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Ms Sue Lloyd
Chair, IFRS Interpretations Committee
IFRS Foundation
30 Cannon Street
London EC4M 6XH
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Our ref MV/288
Contact Mark Vaessen

22 May 2017

Dear Ms Lloyd

Tentative agenda decision: *IFRS 9 Financial Instruments—Modifications or exchanges of financial liabilities that do not result in derecognition*

We appreciate the opportunity to comment on the above IFRS Interpretations Committee (the Committee) tentative agenda decision included in the March 2017 IFRIC Update. We have consulted with, and this letter represents the views of, the KPMG network.

Although we agree with much of the substantive accounting analysis in the Committee's tentative decision, we have the following concerns with the tentative agenda decision.

The tentative agenda decision states that the Committee noted that IFRS 9 had introduced additional wording in paragraph 5.4.3 of IFRS 9 on the accounting for modifications of financial assets. However, IFRS 9.5.4.3 addresses only the accounting for financial assets, not financial liabilities, and so the purpose of this reference is unclear. We believe that any change to the accounting for modifications of financial liabilities is not driven by IFRS 9.5.4.3 but by the changes to the wording of IFRS 9.B5.4.6 compared to IAS 39.AG8 which (especially when read in conjunction with the Basis for Conclusions to IFRS 9) imply that IFRS 9.B5.4.6 may apply to modifications of financial liabilities.

The tentative agenda decision does not mention the requirement in IFRS 9.B3.3.6 for fees incurred to adjust the carrying amount of the liability and be amortised over the remaining term of the modified liability. IFRS 9.B3.3.6 implies that fees paid by the borrower to the lender are excluded from the contractual cash flows accounted for in accordance with IFRS 9.B5.4.6 but instead impact the effective interest rate prospectively.

The tentative agenda decision refers only to applying IFRS 9.B.5.4.6 and discounting at the original effective interest rate. Many constituents believe that, if the unmodified financial liability has a floating rate of interest and the modification reflects movements in market rates of interest, then the effective interest rate should instead be altered in accordance with IFRS 9.B5.4.5, normally resulting in no effect on the carrying amount. A similar question arises if the loan has a fixed rate of interest and the parties agree to modify the interest rate to a current market rate. Because the current treatment under IAS 39 generally is to adjust the effective interest rate, these issues will affect many constituents. The Committee should therefore consider the question of whether it is appropriate to adjust the effective interest rate in these cases, as leaving it unresolved may lead to significant diversity in practice.

The tentative agenda decision observes that, if an entity changes its accounting policy for modifications or exchanges of financial liabilities that do not result in derecognition as a result of the initial application of IFRS 9, then the entity applies the transition requirements in IFRS 9, which require retrospective application subject to particular relief as specified in Section 7.2 of IFRS 9. However, it is not clear what “particular relief” the Committee envisages. There are at least three reliefs that may be relevant: the relief in IFRS 9.7.2.1 from applying the standard to items that have already been derecognised at the date of initial application, the relief in IFRS 9.7.2.15 from restating comparative information and/or the relief in IFRS 9.7.2.11 for when it is impracticable to determine the effective interest rate retrospectively (although it seems unlikely the latter case would apply in practice).

Therefore, we think that the Committee should:

— Clarify that the change to accounting for modifications of financial liabilities is not driven by IFRS 9.5.4.3 but by the changes to the wording of IFRS 9.B5.4.6 compared to IAS 39.AG8;

— Mention the requirement in IFRS 9.B3.3.6 for fees paid to adjust the carrying amount of the liability and be amortised over the remaining term of the liability;

— Consider the question of whether it is appropriate to adjust the effective interest rate if a modification reflects movements in market rates and take action to forestall diversity in practice; and

— Clarify the particular relief(s) envisaged by the reference to Section 7.2 of IFRS 9.

Please contact Mark Vaessen +44 (0)20 7694 8871 if you wish to discuss any of the issues raised in this letter.

Yours sincerely

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