Financial Reporting Council

MONTHLY UPDATES (February 2023) – What's new from the International Accounting Standards Board (IASB)

The topics discussed at the IASB's February 2023 meetings were on the following:

A. Research and standard-setting

B. Maintenance and consistent application

A. Research and Standard Setting

1. Dynamic Risk Management

The IASB met to continue its discussions on the development of the Dynamic Risk Management (DRM) model. The IASB discussed:

- whether financial assets measured at fair value through other comprehensive income (FVOCI) or fair value through profit or loss (FVPL) are eligible for inclusion in the determination of an entity's current net open risk position; and

- whether it is necessary to refine the requirements for the assessment of the performance of the DRM model, including how to reflect in financial statements the effects of any unexpected changes in the model.

Items eligible for designation in the current net open risk position

The IASB tentatively decided that, when an entity determines its current net open risk position under the DRM model, financial assets measured at FVOCI are eligible for designation in the DRM model, but financial assets measured at FVPL are not. The IASB's rationale for its tentative decision is that financial assets measured at FVOCI have the same exposure to variability in future net interest income and fair value as financial assets measured at amortised cost.

Performance assessment and unexpected changes

The IASB tentatively decided not to require an entity to make a retrospective assessment against its target profile because such an assessment would not provide useful information to users of financial statements. However, the IASB tentatively decided to require an entity to assess whether the current net open risk position at the end of the DRM assessment period can realise the expected benefits (in the form of reduced variability in earnings or economic value) represented by the DRM adjustment.

Next step

The IASB will continue its discussions on the topics identified in the project plan.

2. Financial Instruments with Characteristics of Equity

The IASB met on to discuss:

- sweep issues on classification and presentation topics in the project plan; and
- the potential development of specific presentation requirements for equity instruments that are within the scope of IAS 32 *Financial Instruments: Presentation*.

Classification and presentation—Sweep issues

Fixed-for-fixed condition

The IASB discussed how an entity would apply the fixed-for-fixed condition in classifying convertible bonds if the holder had a choice between two fixed conversion ratios with different types of own shares.

The IASB tentatively decided to amend the foundation principle, tentatively agreed in April 2020, which clarifies when the fixed-for-fixed condition is met. The foundation principle, as amended, states the condition is met if the entity knows how many functional currency units it will exchange *per type of* own share if the option is exercised.

Reclassification

The IASB discussed the need for consistency in the use of the term 'reclassification' in IAS 32. The IASB also discussed when an entity applying the proposed general requirements would account for a reclassification between financial liabilities and equity instruments.

The IASB tentatively decided:

a. to replace 'reclassified' and 'reclassification' with alternative wording in paragraph 23 of IAS 32.
b. to require an entity to make a reclassification at the date of the change in circumstances that necessitated the reclassification.

The effects of laws on the contractual terms

The IASB discussed stakeholder feedback on the proposed principles (tentatively agreed in December 2021) that an entity would be required to apply in determining whether rights and obligations arising from a legal requirement are considered in classifying a financial instrument as a financial liability or equity instrument.

The IASB tentatively decided to simplify the proposed principles by requiring an entity to consider, in classifying a financial instrument, only enforceable contractual terms that give rise to rights and obligations in addition to, or more specific than, those established by applicable law.

Obligations to redeem own equity instruments

The IASB discussed whether to amend IAS 32:

a. to clarify further the requirements on accounting for financial instruments containing obligations for an entity to redeem its own equity instruments, including written put options on non-controlling interests; and
b. to ensure consistency between these requirements and the requirements on accounting for financial instruments containing contingent settlement provisions in paragraph 25 of IAS 32.

The IASB tentatively decided:

a. to clarify in paragraph 23 of IAS 32 that, when remeasuring the financial liability, an entity is required to recognise gains or losses in profit or loss;
b. to clarify that an entity is required to use the same approach for initial and subsequent measurement of financial liabilities within the scope of paragraph 23 of IAS 32—that is, the entity would ignore the probability and estimated timing of the holder exercising the written put option in initial and subsequent measurement;
c. to clarify that an entity is required to use the same approach for initial and subsequent measurement of financial liabilities within the scope of paragraph 25 of IAS 32—that is, the entity would ignore the probability and estimated timing of the contingent event in initial and subsequent measurement; and
d. to remove from paragraph 23 of IAS 32 the reference to IFRS 9 *Financial Instruments* about subsequent measurement.

Presentation of financial liabilities containing contractual obligations to pay amounts based on an entity's performance or changes in the entity's net assets

The IASB discussed how the proposed disclosure requirement relates to the presentation requirement in paragraph 41 of IAS 32.

The IASB tentatively decided to delete the second sentence of paragraph 41 of IAS 32.

Presentation of equity instruments

The IASB discussed potential presentation requirements to meet the needs of users of financial statements (particularly investors in ordinary shares), which include:

a. transparency about whether an entity has issued other instruments classified as equity; and
b. clear distinction of the returns to ordinary shareholders.

The IASB tentatively decided to amend the requirements in IAS 1 to ensure *amounts attributable to ordinary shareholders* are clearly visible on an entity's statement of financial position, statement(s) of financial performance and statement of changes in equity. These amendments would require an entity to present:

a. line items on issued capital and reserves attributable to *ordinary shareholders of the parent* separately from issued capital and reserves attributable to other owners of the parent in the statement of financial position (paragraph 54(r) of IAS 1);
b. *each class of ordinary share capital* separately from each class of other contributed equity in the statement of changes in equity (paragraph 108 of IAS 1);
c. profit or loss and comprehensive income for the period attributable to *ordinary shareholders of the parent* separately from the respective amounts attributable to other owners of the parent in the statement(s) of financial performance (paragraph 81B of IAS 1); and
d. the amount of dividends recognised as distributions to *ordinary shareholders* separately from dividends recognised as distributions to other owners during the period, and also present the related amount of dividends per share, either in the statement of changes in equity or in the notes (paragraph 107 of IAS 1).

Next step

The IASB will discuss the remaining topics set out in the project plan.

3. Rate-regulated Activities

The IASB met to redeliberate specific topics included in the plan relating to:

- the threshold for the recognition of regulatory assets and regulatory liabilities;
- the relationship between an assessment of enforceability and the recognition of regulatory assets and regulatory liabilities; and
- the accounting for performance incentives, except those that relate to an entity's performance over several periods (long-term performance incentives).

The recognition threshold

The IASB tentatively decided:

a. to retain the proposal to require an entity to recognise a regulatory asset or a regulatory liability whose existence is uncertain if it is more likely than not that such an asset or liability exists;
b. not to set a recognition threshold based on the probability of a flow of economic benefits;
c. not to set a recognition threshold based on the level of measurement uncertainty, except for those regulatory assets and regulatory liabilities described in paragraph (e);
d. to retain the proposed symmetric recognition threshold for regulatory assets and regulatory liabilities; and
e. to require an entity to recognise a regulatory asset or regulatory liability—whose measurement depends on a regulatory benchmark determined after the financial statements are authorised for issue—when the regulator determines the benchmark.

The IASB will discuss the proposed recognition and measurement requirements for regulatory assets and regulatory liabilities arising from long-term performance incentives at a future IASB meeting.

Enforceability and recognition

The IASB tentatively decided:

a. to reconfirm and clarify the proposed single assessment of the existence of enforceable present rights and enforceable present obligations in the Standard, for the individual regulatory assets or regulatory liabilities.
b. to clarify in the Standard that rights and obligations can be enforceable even if their existence is uncertain.
c. to consider the principles in paragraph 35(c) of IFRS 15 *Revenue from Contracts with Customers* that relate to an entity's right to payment for performance completed to date in developing the Standard. These principles would be used to set the requirements for assessing the existence of enforceable present rights for regulatory returns on an asset not yet available for use, and for assessing the existence of enforceable present rights or enforceable present obligations for long-term performance incentives.

Total allowed compensation—Performance incentives

The IASB tentatively decided to reconfirm in the Standard the proposed requirement relating to performance incentives. The requirement would be that amounts relating to performance incentives should form part of or reduce the total allowed compensation for goods or services supplied in the period in which the entity's performance gives rise to the incentive. These amounts would include those that result from an entity's performance of construction work.

Next step

The IASB will continue to redeliberate the project proposals.

4. Business Combinations—Disclosures, Goodwill and Impairment

The IASB met to discuss its project on Business Combinations—Disclosures, Goodwill and Impairment. In particular, the IASB discussed a management approach to disclosing information about the subsequent performance of business combinations.

The management approach

The IASB tentatively decided:

a. to specify a level of management within an entity to identify the information the entity is required to disclose about the subsequent performance of business combinations; and
b. to describe that level of management as the key management personnel of the reporting entity, as defined in IAS 24 *Related Party Disclosures*.

Other aspects of the management approach

The IASB tentatively decided:

a. to maintain its preliminary view that an entity be required to disclose information about the subsequent performance of a business combination for as long as the entity's management continues to monitor whether the objectives of the business combination are being met (that is, the entity's management compares actual performance with the entity's objectives and targets for the business combination it established when entering into the business combination).
b. to maintain its preliminary view that if an entity's management does not monitor whether its objectives for a business combination are being met, the entity should disclose that fact and the reasons why it does not do so.
c. to maintain its preliminary view that if an entity's management stops monitoring, before the end of the second full year after the year of the business combination, whether its objectives for a business combination are being met, the entity should disclose that fact and the reasons why it has done so.
d. to propose that an entity whose management stops monitoring, before the end of the second full year after the year of the business combination, whether its objectives for a business combination are being met, be required to disclose information about actual performance. The entity will be required to disclose information using the metric set out in the year of acquisition, if (and only if) information about actual performance using that metric is being received by the entity's management.

e. to permit an entity to disclose information about its targets for a business combination as a range or a point estimate.
f. to clarify that an entity will be required to disclose only information about its key objectives—that is, the objectives critical to the success of the business combination.

Next steps

The IASB will make tentative decisions on matters including:

a. clarifying other aspects of the disclosure requirements for business combinations;
b. reducing the cost and complexity of applying the impairment test of cash-generating units in IAS 36 *Impairment of Assets*; and
c. improving the effectiveness of the impairment test of cash-generating units containing goodwill.

Once the IASB has made tentative decisions on all aspects of the project, it will consider whether the package of decisions meets the project objective and whether to publish an exposure draft setting out its proposals.

5. Post-implementation Review of IFRS 9—Impairment

The IASB met:

- to discuss feedback from stakeholders on the first phase of the post-implementation review of the impairment requirements in IFRS 9 *Financial Instruments* and the credit risk disclosure requirements in IFRS 7 *Financial Instruments: Disclosures*;
- to discuss a review of academic literature relevant to this post-implementation review; and
- to decide on matters about which the IASB will ask questions in a request for information.

The IASB plans to ask questions about:

a. the general approach to recognising expected credit losses (ECL), specifically:
    i. the effects of the approach on the usefulness of information about changes in credit risk to the users of the financial statements; and
    ii. the costs and benefits of applying the approach to particular transactions, such as inter-company loans;
b. significant increases in credit risk, specifically:
    i. the use of judgement in determining significant increases in credit risk; and
    ii. the evidence about the causes of and the extent of diversity in how entities assess significant increases in credit risk;
c. the measurement of ECL, specifically:
    i. using multiple forward-looking scenarios; and
    ii. measuring ECL in periods of enhanced economic uncertainty, including the use of post-model management adjustments or overlays;
d. the prevalence of questions from entities on how to apply the ECL requirements for purchased or originated credit-impaired financial assets;
e. the simplified approach to recognising ECL for trade receivables, contract assets and lease receivables, specifically:
    i. the effects of the relief provided by the IASB through this approach; and
    ii. the inclusion of forward-looking information when applying this approach;

f. the accounting for loan commitments, collateral and other credit enhancements held and financial guarantee contracts issued that are within the scope of IFRS 9;
g. the application of the ECL requirements in combination with other requirements in IFRS 9 or in other IFRS Accounting Standards;
h. the effects of transition reliefs provided by the IASB and the balance between reducing costs for preparers of financial statements and providing useful information to users of financial statements; and
i. the credit risk disclosure requirements in IFRS 7, specifically:
    i. whether the combination of disclosure principles and minimum disclosure requirements achieves an appropriate balance between comparable information and relevant information for users of financial statements about the effect of credit risk on the amount, timing and uncertainty of future cash flows; and
    ii. the compatibility of the requirements with digital reporting.

Next steps

The IASB plans to approve the publication of the request for information and set a comment period. The IASB expects to publish the request for information by the end of May 2023.

B. Maintenance and consistent application

The IASB met to discuss the project on Supplier Finance Arrangements and to discuss the project on Lack of Exchangeability and the next cycle of annual improvements to IFRS Accounting Standards.

1. Supplier Finance Arrangements—Transition, effective date and due process

The IASB discussed its proposed amendments to IAS 7 *Statement of Cash Flows* and IFRS 7 *Financial Instruments: Disclosures*. The proposed amendments would add disclosure requirements about an entity's supplier finance arrangements.

The IASB tentatively decided to require an entity to apply the amendments for annual reporting periods beginning on or after 1 January 2024.

The IASB tentatively decided:

a. to permit earlier application and, if an entity applies the amendments for an earlier period, to require the entity to disclose that fact;
b. not to require an entity to disclose comparative information for preceding periods in the annual reporting period it first applies the amendments;
c. not to require an entity to disclose, in its first annual financial statements after the amendments become effective, information as at the beginning of that annual reporting period on:
    i. the carrying amount of financial liabilities recognised in the statement of financial position that are part of a supplier finance arrangement for which suppliers have already received payment from the finance providers; and
    ii. the range of payment due dates of both financial liabilities that are part of a supplier finance arrangement and comparable trade payables that are not part of such an arrangement; and
d. not to require the disclosures required by the amendments for any interim financial reports within the annual period in which an entity first applies the amendments.

Next step

The IASB expects to issue the amendments in the second quarter of 2023.

2. Lack of Exchangeability (Proposed Amendments to IAS 21)—Due process, effective date and other matters

The IASB discussed its proposed amendments to IAS 21 *The Effects of Changes in Foreign Exchange Rates* and tentatively decided:

a. to proceed with the proposed amendments to IFRS 1 *First-time Adoption of International Financial Reporting Standards*; and
b. not to make amendments to IFRS 13 *Fair Value Measurement*.

The IASB tentatively decided to require an entity to apply the amendments for annual reporting periods beginning on or after 1 January 2025 and to permit earlier application.

The IASB decided to finalise the amendments without re-exposure.

Next step

The IASB expects to issue the amendments in the third quarter of 2023.

3. Hedge accounting by a first-time adopter (IFRS 1)—Potential annual improvement

The IASB discussed an inconsistency in wording between paragraph B6 of IFRS 1 and the requirements for hedge accounting in IFRS 9 *Financial Instruments*.

The IASB tentatively decided:

a. to propose amendments to:
   i. paragraphs B5–B6 of IFRS 1 to add cross-references to paragraph 6.4.1 of IFRS 9; and
   ii. paragraph B6 of IFRS 1 to replace the word 'conditions' with 'qualifying criteria';
b. not to develop specific transition requirements for these proposed amendments; and
c. to include these proposed amendments in its next annual improvements cycle.

4. Determination of a 'de facto agent' (IFRS 10)—Potential annual improvement

The IASB discussed an inconsistency between paragraphs B73 and B74 of IFRS 10 *Consolidated Financial Statements* related to how an investor determines whether another party is acting on that investor's behalf.

The IASB tentatively decided:

a. to propose amendments to clarify the requirements in paragraph B74 of IFRS 10;
b. not to develop specific transition requirements for these proposed amendments; and
c. to include these proposed amendments in its next annual improvements cycle.

5. Transaction price (IFRS 9)—Potential annual improvement

The IASB discussed a reference in Appendix A to IFRS 9 to the definition of 'transaction price' in IFRS 15 *Revenue from Contracts with Customers* that could cause confusion.

The IASB tentatively decided:

a. to propose amendments to IFRS 9 to revise the wording in paragraph 5.1.3 of IFRS 9 and to delete the reference to 'transaction price' and the associated references to IFRS 15 from Appendix A;
b. not to develop specific transition requirements for these proposed amendments; and
c. to include these proposed amendments in its next annual improvements cycle.

6. Cost method (IAS 7)—Potential annual improvement

The IASB discussed the use of the term 'cost method' in paragraph 37 of IAS 7, which is no longer defined in IFRS Accounting Standards.

The IASB tentatively decided:

a. to propose an amendment to paragraph 37 of IAS 7 to replace the term 'cost method' with 'at cost';
b. not to develop specific transition requirements for this proposed amendment; and
c. to include this proposed amendment in its next annual improvements cycle.

7. Gain or loss on derecognition (IFRS 7)—Potential annual improvement

The IASB discussed a reference in paragraph B38 of IFRS 7 to paragraph 27A, which has been deleted from IFRS 7.

The IASB tentatively decided:

a. to propose amendments to paragraph B38 of IFRS 7:
   i. to replace the reference to paragraph 27A of IFRS 7 with a reference to paragraphs 72–73 of IFRS 13; and
   ii. to replace the phrase 'inputs that were not based on observable market data' with 'unobservable inputs';
b. not to develop specific transition requirements for these proposed amendments; and
c. to include these proposed amendments in its next annual improvements cycle.

8. Credit risk disclosures—Potential annual improvement

The IASB discussed an inconsistency between paragraphs IG20B and IG20C of the implementation guidance accompanying IFRS 7. Paragraph IG20B identifies the relevant requirements in IFRS 7 that are not illustrated in the example, while paragraph IG20C does not.

The IASB tentatively decided:

a. to propose an amendment to paragraph IG1 of IFRS 7 to add a statement that the implementation guidance accompanying IFRS 7 does not illustrate all the requirements in IFRS 7;
b. to propose an amendment to paragraph IG20B of IFRS 7 to simplify the wording; and
c. to include these proposed amendments in its next annual improvements cycle.

For further information: http://www.ifrs.org

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