HM Treasury

Financial Reporting Advisory Board Paper

IFRS Interpretations Committee meetings – update

Issue:	A summary of the IFRS Interpretations Committee meetings March-June, noting any particular relevance to the public sector.
Impact on guidance:	Potential adaptation or interpretation in the FReM dependent on outcomes of any Standard Setting adjustments.
IAS/IFRS adaptation?	No adaptations or interpretations proposed but further agenda decisions will be considered as needed.
Impact on WGA?	None.
IPSAS compliant?	This would depend on whether IPSASB make adjustments for any new IFRS amendments and interpretations.
Interpretation for the public-sector context?	No adaptations or interpretations proposed.
Impact on budgetary regime and Estimates?	None.
Alignment with National Accounts	No impact on the National Accounts.
Recommendation:	For the Board to note, HM Treasury proposes to make no adaptations or interpretations in relation to any outcome from the IFRS IC meetings summarised below.
Timing:	Ongoing

DETAIL

Introduction

1. This paper provides the Board with a summary of announcements from the IFRS Interpretations Committee between March 2022 and June 2022. The paper is provided for the Board's information and presented by meeting date in chronological order. The paper covers the main agenda decisions of the Interpretations Committee and tentative agenda decisions but does not represent an exhaustive commentary on all agenda items. Relevance to the public sector and any impacts on the FReM have been considered and noted.
2. There were two agenda decisions published since the last update and set out below:
   - 2.1 Agenda decision - Demand Deposits with Restrictions on Use arising from a Contract with a Third Party (IAS 7 Statement of Cash Flows) – March 2022
   - 2.2 Agenda decision - Principal versus Agent: Software Reseller (IFRS 15 Revenue from Contracts with Customers – April 2022

IFRS Interpretation Committee Update 15-16 March 2022

3. Committee's tentative agenda decisions which will return to the Committee for further discussion at a later point:

3.1 Transfer of Insurance Coverage under a Group of Annuity Contracts (IFRS 17 Insurance Contracts) – SEE APPENDIX 1 FOR THE FULL TEXT

Consideration following a request about a group of annuity contracts. The request asked how an entity determines the amount of the contractual service margin to recognise in profit or loss in a period because of the transfer of insurance coverage for survival in that period.

The Committee noted that the entity would apply other requirements in IFRS 17 to recognise in profit or loss—separately from the contractual service margin—the risk adjustment for non-financial risk, representing the entity's compensation for bearing insurance risk and other non-financial risks. Under a group of annuity contracts, an entity could provide other insurance contract services to policyholders in addition to insurance coverage for survival.

The Committee concluded that the principles and requirements in IFRS Accounting Standards provide an adequate basis for an issuer of a group of annuity contracts as described in the request to determine the amount of the contractual service margin to recognise in profit or loss in a period because of the transfer of insurance coverage for survival in that period. Therefore, the Committee decided not to add a standard-setting project to the work plan.

No action for the public sector proposed at this time.

3.2 Lessor Forgiveness of Lease Payments (IFRS 9 Financial Instruments and IFRS 16 Leases) - SEE APPENDIX 2 FOR THE FULL TEXT

Consideration following a request about a lessor's application of IFRS 9 and IFRS 16 in accounting for a particular rent concession. The submitter asked:

a) how the lessor applies the expected credit loss model in IFRS 9 to the operating lease receivable when it expects to forgive payments due from the lessee under the lease contract before the rent concession is granted; and
b) whether the lessor applies the derecognition requirements in IFRS 9 or the lease modification requirements in IFRS 16 in accounting for the rent concession.

The Committee concluded that the lessor accounts for the rent concession described in the request by applying:

a) the derecognition requirements in IFRS 9 to forgiven lease payments that the lessor had included in an operating lease receivable on the date the rent concession is granted; an
b) the lease modification requirements in IFRS 16 to forgiven lease payments that the lessor had not included in an operating lease receivable.

The Committee concluded that the principles and requirements in IFRS Accounting Standards provide an adequate basis for a lessor to determine how to apply the expected credit loss model in IFRS 9 to an operating lease receivable and account for the rent concession described in the request. Therefore, the Committee decided not to add a standard-setting project to the work plan.

No action for the public sector proposed at this time.

Agenda decision for Board consideration:

3.3 Demand Deposits with Restrictions on Use arising from a Contract with a Third Party (IAS 7 Statement of Cash Flows)

The Committee considered feedback on the tentative agenda decision published in the September 2021 IFRIC Update about whether an entity includes a demand deposit as a component of cash and cash equivalents in the statements of cash flows and financial position when the demand deposit is subject to contractual restrictions on use agreed with a third party. The Committee reached its conclusions on that agenda decision. In accordance with paragraph 8.7 of the IFRS Foundation's *Due Process Handbook*, the International Accounting Standards Board (IASB) considered this agenda decision at its April 2022 meeting.

IFRS Interpretation Committee Update 20 April 2022

4. Agenda decision for Board consideration:

4.1 Principal versus Agent: Software Reseller (IFRS 15 Revenue from Contracts with Customers)

The Committee considered feedback on the tentative agenda decision published in the November 2021 IFRIC Update about whether, in applying IFRS 15, a reseller of software licences is a principal or agent. The Committee concluded its discussions on that agenda decision. In accordance with paragraph 8.7 of the IFRS Foundation's Due Process Handbook, the International Accounting Standards Board (IASB) considered this agenda decision at its May 2022 meeting.

Appendix 1

Transfer of Insurance Coverage under a Group of Annuity Contracts (IFRS 17 Insurance Contracts)

The Committee received a request regarding grouped annuity contracts. The request asked how an entity determines the amount of the contractual service margin to recognise in profit or loss in a period because of the transfer of insurance coverage for survival in that period.

Fact pattern

The request described a group of annuity contracts under which the policyholder of each contract:

a. pays the premium upfront and has no right to cancel the contract or seek a refund;
b. receives a periodic payment from the start of the annuity period for as long as the policyholder survives (for example, a fixed amount of CU100 for each year that the policyholder survives); and
c. receives no other services under the contract (for example, no other types of insurance coverage or investment-return service).

The fact pattern referred to groups of contracts for which the annuity period starts immediately after contract inception ('immediate annuity') and also those for which the annuity period starts on a specified date after contract inception ('deferred annuity')—for example, a contract entered into in 2022 for which the annuity period starts in 2042.

Applicable requirements in IFRS 17

Paragraph 44(e) of IFRS 17 requires an entity to adjust the carrying amount of the contractual service margin for the amount recognised as insurance revenue because of the transfer of insurance contract services in the period, determined by allocating the contractual service margin over the current and remaining coverage period applying paragraph B119 of IFRS 17.

Paragraph B119 of IFRS 17 states that an entity recognises in profit or loss in each period an amount of the contractual service margin to reflect the insurance contract services provided under the group of insurance contracts in that period. The amount is determined by:

a. identifying the coverage units in the group. The number of coverage units in a group is the quantity of insurance contract services provided by the contracts in the group, determined by considering for each contract the quantity of the benefits provided under a contract and its expected coverage period.

b. allocating the contractual service margin at the end of the period equally to each coverage unit provided in the current period and expected to be provided in the future.
c. recognising in profit or loss the amount allocated to coverage units provided in the period.

Methods for applying the requirements to the fact pattern

The request sets out two methods of determining, for each contract in the group, the quantity of the benefits of insurance coverage provided in the current period and expected to be provided in the future.

Method 1

Current period	Expected to be provided in the future
Determined based on the annuity payment the policyholder is able to validly claim in the current period.	Determined based on the present value of the annuity payments the policyholder is expected to be able to validly claim in the future until the end of the coverage period (the balance of the expected future annuity payments as at the end of the current period).

Method 2

Current period	Expected to be provided in the future
Determined based on the total of: i. the annuity payment the policyholder is able to validly claim in the current period, and ii. the present value of the annuity payments the policyholder is expected to be able to validly claim in the future until the end of the coverage period (the balance of the expected future annuity payments as at the end of the current period).	Determined based on the present value of the balances of the expected future annuity payments as at the beginning of each future period, until the end of the coverage period.

Applying paragraph B119 of IFRS 17

Applying paragraph B119(a) of IFRS 17, an entity:

a. identifies the insurance contract services to be provided under the group of contracts. In the fact pattern described in the request, insurance coverage for survival is the only insurance contract service provided under the group of contracts.

b. considers the expected coverage period for each contract in the group. In the fact pattern described in the request, the expected coverage period would reflect the entity's expectations of how long the policyholder will survive.
c. considers the quantity of the benefits provided under each contract in the group.

IFRS 17 does not prescribe a method for determining the quantity of the benefits provided under a contract. Instead, an entity is required to use a method that meets the principle in paragraph B119 of reflecting the insurance contract services provided in each period. Different methods may achieve that principle depending on the facts and circumstances.

The definitions of the liability for incurred claims and the liability for remaining coverage in Appendix A to IFRS 17 describe insurance coverage as 'an entity's obligation to investigate and pay valid claims for insured events'. In addition, paragraphs BC140 and BC141 of the Basis for Conclusions on IFRS 17 explain that an entity can accept insurance risk before it is obliged to perform the insurance coverage service. Therefore, in determining the quantity of the benefits of insurance coverage provided under a contract, an entity considers (a) the periods in which it has an obligation to pay a valid claim if an insured event occurs; and (b) the amount of the claim if a valid claim is made.

The Committee observed that, under the contractual terms of the annuity contracts described in the request, an entity is obliged to pay a periodic amount (CU100 in the example) from the start of the annuity period for each year of the policyholder's survival (the insured event). Survival in one year does not oblige the entity to pay amounts that compensate the policyholder for surviving in future years; that is, claim amounts payable to the policyholder in future years are contingent on the policyholder surviving in those future years.

The Committee's conclusion

The Committee concluded that, in applying IFRS 17 to determine the quantity of the benefits of insurance coverage for survival provided under each annuity contract, a method based on:

a. the amount of the annuity payment the policyholder is able to validly claim (Method 1) meets the principle in paragraph B119 of IFRS 17 of reflecting the insurance coverage provided in each period by:
    i. assigning a quantity of the benefits only to periods for which the entity has an obligation to investigate and pay valid claims for the insured event (survival of the policyholder); and
    ii. aligning the quantity of the benefits provided in a period with the amount the policyholder is able to validly claim in each period.
b. the present value of expected future annuity payments (Method 2) does not meet the principle in paragraph B119 of IFRS 17 of reflecting the insurance coverage provided in each period because it would:

i. assign a quantity of the benefits to periods for which the entity has no obligation to investigate and pay valid claims for the insured event (for example, to the deferral period of a deferred annuity contract); and
ii. misrepresent the quantity of the benefits provided in a period by considering amounts the policyholder is able to claim and benefit from only in future periods.

The request asked only about the recognition of the contractual service margin in profit or loss. For the annuity contracts described in the request, the entity accepts insurance risk related to the uncertainty about how long the policyholder will survive. The Committee noted that the entity would apply other requirements in IFRS 17 to recognise in profit or loss—separately from the contractual service margin—the risk adjustment for non-financial risk, representing the entity's compensation for bearing insurance risk and other non-financial risks. The Committee did not discuss these other requirements.

Under a group of annuity contracts, an entity could provide other insurance contract services to policyholders in addition to insurance coverage for survival—for example, insurance coverage for death in a deferral period or an investment-return service. The conclusion in this [draft] agenda decision applies to insurance coverage for survival, regardless of other services provided. If the contracts provide other insurance contract services, the entity would also need to consider the pattern of transfer of those services to the policyholder.

The Committee concluded that, the principles and requirements in IFRS Accounting Standards provide an adequate basis for an issuer of a group of annuity contracts as described in the request to determine the amount of the contractual service margin to recognise in profit or loss in a period, because of the transfer of insurance coverage for survival in that period. Consequently, the Committee [decided] not to add a standard-setting project to the work plan.

Appendix 2

Lessor Forgiveness of Lease Payments (IFRS 9 Financial Instruments and IFRS 16 Leases)

The Committee received a request about a lessor's application of IFRS 9 and IFRS 16 in accounting for a particular rent concession. The rent concession is one for which the only change to the lease contract is the lessor's forgiveness of lease payments due from the lessee under that contract

The fact pattern

The request described a rent concession agreed by a lessor and a lessee on the date the rent concession is granted. For the lessor, the rent concession changes a lease contract classified—applying IFRS 16—as an operating lease. The lessor legally releases the lessee from its obligation to make specifically identified lease payments, some of which are amounts contractually due but not paid (which the lessor had recognised as an operating lease receivable) and some of which are amounts that are not yet contractually due. No other changes are made to the lease contract, nor are there any other negotiations between the lessor and the lessee that might affect the accounting for the rent concession. Before the date the rent concession is granted, the lessor had applied the expected credit loss model in IFRS 9 to the operating lease receivable.

The question

The submitter asked:

a. how the lessor applies the expected credit loss model in IFRS 9 to the operating lease receivable when it expects to forgive payments due from the lessee under the lease contract before the rent concession is granted; and
b. whether the lessor applies the derecognition requirements in IFRS 9 or the lease modification requirements in IFRS 16 in accounting for the rent concession.

Applying the expected credit loss model in IFRS 9 to the operating lease receivable

Paragraph 2.1(b)(i) of IFRS 9 states that 'operating lease receivables recognised by a lessor are subject to the derecognition and impairment requirements' of IFRS 9. Therefore, a lessor is required to apply the impairment requirements in IFRS 9 to an operating lease receivable from the date on which it recognises that receivable.

IFRS 9 defines credit loss as 'the difference between all contractual cash flows that are due to an entity in accordance with the contract and all the cash flows that the entity expects to receive (ie all cash shortfalls)…'. Paragraph 5.5.17 of IFRS 9 states that 'an entity shall measure expected credit losses…in a way that reflects (a) an unbiased and probability-weighted amount that is determined by evaluating a range of possible outcomes; (b) the time value of money; and (c) reasonable and supportable information that is available without undue cost or effort at the reporting date about past events, current conditions and forecasts of future economic conditions'.

Consequently, in the fact pattern described in the request, the lessor applies the impairment requirements in IFRS 9 to the operating lease receivable. The lessor estimates expected credit losses on the operating lease receivable by measuring any credit loss to reflect 'all cash shortfalls. These shortfalls are the difference between all contractual cash flows due to the lessor in accordance with the lease contract and all the cash flows it expects to receive, determined using 'reasonable and supportable information' about 'past events, current conditions and forecasts of future economic conditions'.

Therefore, **the Committee concluded that, in the period before the rent concession is granted, the lessor measures expected credit losses on the operating lease receivable in a way that reflects an unbiased and probability-weighted amount determined by evaluating a range of possible outcomes (as required by paragraph 5.5.17 of IFRS 9), including considering its expectations of forgiving lease payments recognised as part of that receivable.**

Lessor accounting for the rent concession—IFRS 9 and IFRS 16

Applying the derecognition requirements in IFRS 9 to the operating lease receivable

Paragraph 2.1(b)(i) of IFRS 9 states that operating lease receivables recognised by a lessor are subject to the derecognition requirements in IFRS 9. Consequently, on granting the rent concession, the lessor considers whether the requirements for derecognition in paragraph 3.2.3 of IFRS 9 are met.

In the rent concession described in the request, the lessor legally releases the lessee from its obligation to make specifically identified lease payments, some of which the lessor had recognised as an operating lease receivable. Accordingly, on granting the rent concession, the lessor concludes that the requirements in paragraph 3.2.3(a) of IFRS 9 have been met—that is, its contractual rights to the cash flows from the operating lease receivable expire—because it has agreed to legally release the lessee from its obligation and thus has given up its contractual rights to those specifically identified cash flows. Therefore, on the date the rent concession is granted, the lessor derecognises the operating lease receivable (and associated expected credit loss allowance) and recognises any difference as a loss in profit or loss.

Applying the lease modification requirements in IFRS 16 to future lease payments under the lease

The rent concession described in the request meets the definition of a lease modification in IFRS 16. The rent concession is 'a change to the consideration for the lease…that was not part of the original terms and conditions of the lease'. Therefore, the lessor applies paragraph 87 of IFRS 16 and accounts for the modified lease as a new lease from the date the rent concession is granted.

Paragraph 87 of IFRS 16 requires a lessor to consider any prepaid or accrued lease payments relating to the original lease as part of the lease payments for the new lease. The Committee observed that lease payments due from the lessee that the lessor has recognised as an operating lease receivable (to which the derecognition and impairment requirements in IFRS 9 apply) are not accrued lease payments. Consequently, neither those lease payments nor their forgiveness are considered part of the lease payments for the new lease.

In accounting for the modified lease as a new lease, a lessor applies paragraph 81 of IFRS 16 and recognises as income the lease payments to be made by the lessee over the lease term (including any prepaid or accrued lease payments relating to the original lease) on either a straight-line basis or another systematic basis.

The Committee concluded that the lessor accounts for the rent concession described in the request by applying:

a. the derecognition requirements in IFRS 9 to forgiven lease payments that the lessor had included in an operating lease receivable on the date the rent concession is granted; an
b. the lease modification requirements in IFRS 16 to forgiven lease payments that the lessor had not included in an operating lease receivable.

The Committee concluded that the principles and requirements in IFRS Accounting Standards provide an adequate basis for a lessor to determine how to apply the expected credit loss model in IFRS 9 to an operating lease receivable and account for the rent concession described in the request. Consequently, the Committee [decided] not to add a standard-setting project to the work plan.