EY's Annual Financial Reporting Developments Series

Financial services

November 23, 2021

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Today's presenters

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Today's agenda

1. Update on IBOR reform

   Matthew Richardson

2. Other financial institution hot topics and reminders

   Amanda Snjaric and Ulana Oswald

3. Recent IFRS financial reporting developments

   Amanda Snjaric, Matthew Richardson and Ulana Oswald

4. Regulatory updates and perspectives from the Ontario Securities Commission

   Ritika Rohailla and Alex Fisher

5. Update on applying IFRS 17, *Insurance Contracts*

   Bobby Thompson

Update on IBOR reform and financial reporting implications
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Background and update

- The reform was launched by public authorities worldwide in order to improve the reliability and robustness of reference rates, following weaknesses identified in the context of the 2007/2008 global financial crisis:
  - Former process based on declarations, with potential risks of market manipulation
  - Underlying volumes of transactions sometimes insufficient
- Financial instruments that currently reference to Inter Bank Offered Rates (IBOR) rates will need to be modified in order to introduce newly created, more reliable "Risk Free Rates" (RFRs)
- In March 2021, the ICE Benchmark Administration (the administrator of LIBOR), in conjunction with the UK's Financial Conduct Authority (FCA) announced that it will stop publishing the following LIBOR settings based on submissions from panel banks:
  - After December 31, 2021: All GBP settings, all EUR settings, all CHF settings, all JPY LIBOR settings, and one-week and two-month USD LIBOR settings
  - After June 30, 2023: All remaining USD LIBOR settings (i.e., the overnight and the one-, three-, six- and 12-month settings)
- For derivatives and other ISDA contracts, when the LIBORs cease the ISDA fallbacks will be activated to transition the contracts to a designated RFR:
  - DA fallback spread adjustments became fixed on March 5, 2021
  - Bloomberg has published for each LIBOR / RFR pair, fixed spreads for when the fallback is used

The Canadian Dollar Offered Rate (CDOR) and Canadian Overnight Repo Rate Average (CORRA) are Canada's main interest rate benchmarks. Although CDOR is not anticipated to go away immediately, its relevance may decline as markets globally move to RFRs.

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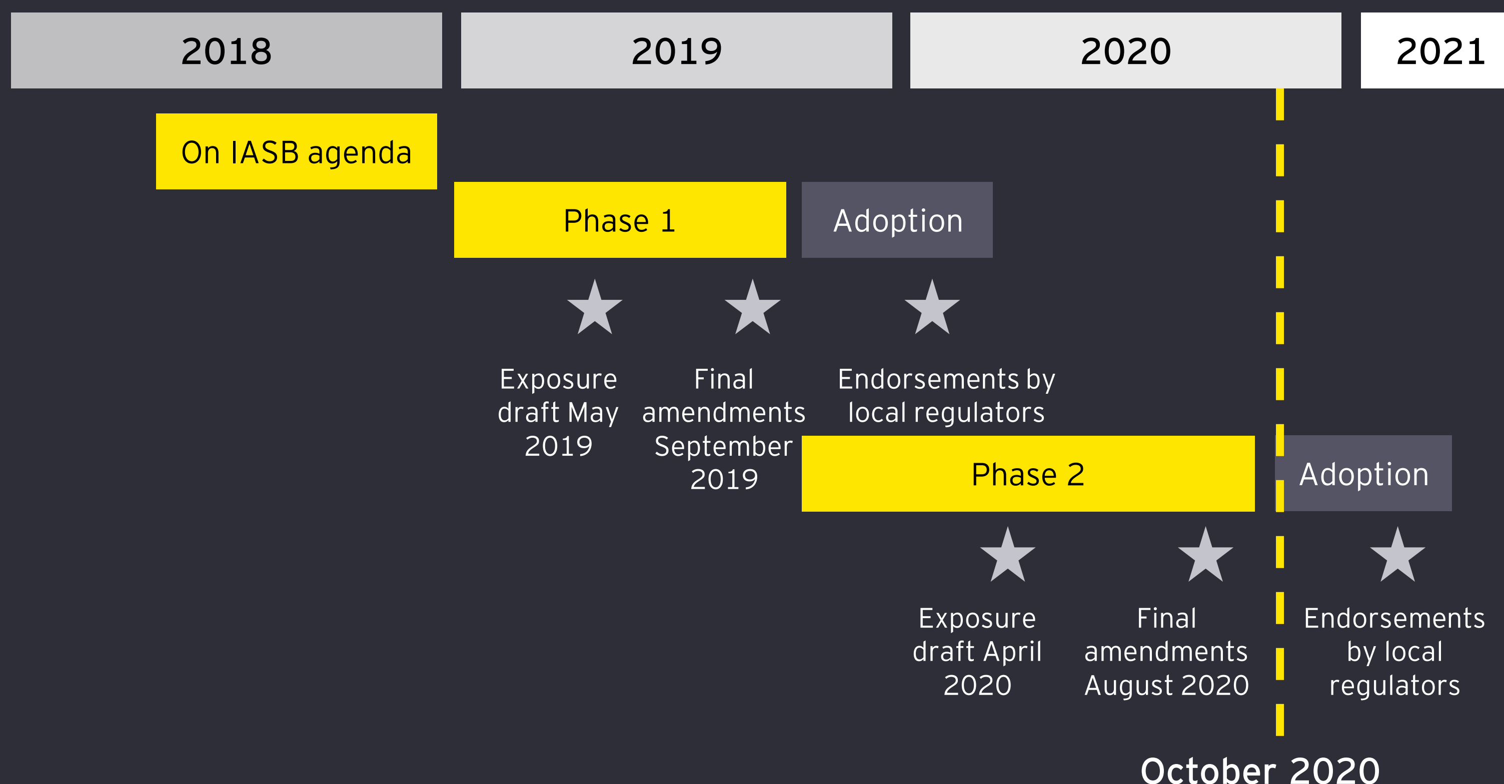
Timeline



Phase 1: Pre-replacement issues

Issues affecting financial reporting in the period before the replacement of an existing interest rate benchmark with an alternative RFR

Phase 2: Replacement issues

Issues that might affect financial reporting when an existing interest rate benchmark is replaced with an alternative RFR.

- The Phase 1 amendments took effect from January 1, 2020, with early adoption permitted
- The Phase 2 exposure draft (ED) was published in April 2020. The amendments were finalized in August 2020, effective from January 1, 2021 with early adoption permitted, e.g., for December 31, 2020 year-end

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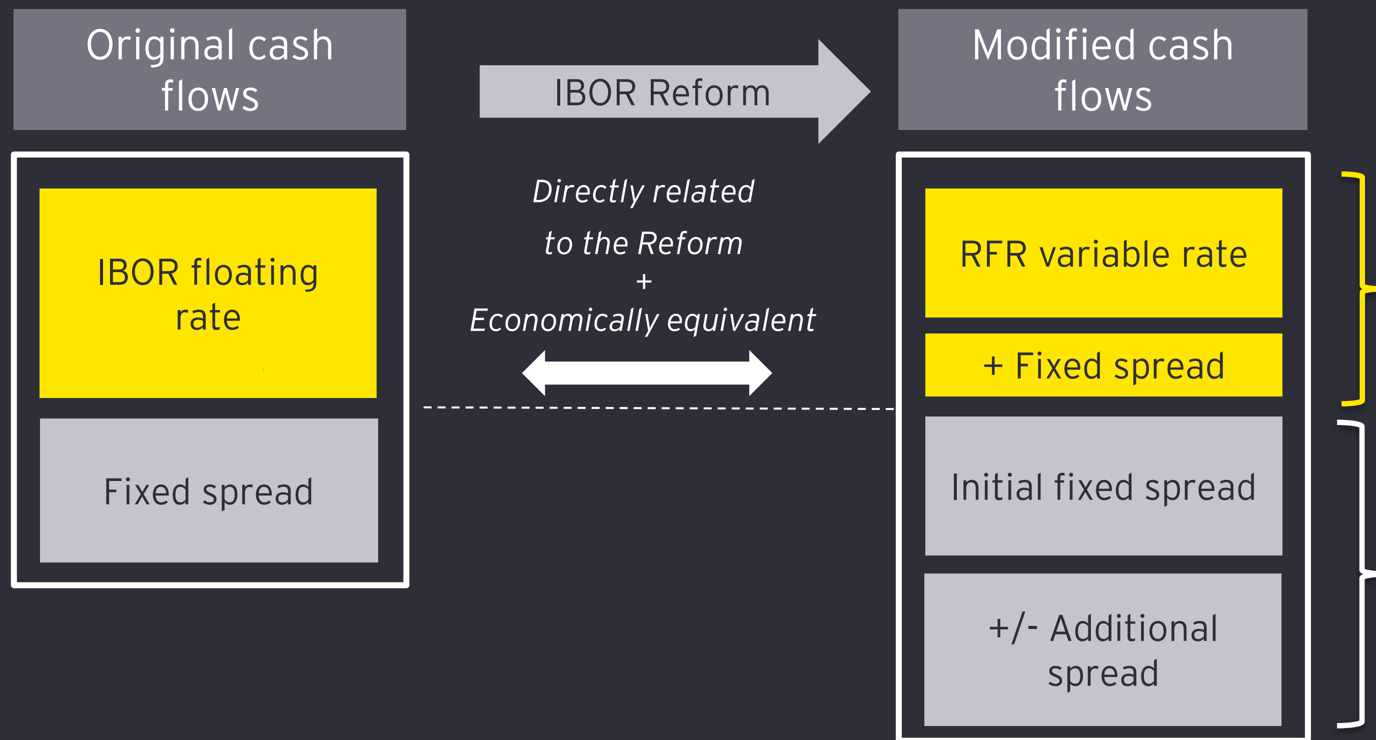
Practical expedient for modifications



Apply the practical expedient:

1. For modifications that relate directly to IBOR reform, update the effective interest rate (EIR), without adjusting the carrying amount
2. If not substantial. Use updated EIR used to recalculate the carrying amount. With any modification gain or loss recognized in profit or loss

If modifications considered substantial, the amended contract is derecognized

Scope of the practical expedient:

- Financial assets/liabilities in the scope of IFRS 9
- Including insurance entities that are still applying IAS 39 (Deferral)
- Similar expedient for lease contracts in the scope of IFRS 16 (Lessee)

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Practical expedient for modifications

Application in practice

Are the changes a "direct consequence" of the IBOR Reform?

- Examples of changes that would be **in scope**:
  - Replacement of an IBOR rate by a RFR, with the addition of a fixed spread
  - Changes to the reset period, reset dates or the number of days between coupon payment dates
- Examples of changes that would be **out of scope**:
  - Changes in maturity and methods of repayment
  - Addition or removal of caps and floors, prepayment and extension options

Do the changes result in "economically equivalent" new contractual cash flows?

- "Economically equivalent" means that the interest rate will be substantially the same before and after the replacement
- Principle-based notion, with a non-exhaustive list of examples provided in the amendments
- Positive presumption when reference is made to a protocol/standard clause (industry-practice)
- In practice, the new basis for determining the cash flows will be considered "economically equivalent" when there is no additional compensation involved apart from the spread between the initial and new benchmark interest rate
- Attention should be paid to situations where the counterparty is able to impose its decision on the new contractual terms

Examples: ISDA fallback provisions, ARRC recommendations

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Practical expedient for modifications

Spread to use when changing from IBOR to RFR

Different types of spreads may be considered when changing from an IBOR to a new RFR

Spot market spread

- Does not reflect the market expectations on forward rates (not present value neutral) and likely to be more volatile than a forward spread
- However, is simple and based on readily available information

Basis spread on the forward market

- Arguably the most "economically equivalent" approach because present value neutral (no value transfer)

Historical spread

- Less volatile than spot rates and captures the tendency of interest rates to fluctuate around a long-term mean → likely to be a better approximation to the forward spread
- Based on readily available information
- The ISDA spread *(median historical spot spread between the relevant IBOR and the compounded RFR over the previous 5 years)* is the de facto "standard" as such spreads are used in the ISDA Fallback Protocol
  - *Spreads published by Bloomberg in March 2021 for LIBOR rates with a cessation date already announced by the FCA*

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Hedge accounting reliefs

Amendments to hedge designations and hedge documentation	▶ If the changes are directly required by the IBOR Reform and if the new basis for determining the contractual cash flows is "economically equivalent" to the previous basis, there is no discontinuation of the hedging relationships ▶ Amend the description of the hedging instrument and / or the hedged item to reference the RFR ▶ Redefine the hedged risk to reference an RFR ▶ Under IAS 39, amend method for assessing hedge effectiveness ▶ A hedging relationship may be amended several times ▶ *The hedge designations must be amended by the end of the reporting period during which the change is made*
Remeasure on transition when hedge designation is amended	▶ Remeasure all items using existing IFRS 9/IAS 39 requirements (no relief on valuation) and recognize any hedge ineffectiveness as required
Hedge effectiveness	▶ For the IAS 39 retrospective test, entities may elect on a hedge-by-hedge basis to reset the cumulative fair value change to zero
Cash flow hedge reserve	▶ Release in the same period that RFR cash flows affect profit or loss
Groups of items	▶ If all the items are not amended at the same time, need to identify and transfer to sub-groups instruments that reference RFRs
Separately identifiable	▶ 24-month relief for the separately identifiable criteria, when designating an RFR as a risk component

Phase 2 disclosures

Disclosure objectives:

- Nature and extent of risks arising from IBOR reform and how the risks are being managed
- Progress in completing the transition from IBORs to RFRs and how the transition is being managed

Specific requirements

1. How the transition to RFRs is being managed
   - Progress at the reporting date; and
   - Risks arising from transition
2. Quantitative information about **financial instruments that have yet to transition to an RFR**, disaggregated by significant IBOR subject to reform
   - Derivatives; and
   - Non-derivative financial assets and liabilities
3. To the extent IBOR reform has resulted in changes to the risk management strategy
   - A description of the changes; and
   - How the entity is managing the risks

Phase 2 disclosure requirements are not just regarding hedge accounting relationships. All financial instruments impacted by the IBOR reform that have yet to transition are in scope.

In practice, clear explanations will be needed in order to clarify the scope of benchmark interest rates that are subject to uncertainties, including:

- Level of granularity
- Scope of the benchmark interest rates included in the disclosures

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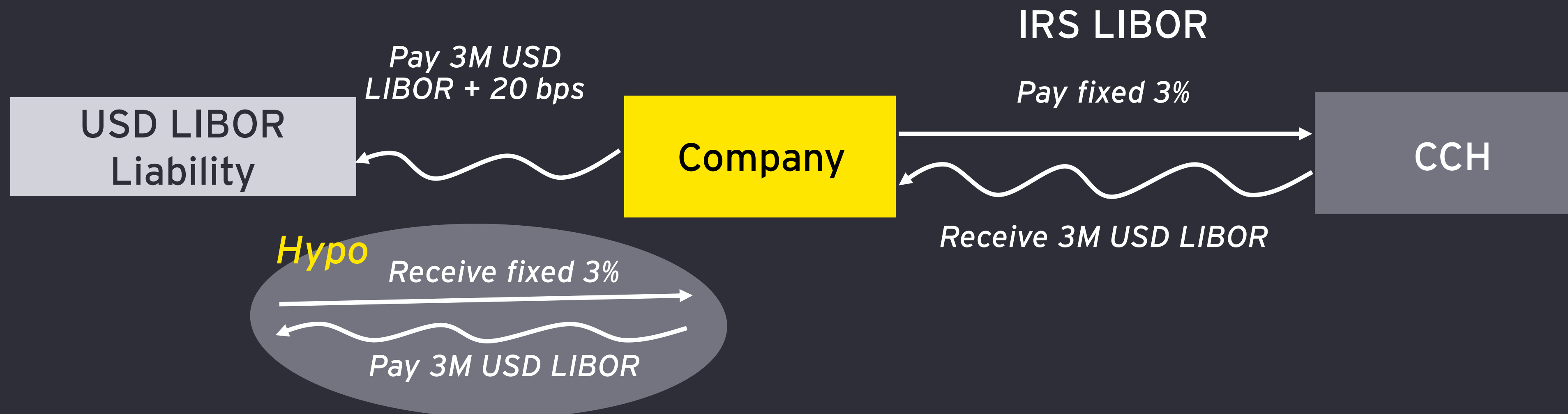
Example – Cash flow hedge

- In January 2020, the IRS is designated in a cash flow hedge
  - For changes in the cash flows of a US dollar LIBOR liability, which has a rate of LIBOR plus 20 basis points and a maturity of 5 years
  - Hedge ineffectiveness is assessed and measured using a hypothetical derivative on which the company receives 3% fixed (fixed leg of a hypothetical swap concluded at inception) and pays 3M USD LIBOR (cash flows of the debt)



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Example – Cash flow hedge

Modification of the hedging derivative

- On January 1, 2021 (residual maturity = 4 years), market rates are the following:
  - 3M USD LIBOR = 0.5%
  - SOFR = 0.2%

  30 bp difference = "market spot spread"

- The swap is amended: the receiving leg becomes indexed to SOFR; the fixed leg is reset to the initial benchmark rate (3%) less 30 bps, becoming thus 2.7%, in order to reflect the current spot spread between LIBOR and SOFR

- Change from 3M USD LIBOR to SOFR is considered to be "economically equivalent"
- The change arises as a direct consequence of IBOR reform
- No other changes are made

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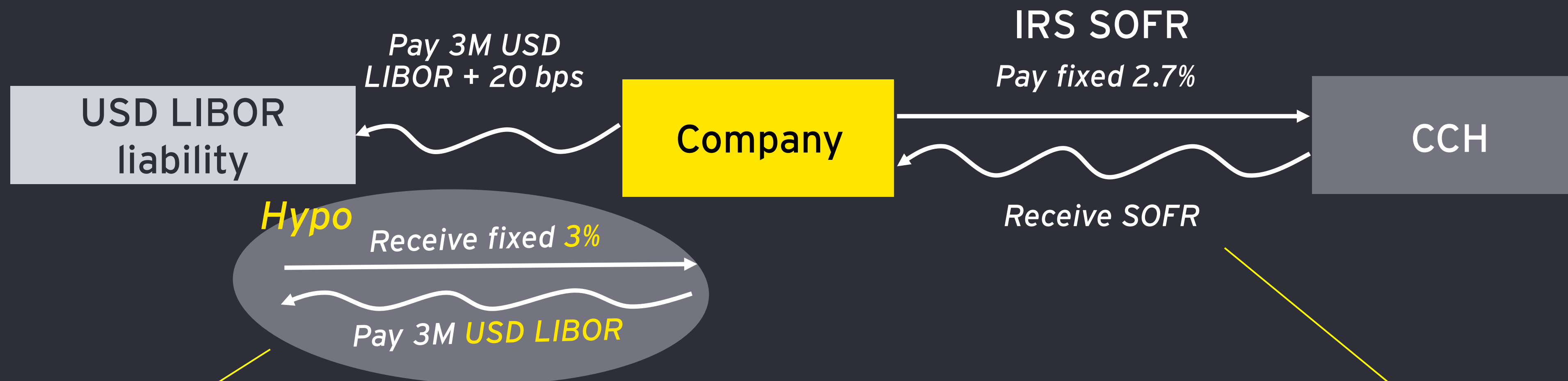
Example – Cash flow hedge

Updating the hedge documentation

- As the changes are a direct consequence of the IBOR Reform, with the new swap being considered "economically equivalent" to the old swap, the formal designation of the hedging instrument is amended without discontinuation
- The hedged risk is not updated and remains LIBOR
- The hypothetical derivative is unchanged (receive fixed 3% and pay 3M USD LIBOR)



The LIBOR-based hypothetical remains unchanged :
(3 - 0.5) x 4 years = 10 || discounted using SOFR

FV of the SOFR-based IRS:
(2.7 - 0.2) x 4 years = 10 || discounted using SOFR

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Example – Cash flow hedge

Remeasurement

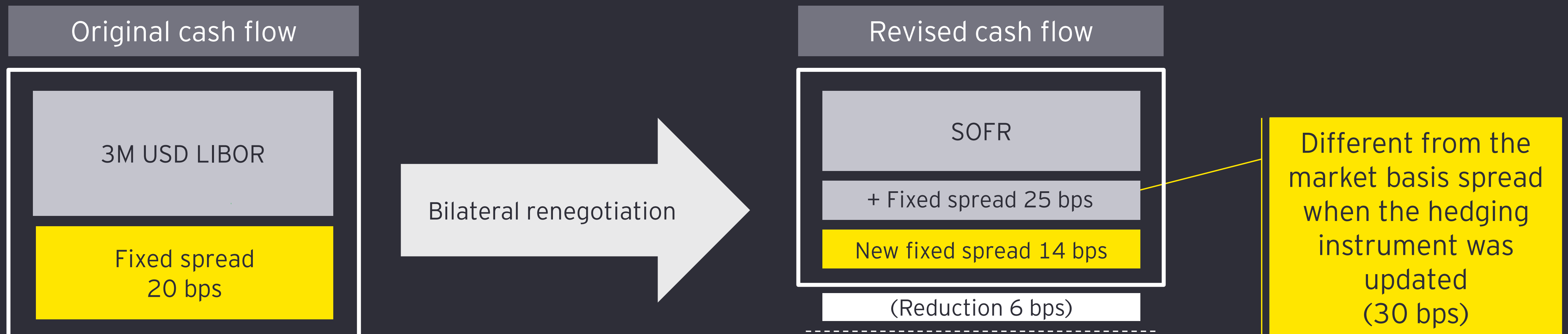
- As the hedged USD debt has not yet been modified, Phase 1 reliefs continue to apply
- As the hypothetical derivative is unchanged, normal hedge accounting is applied, which means that the cash flow hedge reserve is remeasured to the lower of:
  - The cumulative gain or loss in the fair value of the SOFR swap; and
  - The cumulative gain or loss in the fair value of the 3M USD LIBOR hypothetical derivative
- Some hedge ineffectiveness is likely to arise due to the different benchmark interest rates
  - Any hedge ineffectiveness will be measured and recognized as required
  - Under IFRS 9:
    - There must continue to be an "economic relationship" between the hedging instrument and the hedged item, e.g., between LIBOR and SOFR.
  - Under IAS 39:
    - Will not discontinue hedge accounting if the **retrospective test** falls outside the 80-125% range during the period of uncertainty arising from the reform
    - However, the **prospective test** must continue to be met

Example – Cash flow hedge

Amendment to the hedged liability

- On January 1, 2022 (residual maturity = 3 years), market rates are the following:
  - 3M USD LIBOR = 0.55%
  - SOFR = 0.30%

  25 bps difference = "market spot spread"
- On January 1, 2022, the liability is amended to transition from LIBOR to SOFR. The renegotiated terms include a resetting of the credit spread by 6 bps based on current market conditions, with no related cash compensation from the lender



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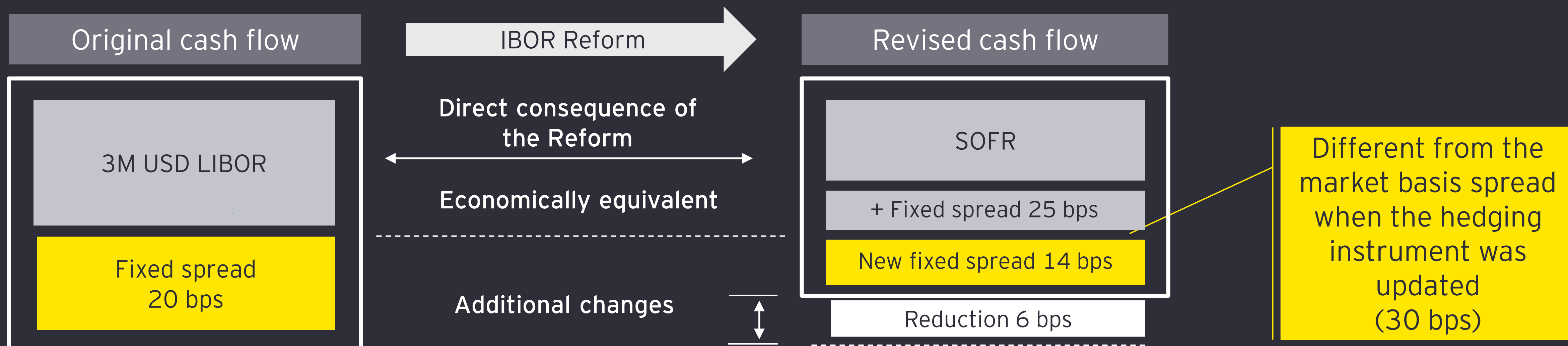
Example – Cash flow hedge

Amendment to the hedged liability (continued)

- On January 1, 2022, the liability is amended to transition from LIBOR to SOFR. The renegotiated terms include a resetting of the credit spread based on current market conditions, with no related cash compensation from the lender



Step 1: Analyze whether the additional changes (modification of the credit spread) are substantial

- In this example the modification of cash flows is analyzed as non substantial. The USD liability is not derecognized

Step 2: For changes that relate directly to IBOR reform, update the effective interest rate (EIR), e.g., SOFR + 45 basis points (initial fixed spread of 20 bps + LIBOR/SOFR basis spread of 25 bps)

Step 3: The updated EIR is used to recalculate the carrying amount for the reduction of 6 bps to the original fixed spread, with a modification gain or loss recognized in profit or loss

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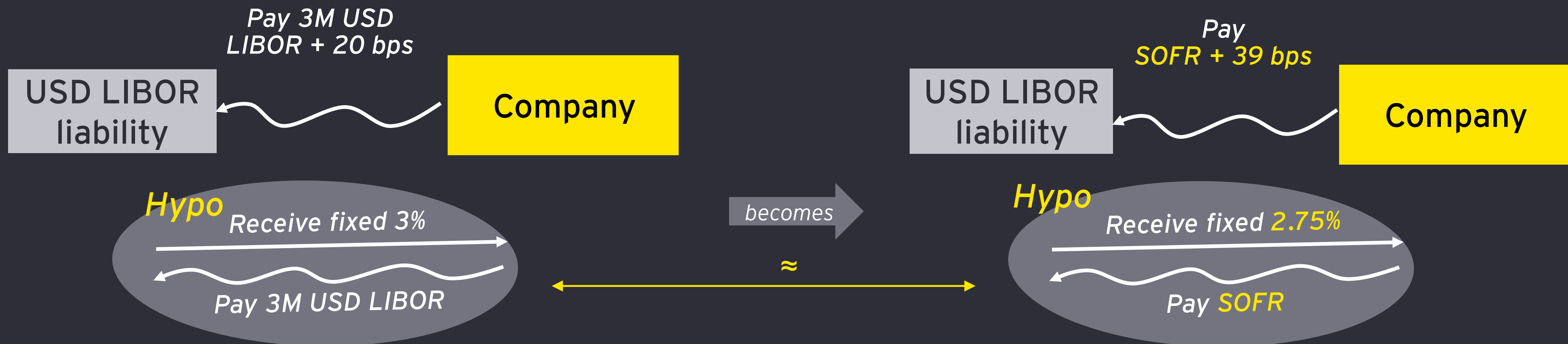
Example – Cash flow hedge

Second update of the hedge documentation

As the modification of the liability does not trigger its derecognition, it does not constitute a discontinuation of the original hedging relationship, but the hedge documentation has to be amended for a second time

- The amended hypothetical derivative is now based on SOFR, but its terms are based on conditions existing at inception (as the hedge is not discontinued)
  - Pay SOFR (liability cash flows), and
  - Receive fixed 2.75% (fixed leg of a hypothetical derivative that would have been set at inception, i.e., 3%, decreased by the SOFR / LIBOR spread, i.e., 25 bps)



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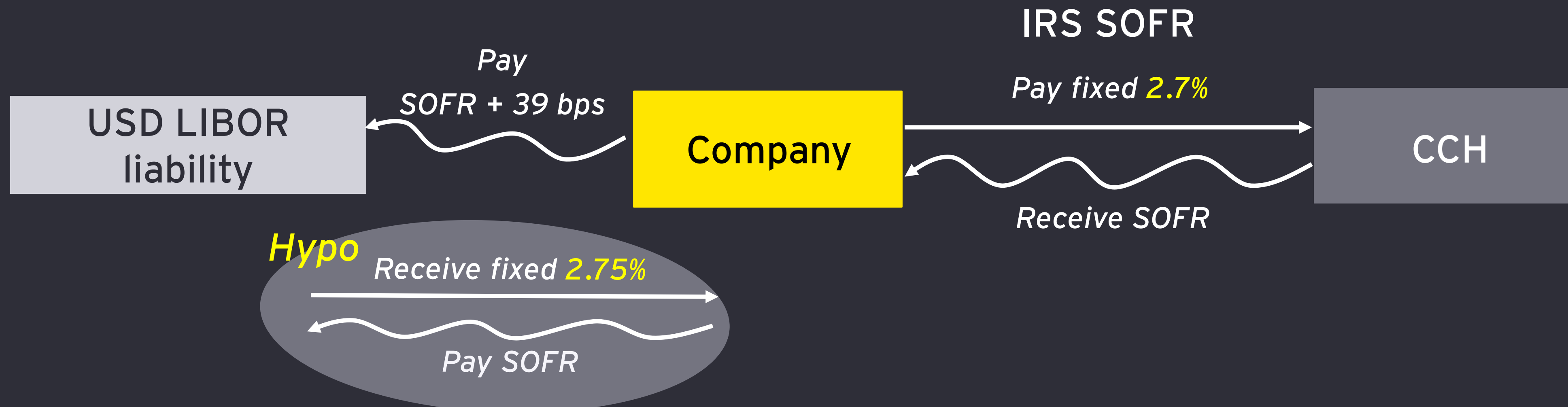
Example – Cash flow hedge

Effectiveness after the second update

The Phase 1 relief now ends as there is no longer uncertainty as to the timing and the amount of the cash flows

- The amount accumulated in the cash flow hedge reserve is now deemed to be based on SOFR, the OCI reserve being subsequently remeasured at the lesser of:
  - Cumulative gain or loss in FV of the SOFR IRS from inception of the hedge, and
  - Cumulative change in FV of the revised hypothetical derivative (now based on SOFR)
- Some ineffectiveness should be measured (difference on fixed rates) and recorded if applicable



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Other financial institution hot topics and reminders
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Key considerations on ECL measurement in the current context

Individual risk analysis

Because support measures tend to "turn off" usual significant increase in credit risk (SICR) backstops (forbearance, days past due), banks need to:

- Consider other indicators to determine whether the borrower's difficulties are temporary (e.g., forced leave) versus longer term (e.g., redundant)
- Define appropriate monitoring for new guaranteed loans
- Assess implementation of governmental initiatives and to what extent they will limit the defaults
- Banks are likely to have less information for retail than wholesale customers and need to design a holistic approach:
  - Economic conditions
  - History of missed payments or adverse credit bureau scores
  - Current data (employment status, current account activity, etc)
  - Use of portfolios approaches and application of expert judgment
- For wholesale exposures, ratings tend to react more quickly based on updated financial information. However, portfolio and sectorial approaches remain critical
- Revise LGD

Collective or sectorial approaches

- Pooling of loans should consider factors such as:
  - Products: mortgages vs. retail unsecured loans, etc.
  - Type of relief measures granted, initially and subsequently
  - Whether the borrower is asking for a renewal of a payment holiday or is a first request
  - Geography (e.g., country-wide support measures)
  - Industry (travel, hospitality, entertainment and services industries)
  - Behavioural information (historic and current)
  - Information collected when granting or renewing payment holidays
- Revised macroeconomic assumptions should be incorporated in the assessment
- Overlay approaches may be needed to capture the uncertainty, limitations of historical data, sector specific risks and possible government actions

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Transparent disclosures on credit risk will remain critical

Reminder of key IFRS 9 ECL disclosures

Macroeconomic scenarios and assumptions

- How new scenarios and weights compare to the previous ones
  - Main differences
  - Underlying rationale
  - Impact on the estimate, e.g., a sharper rebound leading to a decrease in PD and a release in Stage 1 and 2 ECL allowance of XXX
- Overlays related to macroeconomic models and assumptions
  - Including adjustments to inputs, e.g.: averaging variations in GDP over 2020 and 2021
  - Rationale and articulation with other IFRS 9 components of the estimate (risk parameters and Stage 2 transfers)
  - Changes compared to prior reporting periods and impact, e.g., addition of a new overlay to offset modelled release not deemed reflective of underlying risk
- Specific focus on vulnerable sectors
- Sensitivity analysis

COVID-19 crisis loans and government relief measures

- Status of the government support measures on the main markets and impact on credit quality indicators
  - Including expected withdrawal dates and expected impact on credit quality
- Update on COVID-19 measures implemented by the bank and related exposures (State-guaranteed loans and moratoria)
  - New developments, conditions, remaining maturities
  - Impact on risk assessment and classification (Stage 2/forbearance/ default) e.g., borrowers asking for an extension on guaranteed loans have been classified in Stage 2
- Specific risk-monitoring approaches to improve early identification of troubled borrowers
  - Impact on classification and ECL estimate
- Other key accounting estimates on COVID-19 measures
  - Calculation of EIR, e.g., guaranteed loans with step-up rate
  - Effect of guarantees (integral or not)
  - Modification accounting

Transparent disclosures on credit risk will remain critical

Reminder of key IFRS 9 ECL disclosures

ECL movements and outlook

- Analysis of the main movements in ECL allowance and profit & loss effects
  - Stage 3 losses: Trends by main portfolio compared to prior periods, significant single-name losses (if applicable)
  - Movements in Stage 1 and 2 ECL allowance: Trends by portfolio (stable, release, etc.) and drivers
    - In case of release, compare to additional provisions booked in 2020 (or up until Q1 2021)
  - Movements in overlays: Rationale for the overlay, estimation approach, current impact and expectations on timing of withdrawal
    - Allocation by Product/Business /Type of overlay (post-model adjustments due to models working outside historical observations, uncertainty overlays, sectorial overlays, etc)
    - Explain the movements and highlight offsetting effects between different types of overlays, e.g.: reduction of positive overlay for potential default suppression due to government intervention offset by a reduction in negative overlay applied for Retail PD adjustments as models are no longer outside historical observations)
- Recent trends on credit risk indicators (delinquency, forbearance, default) and expectation for 2021
  - Including if and how the bank has changed its risk assessment processes (data, models, governance, expert judgment framework)
- Recent trends on vulnerable and expectation for 2021
  - Concentrations, risk assessment approach, overlays, highlighting any change
- Transfers in and out of Stage 2:
  - Trends by main portfolio and drivers
  - Explain the movement in Stage 2 proportion (new transfer, new production, transfers back to stage 1, defaults, etc.)
  - Triggers: Delinquency? Forbearance? Portfolio approach? Other? (for example, request for an extension of payment holiday)
  - Changes applied to usual transfer triggers - if applicable

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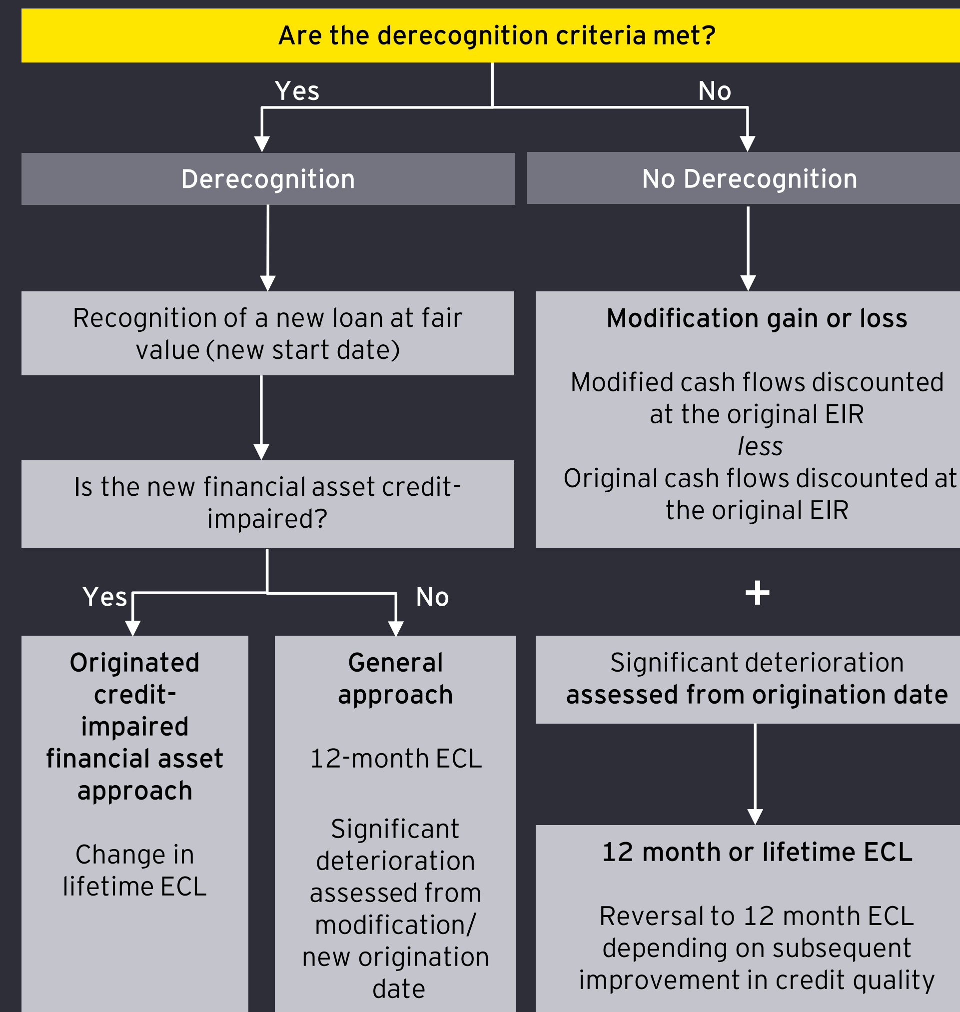
Forbearance measures and debt modifications

- The variety of measures and reliefs requires careful consideration of specific terms and conditions
- Some measures, such as the term extensions, interest or debt forgiveness, **could result in amendment of contractual terms of financial assets**
- Banks need to **apply their existing accounting policies** to determine whether the changes result in the derecognition of the existing financial asset:
  - If yes, the modified asset is considered a "new" financial asset and the lender should assess whether the asset is credit-impaired at initial recognition (e.g., when there was a substantial modification of a distressed asset that resulted in the derecognition)
  - If not, the lender should retain an original EIR and recognize a catch-up adjustment in profit or loss for the changes in expected cash flows discounted at the original EIR, as well as determine whether SICR occurred
    - Entity must first calculate the gain or loss on modification, before revising the ECL on the modified financial asset



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Forbearance measures and debt modifications

- Specific facts and circumstances need to be considered to determine the accounting consequences of various reliefs
- Common examples, which are generally not expected to result in derecognition of financial assets, include:

Payment holidays and term extensions:

- Suspension of payments and extension of the loan repayment date by 6 months
- Bank continues to accrue interest during the suspension period

- Due to interest accruing, there is likely no modification gain or loss to be recognized
- The lender should revise the estimate of ECL, upon determining:
  - For stage 1 assets, whether a SICR occurred (i.e. transfer from stage 1 to stage 2)
    - If the relief is available to all borrowers in a particular country, it may not on its own indicate a SICR
    - If the relief is available only to selected borrowers meeting certain criteria, it could be more likely that SICR occurred
  - For stage 1 and stage 2 assets, whether the exposure should be considered credit-impaired (i.e. transfers to stage 3)

Interest / principal forgiveness:

- Forgiveness of a portion of a financial asset, e.g. 3-months worth of interest

- For stage 1 and 2 assets, due to the change of contractual cashflows, there is likely a modification gain or loss to be recognized, and
- The lender should revise the estimate of ECL (same as in the payment holidays and term extension example)
- For stage 3 assets, if there was no reasonable expectation of recovering a portion of the financial asset that was forgiven, this amount should be written off, as a partial derecognition (reduction of the gross carrying amount before calculating a modification gain or loss)

Green finance and Environmental, Social and Governance (ESG) loans

- ESG issues are increasing world-wide in the leveraged loan market with a number of deals issued in 2021 structured as ESG-linked loans
- The number of investors with broader monitoring of ESG policies and screenings is growing and this could increase potential investor demand
- The application of IFRS 9 requirements to green or 'ESG' financial instruments can lead to difficulties, such as:
  - a) Failing the solely payment of principal and interest test 'SPPI-test' (due to interest rate being indexed to non-interest variables); and
  - b) The 'non-recourse' nature (in case of limitation of a creditor's claim to specified assets of the debtor or to the cash flows from specified assets)

Type of debt	2019	2020	Change ($)	Change (%)
Green bonds	$271.1B	$305.3B	$34.2B	12.6%
Sustainability bonds	37.9	68.7	30.8	81.1
Social bonds	18.0	147.7	129.7	720.3
Green loans	93.4	80.3	-13.0	-14.0
Sustainability-linked loans	140.1	119.5	-20.6	-14.7
Sustainability-linked bonds	5.0	10.6	5.6	112.5
Total	565.5	732.1	166.6	29.5

Source: BloombergNEF

Figure 1 : Sustainable debt issuance, 2019 to 2020 [1]

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ESG Loans

Reminder on the "SPPI" concept under IFRS 9

Contractual cash flows that are solely payments of principal and interest (SPPI)	
Consistent with a **basic lending arrangement**, which includes consideration for:	Do not introduce exposure to risks or volatility unrelated to a basic lending arrangement
▶ Time value of money ▶ Credit risk ▶ Other basic lending risks and costs: ▶ Liquidity risk ▶ Administrative costs ▶ Profit margin	▶ Elements inconsistent with a basic lending arrangement include: ▶ Exposure to changes in equity or commodity prices ▶ Leverage

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ESG Loans

Reminder on the "SPPI" concept under IFRS 9

		Type of deviation from 'pure' principal and interest	
		All types	**Time value of money**
Type of interest rate	All types	*Not genuine?*	*Not significantly different* cash flows compared to 'pure' principal and interest?
		De minimis?	
	Regulated		*Broadly consistent* with time value of money?

+ Exception for some prepayment options that are deeply out of the money

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ESG Loans

Assessing SPPI for loans with 'Green Variability'

The contractual terms may provide for the cash flows to vary depending on ESG metrics or other environmental measures (collectively "Green Measures"):

- Measures relating to compliance with emissions and waste regulation standards, energy efficiency metrics, CO_2 emissions standards, energy consumption standards relating to the asset being financed, or
- A sustainability index that measures the performance of an entity based on a basket of different Green Measures

Key factors to consider when performing the SPPI analysis:

- Does the ESG clause have a more than "de minimis" impact on contractual cashflows ?
- Is the ESG clause "unrelated to a basic lending arrangement"?
- Can it be considered as related to the credit risk of the issuer/commensurate with a change in credit risk?
- Does it represent a decrease of the bank's profit margin in contemplation of marketing/ethical issues?

Careful consideration needs to be given to the mechanism of **tracking and analyzing** these types of loans

- Are these new features captured by the entity's SPPI assessment processes for new products?
- Has the entity defined an accounting framework to assess the impact of ESG features on the SPPI test?
- How does the entity implement the analysis of the link to credit risk or "de minimis" assessment?

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Recent IFRS financial reporting developments
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IASB developments

IASB work plan: Standard-setting projects

Topic	Next milestone	Expected date
Disclosure Initiative – Subsidiaries without Public Accountability Disclosures	Exposure Draft Feedback	H1 2022
Disclosure Initiative – Targeted Standards-level Review of Disclosures	Exposure Draft Feedback	January 2022
Financial Instruments with Characteristics of Equity	Exposure Draft	TBD
Management Commentary	Exposure Draft Feedback	Q1 2022
Primary Financial Statements	IFRS Standard	TBD
Rate-regulated Activities	Exposure Draft Feedback	November 2021
Second Comprehensive Review of the IFRS for SMEs Standard	Exposure Draft	TBD

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Financial instruments with characteristics of equity

The IASB tentatively decided to explore making clarifying amendments to IAS 32 to address common accounting challenges:

- Clarify some underlying principles in IAS 32
- Adding application guidance to facilitate consistent application
- Enhance presentation and disclosure requirements

Timeline of project:

- The Board published the discussion paper *Financial Instruments with Characteristics of Equity* in June 2018
- The Discussion Paper was open for comment until January 7, 2019
- In December 2020, the Board decided to add this project to its standard-setting programme
- Next milestone: Exposure draft

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Financial instruments with characteristics of equity

High-level overview of topics in the discussion paper:

1 Classification

- Still a single distinction (liability or equity)
- Clarified principles
- Limit changes to classification outcomes that are well understood

2 Presentation

- Separate presentation for liabilities (with "equity-like" returns)
- Expanded statement of changes in equity

3 Disclosure

- Consider investor information needs re: dilution, liquidity, solvency, priority on liquidation, terms and conditions

Expected impact:
Simple instruments: no change of classification
More complex instruments: few changes in classification but a clearer rationale for classification

Disclosure initiative - Targeted standards-level review of disclosures

Background:

- Stakeholders have repeatedly told the Board they have three main concerns about information disclosed in financial statements:
  1. not enough relevant information;
  2. too much irrelevant information; and
  3. ineffective communication of the information provided
- The Board underwent a project with the objective to improve how the Board develops and drafts disclosure requirements in IFRS Standards, so that entities applying those requirements provide more useful information to users of financial statements.
- In March 2021, the IASB issued an Exposure Draft titled, 'Disclosure Requirements in IFRS Standards—A Pilot Approach' with proposed amendments to IFRS 13 Fair Value Measurement and IAS 19 Employee Benefits.
- The Exposure Draft is open for comment until January 12, 2022.

Takeaways:

- The Board's intention is to replace what some perceive as a checklist approach with a more objective-defined approach to disclosure requirements.
- The proposed guidance relies on a hierarchy of disclosure requirements, starting with 'Overall disclosure objectives', supplemented by 'Specific disclosure objectives', which are supplemented by mandatory and non-mandatory 'Items of information'.
- The Board expects that this approach to setting disclosure requirements will require more judgment on behalf of preparers, in order to determine which information is material and whether it satisfies the disclosure objectives.

EY

Disclosure initiative – Targeted standards-level review of disclosures

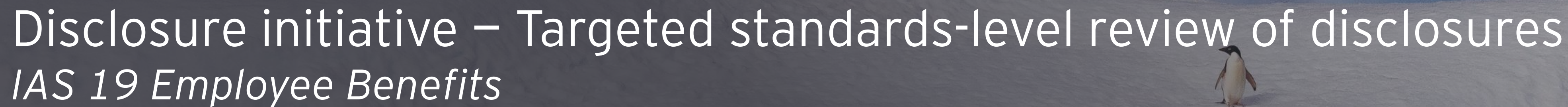
IFRS 13 Fair Value Measurements

IFRS 13 has currently been revised with the disclosure objective to have companies disclose information that enables the users of financial statements to evaluate the Companies exposure to uncertainties associated with fair value measurements of classes of assets and liabilities measured at fair value in the statement of financial position after initial recognition.

Disclosure objectives of IFRS 13 require disclosure of:

- Assets and liabilities within each level of the fair value hierarchy;
- Measurement uncertainties associated with their fair value measurements;
- Reasonably possible alternative fair value measurements;
- Reasons for changes in their fair value measurements;
- The amount, nature and other characteristics of assets and liabilities not measured at fair value in the statement of financial position but for which fair value is disclosed in the notes; and
- How the characteristics relate to the categorization of those classes of assets and liabilities in the fair value hierarchy.

EY



Disclosure initiative – Targeted standards-level review of disclosures

IAS 19 Employee Benefits

IAS 19 has currently been revised with the disclosure objective to have companies disclose information that enables the users of financial statements to:

a. Assess the effect of defined benefit plans on the entity's financial position, financial performance and cash flows; and
b. Evaluate the risks and uncertainties associated with the entity's defined benefit plans.

Disclosure objectives of IAS 19 require disclosure of:

- Amounts in the primary financial statements relating to defined benefit plans;
- The nature of, and risks associated with, defined benefit plans;
- Expected future cash flows relating to defined benefit plans;
- Future payments to members of defined benefit plans that are closed to new members;
- Measurement uncertainties associated with the defined benefit obligation; and
- Reasons for changes in the amounts recognized in the statement of financial position for defined benefit plans.

Similarly for defined contribution plans, the proposed amendments require an entity to disclose information that enables users of financial statements to understand the effect of defined contribution plans on the entity's financial performance and cash flows.

EY

IASB work plan: Completed projects

Topic	Related Standard	Effective date
Interest Rate Benchmark Reform and its Effects on Financial Reporting – Phase 2	IFRS 9, IAS 39, IFRS 7, IFRS 4, IFRS 16	January 1, 2021
IFRS 16 and COVID-19*	IFRS 16	April 1, 2021
Updating References to the Conceptual Framework	IFRS 3, IAS 37, Conceptual Framework for Financial Reporting	January 1, 2022
Property, Plant and Equipment: Proceeds before Intended Use	IAS 16	January 1, 2022
Onerous Contracts – Cost of Fulfilling a Contract	IAS 37	January 1, 2022
Subsidiary as a First-time Adopter	IFRS 1	January 1, 2022
Fees in the '10 per cent' Test for Derecognition of Financial Liabilities	IFRS 9	January 1, 2022
Taxation in Fair Value Measurements	IAS 41	January 1, 2022
Amendments to IFRS 17 Insurance Contracts	IFRS 17	January 1, 2023

* Completed in 2021

EY

IASB work plan: Completed projects

Topic	Related Standard	Effective date
Classification of Liabilities as Current or Non-current	IAS 1	January 1, 2023
Deferred Tax related to Assets and Liabilities arising from a Single Transaction*	IAS 12	January 1, 2023
Definition of Accounting Estimates	IAS 8	January 1, 2023
Disclosure Initiative—Accounting Policies*	IAS 1	January 1, 2023
Insurance Contracts	IFRS 17	January 1, 2023

* Completed in 2021

Fees in the '10 per cent' test for derecognition of financial liabilities

Amendment to IFRS 9

- In May 2020, the IASB issued an amendment to IFRS 9 *Financial Instruments* as part of Annual Improvements to IFRS Standards 2018-2020
- The amendment to IFRS 9 clarifies the fees a company includes when assessing whether the terms of a modified financial liability are substantially different from the terms of the original financial liability (in performing the 10% test)
- When performing the 10% test, a borrower includes in the present value of the new cash flows **only fees paid or received between the borrower and the lender**, including fees paid or received by either the borrower or lender on the other's behalf

The amendment to IFRS 9 is effective for annual periods beginning on or after January 1, 2022. Early application is permitted.

EY

Fees in the '10 per cent' test for derecognition of financial liabilities

Amendment to IFRS 9

Example:

- Entity A modifies the terms of its term loan with the lender
- The present value of the cash flows of the original financial liability, discounted using the original EIR, is $110,000
- The present value of the cash flows under the new terms, discounted using the original EIR, is $100,000 (excluding costs/fees)
- Entity A incurs $5,000 of fees paid to the lender and $2,000 of legal costs (of the borrower, paid by the borrower)

Analysis:

- Only the $5,000 of lender fees would be included in the 10% test
  - Old debt PV= $110,000
  - New debt PV= $5,000 + $100,000 = $105,000
  - Difference= $5,000 or 4.5%

<10%
Not substantially different

EY

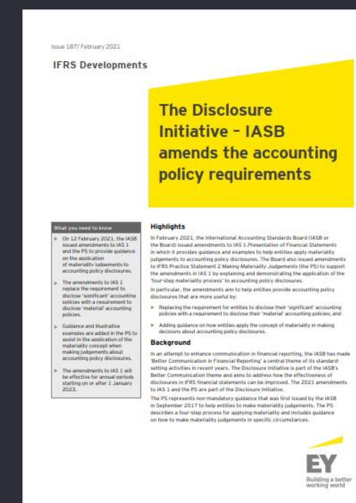
Disclosure of accounting policies

Amendments to IAS 1 and IFRS practice statement 2

Narrow scope amendments to IAS 1 issued in February 2021; changes to IFRS Taxonomy in progress:

- Amendments to IAS 1 require disclosure of **material** accounting policy information rather than a company's **significant** accounting policies
- The amendments are designed to help companies:
  - identify and disclose all accounting policies that provide material information to primary users of financial statements;
  - identify immaterial accounting policies and eliminate them from their financial statements.

- Effective for annual reporting periods beginning on or after January 1, 2023, with earlier application permitted
- Proposed amendments to IFRS Practice Statement 2 provide guidance and examples on how to apply the concept of materiality to accounting policy disclosures



Issue 187/ February 2021

IFRS Developments

The Disclosure Initiative – IASB amends the accounting policy requirements

What you need to know

- On 12 February 2021, the IASB issued amendments to IAS 1 and the PS to provide guidance on the application of materiality judgements to accounting policy disclosures.
- The amendments to IAS 1 replace the requirement to disclose 'significant' accounting policies with a requirement to disclose 'material' accounting policies.
- Guidance and illustrative examples are added in the PS to assist in the application of the materiality concept when making judgements about accounting policy disclosures.
- The amendments to IAS 1 will be effective for annual periods starting on or after 1 January 2023.

Highlights

In February 2021, the International Accounting Standards Board (IASB or the Board) issued amendments to IAS 1 *Presentation of Financial Statements* in which it provides guidance and examples to help entities apply materiality judgements to accounting policy disclosures. The Board also issued amendments to IFRS Practice Statement 2 *Making Materiality Judgements* (the PS) to support the amendments in IAS 1 by explaining and demonstrating the application of the 'four-step materiality process' to accounting policy disclosures.

In particular, the amendments aim to help entities provide accounting policy disclosures that are more useful by:

- Replacing the requirement for entities to disclose their 'significant' accounting policies with a requirement to disclose their 'material' accounting policies; and
- Adding guidance on how entities apply the concept of materiality in making decisions about accounting policy disclosures.

Background

In an attempt to enhance communication in financial reporting, the IASB has made 'Better Communication in Financial Reporting' a central theme of its standard-setting activities in recent years. The Disclosure Initiative is part of the IASB's Better Communication theme and aims to address how the effectiveness of disclosures in IFRS financial statements can be improved. The 2021 amendments to IAS 1 and the PS are part of the Disclosure Initiative.

The PS represents non-mandatory guidance that was first issued by the IASB in September 2017 to help entities to make materiality judgements. The PS describes a four-step process for applying materiality and includes guidance on how to make materiality judgements in specific circumstances.

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Definition of accounting estimates

Amendments to IAS 8

- The amendments:
  - Introduce a definition of accounting estimates;
  - Clarify the distinction between changes in accounting estimates and changes in accounting policies and the correction of errors; and
  - Explain how entities use measurement techniques and inputs to develop accounting estimates
- The amendment clarifies that a **change in measurement technique** or a **change in input** are changes in accounting estimates, if they do not result from the correction of prior period errors.
- The amendments include illustrative examples for each to help stakeholders understand how to apply the new definition of accounting estimates.
- The Board retained the notion that changes in accounting estimates resulting from new information or new developments are not corrections of errors
- Effective for annual periods beginning on or after January 1, 2023

IFRS Developments

The IASB defines accounting estimates

EY

IASB work plan: Maintenance projects

Topic	Next milestone	Expected date
Lease Liability in a Sale and Leaseback	Decide Project Direction	December 2021
Classification of Debt with Covenants as Current or Non-current (IAS 1)	Exposure Draft	November 2021
Initial Application of IFRS 17 and IFRS 9 – Comparative Information (Amendment to IFRS 17)	Final Amendments	December 2021
Lack of Exchangeability (Amendments to IAS 21)	Exposure Draft Feedback	January 2022
Supplier Finance Arrangements	Exposure Draft	November 2021
Availability of a Refund (Amendments to IFRC 14)	Decide Project Direction	TBD
Provisions – Targeted Improvements	Decide Project Direction	TBD

EY

IASB work plan: Research projects

Topic	Next milestone	Expected date
Business Combinations under Common Control	Discussion Paper Feedback	December 2021
Dynamic Risk Management	Decide Project Direction	H1 2022
Equity Method	Decide Project Direction	TBD
Extractive Activities	Decide Project Direction	H1 2022
Goodwill and Impairment	Decide Project Direction	Q1 2022
Pension Benefits that Depend on Asset Returns	Project Summary	TBD
Post-implementation Review of IFRS 10, IFRS 11 and IFRS 12	Feedback Statement	H1 2022
Post-implementation Review of IFRS 9—Classification and Measurement	Request for Information	H1 2022

EY

IASB work plan: Other projects

Agenda consultation – March 2021

- The Board undertakes a public consultation on its activities and its work plan every five years
- The objective of this agenda consultation is to gather views on:
  - The strategic direction and balance of the Board's activities;
  - The criteria for assessing the priority of financial reporting issues that could be added to the work plan; and
  - New financial reporting issues that could be given priority in the Board's work plan.
- Comments were to be provided by September 27, 2021
- Request for Information published in March 2021
- Board expects to discuss feedback in Q4 2021 and publish a feedback statement in Q2 2022

EY

IFRS Interpretations Committee

List of IFRIC Agenda Decisions

September 2020 to September 2021

Topic	Decision	Issued date
IFRS 9: Cash received via electronic transfer as settlement for a financial asset *The recognition of cash received via an electronic transfer system as settlement for a financial asset.*	Tentative	September 2021
IAS 7: Demand deposits with restrictions on use *Does an entity include a demand deposit as a component of cash and cash equivalents in its statements of cash flows and financial position when the demand deposit is subject to contractual restrictions on use agreed with a third party?*	Tentative	September 2021

EY

List of IFRIC Agenda Decisions
September 2020 to September 2021

Topic	Decision	Issued date
IAS 2: Costs necessary to sell inventories *Which costs does an entity include as part of the estimated costs necessary to make a sale when determining the net realizable value of inventories?*	Final	June 2021
IAS 10: Preparation of financial statements when a entity is no longer a going concern *What accounting is applied by an entity that is no longer a going concern?*	Final	June 2021
IFRS 9 and IAS 20: Targeted longer-term refinancing operations (TLTRO) III transactions *How an entity accounts for the third programme of the targeted longer-term refinancing operations (TLTROs) of the European Central Bank.*	Tentative	June 2021
IFRS 16: Economic Benefits from Use of a Windfarm *How an entity applies IFRS 16 where an electricity retailer has the right to obtain substantially all the economic benefits from use of a windfarm throughout the term of an agreement with a windfarm generator.*	Tentative	June 2021

EY

List of IFRIC Agenda Decisions

September 2020 to September 2021

Topic	Decision	Issued date
IFRS 9: Hedging variability in cash flow due to real interest rates *If an entity can apply IFRS 9 hedge accounting to a non-contractually specified real interest rate risk component.*	Final	May 2021
IAS 19: Attributing benefit to periods of service *Over what period of service an entity attributes benefit for a particular defined benefit plan.*	Final	May 2021
IAS 38: Configuration or customisation costs in a cloud computing arrangement *How an entity accounts for costs of configuring or customising a supplier's application software in a Software as a Service (SaaS) arrangement.*	Final	April 2021
Supply chain financing arrangements – Reverse factoring *How an entity presents liabilities to which reverse factoring arrangements relate and what information an entity is required to disclose in its financial statements.*	Final	December 2020

EY

List of IFRIC Agenda Decisions

September 2020 to September 2021

Topic	Decision	Issued date
IFRS 16: Non-refundable Value Added Tax on Lease Payments *How a lessee accounts for any non-refundable value added tax (VAT) charged on lease payments.*	Tentative	March 2021
IAS 32: Accounting for Warrants that are Classified as Financial Liabilities on Initial Recognition *How an entity applies IAS 32 to the reclassification of warrants when the exercise price will be fixed at a future date.*	Tentative	March 2021
IAS 1: Classification of Debt with Covenants as Current or Non-current *How an entity applies the amendments to IAS 1 in determining how to classify debt and other financial liabilities as current or non-current.*	Tentative	December 2020
IFRS 10 and IFRS 16: Sale and Leaseback of an Asset in a Single-Asset Entity *If an entity applies IFRS 16 to a transaction in which it sells its equity interest in a subsidiary that holds one asset and leases that asset back.*	Tentative	September 2020

EY

Accounting for cloud computing costs

Overview

- There is no explicit guidance in IFRS on customer accounting for cloud arrangements or related implementation costs; therefore, an entity will need to apply judgment
- The following diagram summarizes the accounting considerations:

Does the arrangement contain a lease in the scope of IFRS 16?
- Yes → Does the entity elect to separate lease and non-lease components?
  - Yes → Apply IFRS 16 to the lease component and further evaluate the non-lease components
  - No → Apply IFRS 16 to the entire arrangement
- No → Does the arrangement provide a resource to the customer that it can control (i.e., an intangible asset)?
  - Yes → Apply IAS 38 to determine which fees and implementation costs can be capitalized
  - No → Account for the cloud computing arrangement as a service contract and determine whether implementation costs can be capitalized under other IFRS standards

EY

Accounting for cloud computing costs

Implementation costs

- A customer may incur implementation and other up-front costs to get the cloud computing arrangement ready for use
- Accounting for those costs will depend on whether the arrangement includes an intangible asset or is a service contract, and on the type of cost

Accounting for implementation costs in a cloud arrangement		
Types of costs	**Includes an intangible**	**Service contract**
Research	Expense as incurred	Expense as incurred
Hardware costs	Capitalize – IAS 16	Capitalize – IAS 16
Costs to configure or customize underlying software	Generally capitalize – IAS 38	Supplier – determine if services are distinct 3rd party – expense as incurred
Changes to other entity systems	It depends	It depends
Training costs	Expense as incurred	Expense as incurred
Data conversion	Expense as incurred	Expense as incurred
Testing	Accounting linked to what is being tested	

EY

Accounting for cloud computing costs

Costs to configure or customize underlying software

- In its March 2021 meeting, the IFRIC finalized an agenda decision related to treatment of costs to configure or customize a cloud computing solution that is a service contract, which proposed a two-step framework to consider.

Key considerations

- Who provides the configuration or customization services?
  - Cloud arrangement service provider (or subcontractor):
    - If the configuration or customization services are ***distinct*** from the cloud arrangement, expense when the supplier configures or customizes the application software
    - If the configuration or customization services are ***not distinct*** from the cloud arrangement, expense as the supplier provides access to the application software over the contract term
  - Third-party supplier:
    - Expense as services when the third-party supplier configures or customizes the application software

EY

Cash received via electronic transfer as settlement for a financial asset

IFRIC tentative agenda decision (September 2021)

Fact Pattern:

- The electronic transfer system has an automated settlement process that takes 3 working days to settle a cash transfer. All cash transfers made via the system are therefore settled (deposited in the recipient's bank account) 2 working days after they are initiated by the payer.
- An entity has a trade receivable with a customer. At the entity's reporting date, the customer has initiated a cash transfer via the electronic transfer system to settle the trade receivable. The entity receives the cash in its bank account 2 days after its reporting date.

Issue: Can the entity derecognize the trade receivable and recognize cash on the date the cash transfer is initiated (its reporting date), rather than on the date the cash transfer is settled (after its reporting date)?

EY

Cash received via electronic transfer as settlement for a financial asset

IFRIC tentative agenda decision (September 2021)

Analysis and Conclusion:

Trade receivable	In accordance with paragraph 3.2.3 of IFRS 9: ▶ The entity should derecognize the trade receivable on the date on which its contractual rights to the cash flows expire ▶ This is a legal matter, dependent on facts and circumstances; however, would likely be on the transfer settlement date (when cash is received)
Cash	In accordance with paragraph 3.1.1 of IFRS 9: ▶ The entity should recognize the cash received when it becomes a party to the contractual provisions of the instrument ▶ Therefore the cash should only be recognized when deposited, which is when the entity has a right to obtain cash from the bank (same date as settlement of trade receivable)

- Paragraph 3.1.2 of IFRS 9 (regular way purchase or sales) is not applicable as not purchasing or selling a financial asset

Deadline for comment is November 25, 2021

IFRS Discussion Group

List of IDG Topics

September 2020 to September 2021

Topic	Issued date
IAS 2: Costs Necessary to Sell Inventories *Discuss the application of the IFRS Interpretations Committee's Agenda Decision on the accounting for costs necessary to sell inventories.*	September 2021
Accounting for Crypto Assets Held on Behalf of Others *Discuss the factors that should be considered in assessing whether crypto-assets held by an entity on behalf of others should be presented in the entity's statement of financial position.*	September 2021
IFRS 9: Issuer's Accounting for Green Bonds *Discuss the issuer's accounting for green or sustainability-linked bonds under IFRS 9* Financial Instruments.	September 2021
Equity Method Accounting on an Investment in Common and Preferred Shares *Discuss to which instrument the equity method applies when an investor entity holds both voting common and preferred shares in the associate.*	May 2021
Income statement presentation of COVID-19 impacts *Discuss the income statement presentation for various COVID-19 impacts.*	September 2020

EY

List of IDG Topics

September 2020 to September 2021

Topic	Issued date
IAS 38: Configuration and Customization Costs in a Cloud Computing Arrangement *Discuss the application of the IFRS Interpretations Committee's Agenda Decision on the accounting for configuration or customization costs in a cloud computing arrangement.*	May 2021
Issuer's Accounting for Subscription Receipts *Consider a scenario where an entity offers subscription receipts where it receives cash for the promise for a future delivery of common shares subject to the occurrence of certain events. Discuss the issuer's accounting for these subscription receipts.*	May 2021
Accounting for Standby Costs and Penalties Incurred under a Force Majeure Clause *Consider a scenario where a company that owns an asset under construction incurs certain standby costs and other penalties charged back to it by the builder under a force majeure clause. Discuss the company's accounting for these additional costs*	May 2021
Classification of Debt with Covenant as Current or Non-current *Continue discussions on the application of paragraph 72A of IAS 1* Presentation of Financial Statements *when assessing an entity's compliance with covenants that affect the classification of debt as current or non-current considering the December 2020 IFRIC discussion.*	December 2020

EY

List of IDG Topics

September 2020 to September 2021

Topic	Issued date
Disclosures of COVID-19 Impacts *Discuss various disclosure requirements related to COVID-19 that may impact an entity's year-end financial reporting in 2020.*	December 2020
Classification of Limited Recourse Capital Notes by the Holder *Discuss the classification of Limited Recourse Capital Notes by the holder.*	December 2020
Impairment Test on Right-of-Use Assets *Discuss impairment considerations for right-of-use assets when an entity has decided to vacate the property shortly after the decision date.*	December 2020
IAS 1: Application of paragraph 72A to classify a term loan as current or non-current *Discuss the application of the new paragraph 72A of IAS 1* Presentation of Financial Statements *to assess an entity's compliance with covenants that affect the classification of a term loan as current or non-current.*	September 2020
Change to discount rate method *Consider changes made to the discount rate method prescribed by Canadian Institute of Actuaries to calculate the defined benefit obligation in IAS 19* Employee Benefits *and discuss accounting implications for such changes.*	September 2020

EY

Impairment test for right-of-use assets

Change in the use of an ROU asset and impact of change on the CGU determination

- An entity's decision to change the use of an ROU asset (or an entity's conclusion that it has no realistic alternative but to do so) would indicate that an asset, a group of assets or cash-generating units (CGUs) may be impaired

- An impairment test is performed at the individual asset level if any of the below conditions are met. Otherwise, it is performed at the CGU level, which is the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets or groups of assets:
  a) The asset generates cash inflows that are largely independent of those generated from other assets or groups of assets in the entity;
  b) The asset's individual fair value less costs of disposal (FVLCD) exceeds its carrying amount; or
  c) The asset's value in use can be estimated to be close to its FVLCD and the FVLCD can be measured.

Impairment test for right-of-use assets

Change in the use of an ROU asset on CGU determination

- The condition in IAS 36.22(b) that value in use (VIU) can be estimated to be close to FVLCD for an ROU asset for real estate may be judged to be fulfilled where an ROU asset is to be used within its current CGU for only a short period of time before the abandonment or sublease occurs. In such circumstances, the ROU asset will have to be tested for impairment on a stand-alone basis
- When the ROU asset is to be used within the original CGU for only a short period of time before the abandonment or sublease occurs, one might, depending on facts and circumstances, also judge that the ROU asset and the CGU generate largely independent cash inflows. This would also mean that the ROU should be tested for impairment on a stand-alone basis
- The longer the time between the decision to abandon or sublease the ROU asset and the actual change in use occurring, the less likely it is that the decision will immediately impact the level at which any impairment assessment should be performed

Impairment test for right-of-use assets

Change in the use of an ROU asset on CGU determination

- Factors to consider when determining whether the ROU asset should be tested for impairment separately from a CGU include, but are not limited to whether:
  a) Plans for ceasing use of the ROU asset have been finalized and the entity is committed to vacating the property versus expecting to vacate, but not yet committed to vacate the property. When making this assessment, an entity might consider the guidance in paragraph 72 of IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* on assessing when a constructive obligation to restructure arises;
  b) The period of use by the CGU is a more extended period of use versus a relatively short period of use for the ROU asset;
  c) The ROU asset is significant to the cash inflow generation of the CGU;
  d) The ROU asset can be subleased after it is vacated and the period of sublease relative to the period of use by the entity before the property is vacated;
  e) The space is expected to be subleased, considering the level of management and board support and the likelihood of being able to sublease the space (e.g., a signed sublease versus general expectations of market interest in the property);
  f) The entity has engaged real estate brokers to market the ROU asset for sublease;
  g) The entity has communicated to the landlord its decision to cease own use and to sublease;
  h) The entity has told employees about ceasing the use of the office space.

Impairment test for right-of-use assets

Other considerations

When an entity plans to change the use of an ROU asset, what other impacts may that have?

- Reassessment of useful life and residual value
- Restrictions of the use of the ROU asset
- Lease reassessment or modification
- Timing of adjustments
- Sublease considerations

EY

Regulatory updates and perspectives from the Ontario Securities Commission
EY

OSC ONTARIO SECURITIES COMMISSION

Regulatory Update – Ontario Securities Commission

Alex Fisher
Ritika Rohailla
Office of the Chief Accountant

November 2021

Disclaimer

The views I am about to express are my own, and are not necessarily representative of the Ontario Securities Commission or its staff.

Agenda

- **COVID-19 Financial Reporting Considerations**
- **National Instrument 52-112 *Non-GAAP and Other Financial Measures***
- **Climate Related Disclosures**

COVID-19 Financial Reporting Considerations

OSC ONTARIO SECURITIES COMMISSION

CSA Staff Notice 51-362: Some Key Areas of Financial Reporting Focus

Significant judgments & measurement uncertainty

Going concern assessments

Impairment assessments of non-financial assets

Government assistance

Amendments to IFRS 16

- Include **entity-specific** disclosure for significant judgments or measurement uncertainties
- For close call disclosures, provide **mitigating actions** that impacted the determination that the issuer is a going concern
- Update **disclosures and assumptions impacted by COVID-19** (e.g., goodwill and intangible impairment tests, ECL models)
- Identify specific **reasons for impairment** of non-financial assets
- Disclose the **nature and extent of government assistance** or the accounting policy adopted
- Disclose whether the **practical expedient** was applied

CSA Staff Notice 51-362: Non-GAAP Financial Measures (NGFMs)

Observation	• Some isolated instances of potentially misleading NGFMs in relation to COVID-19. For example:
	  • adjusting for expenses attributable to COVID-19 without adjusting for government subsidies, or
	  • 'normalizing' revenue or expenses for the year-to-date period based on more positive results for one quarter

Reminders	• A loss or expense should not be described as **non-recurring, infrequent or unusual** when a similar loss or gain is reasonably likely to occur within the next two years or occurred during the prior two years. • Uncertainty in the current environment, means there may be a **limited basis** for management to conclude that a loss or expense is non-recurring, infrequent or unusual. • Misleading to describe an adjustment as COVID-19 related, if **management does not explain how the adjustment amount was specifically associated with COVID-19**.

CSA Staff Notice 51-362: MD&A Disclosure Reminders

Operations	• **Discuss issuer specific impacts** of COVID-19 on the issuer's operations, including impacts on distribution channels, supply chains and planned developments or projects • **Quantify** impact of each material factor causing variance in financial performance metrics, where possible
Liquidity & Capital Resources	• **Discuss** ability to generate sufficient amounts of cash in the short-term and long-term to maintain capacity or meet planned growth • **Discuss trends** or expected fluctuations in liquidity • **Discuss significant risk of defaults or arrears** on debt covenants or debt payments
Forward-Looking Information	• **Disclose forward-looking information** (FLI) only if the issuer has a reasonable basis for the FLI • Updates to or **notification that FLI is being withdrawn** must be included in the MD&A or in a news release.

OSC ONTARIO SECURITIES COMMISSION

National Instrument 52-112 *Non-GAAP and Other Financial Measures Disclosure*

National Instrument 52-112 Non-GAAP and Other Financial Measures Disclosure

- ***New*** securities law
  - non-GAAP
  - other financial measures
- ***Replaces*** Staff Notice 52-306 *Non-GAAP Financial Measures*
- Disclosures ***outside financial statements*** (e.g., in MD&A, press release, social media, AIF etc.)

Non-GAAP		**Other Financial**		
Non-GAAP Financial Measure	Non-GAAP Ratio	Total of Segments Measure	Capital Mgmt. Measure	Supp. Financial Measure
Example	Example	Example	Example	Example
Adjusted Net Income	Adjusted Net Income per Share	Total of Segments Adjusted EBITDA	Normalized Debt	Same-Store Sales[1]

[1] Assuming "sales" is calculated in accordance with accounting policies used to prepare the sales line item presented in the primary financial statements.

OSC ONTARIO SECURITIES COMMISSION

National Instrument 52-112: Effective Date

Year-end	Initially Applied
October 31	Annual Filings - October 31, 2021
December 31	Annual Filings - December 31, 2021
March 31	Annual Filings - March 31, 2022
August 31	Annual Filings - August 31, 2022
September 30	Annual Filings - September 30, 2022

ONTARIO SECURITIES COMMISSION

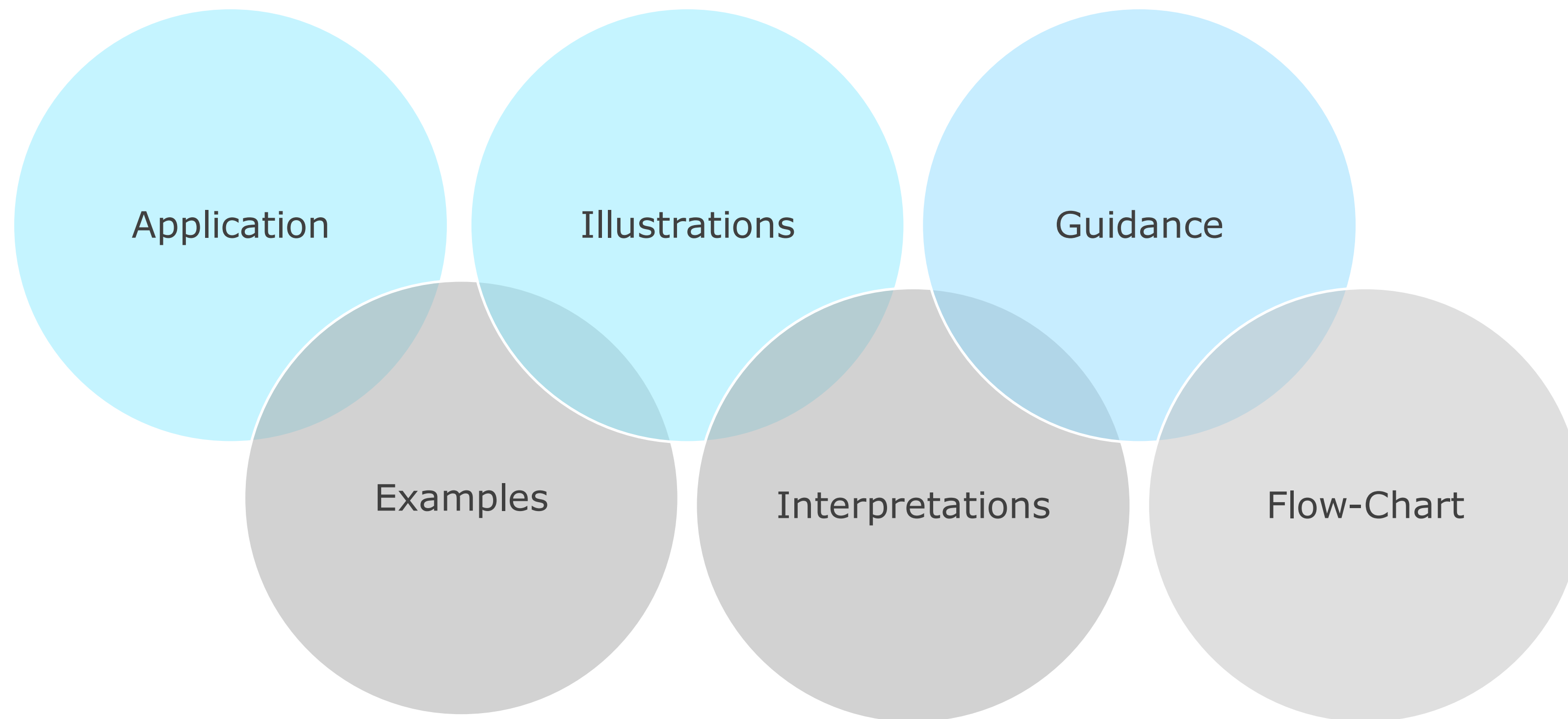
National Instrument 52-112: Disclosure Summary

	Attribute	Disclosures	Non-GAAP: Historical	Non-GAAP: Forward-looking	Non-GAAP: Ratio	Other Financial Measures: Total of Segments Measures	Other Financial Measures: Capital Management Measure	Other Financial Measures: Supp. Fin. Measure
1	**Labelling**	Label appropriately	X	X	X			X
2	**Identification**	Identify as such	X					
		Disclose non-GAAP financial measure		X D	X F		X F	
3	**Relationship**	Disclose most directly comparable primary financial statement measure	X			X		
4	**Prominence**	Present with no more prominence	X	X	X	X	X	
5	**Cautionary**	Explain does not have a standardized meaning and may not be comparable	X		X			
6	**Comparative**	Include comparative period	X C		X C	X C	X C	
7	**Composition**	Explain the composition	X A		X A		X A,G	X A
8	**Usefulness**	Explain how the measure is useful and the additional purposes, if any, for which management uses it	X A		X A		X A,G	
9	**Reconciliation**	Provide a reconciliation to the primary financial statement measure	X A,B	X A,B,E		X A,B	X A,B,G	
10	**Changes**	Explain reasons for changes	X A		X A			

Notes	
A	Ability to incorporate information by reference to the issuer's MD&A.
B	Cannot incorporate information by reference in an earnings release.
C	Comparative information required in MD&A or in an earnings release, subject to certain exceptions.
D	Disclose the equivalent historical non-GAAP financial measure and comply with disclosure requirements for historical non-GAAP financial measures (Section 6).
E	Disclose description of significant differences.
F	Disclose each non-GAAP financial measure used as a component in non-GAAP ratio or capital management measure and comply with requirements for historical non-GAAP financial measures (Section 6).
G	Disclosure not required if such disclosure already made in the notes to the financial statements of the entity to which the measure relates.

Disclaimer: The above is a very simplified summary of the disclosure requirements. To ensure compliance, reference to the specific National Instrument is required.

National Instrument 52-112: Companion Policy

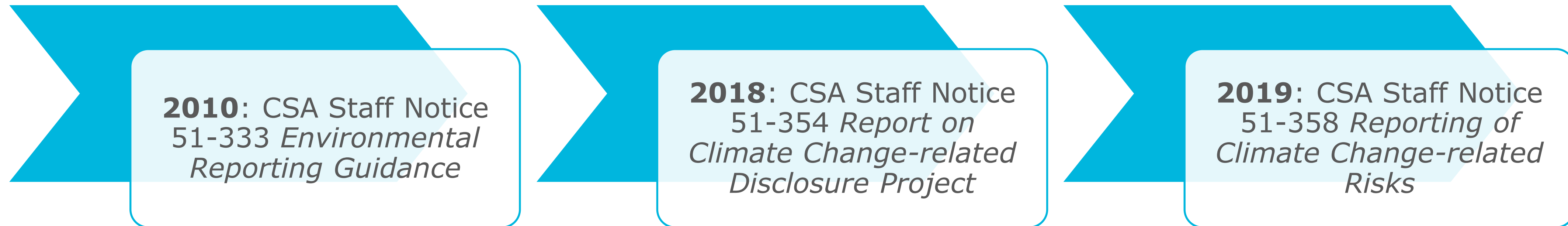


Climate Related Disclosures

OSC ONTARIO SECURITIES COMMISSION

Existing Disclosure Requirements

- Issued various Staff Notices (guidance) over the past decade



- Based on existing securities legislation – requirements (MD&A, AIF) to:
  1. Disclose **material commitments, events, risks or uncertainties** that may affect future performance
  2. Disclose all **material risk factors**
  3. If a company has implemented **environmental policies that are fundamental to operations**, a company must describe those policies and steps taken to implement

OSC ONTARIO SECURITIES COMMISSION

Background - Proposed NI 51-107 *Disclosure of Climate Related Matters*

Background

- Recommendations from the ***Capital Markets Task Force*** and ESG discussed in ***March 2021 Ontario Budget***
- ***On-going concerns*** about climate-related disclosures
  - Completeness, consistency & comparability
  - Limited quantitative information
  - 'Cherry pick' voluntary standards or frameworks
- ***Increased focus*** on climate-related issues
  - Mainstream business issue
  - Investors are seeking improved disclosure on governance processes and the material risks, opportunities and financial impacts of climate change
- ***CSA Review (2021)*** of Climate Related Disclosures
  - 48 issuers from S&P/TSX Composite index across a wide range of industries
  - Issuers are providing more climate-related information in continuous disclosure filings and voluntary reports (compared to previous review in 2017)
  - However, 41% of the disclosures were limited and lacked specificity

Proposed NI 51-107 *Disclosure of Climate Related Matters*

Key Elements

- Disclosures contemplated are **largely consistent with the Task-Force on Climate Related Financial Disclosure *(TCFD)*** recommendations:
  - ***Governance*** **-** board's oversight of and management's role in assessing and managing climate related risks and opportunities
  - ***Strategy*** **-** the short, medium, and long-term climate related risks and opportunities and the impact on business, strategy and financial planning, where such information is material
  - ***Risk Management*** – how climate related risks are identified, assessed and managed and how these processes are integrated into overall risk management
  - ***Metrics & Targets*** – the metrics and targets used to assess and manage climate related risks, opportunities, where information is material

OSC ONTARIO SECURITIES COMMISSION

Proposed NI 51-107 *Disclosure of Climate Related Matters*

Modifications

- Proposed NI 51-107 ***modifies the TCFD recommendations*** in the following ways:
  - ***Scenario analysis (strategy)***– proposals exclude the requirements to disclose 'scenario analysis', which is an issuer's description of the resilience of its strategy within different climate related scenarios, including a 2°C or lower scenario
  - ***GHG Emission Disclosure (metrics & targets)***
    - *Option 1* – Issuers would be required to disclose their Scope 1, Scope 2 and Scope 3 greenhouse gas (GHG) emissions and the related risks, or their reasons for not doing so
    - *Option 2* – Issuers would be required to disclose Scope 1 GHG emissions and would have to provide their reasons for not disclosing Scope 2 and Scope 3 GHG emissions if they choose not to disclose these emissions.

Transition

- Proposed Instrument comes into Force December 31, 2022
- ***Phased in Transition***:
  - ***Non-Venture:*** 1 year transition (disclosure included in annual filings due in 2024)
  - ***Venture:*** 3 year transition (disclosure included in annual filings due in 2026)

Overall Objectives of Proposed NI 51-107 *Disclosure of Climate Related Matters*

- Improve **access to global capital markets** by aligning Canadian disclosure standards with expectations of international investors
- Assist investors in making more **informed investment decisions**
- Facilitate an **equal playing field** for issuers through comparable and consistent disclosure
- **Remove costs** associated with **navigating and reporting based on multiple disclosure frameworks** as well as reducing market fragmentation

International Developments

International Developments	• IFRS Foundation's definitive proposal to establish the International Sustainability Standards Board (ISSB) • Montreal to host one of the central ISSB offices • International Organization of Securities Regulators (IOSCO) – *Technical Experts Group* formed to advise IFRS Foundation on prototype standards

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Update on applying IFRS 17 *Insurance Contracts*
EY

IFRS 17 *Insurance contracts* – status

2017	2018	2019	2020	2021	2022	2023	2024

Implementation period → **Reporting**

- IFRS 17 standard issued
- Publication of Exposure Draft (ED) June 26, 2019
- End of comment period September 25, 2019
- Re-deliberation December 2019-March 2020
- Finalization of amendments to IFRS 17
- Start of IFRS 17 comparative period
- IFRS 17 is effective (January 1, 2023) Early application permitted
- First IFRS 17-compliant annual reports published

EY

How will an insurer's balance sheet change?

IFRS 4	IFRS 17
Assets	**Assets**
Reinsurance contract assets	Reinsurance contract assets
Deferred acquisition costs	Insurance contract assets
Value of business acquired	
Premiums receivable	
Policy loans	
Liabilities	**Liabilities**
Insurance contracts liabilities	Insurance contracts liabilities
Undistributed surplus	Reinsurance contracts liabilities
Unearned premiums	
Claims payable	

Key Changes for IFRS 17 liabilities

- Portfolios of insurance (or reinsurance) contracts that are in an asset position presented separately from groups of insurance (or reinsurance) contracts that are in a liability position
- Acquisition cash flows, premiums receivable and unearned premiums are included in the measurement of insurance liabilities

EY

The statement of comprehensive income – a huge change compared to today

IFRS 4
Net earned premiums
Interest, dividend and other investment income
Incurred claims and benefits
Change in provisions
Profit or loss

IFRS 17
Insurance revenue
Insurance services expense
Incurred claims and expense
Acquisition costs
Gain/loss from reinsurance
Insurance service result
Investment income
Insurance finance expense
Net financial result
Profit or loss
Discount rate changes on insurance liability (optional)
Total comprehensive income

Key Changes

- Insurance contract revenue excludes investment components
- Revenue and expense are recognized as earned or incurred
- Insurance finance expense is excluded from insurance service result and is presented (i) fully in P/L or (ii) in P/L and OCI, depending on accounting policy
- "Written premiums" disclosed in the notes

EY

The statement of comprehensive income – what does it look like?

Statement of comprehensive income	
Insurance revenue	X
Insurance service expenses	(X)
Insurance service result	**X**
Investment income	X
Insurance finance expenses	(X)
Finance result	**X**
Other profit and loss items	**X**
Corporate tax	(X)
Profit after tax	**X**
Other comprehensive income	(X)
Total comprehensive income	**X**

Insurance revenue:

- Release in contractual service margin
- Change in risk adjustment
- Expected claims (in fulfilment cash flows)
- Expected expenses (in fulfilment cash flows)
- Allocating premium relating to the recovery of directly attributable acquisition costs
- Excluding non-distinct investment components

(Expected)

Insurance service expenses:

- Actual claims incurred
- Actual expenses incurred
- Allocating premium relating to the recovery of directly attributable acquisition costs
- Onerous contracts
- Excluding non-distinct investment components

(Actual)

Insurance finance expenses: Calculated using locked-in rates (if the OCI option is selected)

Other comprehensive income: Effect of discount rate changes on BEL (if the OCI option is selected)

EY

Brief refresher – measurement models

The three measurement models

The General Model

- Also known as the General Measurement Model (GMM)
- Default valuation approach
- Insurance contract valued using fulfilment cash flows – the present expected future cash flows, plus a risk adjustment
- Offset by the contractual service margin, which represents unearned profit the insurer recognizes as it provides services under the contract

- Annuities (Non-participating)
- Protection (Non-participating)
- Long duration non-life business

Premium Allocation Approach (PAA)

- Optional simplified approach for contracts with a duration of one year or less, or where it is a reasonable approximation to the General Model
- Many non-life, and some life insurance contracts are expected to meet these criteria
- Insurance contract valued as a pre-claims coverage liability and an incurred claims liability
- Similar approach to existing non-life insurance contract measurement

- Short-duration contract
- Mostly non-life insurance

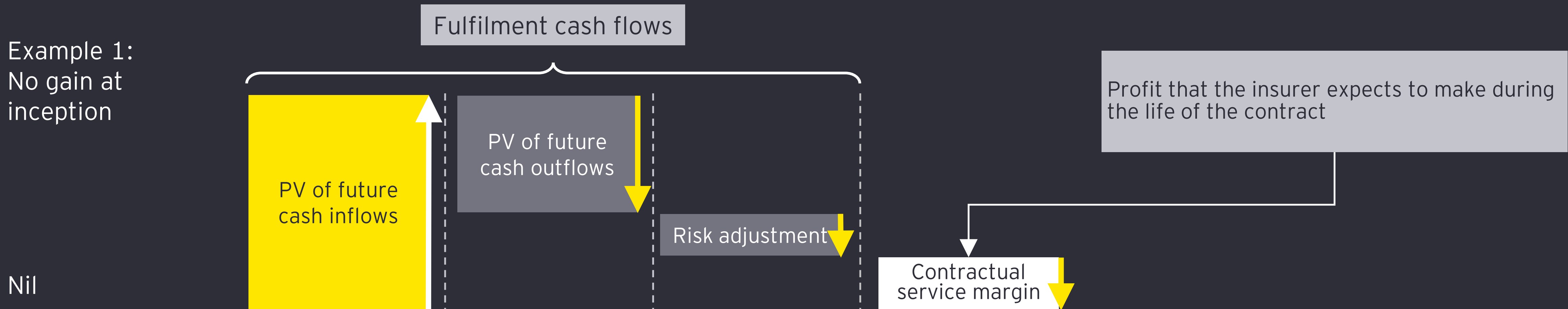
Variable Fee Approach (VFA)

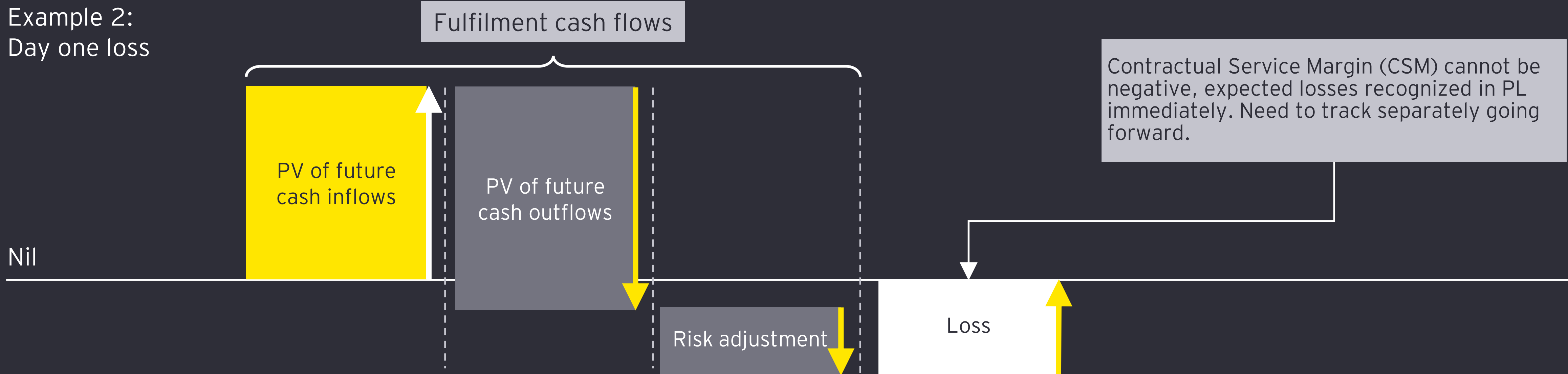
- Applies to participating contracts, as defined by three criteria, based on policyholders having a significant share in the profit from a clearly identified pool of underlying items
- Insurance contract liability based on the obligation for the entity to pay the policyholder an amount equal to the value of the underlying items, net of a consideration charged for the contract – a 'variable fee'

- Investment-linked products
- Participating contracts (with fund segregation)

EY

Brief refresher – general model measurement on initial recognition





EY

Brief refresher – comparison of transition methods

	Full Retrospective Approach (FRA)	Modified Retrospective Approach (MRA)	Fair Value Approach (FVA)
Description	▶ **Default approach** must be adopted if practicable, e.g., identify, recognize and measure each group of insurance contracts **as if IFRS 17 had always applied.**	▶ To **achieve the closest outcome to the retrospective application**, possible to use reasonable and supportable information available without **undue cost or effort.**	▶ The **CSM** is estimated as: ▶ The **fair value** of the group of insurance contracts, less ▶ The **fulfilment cash flows** of the group of insurance contracts
Pros	▶ For non-onerous portfolios, a CSM will be recognized.	▶ Simpler than the FRA to compute. ▶ CSM will also be recognized for non-onerous portfolios.	▶ Mechanically the **simplest to compute** and **fewer data requirements.**
Cons	▶ Very **heavy historical data and calculations requirements** including assumptions and changes at, and since, the time of policy issue such as: ▶ Calculate and track annual changes in CSM and Risk Adjustment (RA) since inception ▶ Changes in assumption recorded against the CSM and amortization of CSM	▶ Although simpler than the FRA, there will still be **issues with transaction data availability and its granularity**, especially the further back contracts incepted. ▶ **Overhead expenses are not currently available** at the "attributable to portfolio" level and require additional allocation analysis. ▶ Varying **premiums and other alterations** would make it difficult to apply.	▶ **Potentially the lowest CSM** (depending on the methodology, e.g., cost of capital), with a **buyer unlikely to take on business on onerous terms and a seller is unlikely to sell the business on too attractive terms to a buyer**. ▶ The main **challenge is to define the assumptions and methodology of "fair value"** consistent with IFRS 13. ▶ Lack of "market data", e.g., sales of portfolios infrequent and transactions may include other elements such as future business. ▶ Methods based on embedded value, etc., may not be "fair value" and may need to be adjusted, particularly for "cost of capital".

MRA or FVA only applicable FRA is impracticable

EY

KPIs – guiding principles for the investor story

Clarity

- Clarity on IFRS and non-GAAP measures
- Understandable to generalist investors/analyzt
- Consistent application
- Reconciliation of non-GAAP measures to IFRS numbers

Market comparability

- In line with market practice but not constrained by it
- Consistent, group-wide approach recognizing business unit specifics
- Flexibility to respond to market and business developments

Volatility

- Level of earnings volatility
- "Accounting" Asset Liability Management (ALM) to manage earnings mismatches
- Link between the business and the earnings story
- Size of CSM vs. shareholder's equity at transition
- Maintain dividend capacity
- Communicable RoE story to the market

Business steering

- Reconciliation between IFRS and internal management reporting
- Seek alignment between IFRS and internal management reporting where appropriate

Operational efficiency

- Ensure efficient reporting streams
- Leverage data, existing processes and methods
- Align steering and reporting frameworks

IFRS 17 changes the language of insurance finance

EY

Impact of IFRS 17 on selected financial KPIs

KPI	Degree of IFRS 17 impact	Future IFRS state of equation	Ability to influence via accounting policy formulation
Net income attributable to common shareholders	High	Continues as defined	Medium
Gross premiums written	Full	Does not exist (alternative required)	None
Premiums earned and fee income	Full	Does not exist (alternative required)	None
Earnings per share	Medium	Continues as defined	Low
Shareholders' equity	Medium	Continues as defined	High
Return on equity in %	Medium	Continues as defined	High
Return on investments in %	Medium	Continues as defined	Medium
Net operating margin in %	Medium	Need to re-define	Low
Combined ratio in %	Medium	Need to re-define	High
Gross cash generation	Low	Continues as defined	Low
Value of new business	Full	New but definitions may diverge more than the past	Medium
Insurance service result	Full	New	Medium
Renewals	High	Need to re-define	High

EY

KPIs – Sources of IFRS 17 earnings

Reinsurance result

(Net) fee income[1]

VFA model – nil (through CSM)

Investment return:
Yield less discount unwind
Plus, return on net assets

Central expenses and finance costs

Tax

Experience variance and assumption changes[2]

Operating profit

VFA model – hedge ineffectiveness

Economic variances

Net income

CSM and Risk Adjustment release

CSM released in the year

Risk adjustment released

Note: assumption changes that relate to FUTURE services flow through CSM balance and not through income

[1] Fee income arising from non-insurance business, such as annual management charge in asset management services, for example.
[2] Includes experience on past and present services and impact on CSM release for changes in assumptions related to future services.

EY

KPIs – CSM acts a store of value, and will make growth profiles more evident

Classification of insurance/non insurance business is accounting driven, not business driven

Main drivers of CSM are:

- New business value (in)
- Variances to stock of CSM (up or down)
- CSM amortization (out)

CSM will be disclosed segmentally, and show business profile's:

- Growth, value or run-off
- Vector of change (flow/stock)
- Duration of in-force
- Accuracy of business management (size and nature of variances)

In-force insurance business

New insurance business

Non-insurance business

Investments[1]

Fee income

Shareholder return

NPV future profits

CSM

CSM earned in year

Earnings

Dividends

Income statement

[1] Excluding underlying items from direct participating contracts.

EY

KPIs – Impact on combined ratio

Insurers/Industry discussing which items are included in claims figures used for ratio: IFRS 17 P&L includes risk adjustment, discounting and loss component. Which elements should be included?

Reserve release/deterioration figures should be able to be derived from notes. IFRS 17 is best estimate reserving.

Expense figures may not appear on income statement but may be available within notes. Which, if any, non-qualifying expenses to include?

Current Year Net Incurred Claims + **Reserve Release/ (Deterioration)** + **Acquisition Costs** + **Other Expenses**

Net Earned Premium (NEP)

Treatment of different kinds of commissions and reinstatement premiums may change – meaning, some removed entirely and others treated differently (claims vs. premium).

Significant transaction/acquisition activity could skew revenue figures with incurred claims run-off now flowing through as revenue.

NEP no longer shown in financial statements but can be estimated. Insurers/Industry discussing gross or net.

Treatment of policy fees varies across markets – exclude from insurance revenue?

IFRS 9 comparative restatement

IAS 39 classification	IFRS 9 classification	Does the change in classification result in changes in: A. Measurement of the financial asset	B. P&L	C. OCI	Change addressed by classification overlay approach?
Amortised cost (Held-to-maturity, and loans and receivables)	Amortised cost	No	Yes (ECL)	No	No
	Fair value through OCI (FVOCI)	Yes	Yes (ECL)	Yes	Yes (A and C only)
	Fair value through profit or loss (FVPL)	Yes	Yes	No	Yes
Available-for-sale debt	Amortised cost	Yes	Yes (ECL)	Yes	Yes (A and C only)
	FVOCI	No	Yes (ECL)	Yes (ECL)	No
	FVPL	No	Yes	Yes	Yes
Available-for-sale equity	FVPL	No	Yes	Yes	Yes
	FVOCI presentation	No	Yes (on disposal)	Yes (on disposal)	Yes
FVPL debt	Amortised cost	Yes	Yes	No	Yes
	FVOCI	No	Yes	Yes	Yes
	FVPL	No	No	No	Not applicable
FVPL equity	FVPL	No	No	No	Not applicable
	FVOCI presentation	No	Yes	Yes	Yes

Update up to October 2021 IASB Board Meeting

Current standard:

- Restating comparatives under IFRS 9 is optional
- If an entity does restate IFRS 9 comparative information, it is prohibited from applying IFRS 9 to any assets that have been derecognized before the initial application date
- This could create mismatches with the accounting treatment applied to insurance contract liabilities restated under IFRS 17. Similar mismatches could arise for insurers who choose not to restate comparatives and instead apply IAS 39 in the comparative period
- Operational challenges could arise from these requirements given the population of derecognized assets would only be known at the end of the comparative period (December 31, 2022)

Amendment:

- Impact would permit an optional classification overlay for financial assets, that an entity can select on an instrument-by-instrument basis in the comparative period
- Can be applied if IFRS 9 has already been adopted or using IAS 39
- The classification overlay approach allows classification of such assets in the comparative period in a way that aligns with how an entity would expect to classify them on initial application of IFRS 9
- No ECL is required on assets where overlay results in amortized cost of FVOCI treatment. Incurred losses recorded in 2021 or prior not impacted
- Can be applied to all assets, not just those backing insurance liabilities as initially drafted

Emerging topics:

- If classification overlay in 2022 from FVPL to FVOCI or Amortized cost, how would incurred losses arising in 2022 be treated?

EY

Questions?

Thank you!

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EY

Appendices

Appendix A: Recent IFRS financial reporting developments
EY

IASB developments

Deferred tax related to assets and liabilities arising from a single transaction

Amendments to IAS 12

- IASB issued amendments to IAS 12 *Income Taxes* to clarify the accounting for assets and liabilities arising from a single transaction, such as leases and decommissioning obligations

The amendments **narrow** the scope of the **initial recognition exception (IRE)** so that it no longer applies to transactions that give rise to equal taxable and deductible temporary differences

- The amendments apply to annual reporting periods beginning on or after January 1, 2023 (earlier adoption permitted)
  - Transition guidance also requires the recording of DTA/DTLs for all temporary differences associated with leases and decommissioning obligations as of the earliest comparative period presented

EY

Deferred tax related to assets and liabilities arising from a single transaction

Amendments to IAS 12

Example scenario:

- Five-year lease of a building with annual payments of \$100; lessee makes an advance lease payment of \$15 and pays initial direct costs of \$5
- Assume 5% discount rate
- Assume tax rate of 20%, tax deductions allowed for lease payments (including advance payments) and initial direct costs, when paid

Lease liability

\$435 = PV(\$100, 5 years, 5% interest)

ROU asset

\$455 = (lease liability + advance payment + direct costs)

Judgment is required

On initial recognition, the lessee entity must determine the tax base of the lease asset and lease liability by determining whether tax deductions are attributable to the **right-of-use asset** or the **lease liability**

Tax deductions attributable to:	ROU asset (excluding advance payment + direct costs)	Lease liability
Asset	tax base = carrying value	tax base = carrying value
Liability	tax base = \$0	tax base = \$0

EY

Deferred tax related to assets and liabilities arising from a single transaction

Amendments to IAS 12

Example, continued:

- The entity concludes tax deductions relate to the lease liability

	Tax base	Carrying value	Temporary difference and deferred taxes @ 20%
Lease liability	$0	$435	Deductible TD = $435 DTA = $87
	Tax base = CV of $435 – tax deductions of $435 (PV lease payments)		
ROU asset – lease liability component	$0	$435	Taxable TD = $435 DTL = $87
	Tax base = $nil tax deductions as lease payments associated to liability		
ROU asset – advance lease payment and initial direct costs	$0	$20	Taxable TD = $20 DTL = $4
	Tax base = $nil tax deductions, as deduction benefit already received upon payment		

- For the advance payment and initial direct costs, the IRE does not apply because the initial transaction (upfront payment) resulted in a tax deduction – a temporary difference is calculated following IAS 12 requirements
- For the lease liability and associated component of the ROU asset, the IRE does **not** apply, because this transaction gives rise to **equal** taxable and deductible **temporary differences**

EY

Deferred tax related to assets and liabilities arising from a single transaction

Amendments to IAS 12

Illustration of annual impact on effective tax rate, post-amendment:

	Y1	Y2	Y3	Y4	Y5
Depreciation [1]	87	87	87	87	87
Interest expense [2]	22	18	14	9	5
Costs before tax	109	105	101	96	92
Current tax expense (benefit) [3]	(20)	(20)	(20)	(20)	(20)
Deferred tax expense (benefit) [4]					
Unwinding of DTA	15	16	17	18	19
Unwinding of DTL	(17)	(17)	(17)	(17)	(17)
Costs after tax	87	84	81	77	74
Effective tax rate	20%	20%	20%	20%	20%

1. Illustration ignores advance lease payment and initial direct cost components of the ROU asset. Depreciation based only on the component of the ROU asset related to the lease liability, assuming no residual value ($435/5 years).
2. Interest expense is based on accretion of lease liability at 5%.
3. Current tax benefit reflects the tax deduction available from the annual $100 lease payment at 20% tax rate.
4. The deferred tax expense (benefit) is calculated based on the uneven unwinding of the DTA and DTL. The top row represents the unwinding of the DTA, the bottom row represents the unwinding of the DTL.

EY

Deferred tax related to assets and liabilities arising from a single transaction

Amendments to IAS 12

Illustration of annual impact on effective tax rate, with IRE applied:

	Y1	Y2	Y3	Y4	Y5
Depreciation [1]	87	87	87	87	87
Interest expense [2]	22	18	14	9	5
Costs before tax	109	105	101	96	92
Current tax expense (benefit) [3]	(20)	(20)	(20)	(20)	(20)
Deferred tax expense (benefit) [4]	(4)	(4)	(3)	(2)	12
Costs after tax	85	81	77	74	84
Effective tax rate	22%	23%	23%	23%	8%

1. Illustration ignores advance lease payment and initial direct cost components of the ROU asset. Depreciation based only on the component of the ROU asset related to the lease liability, assuming no residual value ($435/5 years).
2. Interest expense is based on accretion of lease liability at 5%.
3. Current tax benefit reflects the tax deduction available from the annual $100 lease payment at 20% tax rate.
4. With no initial DTA or DTL on the lease liability or lease ROU, deferred tax arises only from the accretion of the lease liability due to interest expense.

EY

Deferred tax related to assets and liabilities arising from a single transaction

Amendments to IAS 12

Illustration of annual impact on effective tax rate, post-amendment, if lease payments allocated to **ROU asset:**

	Y1	Y2	Y3	Y4	Y5
Depreciation [1]	87	87	87	87	87
Interest expense [2]	22	18	14	9	5
Costs before tax	109	105	101	96	92
Current tax expense (benefit) [3]	(20)	(20)	(20)	(20)	(20)
Deferred tax expense (benefit) [4]	(2)	(1)	0	1	2
Costs after tax	87	84	81	77	74
Effective tax rate	20%	20%	20%	20%	20%

1. Illustration ignores advance lease payment and initial direct cost components of the ROU asset. Depreciation based only on the component of the ROU asset related to the lease liability, assuming no residual value ($435/5 years).
2. Interest expense is based on accretion of lease liability at 5%.
3. Current tax benefit reflects the tax deduction available from the annual $100 lease payment at 20% tax rate.
4. The deferred tax expense (benefit) is calculated based on the movement of the DTA related to the ROU asset. With the lease payments allocated to the ROU asset, there is no initial temporary difference; however, as the carrying value of the ROU asset depreciates on a straight line basis while the tax basis unwinds following an effective interest rate method, new temporary differences are created. No temporary differences arise on initial recognition or subsequently, related to the lease liability.

EY

Onerous contracts – costs of fulfilling a contract

Amendments to IAS 37

In May 2020, the IASB issued amendments to IAS 37 to provide clarity and specify which costs an entity needs to include in assessing whether a contract is onerous.

Key requirements:

- Amendments apply a "directly related cost approach". This includes both:
  - Incremental costs (e.g., costs of direct labour and materials); and
  - Allocation of costs directly related to contract activities (e.g., directly related depreciation, contract management and supervision costs)
- G&A costs ***do not*** relate directly to a contract and are excluded unless specifically chargeable to the counter-party to the contract

Transition:

- Effective for annual periods beginning on or after January 1, 2022
- Earlier application is permitted and must be disclosed
- Amendments must be applied prospectively to all contracts for which an entity has not yet fulfilled all of its obligations at the beginning of the annual period in which it first applies the amendments

EY

Onerous contracts - costs of fulfilling a contract

Amendments to IAS 37

Impact:

- Entities that previously applied the incremental cost approach (e.g., costs of direct labour and materials) will see provisions increase to reflect the inclusion of costs directly related to contract activities
- Entities that previously recognized contract loss provisions using the guidance under the former standard IAS 11 *Construction Contracts* will be required to exclude the allocation of indirect overhead from their provisions
- Judgment will be required to determine which costs are directly related to contract activities, but we believe guidance in other standards such as IAS 2 *Inventories*, IAS 16 *Property, Plant and Equipment*, IAS 38 *Intangible Assets* and IFRS 15 *Revenue from Contracts with Customers* will be relevant

EY

Onerous contracts - costs of fulfilling a contract

Amendments to IAS 37

Fact pattern:

- The economic benefits of the contract: **$110,000** (e.g., transaction price remaining to be recognized under the contract). Revenue on the contract is recognized over time
- Direct labour costs to fulfil the contract: $60,000 (e.g., salaries and wages of employees directly involved with fulfilling the contract)
- Direct materials costs to fulfil the contract: $45,000
- Allocations of costs that relate directly to contract activities to fulfil this contract: $10,000 (e.g., costs of contract management and depreciation of tools, equipment and right-of-use assets)
- The cost of terminating the contract (contractual termination penalty): $120,000

	Incremental cost approach	Direct cost approach *(as per the amendments to IAS 37)*
Costs to terminate	$120,000	$120,000
Costs to fulfil	$105,000 ($60,000 + $45,000)	$115,000 ($60,000 + 45,000 + $10,000)
Onerous contract?	No	Yes

EY

Property, plant and equipment (PP&E): proceeds before intended use

Amendments to IAS 16

Key requirements:

- Amends the standard to prohibit deducting from the cost of PP&E any proceeds from selling items produced while bringing that asset to the location and condition necessary for it to be capable of operating in the manner intended by management.
- Proceeds from selling such items, and the cost of producing those items, are to be recognized in profit or loss. An entity will be required to identify and measure production costs associated with selling volumes before an asset is ready for its intended use in accordance with IAS 2.
- If the sale of such items are not in the ordinary course of business, an entity must separately disclose the sales proceeds and cost of producing those items, and specify the line item within profit or loss where these have been recognized (IAS 16.74A).
- Clarifies the meaning of 'testing' in par. 17(e)—i.e., when testing whether an item of PP&E is functioning properly, an entity assesses the technical and physical performance of the asset, and not its financial performance.

Transition:

- Effective for annual periods beginning on or after January 1, 2022. The amendments will be applied retrospectively only to items of PP&E that are brought to the location and condition necessary for them to be capable of operating in the manner intended by management on or after the beginning of the period the amendments are first applied.
- Earlier application is permitted and must be disclosed.

Rate-regulated activities
Standard-setting project

A regulatory agreement is a set of enforceable rights and obligations that determine a regulated rate to be applied in contracts with customers.

- Not all regulatory agreements are capable of creating regulatory assets or regulatory liabilities

Not all regulatory agreements are in scope of the Exposure Draft

- To be in scope, a regulatory agreement must give rise to:
  - Rights to increase future rates because of goods or services already supplied; or
  - Obligations to decrease future rates because of amounts already charged to customers.

EY

Rate-regulated activities

Standard-setting project

An enforceable present right, created by a regulatory agreement, to add an amount in determining a regulated rate to be charged to customers in future periods because part of the total allowed compensation for goods or services already supplied will be included in revenue in the future.

An enforceable present obligation, created by a regulatory agreement, to deduct an amount in determining a regulated rate to be charged to customers in future periods because the revenue already recognized includes an amount that will provide part of the total allowed compensation for goods or services to be supplied in the future.

Rate-regulated activities

Standard-setting project

Regulatory assets and regulatory liabilities can only exist if:

- An entity is party to a regulatory agreement;
- The regulatory agreement determines the regulated rate the entity charges for the goods or services it supplies to customers; and
- Part of the total allowed compensation for goods or services supplied in one period is charged to customers through the regulated rates for goods or services supplied in a different period (past or future).

EY

Rate-regulated activities
Standard-setting project

Recognition and Measurement

An entity must recognize:

- All regulatory assets and all regulatory liabilities existing at the end of the period; and
- All regulatory income and all regulatory expense arising during the period.

Cash-flow based measurement technique:

- Estimating future cash flows– including future cash flows arising from regulatory interest – and updating those estimates at the end of each reporting period to reflect conditions existing at that date
- Future cash flows are estimated using a 'most likely amount' or 'expected value' approach
- Cash flow estimates would be updated if changes occur
- Estimated cash flows would be discounted using the **regulatory interest rate** unless this rate is not adequate (for regulatory assets)
- Exception for items affecting regulated rates only when related cash is paid or received
- If an estimate is adjusted due to changes that have occurred, the cash flows would be discounted at the rate established at initial recognition, unless the regulatory agreement changes the interest or return rate

EY

Rate-regulated activities

Standard-setting project

Presentation and disclosure

Statement of financial performance

- Regulatory income minus regulatory expense should be presented as a separate line item immediately below revenue
  - Includes regulatory interest income and regulatory interest expense
- Regulatory income or expense will be recognized in Other Comprehensive Income in certain cases

Statement of financial position

- Separate line items for regulatory assets and regulatory liabilities should be presented
  - Classification as current or non-current as appropriate is required
- Offsetting is permitted only if:
  - A legally enforceable right to offset those regulatory assets and regulatory liabilities by including them in the same regulated rate exists; and
  - There is an expectation to include the amounts in the same future period.

EY

Lease liability in a sale and leaseback

Maintenance project

Key requirements

- The IASB intends to amend IFRS 16 to specify the method a seller-lessee uses in initially measuring the right-of-use asset and liability arising in a sale and leaseback transaction and how the seller-lessee subsequently measures that liability
- Such a lease liability includes the present value of variable lease payments regardless of whether they depend on an index or rate

This represents a departure from the general leases model, which requires variable lease payments that do not depend on an index or rate to be recognized in profit or loss in the period in which the event or condition that triggers those payments occurs.

- The proposed amendment would apply to sale and leaseback transactions, in which applying paragraph 99 of IFRS 16, the transfer of the asset satisfies the requirements to be accounted for as a sale of the asset

EY

Lease liability in a sale and leaseback

Maintenance project

Status

- The Board issued an exposure draft of the proposed amendment in November 2020, which was open for comment until March 2021.
- In May 2021, the Board considered the feedback received on the exposure draft.
- Only a minority of respondents agreed with the proposed amendments; a large majority disagreed with, or expressed concerns about, aspects of the proposals.
- The Board is considering the project's direction and has asked the IFRIC to provide their input and views on possible ways forward.
  - The possible project direction was discussed at the September 2021 IFRIC meeting where two approaches were proposed.

EY

Going concern disclosure reminders

Other project

- In September 2020, the IAASB published a Discussion Paper (DP), *Fraud and Going Concern in an Audit of Financial Statements*.
- In January 2021, the IFRS Foundation (IASB) released an educational document with disclosure reminders related to going concern.
- No changes in IFRS requirements – the intention is a **reminder** of the IFRS requirements for going concern assessments and the related disclosures.
- IAS 10 *Events after the Reporting Period* specifically requires management to reflect on the effect of events occurring after the end of the reporting period up to the date that the financial statements are authorized for issue.

Going concern disclosure reminders

Other project

... entity situation deteriorating ...

Scenario	1 No significant doubts about going concern	2 Significant doubts about going concern but mitigating actions judged sufficient to make going concern appropriate Entity determines no material uncertainties	3 Significant doubts about going concern but mitigating actions judged sufficient to make going concern appropriate Material uncertainties about going concern remain after considering mitigating actions	4 Intends to liquidate or to cease trading, or no realistic alternative but to do so
Basis of preparation	Going concern			Alternate basis (not going concern)
Disclosure	Basis of preparation No specific disclosures	Basis of preparation Significant judgements?	Basis of preparation Material uncertainties Significant judgements?	Limited specific requirements

Disclose the alternative basis and reasons why

Consideration of disclosure of significant judgments

Disclose material uncertainties **and** significant judgments

EY

Business combinations under common control

Research project

Summary of preliminary views:

a) The project's objective, scope and focus

- Apply to all transactions under common control.
- No differentiation on the basis of economic substance
- Affect receiving companies (acquirer) not transferring company or the transferred company (acquiree).

b) Selection of the accounting method:

- Does the transaction affect non-controlling shareholders of the receiving company?
  - No → Book-value method
  - Yes → Are the receiving company's shares traded in a public market?
    - Yes → Acquisition method
    - No → Are all non-controlling shareholders related parties of the receiving company?
      - Yes → Book-value method
      - No → Has the receiving company chosen to use a book-value method, and have its non-controlling shareholders not objected?
        - Yes → Book-value method
        - No → Acquisition method

EY

Goodwill and impairment

Research project

- The IASB started a research project to explore possible improvements to IFRS 3 and IAS 36
- Discussion paper was issued in March 2020 and Feedback deadline was in May 2021
- The Board researched whether:
  - Companies can provide better information on acquisitions (Disclosures)
  - It could make the impairment test more effective
  - It should reintroduce amortization of goodwill
  - It should amend the impairment test to reduce its cost and complexity
  - It should include some intangible assets within goodwill

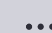
EY

Goodwill and impairment

Research project

The Board's preliminary view:

Possible changes the Board considered	Objectives		Board's preliminary view
	More useful information	Reduce cost	
Improve disclosures about acquisitions	✓	✗	Yes, change
Amortize goodwill	✗	✓	No, do not change
Provide relieve from mandatory annual impairment test	…	✓	Yes, change
Amend how value in use is estimated	✓	✓	Yes, change
Present total equity excluding goodwill	✓	…	Yes, change
Include some intangible assets in goodwill	✗	✓	No, do not change

In line with objective In conflict with objective  No significant impact

EY

IFRS Interpretations Committee

Amendments to IAS 1: *Classification of Liabilities as Current or Non-current*

Overview

Background:

- In January 2020, IASB issued amendments to IAS 1 *Presentation of Financial Statements*, to specify the requirements for classifying liabilities as current or non-current, clarifying:
  - What is meant by a **right to defer** settlement
  - That a right to defer must exist **at the end of the reporting period**
  - That classification is **unaffected by the likelihood** that an entity will exercise its deferral right
  - That only if an embedded derivative in a convertible liability is itself an equity instrument, would the terms of a liability not impact its classification

- The amendments were initially made effective from annual reporting periods beginning on or after January 1, 2022, but have subsequently been deferred

Amendments to IAS 1: *Classification of Liabilities as Current or Non-current*

IFRIC Tentative Agenda Decision (December 2020)

December 2020 update:

- Subsequent to the issuance of the amendments, the IFRS Interpretations Committee discussed how an entity would apply the amended guidance in IAS 1 for a series of fact patterns, summarized in a Tentative Agenda Decision (TAD)
- Comment letter responses raised concerns that the conclusions from the TAD produced outcomes that were not useful to financial statement users

	Case 1	Case 2	Case 3	
Required working capital ratio	Above 1.0	Above 1.0	Above 1.0	Above 1.1
Testing date	December 31, March 31, June 30, September 30	March 31	December 31, 20X1	June 30, 20X2 and each June 30 thereafter
Conditions at December 31, 20X1 (reporting date)	Ratio is 0.9	Ratio is 0.9	Ratio is 1.05	
	Entity obtains a 3-month waiver for the breach before December 31, 20X1. The entity expects the ratio to be above 1.0 at all testing dates in 20X2	Entity expects the ratio to be above 1.0 at March 31, 20X2	Entity expects the ratio to be above 1.1 at June 30, 20X2	
Classification	Current	Current	Current	

EY

Amendments to IAS 1: *Classification of Liabilities as Current or Non-current*

IFRIC Tentative Agenda Decision (June/July 2021)

June/July 2021 update:

- The Board tentatively decided to propose several new amendments to the IAS 1 amendments originally made in January 2020
- In particular, the Board decided to further amend IAS 1:
  - To specify that if the right to defer settlement for at least 12 months is subject to a company complying with conditions ***after the reporting period***, then such conditions would not affect whether the right to defer settlement exists at the end of the reporting period for the purposes of classifying a liability as current or non-current;
  - To include additional disclosure requirements for non-current liabilities subject to conditions; and
  - To require that the statement of financial position separately present non-current liabilities subject to conditions in the next 12 months.
- The effective date is tentatively deferred to no earlier than January 1, 2024
- An exposure draft is expected in Q4 2021

EY

Costs Necessary to Sell Inventories

IFRIC Final Agenda Decision (June 2021)

Question posed to the IFRIC: Which costs does an entity include as part of the estimated costs necessary to make a sale when determining the net realizable value of inventories?

- Background:
  - IAS 2.9 requires an entity to measure inventories “at the lower of cost and net realisable value”
  - IAS 2.6 defines net realizable value as: “the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale”
- View 1: An entity includes all costs needed to make the sale (e.g., ordinary sales staff and advertising costs that are attributable to the inventory)
- View 2: An entity includes only additional costs required by the particular conditions of the inventories to make the sale (e.g., special promotion campaigns)

EY

Costs Necessary to Sell Inventories

IFRIC Final Agenda Decision (June 2021)

- The Committee observed that:
  - IAS 2.28 sets out the objective of writing down inventories to their net realisable value (NRV) – to avoid inventories being carried "in excess of amounts expected to be realised from their sale"
  - IAS 2 requires an entity to estimate the costs necessary to make the sale in determining NRV. The costs are not limited to only those that are incremental
  - Including only incremental costs could fail to achieve the objective in paragraph 28
- The Committee concluded that:
  - View 1 is appropriate
  - When determining the net realizable value of inventories, an entity estimates the costs necessary to make the sale in the ordinary course of business
  - Judgment is used to determine which costs are necessary to make the sale considering specific facts and circumstances, including the nature of the inventories
  - The principles and requirements in IFRS provide an adequate basis for an entity to determine if costs are incremental

EY

Costs Necessary to Sell Inventories

IDG Meeting (September 2021)

Question posed to the IDG: What additional costs, other than incremental costs, should be considered when determining the "costs necessary to make the sale"?

- Direct costs incurred **only at point of sale**
- Direct costs **leading up to point of sale**
- **Directly attributable costs** necessary for inventory to be sold
- Allocation of **indirect costs** only at point of sale
- Allocation of **indirect costs** leading up to and including point of sale

- IDG members concluded:
  - The inclusion of costs will be facts-and circumstances-specific
  - Disclosure of policy and significant judgment applied will be necessary

EY

IAS 19: Attributing benefit to periods of service

IFRIC Final Agenda Decision (May 2021)

In December 2020, the IFRIC was asked how to attribute benefits to periods of service under IAS 19 Employee Benefits, for a particular fact pattern:

- Defined benefit plan where employees are entitled to a retirement benefit only when they reach retirement age (62), if still employed by Entity

Retirement benefit ($)[1] =	one month of final salary x each year of service before retirement date[2]

[1] Benefit is capped at 16 years of service (i.e., 16 months of final salary)

[2] Years of service are calculated using only consecutive years of employee service immediately before retirement

What periods of service does the Entity attribute the retirement benefit to?

EY

IAS 19: Attributing benefit to periods of service

IFRIC Final Agenda Decision (May 2021)

- View A: Attribute the retirement benefit to periods of service starting from when the employee starts working with the entity until retirement date, even if longer than 16 years
- View B: To only the first 16 years of employee service (or from date employment commences until retirement date, if employee joins with less than 16 years to retirement)
- View C: To only the last 16 years of employee service (or from date employment commences until retirement date, if employee joins with less than 16 years to retirement)

EY

IAS 19: Attributing benefit to periods of service

IFRIC Final Agenda Decision (May 2021)

IAS 19 requires:

- An entity to attribute benefit to periods of service from the date when employee service first leads to benefits under the plan, until the date when further service will lead to no material amount of further benefits
- An entity to attribute benefit to periods in which the obligation to provide benefit arises (as employees render services in return for benefits the entity expects to pay)

Employees who join before 46	Employees who join on or after 46
Any service rendered before 46 does not lead to benefit – Entity's obligation arises only after age 46	All service rendered leads to benefits under the plan – Entity's obligation arises from the date of employment

- Each year of service between 46 and 62 leads to additional benefit
- An employee receives no material amount of further benefit after 62, thus retirement benefit attributed to service periods only until 62
- Analysis consistent with View C

EY

Economic benefits from use of a windfarm

IFRIC Tentative Agenda Decision (June 2021)

Fact Pattern:

- The electricity retailer (customer) and windfarm generator (supplier) are registered participants in an electricity market
- Purchases and sales of electricity are made via the market's electricity grid
- The customer enters into a 20-year agreement with the supplier to supply electricity
- Under the terms of the contract, customer pays a fixed price per megawatt, and the difference between the spot price and fixed price is settled net in cash
- The renewable energy credits that accrue from windfarm are transferred to the customer

Does the electricity retailer have the right to obtain substantially all the economic benefits from use of a windfarm?

EY

Economic benefits from use of a windfarm

IFRIC Tentative Agenda Decision (June 2021)

Analysis:

- Paragraph 9 of IFRS 16: *"a contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration"*
- To control the use of an asset the customer must have both the right to obtain substantially all the economic benefits from use of the asset and the right to direct the use of that asset
- Paragraph B21 of IFRS 16: *"a customer can obtain economic benefits from use of an asset directly or indirectly in many ways, such as by using, holding or sub-leasing the asset. The economic benefits from use of an asset include its primary output and by-products (including potential cash flows derived from these items), and other economic benefits from using the asset that could be realised from a commercial transaction with a third party"*
- Economic benefits are the electricity generated from the windfarm and the renewable energy credits, which are a by-product of the windfarm
- The windfarm is first selling to the grid and then the customer is buying the electricity from the grid
- The customer is not necessarily buying the electricity the windfarm generated

Tentative conclusion: The electricity retailer does **not** have the right to obtain substantially all the economic benefits from use of a windfarm

EY

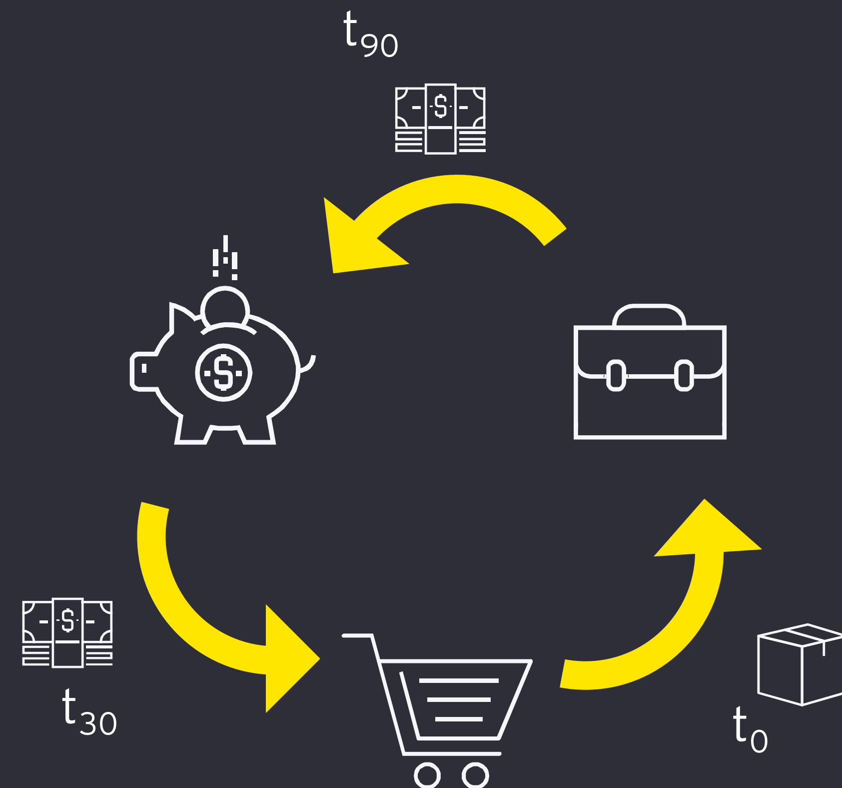
Supply chain financing arrangements – reverse factoring

IFRIC Final Agenda Decision (December 2020)

In April 2020, the IFRIC was asked about presentation and disclosure of supply chain financing

- How should an entity classify its rights and obligations (i.e., the obligation to pay for goods/services received when invoices are part of a supply chain financing arrangement)?
- What is an entity required to disclose?

- Supply chain financing commonly refers to reverse factoring:
  - Reverse factoring is an arrangement involving three parties: an entity that purchases a good/service, a supplier, and a financial institution
  - The arrangement typically allows the supplier to be paid by the financial institution at an earlier date than the entity pays the financial institution



EY

Supply chain financing arrangements – Reverse factoring

IFRIC Final Agenda Decision (December 2020)

Presentation in the statement of financial position:

- IAS 1 Presentation of Financial Statements requires that "trade and other payables" be presented separate from other liabilities
- An entity presents a financial liability as a trade payable only when it:
  - Represents a liability to pay for goods or services;
  - Is invoiced or formally agreed with the supplier; and
  - Is part of the working capital used in the entity's normal operating cycle
- An entity assesses whether liabilities should be presented separately, considering factors such as:
  - Amounts, nature and timing of liabilities
  - Whether additional security is provided as part of the arrangement
  - The extent to which terms of the liabilities differ from terms of the entity's trade payables that are not part of the arrangement

EY

Supply chain financing arrangements – reverse factoring

IFRIC Final Agenda Decision (December 2020)

Derecognition:

- IFRS 9 Financial Instruments must be considered to determine whether a trade payable to a supplier needs to be derecognized and a new financial liability to a financial institution needs to be recognized

Presentation in the statement of cash flows:

- IAS 7 Statement of Cash Flows defines operating and financing activities
- An entity in a reverse factoring arrangement must determine how to classify cash flows related to the arrangement - the assessment of the nature of liabilities for balance sheet classification may guide cash flow analysis
- If no cash flows are transferred in a reverse factoring arrangement, there are no cash flows to be presented on the CF statement

Supply chain financing arrangements – reverse factoring

IFRIC Final Agenda Decision (December 2020)

Disclosure:

- IFRS 7 *Financial Instruments*: Disclosure requires an entity to provide information about nature and risks arising from financial instruments
- Reverse factoring arrangements often give rise to liquidity risk because:
  - An entity has concentrated a portion of its liabilities with one financial institution rather than a diverse group of suppliers
  - An entity may become reliant on extended payment terms; or a supplier may become reliant on earlier payment
- Judgment is required to determine whether to provide additional disclosures in the notes:
  - Consider the judgment applied in assessing how to classify liabilities and cash flows
  - Consider the materiality of arrangements in determining whether additional information is relevant to understanding the financial statements
- IAS 7 *Statement of Cash Flows* requires disclosures relating to changes in liabilities arising from financing activities

EY