IFRS 9 Post implementation review – Impairment

Feedback

AOSSG Interim Meeting

September 2023

Agenda

- Overview and status of IFRS 9 Post-implementation Reviews
- Overview of requirements
- Share AOSSG members feedback
- Group discussion

Note: Some feedback are still preliminary

IFRS 9 PIRs – overview & status

IFRS 9 was issued in July 2014 and:

- Became effective for annual reporting periods beginning on or after 1 January 2018
- Improved and simplified accounting that replace IAS 39, including addressing the delayed recognition of credit losses and complexity of multiple impairment models

Stages	Description	Status
Classification and measurement	A single logical classification approach driven by contractual cash flow characteristics and how the instrument is managed	PIR comment period closed
Impairment	A much needed and strongly supported forward-looking expected credit model	PIR started in H2 2022
Hedge accounting	An improved and widely welcomed model that better aligns accounting with risk management	IASB will consider in H2 2022 when to begin this PIR

Graphics and some other information used in these slides are sourced from IASB materials

IFRS 9 PIRs – overview & status

PIR—what is the objective?

OBJECTIVE	To **assess** whether the effects of applying the new requirements on users of financial statements, preparers, auditors and regulators are as intended when the IASB developed those new requirements
Overall, are the requirements working as intended?	**Fundamental questions** (ie 'fatal flaws') about the core objectives or principles—their clarity and suitability—would indicate that the new requirements are not working as intended
Are there specific application questions?	**Specific application questions** would not necessarily prevent the IASB from concluding that the new requirements are operating as intended but may nonetheless need to be addressed, if they meet the criteria for whether the IASB would take further action

Source: https://www.ifrs.org/content/dam/ifrs/meetings/2022/september/asaf/ap3-pir-of-ifrs-9-impairment.pdf

IFRS 9 PIRs – overview & status

PIR—how does the IASB respond to findings?

1 Consider whether to take action, based on the extent to which:

- the **objective** of the new requirements is not being met;
- **benefits** to users are significantly lower than expected
- **costs** of applications are significantly higher than expected

2 Determine the prioritisation of the findings based on the extent to which :

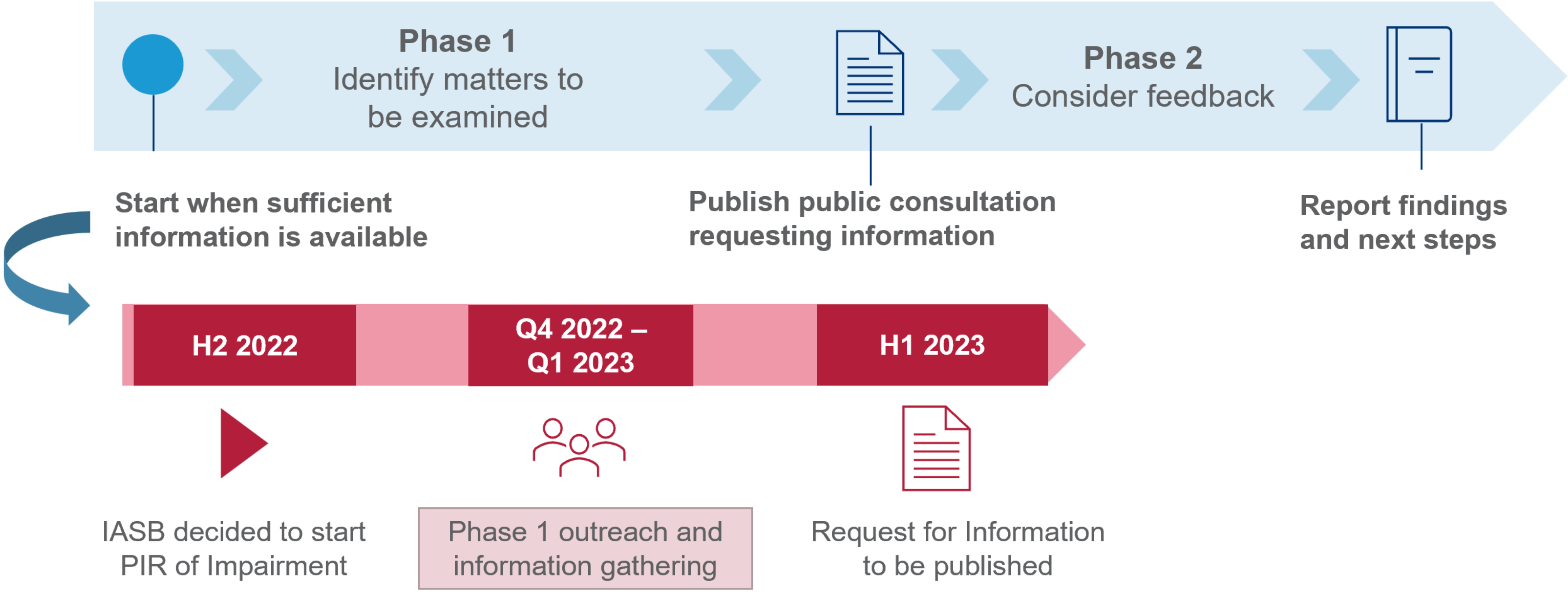
- finding has **substantial consequences**
- finding is **pervasive**
- finding arises from an issue that **can be addressed** by the IASB or the Interpretations Committee
- the benefits of any action would be expected to **outweigh** the costs

3 Determining the timing of taking action

High priority	to be addressed as soon as possible
Medium priority	to be added to the IASB or the IFRIC research pipeline
Low priority	to be considered in the next agenda consultation
No action	require no further action

IFRS 9 Impairment PIR

PIR—what is the process and where are we?



Source: https://www.ifrs.org/content/dam/ifrs/meetings/2022/september/asaf/ap3-pir-of-ifrs-9-impairment.pdf

Feedback

Q1) Do the impairment requirements in IFRS 9 result in:

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

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

No fatal flaws identified.

However, stakeholders in some jurisdictions:

- consider the ECL model could result in “too much too soon” impairment;
- diversity in practice;
- challenges in addressing credit risk modelling approaches under IFRS 9 and the Basel Framework for financial institutions - more alignment desired.

Feedback

Q3 Determining significant increases in credit risk

a) Are there fundamental questions (fatal flaws) about the assessment of significant increases in credit risk? If yes, what are those fundamental questions?

b) Can the assessment of significant increases in credit risk be applied consistently?

There is diversity in practice as feedback from stakeholders noted:

- the inconsistency in the application when assessing SICR); and
- the non-financial services sector entities not having an explicit internal policy addressing credit risk, or they do not clearly define the default event, making it difficult to enforce impairment when there is no indication of SICR.

Feedback

Q4) Measuring expected credit losses (ECL)

a) Are there fundamental questions (fatal flaws) about requirements for measuring expected credit losses? If yes, what are those fundamental questions?

b) Can the measurement requirements be applied consistently?

Stakeholders consider there is a lack of consistency in measuring ECL and diversity in the application of judgement. In particular:

(a) diversity in the modelling assumptions and the number of scenarios and overlays used;

(b) application challenges when 'incurred loss' model used or lack of historical data; and

(b) meaning of credit loss is unclear (Appendix A of IFRS 9 defines as 'all cash shortfalls' vs. objective of ECL model seem to imply measurement should only be driven by credit-related factors.)

Users feedback:

(a) allows changes to assumptions to achieve a desired outcome;

(b) disclosures about overlays are inconsistent; and

(c) Difficult to understand drivers of the movements in provisions.

Feedback

Q2 The general approach to recognizing expected credit loss
Q5 Simplified approach for trade receivables, contract assets and lease receivables
Q6 Purchased or originated credit-impaired financial assets

Feedback from stakeholders consider:

Q2) general model too complex for intercompany loans;

Q5) addressing variables using forward-looking models under dynamic circumstances is challenging and incorporating forward-looking information is too complex for some smaller corporate entities; and

Q6) making determination whether changes to the contractual cashflows are substantial or otherwise is often challenging.

Feedback

Q7 Application of the impairment requirements in IFRS 9 with other requirements
Q9 Credit risk disclosures
Q10 Other matters

Stakeholders consider:

Q7)
i. assessing whether the modification is substantial or not is often challenging and has an impact on the ECL calculation, and
ii. unclear guidance on treatment of losses from modification of financial assets, and
iii. unclear guidance on derecognition of restructured financial assets.

Q9) specific disclosure requirements on the use of overlays.

Q10) in some jurisdictions,
i. guidance required for financial guarantee contracts; and
ii. educational material on scope.

Questions?

1. General model - overview

12-month ECLs:

- are expected shortfall in all contractual cash flows given probability of default occurring in next 12 months

not

- expected cash shortfalls in next 12 months
- credit losses on assets expected to default in next 12 months

Change in credit risk since initial recognition

	Stage 1 'Performing'	Stage 2 'Underperforming'	Stage 3 'Non-performing'/ Credit-impaired
Impairment	12-month expected credit losses	Lifetime expected credit losses	Lifetime expected credit losses
Interest revenue	Gross basis	Gross basis	Net basis

Lifetime ECLs:

- result from all possible default events over the expected life of a financial instrument
- are weighted average credit losses with the probability of default as the weight
- are reflective of amount and timing—a loss arises even if the entity expects to be paid in full but later than contractually due

2. Measurement of ECLs

ECLs need to reflect:

Probability-weighted outcome
Must consider at least possibility that default will/will not occur

Time value of money
Discount at effective interest rate or an approximation thereof

Reasonable and supportable information
Available without undue cost or effort at the reporting date about past events, current conditions and forecasts of future economic conditions

Particular measurement methods are not prescribed—designed to accommodate different information availability

An entity may use various sources of data that may be internal (entity-specific) and external

Information does not necessarily need to flow through a statistical model or credit-rating process in order to determine whether it is reasonable and supportable

Historical information can be used as a base but must be updated with current observable data to reflect the effects of current conditions and forecasts of future conditions

Information should not be excluded simply because:

- the event has a low or remote likelihood of occurring; or
- the effect of that event on the credit risk or the amount of expected credit losses is uncertain

3. Disclosures

Objective Enable users to understand the **effect of credit risk** on the amount, timing and uncertainty of future cash flows		Entities' credit risk management practices and how they relate to recognition and measurement of ECLs
		Quantitative and qualitative information to evaluate amounts in the financials arising from ECLs
		Entities' credit risk exposure including significant credit risk concentrations

Amounts arising from ECLs	• Reconciliation of the loss allowance • Significant changes in the gross carrying amounts contributing to changes in the loss allowance • Inputs and assumptions used to measure 12-month and lifetime ECLs • Write-offs, modifications, collateral
Effect of deterioration, improvement in credit risk	• Carrying amount by credit risk rating grades • Inputs and assumptions used in determining whether SICR has occurred • Carrying amount of assets evaluated on individual basis

Sign up for our **newsletter!**

Thank You.

Helena Simkova

hsimkova@aasb.gov.au

www.aasb.gov.au

Australian Government
Australian Accounting Standards Board