / optional**[1]	**Metrics or evidence**	**UKEB Secretariat comments**
Communications (continued)			
Project webpage	Optional	Project webpage contains a project description with up-to-date information on the project.	**Complete**: The project webpage was created and updated regularly with the project status and additional materials.
News Alerts [DPH A4d]	Optional	Evidence that subscriber alerts have occurred	**Complete:** Subscribers were alerted via email 5 days before each Board meeting, with links to the agenda, papers and the option to dial in to observe the discussion. A News Alert was also issued, alerting subscribers to the Draft Comment Letter publication.
Outreach			
Outreach activities [DPH 5.11]	Mandatory	Gather input from investors, preparers and accounting firms and institutes as outlined in the PIP.	**Complete:** More than 60 stakeholders, representing users of financial statements, preparers of financial statements, accounting firms and regulators were consulted during the project. Further detail can be found in the Feedback statement.

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Step	Mandatory / optional[1]	Metrics or evidence	UKEB Secretariat comments
Preparation of Documents for public comment			
DCL published for comment **[DPH 5.13 to 5.17]**	Generally mandatory	DCL published on website.	**Complete:** The Secretariat published the approved DCL on the UKEB website for a 30-day comment period from 26 May 2023 to 26 June 2023.
Project finalisation and project closure			
FCL submitted before comment period ends. [DPH 5.18]	Mandatory	Submitted before 10 March 2023 and published on UKEB website.	***[Pending:*** *The FCL was approved for issue at the Board meeting on 13 July 2023.* *FCL submitted to the IASB on 19 July 2023.*]
Feedback statement and due process compliance statement for influencing stage of project **[DPH 5.19, 5.23-5.26]**	Mandatory	This document and Feedback Statement published on website.	***[Pending****:* *The Secretariat published Feedback Statement and Due Process Compliance Statement on the UKEB website on 19 July 2023.]*

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Conclusion
This document sets out the main due process activities performed as part of the UKEB's due process to issue its comment letter on the Amendments. In the Secretariat's opinion, overall, this project complies with the applicable due process steps, as set out in the Handbook at the time of writing.