18 July 2023

Dr. Andreas Barckow
Chair
International Accounting Standards Board
7 Westferry Circus
Canary Wharf London, E14 4HD
United Kingdom

Dear Dr. Barckow,

The Asian-Oceanian Standard-Setters Group (AOSSG) is pleased to provide comments on the International Accounting Standards Board (IASB) Exposure Draft (ED/2023/2) *Amendments to the Classification and Measurement of Financial Instruments* proposing amendments to IFRS 9 *Financial Instruments* and IFRS 7 *Financial Instruments: Disclosures*. In formulating these comments, the views of the constituents within each jurisdiction were sought and considered.

The AOSSG currently has 28 member standard-setters from the Asian-Oceanian region: Australia, Bangladesh, Brunei, Cambodia, China, Dubai, Hong Kong, India, Indonesia, Iraq, Japan, Kazakhstan, Korea, Macao, Malaysia, Maldives, Mongolia, Nepal, New Zealand, Pakistan, Philippines, Saudi Arabia, Singapore, Sri Lanka, Syria, Thailand, Uzbekistan, and Vietnam. To the extent feasible, this submission to the IASB reflects in broad terms the collective views of AOSSG members. The intention of the AOSSG is to enhance the input to the IASB from the Asia-Oceania region and not to prevent the IASB from receiving the variety of views that individual member standard-setters may hold. This submission has been circulated to all AOSSG members for their comments. In responding to the ED, AOSSG members have provided their responses to the questions in the ED as described in the Appendix of this submission.

The AOSSG acknowledges the efforts of the IASB to respond to feedback received from the Request for Information on the Post-implementation Review of the classification and measurement requirements of IFRS 9 issued in September 2021.

Most of the AOSSG members that responded supported the proposed changes in the exposure draft. However, there are several areas where they have requested amendments to the drafting, further clarification, guidance or illustrative examples. The most common areas of concern are summarised below:

Question 1— Derecognition of a financial liability settled through electronic transfer.

The majority of the members that responded were concerned that limiting the recognition and derecognition requirements in IFRS 9 (Chapter 3) to settlement date accounting might have consequences beyond clarifying current requirements. For example, how the proposed paragraph B3.1.2A will interact with the definition of settlement date accounting in paragraph B3.1.6 for regular way purchases and sales of financial assets, the implications for how to account for the credit entry when applying the guidance in paragraph B3.3.8 and the timing of derecognition of liabilities paid by cheque might result in practical issues. Several members also suggested improvements to the wording of paragraphs B3.3.8(a) and (b).

Question 2—Classification of financial assets – contractual terms that are consistent with a basic lending arrangement.

The majority of members that responded considered the proposed paragraphs B4.1.8A and B4.1.10A are unclear and have requested the drafting to be amended. Several members also suggested that it would be helpful to have additional illustrative examples to supplement those provided in paragraphs B4.1.13 and B4.1.14.

Question 3—Classification of financial assets – financial assets with non-recourse features

The majority of members that responded requested additional application guidance or illustrative examples about how to evaluate the legal and capital structure of the debtor when assessing the contractual cashflows of a financial asset with non-recourse features (paragraph B4.1.17A). Some members considered that paragraph B4.1.16A might be more restrictive than existing requirements or could be difficult to apply in some cases.

Question 4—Classification of financial assets – contractually linked instruments

The majority of members that responded requested clarifications to the proposals; however, the most frequent request was for the IASB to provide a more complete rationale for the example of transactions that may contain multiple debt instruments but are not contractually linked instruments in paragraph B4.1.20A. In part, this was connected to concerns about transaction structuring.

Question 5—Disclosures – Investments in equity instruments designated at fair value through other comprehensive income.

Members that responded expressed mixed views with some of them supporting the proposals and others suggesting changes either to the requirement on disclosing fair value information

in aggregate or separately disclosing information relating to investments that have been disposed.

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

A majority of members that responded questioned the scope of the disclosures proposed in paragraph 20B and thought they could be onerous and costly to prepare. Members also observed that some of the requirements overlap with existing disclosure requirements and asked for illustrative examples.

Question 7—Transition

Members that responded supported the transition requirements. Some members asked whether it would be permitted to implement the changes in stages and another thought potential changes to the classification of existing financial assets could have practical challenges for larger financial institutions.

The Appendix to this submission provides detailed comments by the respective AOSSG members on the questions in the ED.

If you have any questions regarding this submission, please contact either one of us.

Yours sincerely,

Nishan Fernando

Chair of the AOSSG

Dr. Keith Kendall

Leader of the AOSSG Financial Instruments and Liabilities Working Group

**Appendix – Comments from AOSSG members**

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

**Questions for respondents**

| **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 specific 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.<br><br>Paragraphs BC5–BC38 of the Basis for Conclusions explain the IASB's rationale for this proposal.<br><br>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? |

**[Australia]**

The AASB is concerned that proposed paragraph B3.1.2A and aspects of the drafting of paragraphs B3.3.8 and B3.3.9 could have consequences beyond clarifying current practice and should be further considered or clarified. Specific comments and suggestions are as follows:

(1) The proposed paragraph B3.1.2A states that when recognising or derecognising a financial asset or financial liability, an entity shall apply settlement date accounting (except for regular way purchases and sales). Reducing the recognition and derecognition requirements in IFRS 9 (Chapter 3) to settlement date accounting could have consequences beyond clarifying current requirements. For example, some stakeholders noted there are exceptions to settlement date accounting in IFRS 9 and B3.1.2A might cause confusion.

(2) The proposed paragraph B3.3.8 would permit entities to discharge financial liabilities settled with cash using an electronic payment system (e.g. trade payables) before the settlement date if certain conditions are met. We note that some stakeholders thought the nature of the corresponding credit entry was unclear due to the overarching requirement to apply settlement date accounting for financial assets in paragraph B3.1.2A (as drafted).

(3) Paragraphs B3.3.8(a)-(c) and B3.3.9 set out the proposed requirements an entity must meet if they wish to deem that a financial liability settled with cash using an electronic payment system is discharged before the settlement date. While it is not immediately apparent that this would have significant implications for Australian entities, we suggest the drafting should be clarified. For example:

(a) Paragraph B3.3.8(a) requires that after a payment is initiated, an entity should have "no ability" to withdraw, stop or cancel the payment, while paragraph B3.3.8(b) says the entity should have "no practical ability" to access the cash. Some stakeholders thought the requirement in B3.3.8(a) might be difficult to ascertain for Australian entities. Further, it is not clear why paragraph B3.3.8(a) appears to be an absolute requirement (with possible legal implications) while B3.3.8(b) refers to practical ability. We suggest that if the proposed drafting is amended, B3.3.8(a) may not be required. Alternatively, B3.3.8(a) could be changed to refer to a practical ability if the term was defined.

(b) Paragraph B3.3.8(c) would require an insignificant settlement risk associated with the electronic payment system. B3.3.9 clarifies this requirement stating that the period between initiating a payment instruction and the cash being delivered must be short. There should be a clear definition of what the word 'short' means.

**[China]**

Overall, we agree with this proposal.

Besides, we suggest the IASB further clarify the following issues: firstly, the criteria may lead to inconsistency in practice in the point of derecognition of financial assets by the recipient and financial liabilities by the payer, and how to solve the problem of difficulty in offsetting internal transactions at the group level when preparing consolidated statements when both parties to the transaction are intra-group entities; secondly, whether the entity should derecognise the corresponding financial assets when financial liabilities settled by electronic transfer can be elected to be derecognised on the transaction date if the specific criteria are met.

**[Hong Kong]**

(1) Our respondents provided the following comments regarding the proposal in B3.3.8:

(a) It is unclear whether B3.3.8(a) is considered to be met or not when an entity is subject to a penalty if it withdraws, stops or cancels the payment instruction and whether this depends on the size of the penalty.

(b) It is unclear what 'practical ability' in B3.3.8(b) means and how to assess it, e.g. whether it can be based on an entity's intention and past practice; and how it is different from 'ability' as referred to in B3.3.8(a).

(c) Some respondents suggested deleting the last sentence in B3.3.9 *'settlement risk would not be insignificant if the completion of the payment instruction is subject to the entity's ability to deliver cash on the settlement date'*, as it confuses criteria (a) and (b) of B3.3.8 (i.e. the ability of the entity to stop the payment instruction or deliver cash) with criteria (c) (i.e. settlement risk).

(d) The proposed requirements are unclear regarding whether and how the exception to derecognising a financial liability applying B3.3.8 would apply in cases where the cash, which is used to settle the financial liability in the electronic transfer system, comes from an overdraft or other similar facility with a negative balance.

It is noted that paragraph B3.3.8 refers to 'settled with cash' and (b) of that paragraph refers to 'access the cash'. This raises a question as to whether 'cash' is defined as in IAS 7.6 as 'cash on hand and demand deposits' and so only refers to positive cash balances, or the broader definition in IAS 7.7 which acknowledges that 'bank overdrafts which are repayable on demand form an integral part of an entity's cash management' and '[i]n these circumstances, bank overdrafts are included as a component of cash and cash equivalents' and so can include negative balances. It would be useful for the IASB to clarify this aspect and whether the fact that the overdraft facility is committed or uncommitted would make a difference to the ability to use the election in B3.3.8.

(2) We therefore recommend the IASB provide clarifications with guidance and examples to address those comments so as to avoid the potential diversity in application in those areas. Furthermore, given the significance of settlement risk as one of the criteria for applying the exception under B3.3.8, we recommend the IASB consider defining 'settlement risk' in Appendix A of IFRS 9 instead of explaining the term in BC33.

(3) Some respondents noted that B3.1.2A would change the current practice for derecognition of financial liability which is settled by cheques in Hong Kong because entities would be required to derecognise their financial liabilities only when cheques are cleared by the bank instead of when they are issued. To increase the market receptiveness to the proposed amendments and raise public awareness of their impact, we recommend the IASB provide relevant educational material on the impact of the proposals on cheque payments. We also suggest the IASB consider providing sufficient time for the market to implement the change when it determines the effective date of the amendments.

(4) A few respondents noted that the term 'settlement date' and 'settlement date accounting' are currently used in IFRS 9 with a reference to a 'regular purchase or sale of a financial asset' only (B3.1.6). IFRS 9 provides special accounting (trade date or settlement date accounting) for regular way purchases or sales because of the nature of such transactions as explained in BA.4. Accordingly, the concept of settlement date accounting is irrelevant to other types of transactions under the extant IFRS 9 including derecognition of financial liabilities and those involving derivatives. These respondents are concerned that B3.1.2A seems to extend the 'settlement date accounting' to other types of transactions that are not even sales or purchases or which are not 'regular way'.

(5) If the IASB intends to apply settlement date accounting to other transactions, we recommend that the IASB provide guidance and examples to demonstrate how to apply it to transactions other than regular way purchases or sales. Otherwise, the IASB should consider taking out the entire paragraph of or redrafting B3.1.2A to avoid any confusion or potential impact to other IFRS 9 requirements if the primary purpose of the amendments is to provide an exception (i.e. B3.3.8) for entities to derecognise their financial liabilities before the settlement date for payment transactions settled through electronic transfers.

**[Malaysia]**

We agree with the proposal.

**[New Zealand]**

(1) We agree with the proposals to allow a financial liability that is settled via an electronic payment system to be derecognised on the date of initiating the payment instruction (provided that the 'settlement risk' is low) – as opposed to requiring entities to wait until the settlement date before the liability can be derecognised.

(2) However, we recommend stating the principle for determining whether a type of electronic payment is within the scope of the accounting policy choice, to help preparers determine whether and when the accounting policy choice applies, and in order to 'future proof' these requirements for new types of electronic payments.

(3) Furthermore, it may be challenging and time-consuming for entities to ascertain the exact point at which the criteria in paragraph B3.3.8(a) would be met, i.e. whether and for how long the entity has the ability to cancel or withdraw an electronic payment instruction – particularly when an entity uses the services of various banks in different countries, whose electronic payment systems might operate differently in this regard. We recommend addressing this matter by making one or more of the following changes.

   (a) Updating paragraph B3.3.8(a) to refer to the practical ability to withdraw or cancel the payment instruction – rather than the ability to do so in general. This would make the principle of this requirement consistent with paragraph B3.3.8(b) – which refers to the entity having no practical ability to access the cash to be used for settlement of the liability).

   (b) Reducing the de-recognition criteria in paragraphs B3.3.8(a) and B3.3.8(b) into a single criterion that refers to *practical ability*. We understand that it is very unlikely for an entity to meet one criterion and not the other. That is, the criterion of not being able to stop, cancel or withdraw the payment instruction and the criterion of not being able to access the cash to be used for settling the liability are generally met at the same time. Reducing these two criteria into a single criterion that refers to *practical* ability, would streamline the requirements and make it easier for entities to determine when they can de-recognise a financial liability before the settlement date.

   (c) Providing additional guidance to help entities assess when practical ability to cancel or withdraw the payment and/or access the related cash exists.

**[Saudi Arabia]**

We agree with the proposed amendments to paragraph B3.3.8 of IFRS 9 when the specified criteria are met, for an entity to 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. However, we anticipate that preparers in the financial services sector will face significant difficulties in fulfilling the set criteria as a result of the existing payment recall mechanisms.

Example: Chargebacks relating to credit card transactions, Wire transfer recalls, Automated clearing house reversals, PayPal disputes etc.

In addition, we would like to suggest expanding the criteria to include regulatory and operational requirements. Depending on the jurisdiction and the nature of the financial liability, there may be regulatory and operational requirements that need to be fulfilled before considering the amount settled and for the liability to be derecognised. Compliance with relevant laws, regulations, and internal policies should be evaluated prior to derecognizing the financial liability.

Also, we would like to raise the question as to how currency risk would be addressed when payment involves cross-border transactions & different currencies. The risks associated with currency exchange rates or conversion fees may impact settlement of the financial liability. We therefore believe the proposed amendments will require changes to the information technology systems used by preparers. The implementation process may be time consuming and cumbersome, particularly for organisations with large and complex financial instrument portfolios.

Comments received from preparers during an outreach carried out by SOCPA indicated that they believed that this amendment provides more flexibility to preparers, however it creates inconsistencies between the 2 parties involved in any given financial liability cycle due to the mismatch between the liability derecognition date and the asset recognition date from the other party. In addition, there were also suggestions to include in B3.3.8, “redirect payment source” to cover cases where the payer may be able to redirect payment source and hence the liability may not be discharged.

**[Thailand]**

We agree with this proposal to add paragraph B3.3.8 to specify the criteria that permit an entity to derecognise a financial liability that is settled using an electronic payment system. Nonetheless, we would like to provide some input as follow.

Firstly, we recommend that an additional guidance shall be provided to explain how settlement date accounting shall apply to financial liabilities as existing guidance only relates to purchases or sales of financial assets.

Secondly, an 'electronic payment system' in the context of the proposal is unclear. Therefore, we recommend that it shall be clearly defined.

| **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:<br>(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.

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?

**[Australia]**

The drafting of paragraphs B4.1.8A and B4.1.10A is unclear and does not sufficiently clarify the principles of the classification assessment. Specific comments and suggestions are as follows:

(1) The proposed paragraph B4.1.8A explains that some payment types are inconsistent with the definition of a basic lending arrangement. The wording of this paragraph could be clarified as suggested below:

   (a) Paragraph B4.1.8A states that in assessing whether the contractual cash flows of a financial asset are consistent with a basic lending arrangement, an entity may have to consider the different elements of interest separately. It would be helpful to add the IASB's wording from the Basis for Conclusions (BC47) that the elements of interest specified in paragraph B4.1.7A (i.e., consideration for the time value of money, credit risk, liquidity risk, costs and profit margin) are not an exhaustive list.

   (b) Further, paragraph B4.1.8A states, "… a change in contractual cash flows 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." The wording in the Basis for Conclusions (BC52), which explains that a change in contractual cash flows must be directionally consistent with and proportionate to a change in lending risks or costs, is clearer than the double negative employed in B4.1.8A and avoids the need to clarify the new term 'magnitude.'

(2) The proposed paragraph B4.1.10A requires that to be consistent with a basic lending arrangement, the occurrence of a contingent event must be specific to the debtor. We request clarification of the following matters:

   (a) When evaluating the terms that change the timing or amount of contractual cashflows, paragraph B4.1.10 requires the entity to determine whether the contractual cashflows that could arise over the life of the instrument are solely payments of principal and interest (SPPI). In doing so, the entity may evaluate the nature of possible contingent events. For the purpose of this evaluation, whether

or not the contingent event is specific to the debtor is treated as indicative rather than determinative. The requirement in B4.1.10A appears more restrictive than B4.1.10. We request confirmation that this is an intended change or clarification of the matter if it is not a change.

(b) If the requirement that a contingent event must be specific to the debtor is intended to be determinative (as noted above), further guidance may be needed in some circumstances, for example, to illustrate how the requirement might apply in a group context. As currently drafted, it is unclear how to apply the guidance in situations when the loan is provided to one legal entity (perhaps a holding company or financing entity) but the ESG-related metrics are determined with reference to all companies in the group or to an operating subsidiary's emissions.

(3) Our stakeholders asked for more complex examples than those in B4.1.13 and B4.1.14. However, clarification of the principles of the classification assessment should mitigate the need for additional illustrative examples.

**[China]**

We generally agree with the IASB's proposed amendments.

We have the following suggestions for some specific proposed amendments:

(1) Regarding the magnitude of the change in contract cash flow:

(a) we note that there are different understandings in practice, and we suggest adding specific examples to provide further guidance. For example, according to paragraph B4.1.9, leverage increases the variability of the contractual cash flows such that they do not have the economic characteristics of interest. It appears that if a financial asset's interest rate is determined by a floating rate multiplied by a positive factor more than 1 (e.g. interest rate benchmark times 2), then it would be leveraged and is not consistent with a basic lending arrangement. On the contrary, the practical view is that if it is multiplied by a positive factor less than 1 (e.g. interest rate benchmark times 0.8), then it would not be leveraged and is consistent with a basic lending arrangement. We propose that the IASB clarify whether multiplied by a positive factor less than 1 represents it is aligned with the magnitude.

(b) we propose that the IASB carefully consider whether the amendment may have unintended consequences. For example, when the credit quality of the borrower deteriorates, the loan contract may require a large jump in the interest rate that is disproportionate to the credit deterioration, in order to force the borrower to refinance at market rates and prepay the original loan, which is a common arrangement in the credit market, and the change of the interest rate is closely related to credit risk. Under the revised requirements, arrangements considered to be consistent with the basic lending arrangements in current practice would be considered inconsistent as a result of changes in contractual cash flows that may be considered it is not aligned with the magnitude of the change in basic lending risks, thereby changing the currently accepted practice treatment. we propose that

the IASB fully consider whether this result is contrary to the intention of the amendment.

(2) regarding the assessment of contractual terms consistent with basic lending arrangement, paragraph B4.1.8A of the draft amendments to IFRS 9 provides that the assessment of interest should *what* an entity is being compensated for, rather than *how* much compensation an entity receives. We consider that although this requirement is derived from paragraph BC4.182(b), there may be ambiguity in its inclusion in the standard provision. For example, the requirement may be interpreted as requiring *only* an analysis of what an entity is being compensated for, *not* how much compensation an entity receives, and contradicting the requirement to assess whether a change in contract cash flows is aligned with the magnitude of changes in basic lending risks or costs. we propose that the IASB further consider the wording.

(3) regarding paragraph B4.1.10A of the draft amendments to IFRS 9 stipulates that the occurrence (or non-occurrence) of the contingent event must be specific to the debtor. We note that there may be two situations in practice that the occurrence (or non-occurrence) of the contingent even do not be specific to the debtor but are generally considered to be consistent with a basic lending arrangement: (a) lenders will pass on to borrowers the increased costs of the occurrence of the contingent event (such as changes in regulatory or tax policy) to secure their profit margins, although the occurrence of the contingent event do not specific to the debtor but the creditor. However, we consider that this is the rate of profit listed in paragraph B4.1.7A that is consistent with a basic lending arrangement. (b) The occurrence (or non-occurrence) of certain contingent event does not specific to the debtor, but is linked to the overall situation of the debtor's group (e.g. group-wide greenhouse gas emissions). Although the contingent event does not specific to the debtor, it does have an indirect relationship. We consider that it is likely not the IASB's intention to treat these two cases as non-basic lending arrangements, and propose that the IASB reconsider the scope of the provision. Furthermore, the prepayment and extension options stated in paragraph B4.1.11 to satisfy SPPI do not require the contingent event must be specific to the debtor. Therefore, the proposed amendments may result in logical inconsistencies with the existing provisions in IFRS 9.

(4) paragraph B4.1.10A of the draft amendments to IFRS 9 stipulates that the resulting contractual cash flows must represent neither an investment in the debtor nor an exposure to the performance of specified assets, while the example in paragraph B4.1.16 is only for an investment in specified asset. There is confusion, and we suggest adding concrete examples to provide further guidance. For example, tere is a loan with a "cross-sell clause", where the interest rate on the loan is contractually agreed to increase by a specific amount of basis points if the borrower does not enter into other specific transactions or business arrangements with the bank in the future, we propose that the IASB clarify whether the clause represents an investment in the debtor.

(5) in order to achieve better alignment and application between the exposure draft and the existing guidelines, and to avoid different interpretations in practice, we recommend that the IASB explicitly clarify the following points in one way or another: (a) paragraph B4.1.7A is the basic principle for assessing whether the contractual cash flow of financial assets is solely payments of principal and interest on the principal

amount outstanding, and should be used for all analyses; (b) paragraphs B4.1.7A to B4.1.10A should be applied sequentially; (c) all requirements should be taken into account in assessing whether the contractual cash flows of financial assets are consistent with a basic lending arrangement, and no one of these guidance should be applied in isolation.

**[Hong Kong]**

Elements of interest in a basic lending arrangement (B4.1.7A)

(1) Most respondents expressed concerns about the proposal requiring entities to assess both the direction and magnitude of the change in basic lending risks or costs when determining whether the contractual cash flows are consistent with a basic lending arrangement because it would be difficult to model the change and assess the reasonableness of such a change against movements in the market. There is insufficient evidence in the market to demonstrate how ESG factors correlate with credit risk and other basic lending risks.

(2) Some respondents noted that there appears to be an inconsistency within B4.1.8A. In assessing the elements of interest, although the IASB clarified that an entity should not focus on 'how much' compensation it receives, the proposal requires an entity to consider the 'magnitude' of the change in basic lending risks or costs in the same paragraph.

(3) We acknowledge the challenges in assessing both the direction and magnitude of the change in basic lending risks or costs in the absence of adequate market information. Accordingly, we recommend that the IASB clarify the core principle and supplement the principle with guidance and examples on how to apply it to instruments with different ESG characteristics.

(4) In addition, we recommend that the IASB:

   (a) clarify how the concept of 'magnitude' as introduced in B4.1.8A interact with the existing 'leverage' concept stipulated in B4.1.9 in assessing a basic lending arrangement; and
   (b) move the last sentence in B4.1.8A '*A change in contractual cash flows 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*.' to B4.1.10A as it relates to a change in contractual cash flows and it would be more appropriate to include it in B4.1.10A instead of B4.1.8A.

Contractual terms that change the timing or amount of contractual cash flows (B4.1.10A)

(5) Some respondents expressed concerns about the proposed requirement that 'contingent event must be specific to the debtor' in order for a change in contractual cash flow to be consistent with a basic lending arrangement for the following reasons:
   (a) Even though the consideration of contingent events is an extant requirement of IFRS 9, the term 'contingent event' is not defined and it could be very broad. In practice, many financial instruments with contractual terms that introduce

variability to contractual cash flows are currently considered as compatible with SPPI, regardless of whether they are considered contingent events under B4.1.10, for example, an instrument with fall-back clauses triggered by the disappearance of the relevant benchmark rate. If these events are considered to be contingent events, that instrument would fail to meet the SPPI requirements under B4.1.10A as they are not specific to debtors.

(b) It is unclear as to why the contingent event has to be specific to debtors but not lenders, given that the elements of interest are meant to compensate the lenders for undertaking lending risks and costs and thus interest can also include a profit margin for lenders as stipulated in B4.1.7A. In practice, many loan contracts include clauses that are specific to lenders to protect their interests e.g. a lender's contractual right to adjust the amount to be received due to new tax provisions or compensation for additional costs. Therefore, the proposal could change the current practice, as these loans would fail to satisfy the SPPI requirements under the proposals.

(c) Some respondents commented that the meaning of 'specific to the debtor' lacks clarity, particularly in terms of whether it is only restricted to 'the debtor achieving a contractually specified target' as indicated in B4.1.10A. They also questioned whether a contingent event relating to a debtor's asset would be considered as 'specific to the debtor' under the proposal. For example, it is not clear whether a provision in a collateralised lending arrangement that could accelerate repayment of the loan if the quality of the collateral deteriorates (e.g. a significant drop in the fair value of the property that is subject to a mortgage loan) would be considered a contingent event that is 'specific to the debtor', or a contingent event that is specific to 'an asset of the debtor' (being the property) as opposed to the debtor as a whole.

(6) B4.1.10A states that to meet the SPPI requirements, an instrument's cash flows resulting from the occurrence of a contingent event must not represent an investment in the debtor. The ED only provides an example on what could be an 'investment in the debtor' in BC 70 but does not provide a clear definition or explanation of the concept. A few respondents considered that the term 'investment in the debtor' is broad and can be interpreted in different ways, leading to inconsistent practices. For instance, it is unclear whether an instrument that adjusts its interest rate upwards or downwards by a fixed number of basis points when a certain level of profits or revenue is reached would be considered 'a share of the debtor's revenue or profit' under BC 70. One school of thought is that the adjustment to the interest rate constitutes a share of the debtor's revenue or profit because it affects the share of profit for ordinary shareholders. Others contend that it is not a share of the debtor's revenue or profit because the participation in higher profits is limited by the fixed adjustments to the interest rates. The fact that BC 69 of the ED states that 'contractual cash flows that change based on the level of a debtor's revenue or profits in a specific period would not generally be considered to be consistent with a basic lending arrangement' is likely to add further confusion to this issue.

(7) In light of the above, we consider that more clarity on what constitutes 'contingent events' is necessary to ensure consistent application and avoid any unintended

consequences. In particular, if the IASB intends to exclude contingent events associated with the time value of money or prepayment features (BC 69 of the ED), we consider that the proposed requirements should explicitly state this. Furthermore, the IASB should also provide a clear rationale on why a contingent event must be specific to the debtor in order to be consistent with a basic lending arrangement and provide more guidance on what 'specific to the debtor' intends to encompass under the proposal. Given that the proposed requirement of 'contingent event specific to the debtor' could affect the classification of certain financial instruments currently meeting the SPPI requirements, we strongly recommend the IASB evaluate the implications of the proposals on the current classification of financial instruments, regardless of whether they have ESG-linked features, and consider whether this is the intention of the proposal.

<u>New examples of applying the proposed requirements (B4.1.13 and B4.1.14)</u>

(8) Most respondents generally considered that the two new examples are not sufficiently clear in demonstrating how instruments with ESG-linked features are assessed for SPPI requirements under the proposals and how paragraphs B4.1.8A and B4.1.10A interact.

(9) For example, B4.1.13 illustrates that the instrument is SPPI compatible purely because the occurrence or non-occurrence of the contingent event is specific to the debtor (B4.1.10A), without considering the direction and magnitude of the change in basic lending risks or costs (B4.1.8A). There is a risk that this example will be cited as providing a definitive answer in its own right without the need to look at any other requirements in the SPPI assessment.

(10) Hence, we consider that further guidance and examples are needed to explain the application of the concepts of 'aligned with the direction and magnitude' and 'contingent event specific to the debtor'.

**[Malaysia]**

We agree with the proposals.

**[New Zealand]**

(1) We have specific recommendations on the proposals that relate to the assessment of whether cash flows are consistent with a 'basic lending arrangement' for the purpose of applying the 'solely payments of principal and interest test' ('SPPI test'), including the proposals relating to financial assets with ESG-linked features. However, we support the IASB's initiative to assist entities in the application of the abovementioned assessment.

*Support for the initiative to provide further guidance on 'basic lending arrangement' and the classification of financial assets with ESG-linked features*

(2) We agree that it is important to ensure that entities have sufficient guidance for the classification of financial assets with ESG-linked features, and to ensure that the requirements result in appropriate outcomes. The following are comments that stakeholders raised during the PIR of IFRS 9 and/or the current consultation on the ED.

(a) During the first stage of the PIR of IFRS 9, stakeholders noted that under the current requirements of IFRS 9, it can be unclear whether a loan with ESG-linked features is consistent with a 'basic lending arrangement' and therefore whether it passes or fails the 'SPPI test' (when the ESG-linked features are not 'de minimis' – see below). Stakeholders noted that generally, classification of such loans at amortised cost seems the appropriate outcome and would provide useful information – but without further clarification of the existing requirements in IFRS 9, there is a risk that such loans would fail the SPPI test and would need to be measured at fair value. This could have the unintended consequence of discouraging banks and other financial institutions from offering such loans, which are proving useful for encouraging responsible corporate behaviour.

(b) Stakeholders noted that it is timely to address this matter. They acknowledged that, loans with ESG-linked features are currently not highly prevalent in New Zealand, and that contractually-specified changes in interest rates resulting from ESG-linked features are mostly 'de-minimis' at this stage (and therefore do not materially impact the classification and measurement of such loans). However, they noted that loans with ESG-linked features are likely to become more common in the future. Also, it is expected that when financial assets with ESG-linked feature become more prevalent and as the market gains more experience with such instruments, the impact of ESG-linked features on interest would become more substantial – as it will become more and more challenging to prove that a loan is 'green' if the ESG-linked features have a 'de-minimis' impact on the interest.

*Recommendation to explain how financial assets with ESG-linked features are consistent with a 'basic lending arrangement*

(3) We note that the ED proposes to include the following example underneath paragraph B4.1.13, in relation to financial assets with ESG-linked features:

"Instrument EA is a loan with an interest rate that is periodically adjusted by a specified number of basis points if the debtor achieves a contractually specified reduction in greenhouse gas emissions during the preceding reporting period."

(4) The ED says that this instrument meets the SPPI test, noting that "the occurrence of the contingent event (achieving a contractually specified reduction in greenhouse gas emissions) is specific to the debtor", and the contractual cash flows are "in all circumstances solely payments of principal and interest on the principal amount outstanding".

(5) It is not clear from the wording of this example (or from the other proposed amendments in the ED) how and why the cash flows of Instrument EA are consistent with a 'basic lending arrangement' and therefore meet the SPPI test.

(a) The proposed additional requirements about cash flows that are subject to change based on contingent events do not change the fact that such cash flows still need to be consistent with a 'basic lending arrangement', as described in existing paragraph B4.1.7A, in order for the financial asset to pass the SPPI test.

(b) Existing paragraph B4.1.7A states that in a basic lending arrangement, interest typically reflects the debtor's credit risk and the time value of money, as well as other basic lending risks and costs associated with holding the asset, such as liquidity risk, and a profit margin.

(c) While it is clear from the 'Instrument EA' example that the changes in the cash flows are specific to the debtor, which is consistent with the new guidance in paragraph B4.1.10A, this fact alone is not sufficient for meeting the description of 'basic lending arrangement' in paragraph B4.1.7A.

(6) We have the following recommendations to address the abovementioned lack of clarity.

(a) Regarding the changes in the cash flows of 'Instrument EA' that are based on the achievement of greenhouse gas emissions targets, we recommend explaining which of the basic lending risks or costs *described in paragraph B4.1.7A* do these changes in cash flows relate to. For example, if the achievement of greenhouse gas emission target is considered to be related to the debtor's credit risk, then it is important to explain this.

(b) It is important that the principles driving the decision that 'Instrument EA' is consistent with a basic lending arrangement and meets the SPPI test are clearly articulated. Preparers can then use this when applying these principles to other types of financial assets with ESG-linked features, and to other types of assets with variable contractual cash flows that depend on a contingent event.

*Recommendation relating to the proposed requirement for a contingent event to be specific to the debtor*

(7) Proposed paragraph B4.1.10A states: "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." There is a risk that this proposal could cause financial assets that are not consistent with a 'basic lending arrangement' to meet the 'SPPI test', and to be reclassified from fair value through surplus or deficit to amortised cost, which would not be appropriate. It is important to ensure that the proposed requirement does not unintentionally bring financial assets that are more usefully measured at fair value into the amortised cost category.

(8) We recommend explaining in paragraph B4.1.10A that when the occurrence or non-occurrence of the contingent event is specific to the debtor, this fact on its own does not mean that the change in contractual cash flows is consistent with a basic lending arrangement – and that it is necessary to consider the description of 'basic lending arrangement' in paragraph B4.1.7A when assessing whether a change in contractual cash flow that is subject to a debtor-specific contingent event is consistent with a basic lending arrangement for the purpose of the SPPI test.

(9) We are also aware of certain loans with ESG-linked features where, under the ED proposals, it could be challenging to determine whether an ESG-linked target represents a contingent event that is specific to the debtor. This is the case for the following types of loans.

(a) Loans where achievement of the ESG-linked target is partially dependent on the debtor: For a loan contract where interest is adjusted based on whether the debtor is in the top X% of sustainability leaders for a particular industry or group, it is not clear from the ED whether the condition of meeting the 'top X%' target qualifies as a contingent event that is specific to the debtor. Meeting this target is partially dependent on the debtor's actions, but it is also dependent on the actions of other entities.

(b) Loans where the ESG-linked target relates to the group that the debtor is part of: In some loans with ESG-linked features, the ESG-based target relates to the group that the debtor is part of, rather than debtor entity itself. For example, the interest on a loan may be adjusted based on whether the debtor's parent entity achieves certain ESG-based targets. It is not clear whether such a target constitutes a contingent event that is specific to the debtor.

(10) Therefore, we recommend further amendments to help reporting entities determine how the assessment of whether a contingent event is specific to the debtor should be applied to the types of situations above. This could be done by way of examples, similarly to the examples added for 'Instrument EA' and 'Instrument I', taking into account our recommendations above to clearly articulate the principles driving the decisions in the examples. Alternatively, this could be done by adding paragraphs with guidance on contingent events that are dependent partially on the debtor and partially on external factors, and contingent events that are specific to the group that the debtor is part of, but not the debtor itself.

**[Saudi Arabia]**

We recognise the urgent need for the issuance of guidance due to the continuous increase in investments in financial instruments with ESG-linked features. It appreciates the efforts made by the IASB in this regard. SOCPA also concurs with the IASB's decision to adopt a broad approach by not granting a specific exemption from the contractual cash flow characteristics requirements in IFRS 9 for financial assets with ESG-linked features.

Additionally, SOCPA holds the view that the Basis for Conclusion provides comprehensive explanations and clarifications regarding the assessment of whether the contractual cash flows of financial assets with ESG-linked or comparable features satisfy the SPPI requirements. It suggests that certain portions (example: BC68 & BC69 of Basis for Conclusion) of these explanations and clarifications could be incorporated into the main body of the standard to offer preparers more pertinent information for making informed determinations. This approach would not only enhance consistency among preparers but also ensure that they have access to the most relevant guidance.

Furthermore, we are of the opinion that the examples provided in B4.1.13 and B4.1.14 are insufficient. Given the substantial rise in financial instruments incorporating ESG-linked features, as well as the projected significant growth in their volume, SOCPA highlights the need for additional examples. Given the unique nature of ESG-linked features and the associated complexities, including more illustrative examples would be beneficial.

Comments received from preparers during an outreach carried out by SOCPA indicated that they believe basic lending risks are a relative term and greatly vary, for example, between a simple retail bank vs an investment bank. A sophisticated bank with lending compensation covering derivative arrangements such a swap fee may consider this as a basic lending arrangement for its business model. It would also be helpful to give further clarity regarding compensation, which do not directly vary with time but cover other risks such as hedging.

Preparers also stated that such an approach is principle-based and would provide more flexibility in the future if new instruments with similar types of features emerge. They suggest that the IASB provides a definition and examples of what constitutes a "contingent event", and to clarify that the "de Minimis" guidance remains applicable when applying SPPI requirements.

**[Thailand]**

The proposal is unclear whether these amendments shall be applied to ESG-linked instruments only as some amendments contradict with existing guidance. For example, instruments that contractual cash flow does not meet SPPI will be assessed to be SPPI under B4.1.10A for example the change of contractual cash flow when certain sales target can be met, as it is specific to debtor.

| **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'.<br><br>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.<br><br>Paragraphs BC73–BC79 of the Basis for Conclusions explain the IASB's rationale for these proposals.<br><br>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? |

**[Australia]**

The drafting of paragraph B4.1.16 may have consequences beyond the clarification of existing practice and should be further considered. Specific comments are as follows:

(1) The existing paragraph B4.1.16 refers to non-recourse features where a *creditor's claim* is limited to specified assets of the debtor or the cash flows from specified assets. However, this would be replaced by paragraph B4.1.16A, which states, "A financial asset has non-recourse features if an entity's contractual right to receive cash flows is limited to the cash flows generated by specified assets *both* over the life of the financial assets *and* in the case of a default" [emphasis added]. Although we do not expect this

clarification will significantly change existing practice, the proposed 'both/and' requirement might (in some cases) be more restrictive than current requirements.

(2) We note that according to the Basis for Conclusions (paragraph BC74) stakeholders asked the IASB to clarify the difference between financial assets with non-recourse features and financial assets for which the creditor's claim is secured by assets pledged as collateral. The explanation in paragraph BC75 more clearly answers this question and may be less restrictive than the wording in paragraph B4.1.16A.[1]

**[China]**

We generally agree with the IASB's proposed amendments and believe that the proposed amendments can effectively address the issues existing harmonize practices and avoid diversity of practices.

We have the following suggestions and concerns regarding some specific proposed amendments:

(1) regarding the requirement in paragraph B4.1.17A of the draft amendments to IFRS 9 that an entity may also need to consider factors such as the legal and capital structure of the debtor, we consider the requirement in the exposure draft is too principled and suggest adding concrete examples to provide further guidance, For example, how much proportion of subordinated debt or equity instruments will be considered that the "no recourse" feature does not affect satisfying SPPI.

(2) different accounting results may be achieved by constructing a SPE to hold underlying assets that do not satisfy SPPI. For example, SPE shares, such as trust shares and conduct financial transactions products shares, do not distinguish between senior and junior tranche. All investors receive a portion of the cash flows after taking out a fixed management fee to the asset manager. Cash flows are generated by multiple underlying assets, such as an investment in an equity instrument and a fixed amount repurchase commitment from a major shareholder. Since there is no concentration of credit risk, contractual linked instruments are not applicable according to the exposure draft. We propose that the IASB clarify whether the requirements of financial assets with non-recourse features should be applied to such SPE shares. If yes, the contractual cash flows of the SPE share may be consistent with a basic lending arrangement. However, if the entity directly holds the underlying assets, the contract cash flows are not solely payments of principal and interest on the principal amount outstanding. We propose that the IASB clarify whether it is reasonable to achieve different accounting results by creating structured entities in such cases.

(3) it is uncertain if the "*look through to*" assessment follows the criteria in B4.1.22., i.e. "*an entity must look through until it can identify the underlying pool of instruments that*

[1] Paragraph BC75 explains that non-recourse features refer to the absence of a liability on the part of the debtor beyond any underlying assets pledged as collateral. This is in contrast to a collateralised loan, where the creditor's claim is secured by the collateral only in the case of default. Therefore, throughout the life of a collateralised loan, the creditor has recourse only to the debtor for repayment.

*are creating (instead of passing through) the cash flows. This is the underlying pool of financial instruments*", and we recommend that the IASB clarify this issue.

**[Hong Kong]**

(1) Some respondents from the banking industry expressed concerns regarding the narrow description of 'non-recourse' features proposed in B4.1.16A. They noted that it could be read to apply only to cases where there is a contractual recourse to cash flows of the specified assets during the life of the financial asset and in the case of default. However, in current practice, non-recourse consideration could also apply when a creditor's claim is limited to specific assets or other cash flows, either contractually or in substance, and whether over the life of the instrument or in the case of default.

(2) In light of the above, we recommend that the IASB clarify the description of 'non-recourse' feature in B4.1.16A, and the key differences between 'non-recourse' and CLI by providing examples that incorporate typical features of non-recourse and CLI used in current practice (see our responses to Question 4 below).

(3) In addition, we have the following comments and recommendations to improve the clarity of the assessment in B4.1.17A.

  (a) The IASB should clarify how the two factors as set out in B4.1.17A should be applied, in particular, whether a qualitative and/or a quantitative assessment would be needed under the proposal.

  (b) In addition to the two factors in B4.1.17A, there are a number of other factors used by current practice for assessing whether the contractual cash flows of a financial asset with non-recourse features are SPPI (e.g. consideration of Loan-to-Value (LTV) ratios). We suggest that the IASB explore those factors and incorporate them into B4.1.17A where appropriate so that the market has more guidance and reference on how to perform the 'look-through' assessment to evaluate whether the non-recourse features are SPPI.

**[Malaysia]**

We agree with the proposals.

We noted that paragraph B4.1.17A suggests that an entity may need to consider the legal and capital structure of the debtor when assessing whether the contractual cash flows of a financial asset with non-recourse features are solely for principal and interest. It would be helpful to elaborate using real-life cases being practiced on how the legal and capital structure of the debtor could impact or have impacted the assessment, perhaps to also consider incorporating the explanation in paragraph BC76 into the application guidance.

**[New Zealand]**

No comment.

**[Saudi Arabia]**

We believe the proposed inclusion of paragraph B4.1.16A in IFRS 9 which clarifies the term "non-recourse features" will result in preparers having to use judgement when determining whether a financial product includes non-recourse features. This could be challenging in certain instances, specifically when there are contractually linked instruments. The linkage between these instruments can create complex financial arrangements and may require careful analysis and evaluation of their combined effects.

The implementation of this proposal will require some effort, particularly for organisations with large and complex financial instrument portfolios.

Comments received from preparers during an outreach carried out by SOCPA indicated that The term "non-recourse" could also encompass situations where there are no designated assets, and recourse is limited to the occurrence or non-occurrence of an event for recovery. It would be helpful to cover this as well.

**[Thailand]**

We generally support the proposed description of non-recourse features and examples of the factors to consider for the long through test.

Nonetheless, it would enhance better understanding should examples regarding the legal and capital structure as factors to consider the contractual cash flows of a financial assets with non-recourse features be provided.

| **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.<br>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.<br>Paragraphs BC80–BC93 of the Basis for Conclusions explain the IASB's rationale for these proposals.<br>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? |

**[Australia]**

The AASB supports the IASB's intention to clarify the assessment of the contractual cash flow characteristics of financial assets that are contractually linked instruments. However, some stakeholders noted that the wording of the proposed paragraph B4.1.20A is quite specific and could have consequences beyond clarification of the existing practice (e.g. implications for structuring transactions). We ask the IASB to reconsider the drafting.

**[China]**

We agree with the IASB's proposed amendments.

We have the following suggestions and concerns regarding some specific proposed amendments:

(1) We consider that paragraph B4.1.20A does not adequately explain the reason such transactions do not contain multiple contractually linked instruments (i.e. the structured entity is created to facilitate the lending transaction from a single creditor) and We recommend that the IASB further analysis based on the definition of the contractually linked instrument, and propose to clarify whether a transaction contains multiple contractually linked instruments if it is created to facilitate the lending transaction from two or more creditors with the same priority.

(2) Paragraph B4.1.20A does not require the debtor to hold junior debt instrument during the life of the transaction, and since the classification of financial assets is no longer reassessed after initial recognition, if the debtor can sell the junior debt instrument held during the life of the transaction, We consider that if the creditor apply the requirements in paragraphs B4.1.7-B4.1.19 to the classification of the senior debt instrument at the time of initial recognition, rather than the contractual linked instruments, there is a possibility of structuring the transaction to achieve a specific accounting outcome, and we recommend that the IASB consider this situation.

(3) There are doubts about "*concentration of credit risk* " and we suggest adding specific examples to provide further guidance. For example, for the widely existing structured entity shares, such as trust shares and conduct financial transactions products, that do not distinguish between junior and senior tranches in China. Cash flow generated by the underlying assets is allocated to the investor to the expected yield (such as 5%) stated in the contract, the remaining cash flows will be paid to the asset manager as an excess management fee. Whether the excessive management fees enjoyed by managers have created a concentration of credit risk, we recommend that the IASB further clarify how this situation should be classified under IFRS 9. In addition, paragraph B4.1.17A (b) of the draft amendments requires that the shortfall in cash flows generated by the underlying assets is expected to be absorbed by subordinated debt or equity instruments issued by the debtor. We propose that the IASB clarify whether the absorption of the shortfall in cash flows creates a concentration of credit risk.

(4) The expression of "*underlying pool of financial instruments*" in paragraph B4.1.22 may lead the entity to believe that the underlying pool of instruments of contractually linked instruments can only contain financial instruments. We propose to change the term to *"underlying pool of instruments "*.

(5) In order to avoid the misconception in practice that all contract cash flows of lease receivables are equivalent to payments of principal and interest on the principal amount outstanding, we propose to include in paragraph B4.1.23 of the exposure draft the reasons why the contractual cash flow of part of the lease receivables are not solely payments of principal and interest on the principal amount outstanding (mainly due to many finance lease receivables are subject to residual value risk or some leases might have variable lease payments that many be linked to an index).

**[Hong Kong]**

(1) Most respondents considered that the last sentence in B4.1.20 (i.e. *'... which means the tranches have non-recourse features (see paragraph B4.1.6A'*) inappropriately links the assessment criteria for non-recourse features with those for contractually linked instruments (CLI):

(a) The current wording seems to imply that the presence or absence of non-recourse features depends on whether there is a waterfall payment structure, which is inconsistent with the extant guidance on financial assets with non-recourse features. BC 89 states that non-recourse feature means that the holders have recourse only to the cash flows from the underlying pool of financial instruments, which is unrelated to the seniority and payment ranking of different tranches.

(b) It is inappropriate to include 'non-recourse' as a feature of CLI (i.e. essentially treating CLI as a subset of financial assets with non-recourse features) because these two types of instruments are subject to different assessment criteria that cannot be reconciled by treating one type of instrument's being a subset of the other.

(2) A respondent suggested changing *'disproportionate allocation of **losses**'* to *'disproportionate allocation of **cash flows**'* in B 4.1.20 because the contractual terms of CLI normally set out the holders' right to cash flows instead of losses.

(3) A few respondents have the following comments on the example in B4.1.20A:

(a) The fact pattern is over-simplified as the example does not consider the characteristics of CLI, such as the prioritisation of payments, whether the senior and junior debt instruments are entitled to cash flows from the same specified assets, and whether there is any linkage between the junior and senior debt instruments, before arriving at the conclusion that the transaction does not contain CLI. This may create the confusion that transactions with only senior and junior debt instruments would automatically be assessed as having 'non-recourse' features and not containing CLI.

(b) It is unclear how the example could be applied to situations where, at inception of the lending arrangement, there are multiple tranches with cash flow entitlements from the same specified assets and a disproportionate allocation of cash flows, but only one tranche is issued to the market and the mezzanine tranche is issued at a later date.

(c) Questions also arise as to whether the classification needs to be re-assessed if the debtor subsequently disposes of the junior tranche of an instrument that has been assessed as CLI at inception.

(4) To clarify the key differences between 'non-recourse features' and CLI, we recommend the IASB consider adding an example with a similar fact pattern as B4.1.20A but in that example there is linkage between the junior and senior tranches and prioritisation of payments, which then requires the entity to apply the CLI requirements. Building on those examples, the IASB can further elaborate whether the classification should be re-assessed when there is a change in circumstances (e.g. the scenarios as mentioned in (a), (b) and (c) of the above paragraph) by applying the relevant existing guidance in IFRS 9 where appropriate.

**[Malaysia]**

We agree with the proposals.

We noted that the proposed amendment in paragraph B4.1.20 states that "…In such situations, the holders of a tranche have the right to payments of principal and interest on the principal amount outstanding only if the issuer generates sufficient cash flows to satisfy higher-ranking tranches, which means the tranches have non-recourse features…".

In paragraph BC89, the IASB explains that "…the holders of the different tranches have recourse only to the cash flows from the underlying pool of financial instruments. Such transactions therefore have non-recourse features…".

We suggest that paragraph B4.1.20 makes reference to the underlying pool of financial instruments (instead of the issuer) which generate cash flows to pay the holders of each tranche as explained in paragraph BC89. We believe this would better explain why the tranches have non-recourse features by looking through the issuer to underlying assets.

**[New Zealand]**

No comment.

**[Saudi Arabia]**

We are aware that many preparers face significant issues when accounting for transactions containing multiple contractually linked instruments. There is a lack of consensus regarding the interpretation of terms used in the Standard to describe the types of instruments to which the requirements are applicable. This has led to diversity in practice. Therefore, we welcome the effort by the IASB to clarify the scope of the requirements in B4.1.20–B4.1.26 of IFRS 9

**[Thailand]**

We generally support the proposal to include the characteristics of multiple contractually linked instrument in B4.1.20, 20A and 21, and underlying pool in B4.1.23. Nonetheless, we recommend that the rationale behind the conclusion of the example in B4.1.20A shall be provided such that we can apply that rationale to analyse other cases. In addition, we also recommend that examples of non-recourse features and CLI shall be provided.

**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

**[Australia]**

The AASB welcomes the proposed enhancements to the disclosure requirements for investments in equity instruments designated at fair value through other comprehensive income. However, the lists of individual disclosure requirements in paragraphs 11A and 11B together with illustration of the requirements in paragraphs IG11A and IG11B may be confusing. We suggest that the reconciliation provided as an illustrative example in the Implementation Guidance would provide a better framework for the disclosures, and the information would be more useful to users. Alternatively, some stakeholders requested that the IASB cross reference the line items in the illustrative example to the applicable sub-sections in paragraphs 11A and 11B to improve clarity.

**[China]**

We agree with this proposal.

**[Hong Kong]**

We do not have any significant concerns on Question 5. Nevertheless, some respondents from the banking industry believe that disclosing the fair value of equity instruments on an aggregated basis instead of an individual basis, as proposed in 11A(c), may obscure relevant information and reduce the understandability of individual equity instruments to users of the financial statements.

**[Malaysia]**

We are generally supportive of the proposals for better information to the users of financial statements.

That said, some stakeholders disagree with the proposed disclosures in paragraph 11A(f) to separately disclose fair value changes during the period that is attributable to investment in equity instruments designated at fair value through other comprehensive income ("FVOCI") that had been derecognised during the period and those held at the end of the period.

These stakeholders do not believe the proposed disclosure would add value by citing the following reasons:

(1) IFRS 7.11B(c) already requires disclosure of the cumulative gain or loss on disposal of investment in equity instruments designated at FVOCI during the period;

(2) The disclosure which relates only to the fair value changes during the reporting period would not address stakeholders' feedback on the lack of information on the performance of these equity instruments due to the prohibition to reclassify fair value changes recognised in other comprehensive income to profit or loss.

**[New Zealand]**

No comment.

**[Saudi Arabia]**

We are of the view that in order for a user to fully understand the financial performance of equity investments, when an investment is disposed of, the user would want to know the fair value changes accumulated in other comprehensive income up to the date of disposal. This information is currently not available to a user as these amounts are not recycled to profit or loss. Recycling realised gains and losses from OCI to profit or loss raises a fundamental question and necessitates a more comprehensive understanding of the specific purpose of profit or loss in comparison to OCI. Therefore, we consider the suggested modifications to IFRS 7 to be reasonable and in this context the addition of paragraph 11A(f) of IFRS 7 is welcome.

Comments received from preparers during an outreach carried out by SOCPA indicated that removing the instrument-by-instrument disclosure may result in loss of useful information (especially for level 3 instruments) and hence those preparers do not support disclosure at an aggregate level.

**[Thailand]**

We agree with the proposed amendments, (a) and (b) because they would provide users of financial statements with useful and more comprehensive information about performance of equity instruments.

**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?

**[Australia]**

The AASB agrees that users may find information about the effect of contractual terms that could change the timing or amount of contractual cash flows useful. However, we suggest the IASB clarifies the objective of the suggested disclosures (e.g. existence of the contingent event and its effect on the pricing) and assesses the cost of the proposed disclosures relative to the expected benefit to financial statements users. Specific feedback from our stakeholders is below:

(1) Preparers thought entities might have difficulty capturing the quantitative information in paragraphs 20B(b) and (c) as it could be located in different systems across a business. This could make the disclosure very costly. They also noted that the disclosure would apply to all loans with contingent features, not just those with ESG-linked features.

(2) Concerns were also expressed around commercial sensitivity if entities disclose the extent of their involvement with loans that have ESG features and their pricing (even at an aggregated level), as required by paragraphs 20B(b) and (c).

(3) It was also suggested that the existing requirements in IFRS 7 (paragraphs 31-42) may already meet this need or could be amended to provide useful information with less cost to preparers. For example, the Implementation Guidance (B10A) already requires entities to disclose when cash outflows could be of different timing or amount.

(4) Users thought the proposed disclosure would be useful; however, they offered little feedback on how the disclosures might be used. Specifically, they discussed that the disclosure provides information about the possible range of changes to contractual cashflows, which is difficult to relate to interest income and expense.

**[China]**

We agree with the disclosure requirements proposed by the IASB and make the following recommendations:

(1) the scope of application of the new disclosure requirements is broadly defined and largely exceeds the scope of financial assets that will change according to the requirements of this amendment, which may not achieve the purpose of usefulness of information decision-making to a certain extent and will also increase the disclosure costs of the entity. It is suggested that the scope of application of the disclosure requirements should be further narrowed to focus more on special key matters, such as applying only to the financial assets involved in this amendment (e.g. ESG-linked financial assets).

(2) the disclosure requirements for financial institutions should be exempted or simplified. For financial institutions such as commercial banks that carry out a wide range of loans and investments, the disclosure requirements involve a wide and frequent range of transaction types. The collection, collation and aggregation of the disclosed information involves not only the transformation of the relevant front, middle and back office systems, but also the changes in the relevant business and management processes, which is expected to bring about higher costs for the implementation of the standard, and it is difficult to ensure the completeness and accuracy of the information. Considering that such transactions of financial institutions do not account for a significant proportion of the overall transaction scale, based on the principle of cost-benefit, it is recommended that financial institutions be exempted from disclosing such information, or that the disclosure be appropriately simplified under the characteristics of financial institutions.

**[Hong Kong]**

Our respondents expressed mixed views on the proposed disclosures regarding the contractual terms that could change the timing or amount of contractual cash flows. Respondents who agreed with the proposed disclosures considered that the proposal could help users of financial statements to ascertain the impact of a contingent event specific to the debtor on an entity's future cash flows. Other respondents (including preparers from the banking industry) have raised the following concerns:

(1) The proposed qualitative and quantitative disclosures would be onerous and costly to implement, especially for entities such as financial institutions that have a large number of financial instruments containing diverse contingent terms that are specific to debtors as well as a myriad of sustainable finance products with various ESG-linked features. The disclosure of quantitative information regarding the range of changes to contractual cash flows resulting from these terms would also be challenging. Hence, the costs of implementing the proposal may outweigh the benefits that users of financial statements would obtain.

(2) Some respondents raised concerns regarding the objective and usefulness of the proposed disclosures as they only focus on contingent events *specific to debtors* but not others that could also change the contractual cash flows of the financial instruments.

They also considered that the lack of clarity on the meaning of 'contingent event specific to the debtor' (refer to our responses to Question 2 above) may lead to inconsistent practices.

(3) Some also considered that the proposals may overlap with the requirements in other accounting standards that require entities to provide information about the expected timing and amount of contractual cash flows of financial instruments:

   (a) Disclosure of maturity analysis of financial instruments under IFRS 7

   (b) Disclosure of information about covenants and how they could affect the settlement of liabilities under paragraph 76ZA of Amendments to IAS 1 N*on-current Liabilities with Covenants*

(4) A respondent questioned the necessity of the proposed disclosures in 20B of the ED for financial liabilities measured at amortised cost, given the origin of the issue relates to the classification of financial assets, not financial liabilities. This respondent was concerned that excessive disclosures could overburden the financial statements which would not be useful for decision making.

(5) In light of the above concerns, we recommend that the IASB reconsider the costs and benefits of the proposed disclosures. In particular, it is important to reconsider whether including financial liabilities into the scope of the proposal would bring significant benefits, given other standards have already set out similar disclosure requirements regarding the expected timing and amount of contractual cash flows. If the inclusion of financial liabilities is necessary, we suggest that the IASB clarify how the proposal would interact with other existing disclosures in IFRS 7 and IAS 1.

(6) In addition, we also recommend that the IASB:

   (a) clarify how the quantitative disclosures requirement should be determined if a sensitivity analysis or a quantification of the likely effect of the contingent events is not required (BC103 of the ED); and

   (b) provide examples of contingent events that would be captured under the proposed disclosures to clarify which types of financial instruments would be subject to the disclosures.

**[Malaysia]**

We are generally supportive of the proposed disclosures for better information and transparency to the users of financial statements.

That said, some stakeholders raised the following concerns:

(1) The proposed disclosures appear wide in scope. Contingent events specific to the debtor could potentially include many clauses typical in loan agreements such as compliance to loan covenants and timely repayments, which in the event of a default would change the timing or amount of contractual cash flows e.g. due to penalties, adjustments to interest rates or repayable immediately.
If this is the intended scope, the proposed disclosures would be onerous and not necessarily useful.

If this is not the intention, it would be helpful to clarify the scope of the proposed disclosures such that not all contingent events specific to the debtor would come within the ambit of paragraph 20B.

(2) The proposed disclosures required in paragraph 20B in respect of financial liabilities appear to overlap with the existing IFRS 7.B10A disclosure which already requires an entity to provide quantitative information that enable users of its financial statements to evaluate the extent of the risk if the outflows of cash could either occur significantly earlier or be for significantly different amounts from the contractual maturity analyses disclosed in accordance with IFRS 7.39. These stakeholders would suggest that the IASB considers excluding financial liabilities from the requirements of paragraphs 20B and 20C.

The proposed disclosure required in paragraph 20B(b) with regard to quantitative information about the range of changes to contractual cash flows that could result from those contractual terms appears to require entities to quantify the impact of the change to total contractual cash flows. However, we also noted that the IASB has provided as an example in paragraph BC103, that this would entail disclosing a range of adjustments to the contractual interest rates (rather than the probabilities-weighted financial impact to carrying amount of the financial instrument) that could arise from contingent events linked to ESG targets. It would be helpful for the IASB to clarify the extent of the disclosures required in paragraph 20B(b).

**[New Zealand]**

No comment.

**[Saudi Arabia]**

We believe that a significant effort may be necessary to acquire the quantitative and qualitative data for disclosing information related to financial instruments with contingent features as required by the proposed paragraph 20B unless the entity's risk management processes include the routine collection and analysis of such data.

Therefore, in order to ensure preparers are not burdened with such requirements, SOCPA suggests the disclosures required by proposed paragraph 20B(a) and 20B(b) be made optional unless the entity's risk management processes include the routine collection and analysis of such data. From BC 103 of the Basis for Conclusions it is apparent that the IASB is aware of the costs for preparers in obtaining this information and therefore SOCPA suggests the IASB revisits the proposed requirement.

Comments received from preparers during an outreach carried out by SOCPA indicated that it would be helpful if the standard would also provide specific details of what needs to be disclosed for each type of asset (i.e. assets at amortized cost, FVOCI and financial liabilities measured at amortized cost).

**[Thailand]**

We support the proposal because it helps users of financial statements understand the effect of contractual terms that could change the timing or amount of contractual cash flows based on occurrence (or non-occurrence) of a contingent event.

It would enhance better understanding should an illustrative disclosure in accordance with these requirements be provided.

| **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.<br>Paragraphs BC105–BC107 of the Basis for Conclusions explain the IASB's rationale for these proposals.<br>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? |

**[Australia]**

The AASB requests the IASB to clarify whether the transition requirements could be implemented individually or must be implemented at the same time.

**[China]**

We agree with this proposal.

**[Hong Kong]**

(1) As explained in Questions 2- 4 above, some respondents considered that the proposal might change the classification and measurement of the existing financial instruments. They were concerned that the proposed requirements would create significant practical challenges to preparers, especially financial institutions and entities with lending as their main business, as these entities would need to reassess all the instruments held. Also, some financial instruments which have been measured at amortised cost might need to be measured at FVTPL under the proposals. It would be challenging for entities to apply the proposals retrospectively. Hence, we consider that the IASB should first understand and assess the potential impact that would be brought by the ED to the market and then further consider the practicability and the extent of retrospective application when developing the transition provisions.

(2) In terms of voluntary early adoption of the amendments, we recommend that the IASB consider allowing an entity to early adopt the amendments on the classification of

financial assets, without early adopting the amendments on the derecognition of financial liabilities for the following reasons:

(a) The proposals on the classification of financial asset and the derecognition of financial liability are conceptually separate and they do not interact with each other; and

(b) The above suggestion would help entities that wish to early adopt the amendments on classification of financial assets for their ESG-linked instruments but need more time to assess the practical implications of applying the exception to derecognise financial liabilities before settlement date under B3.3.8 and to address preparers' concern in changing the long standing diversity in practice relating to derecognition of a financial liability that is settled by cheque.

**[Malaysia]**

We agree with the proposals.

**[New Zealand]**

No comment.

**[Saudi Arabia]**

We agree with the proposed transition requirements, which are consistent with what was required on initial application of IFRS 9. SOCPA believes this approach is expected to be cost beneficial as entities would incur minimal costs as they would have access to transition information and would not be obliged to restate previous periods. In any case, it is very unlikely that most preparers would be capable of preparing restated comparative information, without employing hindsight when considering those transactions.

**[Thailand]**

We agree with these proposals. We also agree with the disclosure for each class of financial assets that changed measurement category as a result of applying the amendments.