Introduction

**Purpose of this paper**

1. The Exposure Draft ED/2013/3 *Financial Instruments: Expected Credit Losses* (‘the ED’) proposed that if the contractual cash flows of a financial asset are renegotiated or otherwise modified, and that modification does not result in derecognition, the entity should adjust the gross carrying amount of the asset to reflect the revised contractual cash flows. The gross carrying amount should be the present value of the estimated future contractual cash flows discounted at the asset’s original effective interest rate (EIR).

2. This paper analyses the responses received on the proposed modification requirements. However, this paper does not consider the disclosure requirements for financial assets that have been modified. The complete package of disclosure requirements will be discussed at a future meeting.
Summary of the feedback received

3. The vast majority of respondents agreed with the accounting treatment proposed in the ED, and felt that the proposals would provide useful information and reflect the economics of a modification.

4. However, respondents raised a number of concerns and requested clarification on the following matters:
   (a) scope of the modification requirements;
   (b) how the model applies to modified assets (for example whether a 12-month ECL can be recognised post-modification);
   (c) operational concerns related to the tracking of modifications over the remaining life; and
   (d) the presentation of modification gains or losses.

Staff recommendation

5. The staff is recommending that the IASB confirm the proposals for modified financial assets proposed in the ED, subject to some minor clarifications as summarised in paragraph 56 (a)–(f).

Paper structure

6. The detailed feedback received and staff analysis are set out as follows:
   (a) What the ED proposed; (paragraph 7–10)
   (b) Detailed feedback received; (paragraph 11–18)
   (c) Staff analysis of the feedback received: (paragraph 19–55)
      (i) Scope of modifications; (paragraph 19–29)
      (ii) When does a modification result in derecognition; (paragraph 30–33)
      (iii) Derecognition and subsequent recognition of modified financial assets; (paragraph 34–39)
(iv) Application of the symmetry of the general model; (paragraph 40–46)

(v) Operational concerns; (paragraph 47–50)

(vi) Presentation requirements; and (paragraph 51–55)

(d) Staff recommendations and question to the IASB. (paragraph 56)

What the ED proposed

7. The ED proposed that if the contractual cash flows of a financial asset are renegotiated or otherwise modified, and that modification does not result in a derecognition, the gross carrying amount of the asset should be recalculated to reflect the modified contractual cash flows. A corresponding modification gain or loss should be recognised in profit or loss. The gross carrying amount is recalculated as the present value of estimated future contractual cash flows discounted at the original EIR.¹

8. For the purposes of determining whether a significant increase in credit risk has occurred, the entity shall compare the credit risk at the reporting date based on the modified contractual terms to the credit risk at initial recognition based on the original, unmodified contractual terms. When an entity determines that a significant increase in credit risk has not occurred, or the asset is determined to have low credit risk at the reporting date, expected credit losses should be measured at 12-month expected credit losses.

9. If the renegotiation or modification results in the derecognition of that financial asset, the date of modification shall be treated as the date of the initial recognition of the modified financial asset.

10. Question asked in the ED:

Question 8

¹ Or original credit-adjusted EIR for purchased or originated credit-impaired financial assets, or, when applicable, the revised EIR calculated in accordance with paragraph 92 of IAS 39.
Do you agree with the proposed treatment of financial assets on which contractual cash flows are modified, and do you believe that it provides useful information? If not, why not and what alternative would you prefer?

**Detailed feedback received**

**Scope of modifications**

11. Although the vast majority of respondents agreed with the proposed guidance on modifications, many asserted that it should be limited to modifications of credit-impaired assets or modifications undertaken for credit risk management purposes. A few respondents suggested aligning the proposed modification requirements to the financial assets that are included in the forbearance guidance developed by the European Banking Authority (EBA).

12. These respondents felt that the proposed guidance does not represent the economics of modifications performed for commercial or other reasons that are unrelated to credit risk management and that it would be inappropriate to recognise modification gains or losses in these circumstances.

**When does a modification result in derecognition?**

13. Many respondents requested clarification on when a modification results in derecognition, because neither IAS 39 *Financial Instruments: Recognition and Measurement* nor IFRS 9 *Financial Instruments* currently provide guidance on this topic for financial assets. Some respondents noted that current practice is to apply, by way of analogy, the guidance in IAS 39 and IFRS 9 for the derecognition of financial liabilities. A few also mentioned this within the context of the September 2012 IFRIC decision for Greek Government Bonds (refer to Appendix A).

14. A number of respondents, however, noted that developing guidance on derecognition for modified assets would be a significant undertaking and urged
that it should not delay the general impairment model, but should instead be addressed as a separate project.

**Derecognition and subsequent recognition of modified financial assets**

15. A small number of respondents, most notably regulators, were concerned about circumstances in which the modification of distressed financial assets results in the derecognition of the financial assets and subsequent recognition of new financial assets in Stage 1 of the proposed model. They felt that measuring the loss allowance for such financial assets at an amount equal to 12-month expected credit losses (ECL) would be inappropriate and expressed concern about whether the newly recognised asset would be adequately assessed for increases in credit risk and objective evidence of impairment.

**Application of the symmetry of the general model**

16. A small number of respondents, again most notably regulators, were concerned about the symmetry of the proposed model, which requires the loss allowance on modified financial instruments to revert to being measured at 12-month ECL when the lifetime ECL criterion is no longer met. They were of the opinion that a modification should not be considered to indicate an improvement in credit quality, because the assessment could be based on overly optimistic projections, which could result in inappropriate movements to Stage 1. They recommended that financial assets modified for credit reasons should be subject to lifetime ECL measurement.

**Operational concerns**

17. A few respondents cited concerns that the proposals would be operationally difficult; in particular, that they would necessitate a burdensome tracking of the credit risk at initial recognition and subsequent monitoring of modifications on an individual basis. There was also a concern that recalculating the gross carrying amount on the basis of the renegotiated or modified contractual cash flows, and discounting the modified cash flows at the original EIR, would be too complex.
Presentation requirements

18. A small number of respondents observed that the proposals do not prescribe the line item in which a modification gain or loss should be recognised. These respondents felt that modification gains or losses represented a change in credit risk, and that for modifications performed for credit risk reasons, the modification gain or loss should be recognised within the impairment line item.

Staff analysis of feedback received

Scope of modifications

19. The staff note that the proposed modification requirements are consistent with the current requirements in paragraph AG8 of IAS 39 (which has been carried forward to the ED as paragraph B3), which states:

   If an entity revises its estimates of payments or receipts, the entity shall adjust the carrying amount of the financial asset or financial liability (or group of financial instruments) to reflect actual and revised estimated cash flows. The entity recalculates the carrying amount by computing the present value of estimated future cash flows at the financial instrument’s original effective interest rate or, when applicable, the revised effective interest rate calculated in accordance with paragraph 92. The adjustment is recognised in profit or loss as income or expense...

20. IAS 39 therefore does not distinguish between modifications for credit or commercial reasons and the modification requirements proposed in the ED did not alter the scope of the existing requirements for modifications of financial assets. Instead, because amortised cost is a measurement method whereby the carrying amount equates to the present value of the contractual cash flows discounted at the EIR, IAS 39 requires that the amortised cost amount be updated in all cases in which those cash flows are modified (or expectations other than in respect of impairment change).
The IASB has previously considered the difficulty of identifying the reason for modifications. Before May 2010, IFRS 7 *Financial Instruments: Disclosures* required the disclosure of the carrying amount of financial assets that would otherwise be past due or impaired but whose terms have been renegotiated. The IASB received feedback from constituents that it is operationally difficult to determine the purpose of modifications (ie whether they are performed for commercial or credit risk management reasons). As a result of this, the IASB deleted the requirement in paragraph 36(d) of IFRS 7 and added paragraph BC54A to the Basis for Conclusions of IFRS 7, which states:

*BC54A In *Improvements to IFRSs* issued in May 2010, the Board addressed a practical concern relating to the disclosure requirements for renegotiated financial assets. The Board deleted the requirement in paragraph 36(d) to disclose the carrying amount of financial assets that would otherwise be past due or impaired whose terms have been renegotiated. The Board considered the difficulty in identifying financial assets whose terms have been renegotiated to avoid becoming past due or impaired (rather than for other commercial reasons). The Board noted that the original requirement was unclear about whether the requirement applies only to financial assets that were renegotiated in the current reporting period or whether past negotiations of those assets should be considered. Moreover, the Board was informed that commercial terms of loans are often renegotiated regularly for reasons that are not related to impairment. In practice it is difficult, especially for a large portfolio of loans, to ascertain which loans were renegotiated to avoid becoming past due or impaired. (Emphasis added in bold)*
22. Some suggested that the scope should be limited and aligned to the EBA’s proposed description of forbearance. The EBA consultation\textsuperscript{2} on forbearance and non-performing loans describes forbearance measures as:

…contracts, the terms of which the debtor is considered unable to comply with due to its financial difficulties so that the institution decides either to modify the terms and conditions of the contract to enable the debtor to service the debt or to refinance, totally or partially, the contract. Refinancing refers to the use of contracts to ensure the total or partial payment of other contracts the current terms of which the debtor is unable to comply with.

…the following situations shall be treated as forbearance measures:

- a modified contract includes more favourable terms than those that the debtor could have obtained in the market;
- a modified contract was classified as non-performing or totally or partially past-due more than 30 days (without being non-performing) at least once during the three months prior to its modification;
- a modified contract would without its modifications be classified as non-performing or totally or partially past-due more than 30 days (without being non-performing);
- the modification made to a contract implies a total or partial cancellation by write-offs of the debt, or repayments made by taking possession of collateral.

23. The staff consider the description above of forbearance to be more akin to the notion of default, which the IASB discussed at its September meeting\textsuperscript{3}.

\textsuperscript{2} EBA Consultation Paper EBA/CP/2013/06 Draft Implementing Technical Standards: \textit{On Supervisory reporting on forbearance and non-performing exposures under article 95 of the draft Capital Requirements Regulation} Publicly available at: \url{http://www.eba.europa.eu/-/eba-consultation-paper-on-supervisory-reporting-on-forbearance-and-non-performing-exposures}
Restricting the modification requirements only to this population would be narrower than applying them to say when significant deterioration has occurred, which is the main focus of the model. In other words, it would link more closely to the Stage 3 population rather than Stage 2 and thus not provide timely information about modifications arising as a result of increased credit risk.

24. Furthermore, the staff believe that even if the *intention* of a modification could be clearly identified to be for commercial purposes, any change in the contractual terms will have a consequential effect on the credit risk of a financial asset since initial recognition and will affect the measurement of the loss allowance. Limiting the scope of the modification requirements to those undertaken for credit reasons could therefore result in different accounting treatments for the same economic event.

25. The staff are also concerned that the difficulty involved with discerning the purpose of modifications, and to what extent a modification is related to credit risk reasons, could create opportunities for manipulation. This could happen if entities were able to select a ‘preferred’ treatment for modifications simply because of the purpose of the modification.

**Staff recommendation**

26. The staff consider the requests to limit the modification requirements to those undertaken for credit reasons, to be contrary to the feedback previously received about the difficulty of identifying which assets have been modified for that purpose.

27. The staff also note that an amortised cost carrying amount equates to the present value of the expected contractual cash flows discounted at the EIR. Consequently, the carrying amount should reflect changes in those contractual cash flows (discounted at the EIR), irrespective of the reason for the modification occurring.

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3 Agenda Paper 5D Definition of Default  
[http://www.ifrs.org/Meetings/MeetingDocs/IASB/2013/September/05D%20Impairment-Definition%20of%20default.pdf](http://www.ifrs.org/Meetings/MeetingDocs/IASB/2013/September/05D%20Impairment-Definition%20of%20default.pdf)
28. Additionally, the staff note that a modification of contractual terms will always have an impact on credit risk, and that requiring different accounting treatments for changes in credit risk attributed to different reasons would create opportunities for manipulation.

29. **The staff therefore recommend that the proposed guidance should continue to apply to all modifications, regardless of the reason for the modification.**

**When does a modification result in derecognition?**

30. The derecognition of financial assets has previously been considered in a separate project, which resulted in the publication of an Exposure Draft in March 2009⁴. That Exposure Draft was met with largely negative feedback and the IASB decided to focus on improving the transparency and comparability of accounting for derecognised financial assets through the improvement of disclosure requirements. This resulted in the 2010 amendments to IFRS 7 that increased the disclosure requirements for transfers of financial assets⁵.

31. The IFRS Interpretations Committee (‘the Interpretations Committee’) also considered the topic of derecognition when addressing the accounting for different aspects of restructuring Greek Government Bonds in September 2012. However, because of the narrowness of the fact pattern submitted, the Interpretations Committee decided not to add the issue to its agenda and noted that developing a new derecognition model for financial instruments goes beyond the scope of the type of issue that can be addressed by way of an interpretation. The Interpretations Committee agenda decision has been included in the 2013 *A Guide through IFRS 2013 (Green Book)* as footnote E1 to IFRS 9.3.2.3(a) and has been reproduced in this paper in Appendix A.

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Staff recommendation

32. The staff acknowledge the requests for further guidance on when the modification of a financial asset will result in derecognition. However, this is a non-trivial question and the development of such guidance is currently outside the scope of the Impairment project. The staff also note that the time and resources required to develop such guidance would be substantial and could result in delaying finalisation of the Impairment project if it were to be developed in parallel.

33. The staff therefore recommend that no further guidance on when a modification of a financial asset results in derecognition should be developed within the confines of the Impairment project.

Derecognition and subsequent recognition of modified financial assets

34. Paragraph B23 of the ED states:

If the contractual cash flows of a financial asset are renegotiated or otherwise modified and the renegotiation or modification results in a derecognition of that financial asset, when this [draft] IFRS is applied to the modified financial asset the date of the modification shall be treated as the date of the initial recognition of that financial asset.

35. When the modification of a financial asset results in the derecognition of the asset and the subsequent recognition of the modified financial asset, the modified asset is considered a ‘new’ asset from an accounting perspective. Even if the modified asset is subsequently issued to the same customer, the terms and pricing of that asset reflect the newly assessed credit risk of the customer. In such a case, the treatment of the modified asset within the requirements of the general model is therefore representative of the economics of the transaction. This typically means recognising 12-month ECL until the requirements for the recognition of lifetime ECL are met.

36. However, paragraph BC139 of the ED acknowledges that in some circumstances following a modification, there may be objective evidence that the newly recognised financial asset is originated as credit-impaired:
The IASB noted that, while the scope usually relates to purchased financial assets, in unusual circumstances financial assets could be originated that would be within this scope. However, this does not mean that all financial assets originated at a low credit quality are within the scope—there has to be objective evidence of impairment on initial recognition. The IASB considered a situation in which there was a substantial modification of a distressed asset that resulted in derecognition. In such a case, it would be possible for the modification to constitute objective evidence that the new asset is impaired. [emphasis added]

37. Entities should therefore consider whether a modified financial asset is originated credit-impaired at initial recognition (ie there is objective evidence of impairment). If it is, then lifetime ECL would be recognised at initial recognition by adjusting the EIR.

**Staff recommendation**

38. For the reasons described in paragraph 35, the staff consider that accounting for a ‘new’ financial asset in accordance with the general model remains appropriate. However, the staff acknowledge that the interaction between the recognition of a modified financial assets and the requirements for financial assets that are originated credit-impaired could be clarified.

39. The staff therefore recommend that no changes should be made to the requirements of the proposed general model, but that the application guidance should be clarified to require an entity to consider whether there is objective evidence of impairment upon the initial recognition of a modified financial asset.

**Application of the symmetry of the general model**

40. During the development of the proposed model, the IASB considered whether financial instruments with modified contractual cash flows should be prohibited from having a loss allowance at an amount equal to 12-month ECL or whether
instead additional requirements should be required to be satisfied for this to occur (for example, that a number of payments were made on a timely basis). However, the IASB decided to require a symmetrical approach, as set out in paragraph BC125 in the ED:

The IASB observed that it is not unusual for distressed financial instruments to be modified more than once and, therefore, the assessment of whether lifetime expected credit losses is required for modified financial instruments may be based on projections that are too aggressive or optimistic. The IASB considered prohibiting the ability for modified financial instruments to change to a loss allowance at an amount equal to 12-month expected credit losses or proposing more restrictive criteria than usual before allowing 12-month expected credit losses to be re-established. However, the IASB concluded that the proposed deterioration model should allow the loss allowance on modified financial instruments to revert to being measured at an amount equal to 12-month expected credit losses when they no longer meet the lifetime expected credit loss criterion, which is consistent with the proposed treatment of unmodified financial instruments. In the IASB’s view, such a model faithfully represents the economics of the transaction and it should not override that faithful representation for anti-abuse purposes. In addition, the IASB observed that entities do not only modify financial instruments because of credit deterioration.

41. Furthermore, paragraph B24 of the ED states that the credit risk on a financial asset will not automatically decrease merely because the contractual cash flows have been modified. It further states that evidence that the criteria for the recognition of lifetime ECL are no longer met may include a history of full and timely payment performance against the revised contractual cash flows.

42. The staff acknowledge the concerns of some respondents about the potential to avoid recognising lifetime ECL simply by modifying the contractual terms. However, the staff note that the ED requires an entity to base its assessment of
significant increases in credit risk since initial recognition on all reasonable and supportable information. This includes historical and forward-looking information and an assessment of the credit risk over the remaining life of the instrument, which should include the circumstances that led to the modification.

43. The staff note that because the recognition of lifetime ECL is determined by reference to the initial credit risk based on the original terms, financial assets will not automatically move to Stage 1 as a result of a modification. Informal outreach performed indicated that the assessment of credit risk is generally determined by the payment behaviour of a customer. A history of bad payment behaviour cannot be erased by simply making one payment on time following a modification of the contractual terms. Participants in the informal outreach indicated that typically a customer would need to demonstrate consistently good payment behaviour over a period of time before the credit risk was considered to have decreased.

44. For the reasons discussed in paragraphs 19–29 above, the staff note that it would furthermore be difficult from an operational standpoint to prescribe asymmetrical guidance for assets that have been modified because of credit risk factors. This is because it is often difficult to differentiate the reasons for modifications. Such a prescription could also actually result in entities attempting to manipulate the restriction by issuing new loans rather than modifying old loans.

Staff recommendation

45. The staff do not agree with the suggestions to exclude modified financial assets from the general symmetrical treatment. However, the staff acknowledge that the guidance in paragraph B24 may be seen to apply only to financial assets that are assessed on the basis of past due information.

46. The staff therefore recommend confirming that the symmetrical treatment of the general model should apply equally to modified financial assets. However, the staff also recommend that the application guidance in paragraph B24 should be clarified to ensure it is clear that it applies to all modified financial assets.
**Operational concerns**

47. A few respondents raised concerns about the difficulty of comparing the credit risk of the modified asset with its initial credit risk. The staff do not consider the requirements relating to the assessment of significant increases in credit risk on modified financial assets to be operationally any more challenging than for other financial instruments within the scope of the general model.

48. Furthermore, as discussed in Agenda Paper 5A of this meeting, the staff note that the proposals do not require financial instruments to be tracked on an individual basis. In addition, the recalculation of the gross carrying amount on the basis of the modified contractual cash flows and discounting them at the original EIR is consistent with the existing requirements in IAS 39 paragraph AG8 (as discussed in paragraph 19).

49. The assessment of significant deterioration for modified assets is furthermore the same as for the general model, and all the existing practical expedients are available. The guidance for modifications does not require anything not already prescribed by the general model.

**Staff recommendation**

50. The staff intend to address these operational concerns by clarifying in drafting that tracking on an individual basis or the use of a mechanistic approach to tracking is not required (see Agenda Paper 5A of this meeting). No further recommendations are made to specifically address modified financial assets.

**Presentation requirements**

51. The staff consider the emphasis of the ED to be on the requirement to recognise a modification gain or loss in profit or loss, rather than on how it is to be presented.

52. A modification gain or loss is an amount arising from adjusting the gross carrying amount of a financial asset to reflect modified contractual cash flows, and is different from a change in expected credit losses. Though a modification gain or loss may crystallise expected credit losses and affect the loss allowance, the
amount of the adjustment to the contractual cash flows and the subsequent effect on the loss allowance may not necessarily perfectly match.

53. Furthermore, not all modifications are performed for credit risk reasons, and so it would be inappropriate to require the presentation of modification gains or losses together with impairment losses (or gains). As mentioned in paragraphs 19–29 above, the IASB was told previously that it is difficult to determine whether modifications are performed for credit risk reasons or otherwise. Prescribing presentation requirements for a subset of modifications would therefore impose operational challenges and raise the question of how to distinguish and present modifications undertaken for commercial or other purposes.

54. The staff therefore do not think it will appropriate to prescribe where modification gains or losses should be presented in profit or loss (ie in which line item) and that judgement should be applied when considering the appropriate presentation. Furthermore, IAS 1 *Presentation of Financial Statements*, paragraph 85 will require the separate disclosure of a modification gain or loss when it relevant to an understanding of the entity’s financial performance.

*Staff recommendation*

55. **The staff recommend that no specific presentation requirements for modification gains or losses should be included in the final requirements. It should simply be confirmed that this amount should be recognised in profit or loss.**

*Summary of staff recommendations and questions to the IASB*

56. The staff analysis and recommendations on individual matters were provided in paragraphs 19-55 above. The staff are recommending that the IASB should confirm the proposals for modified financial assets proposed in the ED, subject to the minor clarifications below. For ease of reference the staff recommendation on each matter can be summarised as follows:
(a) **Scope of modifications**—that the proposed guidance should continue to apply to all modifications, regardless of the reason for the modification.

(b) **When does a modification result in derecognition**—that no further guidance on when a modification of a financial asset results in derecognition should be developed within the confines of the Impairment project.

(c) **Derecognition and subsequent recognition of modified financial assets**—that no changes should be made to the requirements of the proposed general model, but that the application guidance should be clarified to require an entity to consider whether there is objective evidence of impairment upon the initial recognition of a modified financial asset.

(d) **Application of the symmetry of the general model**—that the symmetrical treatment of the general model should apply equally to modified financial assets. However, the staff also recommend that the application guidance in paragraph B24 should be clarified.

(e) **Operational concerns**—no specific recommendations are made in this paper to address modified financial assets. Refer to Agenda Paper 5A of this meeting.

(f) **Presentation requirements**—that it should be confirmed that modification gains or losses must be recognised in profit or loss, but not to include any specific presentation requirements in the final requirements.

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<th>Question to the IASB</th>
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<tr>
<td>Does the IASB agree with the staff recommendation to confirm the proposals for modified financial assets subject to the clarifications as set out in paragraph 56(a)-(f)? If not, why not and what would the IASB prefer?</td>
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Appendix A—Footnote E1 to IFRS 9.3.2.3(a) (2013 A Guide through IFRS)


The Interpretations Committee received a request for guidance on the circumstances in which the restructuring of Greek government bonds (GGB) should result in derecognition in accordance with IAS 39 (replaced by IFRS 9) of the whole asset or only part of it. In particular, the Interpretations Committee has been requested to consider whether:

(a) the portion of the old GGBs that are exchanged for twenty new bonds with different maturities and interest rates should be derecognised, or conversely accounted for as a modification or transfer that would not require derecognition?

(b) IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors would be applicable in analysing the submitted fact pattern?

(c) either paragraphs AG8 or AG62 of IAS 39 (paragraph AG62 of IAS 39 is now replaced by paragraph B3.3.6 of IFRS 9) would be applicable to the fact pattern submitted if the GGBs were not derecognised?

The Interpretations Committee noted that the request has been made within the context of a narrow fact pattern. The narrow fact pattern highlights the diversity in views that has arisen in relation to the accounting for the portion of the old GGBs that is exchanged for twenty new bonds with different maturities and interest rates.

The submitter asked the Interpretations Committee to consider whether these should be derecognised, or conversely accounted for as a modification or transfer that would not require derecognition. In addition, the Interpretations Committee has been asked to consider whether IAS 8 would be applicable in analysing the submitted fact pattern, and whether the exchange can be considered to be a transfer within the scope of paragraph 17(b) of IAS 39 (now paragraph 3.2.3(b) of IFRS 9).
The Interpretations Committee observed that the term ‘transfer’ is not defined in IAS 39. However, the potentially relevant portion of paragraph 18 of IAS 39 (now paragraph 3.2.4 of IFRS 9) states that an entity transfers a financial asset if it transfers the contractual rights to receive the cash flows of the financial asset. The Interpretations Committee noted that, in the fact pattern submitted, the bonds are transferred back to the issuer rather than being transferred to a third party.

Accordingly, the Interpretations Committee believed that the transaction should be assessed against paragraph 17(a) of IAS 39 (now paragraph 3.2.3(a) of IFRS 9). In applying paragraph 17(a), the Interpretations Committee noted that, in order to determine whether the financial asset is extinguished, it is necessary to assess the changes made as part of the bond exchange against the notion of ‘expiry’ of the rights to the cash flows. The Interpretations Committee also noted that, if an entity applies IAS 8 because of the absence in IAS 39 of an explicit discussion of when a modification of a financial asset results in derecognition, applying IAS 8 requires judgement to develop and apply an accounting policy. Paragraph 11 of IAS 8 requires that, in determining an appropriate accounting policy, consideration must first be given to the requirements in IFRSs that deal with similar and related issues.

The Interpretations Committee noted that, in the fact pattern submitted, that requirement would lead to the development of an analogy to the notion of a substantial change of the terms of a financial liability in paragraph 40 of IAS 39 (now paragraph 3.3.2 of IFRS 9). Paragraph 40 sets out that such a change can be effected by the exchange of debt instruments or by modification of the terms of an existing instrument. Hence, if this analogy to financial liabilities is applied to financial assets, a substantial change of terms (whether effected by exchange or by modification) would result in derecognition of the financial asset. The Interpretations Committee noted that, if the guidance for financial liabilities is applied by analogy to assess whether the exchange of a portion of the old GGBs for twenty new bonds is a substantial change of the terms of the financial asset, the assessment needs to be made taking into consideration all of the changes made as part of the bond exchange.
In the fact pattern submitted, the relevant facts led the Interpretations Committee to conclude that, in determining whether the transaction results in the derecognition of the financial asset, both approaches (ie extinguishment under paragraph 17(a) of IAS 39 (now paragraph 3.2.3(a) of IFRS 9) or substantial change of the terms of the asset) would result in derecognition.

The Interpretations Committee considered the following aspects of the fact pattern in assessing the extent of the change that results from the transaction:

(a) A holder of a single bond has received, in exchange for one portion of the old bond, twenty bonds with different maturities and cash flow profiles as well as other instruments in accordance with the terms and conditions of the exchange transaction;

(b) All of the bond-holders received the same restructuring deal irrespective of the terms and conditions of their individual holdings. This indicates that the individual instruments, terms and conditions were not taken into account. The different bonds (series) were not each modified in contemplation of their respective terms and conditions but were instead replaced by a new uniform debt structure;

(c) The terms and conditions of the new bonds are substantially different from those of the old bonds. The changes include many different aspects, such as the change in governing law; the introduction of contractual collective action clauses and the introduction of a co-financing agreement that affects the rights of the new bond holders; and modifications to the amount, term and coupons.

The Interpretations Committee noted that the starting point that it used for its analysis was the assumption in the submission that the part of the principal amount of the old GGBs that was exchanged for new GGBs could be separately assessed for derecognition. The Interpretations Committee emphasised that this assumption was more favourable for achieving partial derecognition than looking at the whole of the old bond. Hence, its conclusion that the old GGBs should be derecognised would apply even more so when taking into account that the exchange of the old GGBs was, as a matter of fact,
the result of a single agreement that covered all aspects and types of consideration for surrendering the old GGBs. As a consequence, the Interpretations Committee noted that partial derecognition did not apply. Consequently, the Interpretations Committee decided not to add the issue to its agenda.

**Application of paragraphs AG62 or AG8 of IAS 39 to the submitted fact pattern**

The Interpretations Committee noted that the questions raised by the submitter assume that the old GGBs in the fact pattern would not be derecognised. In the submitted fact pattern, the Interpretations Committee concluded that the old GGBs are derecognised. The Interpretations Committee noted that, because of its conclusion on derecognition, these questions did not need to be answered.