UKEB
UK Endorsement Board

Invitation to Comment

Call for comments on the UKEB Draft Comment Letter - Request for Information–Post-implementation Review: IFRS 9 *Financial Instruments* – Impairment

Deadline for completion of this Invitation to Comment:

Midday, Friday 8 September 2023

Please submit to:

UKEndorsementBoard@endorsement-board.uk

Introduction

The objective of this Invitation to Comment is to obtain input from stakeholders on the UKEB's Draft Comment Letter on the Request for Information (RfI) on the Post-implementation Review (PIR) of *IFRS 9–Impairment*, published by the International Accounting Standards Board (IASB) on 30 May 2023. The IASB's comment period ends on 27 September 2023.

UK endorsement and adoption process

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 (Foundation) on the development of new standards, amendments and interpretations. This letter is intended to contribute to the IASB'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.

Who should respond to this Invitation to Comment?

Stakeholders with an interest in the quality of accounts prepared in accordance with international accounting standards.

How to respond to this Invitation to Comment

Please download this document, answer any questions on which you would like to provide views, and return it together with the 'Your Details' form to UKEndorsementBoard@endorsement-board.uk by midday on Friday 8 September 2023.

Brief responses providing views on individual questions are welcome, as well as comprehensive responses to all questions.

Privacy and other policies

The data collected through responses to this document will be stored and processed by the UKEB. By submitting this document, you consent to the UKEB processing your data for the purposes of influencing the development of and adopting IFRS for use in the UK. For further information, please see our Privacy Statements and Notices and other Policies (e.g. Consultation Responses Policy and Data Protection Policy)[1].

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1 These policies can be accessed from the footer in the UKEB website here: https://www.endorsement-board.uk

Questions

Overview

Question One

1a Do you consider that there are any fundamental questions ("fatal flaws") about the IFRS 9 impairment requirements?

Yes	☐	No	☒

Please include any comments you may have in response to question 1a:

In our view there are no fatal flaws with the impairment requirements in IFRS 9. However, the recent decision by the IFRS Interpretation Committee in relation to *Lessor Forgiveness of Lease Payments (IFRS 9 Financial Instruments and IFRS 16 Leases)* has raised doubts over which events should be taken into account when determining possible cash shortfalls. It could be helpful for the IASB to explore with stakeholders possible consequences of this decision, for example the effects on loans when there is a change in the legal framework or the effect of litigation.

1b Are you aware of any areas of IFRS 9 where the cost of applying IFRS 9 exceeds the benefit provided by the information produced?

Yes	☐	No	☐

Please include any comments you may have in response to question 1b:

No comment to this question.

Question Two

2. Do you consider the impairment requirements in IFRS 9 result in:

a) more timely recognition of credit losses compared to IAS 39 and address the complexity caused by having multiple impairment models for financial instruments?

Yes	☒	No	☐

Please explain why or why not.

The IFRS 9 model explicitly requires the use of forward looking information and is designed to be more responsive to possible future credit loss events than the model under IAS 39, which may result in more timely recognition of credit losses.

Nevertheless, the model is complex to operationalise and involves significant judgements, which may impair comparability and understandability. The application of a single impairment model has removed some complexity of the IAS 39 model, however, as identified by the UK Endorsement Board in relation to some financial assets such as intragroup financial assets, that single model may not provide decision useful information for all financial assets.

b) an entity providing useful information to users of financial statements about the effect of credit risk on the amount, timing and uncertainty of future cash flows?

Yes	☒	**No**	☐

Please explain why or why not.

The additional information and disclosures generated under IFRS 9 and IFRS 7 provide users of financial statements with enhanced information over credit risk and expected credit losses. However, it is less obvious that the model under IFRS 9 is significantly better at predicting the actual credit loss experience of an entity compared to the model under IAS 39.

General approach

Question Three

3. At paragraph A3 we recommend the IASB further considers the approach to calculating credit losses on intra-group lending. Do you agree with this recommendation?

Yes	☒	No	☐

Please explain why or why not.

We concur with the UK Endorsement Board's observation regarding the application of the IFRS 9 model to loans that may be based on non-commercial terms, which includes many intragroup financial assets. For such instruments it can be difficult or even impossible to establish the necessary parameters for the IFRS 9 model, as highlighted by the UK Endorsement Board in paragraph A2 of the draft comment letter. However, a solution to that problem which can attract broad consensus may not be easy to find. The UK Endorsement Board's proposed solution would involve defining which financial assets are in and out of the IFRS 9 model, such bright lines are often controversial. In addition, there would no longer be a single impairment model for all financial assets, one of the key objective of the IASB when replacing the IAS 39 impairment requirements.

On balance we support a scope exemption for intragroup financial assets as proposed by the UK Endorsement Board, but the proposed solution may require some refinement in terms of scope. We propose that a scope is based on the definition of a net investment in a foreign operation in IAS 21 paragraph 15.

Significant increase in credit risk (SICR)

Question Four

4. **(a)** At paragraph A8 we propose an amendment to IFRS 9 to incorporate guidance on assessing SICR that was issued by IASB during the pandemic. Do you agree with this recommendation?

Yes	☐	No	☒

Please explain why or why not.

From the explanation in paragraph A8 it is not clear which aspects the UK Endorsement Board believes are relevant to include in the standard. We would have concerns if the IASB would include a requirement for entities to consider prudential regulatory guidance or requirements as part of their financial reporting. Prudential regulators have policy objectives other than decision useful information for investors and there could be a conflict between the requirements of prudential regulators and those in IFRS 9.

(b) At paragraph A10 we propose an amendment to IFRS 9 that, for financial assets that have become credit impaired, would require entities to apply the effective interest rate requirements to the asset no later than the beginning of the subsequent reporting period. Do you agree with this recommendation?

Yes	☒	**No**	☒

Please explain why or why not.

We would welcome a clarification by the IASB, but it may not require an amendment, to the standard, which would trigger possible restatement by some entities.

(c) Are there any other aspects of the assessment of significant increase in credit risk requirements that give rise to significant challenges that could be resolved through standard-setting?

None identified.

Measurement

Question Five

5. **(a)** At paragraph A14 we recommend the IASB consolidates certain sections of non-authoritative guidance produced by the IFRS Transition Resource Group into the Standard. Do you agree with this recommendation?

Yes	☒	**No**	☐

Please explain why or why not.

We concur that paragraph 5.5.18 of IFRS 9 and the related application guidance could be refined so the intentions of the IASB in terms of the use of scenarios as part of the IFRS 9 model are clearer. For example paragraph 5.5.18 refers to "…*consider the risk or probability that a credit loss occurs by reflecting the possibility that a credit*

loss occurs and the possibility that no credit loss occurs…”, which could imply entities are to develop two binary scenarios, one where the expected outcome is a credit loss and one where no credit loss is expected to occur. It also does not allow for the situation where under any realistic scenarios and based on historical experience no credit loss is expected.

(b) At paragraph A15 we recommend that the IASB provides a definition of a post-model adjustment in the Standard. Do you agree with this recommendation?

Yes	☒	**No**	☐

Please explain why or why not.

We concur with the UK Endorsement Board that the IASB should explore the phenomena of post-model adjustments or management overlays. In our view it is important that such adjustments remain permissible under IFRS 9, but clarification of how they fit into the IFRS 9 model could be helpful for preparers and users. We are also supportive of suggestions to enhance the disclosures over post-model adjustments, although such disclosures should be proportionate to the extent of use of post-model adjustments and not introduce further complexities and judgements over what qualifies as post-model adjustments and what does not.

(c) At paragraphs A17-A18 we recommend that the IASB provides further guidance in the Standard for impairment requirements for loan commitments and financial guarantees. Do you agree with these recommendations?

Yes	☒	**No**	☐

Please explain why or why not.

The application guidance in respect of when a credit enhancement is considered an integral part of the contractual terms of a financial asset or not could be enhanced by the IASB. We have seen questions in that regard raised by entities in the non-financial sector. We would add that application guidance on the measurement of financial guarantee contracts from an issuer’s perspective could also be helpful, in order to clarify how the IFRS 9 impairment requirements should be applied to such instruments.

(d) Are there any other aspects of the credit loss measurement requirements that give rise to significant challenges that could be resolved through standard-setting?

None identified.

Simplified approach

Question Six

6. Are there any aspects of the simplified approach for trade receivables, contract assets and lease receivables that give rise to significant challenges that could be resolved through standard-setting?

None identified.

Purchased or originated credit-impaired financial assets (POCI)

Question Seven

7. Are there any aspects of the requirements for purchased or originated credit-impaired assets that give rise to significant challenges that could be resolved through standard-setting?

In our experience the holdings of such instruments are not significant for banks. The cost of the application of a different model to such instruments when they are insignificant outweighs the benefits. As a possible solution we suggest that the use of the impairment requirements for POCI is limited to situations where the business model is based on the management of distressed assets.

Interaction with other requirements

Question Eight

8. **(a)** At paragraphs A21-A25 we recommend that the IASB provides further guidance in the Standard on the interaction between the derecognition, modification and expected credit loss requirements for financial assets. Do you agree with these recommendations?

Yes	☒	**No**	☐

Please explain why or why not.

We concur with the observations of other stakeholders noted in the UK Endorsement Board's draft comment letter.

(b) Are there any other aspects of the application of the impairment requirements alongside other IFRS accounting standard requirements that give rise to significant challenges that could be resolved through standard-setting?

None identified.

Disclosure

Question Nine

9. **(a)** At paragraph A31 we recommend disclosure should be made of expected credit loss by sector. Do you agree with this recommendation?

Yes	☒	**No**	☐

Please explain why or why not.

In addition to the items noted in the UK Endorsement Board's draft comment letter, disclosures may be enhanced on the judgements and criteria applied to determine significant increases in credit risk and the methodologies applied to perform sensitivity analysis.

(b) At paragraph A33 we recommend the IASB provides further educational materials to assist preparers and auditors apply the proportionality guidance at IFRS 7 35D when using the simplified approach. Do you agree with this recommendation?

Yes	☒	**No**	☐

Please explain why or why not.

No further comments.

(c) Are there any other aspects of the credit risk disclosure requirements that give rise to significant challenges that could be resolved through standard-setting?

None identified.

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Overview

Question 10

10. **(a)** Are there any other comments you would like to make on the IFRS 9 impairment requirements?

No.

Thank you for completing this Invitation to Comment

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