Canadian Accounting Standards Board
277 Wellington Street West,
Toronto, ON Canada M5V 3H2
T. 416 977.3222 F. 416 204.3412
www.frascanada.ca

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Submitted electronically via www.ifrs.org

International Accounting Standards Board
Columbus Building
7 Westferry Circus, Canary Wharf
London E14 4HD
United Kingdom

Dear Sirs:

Re: Interest Rate Benchmark Reform (ED/2020/1)

This letter is the response of the Canadian Accounting Standards Board (AcSB) to the International Accounting Standards Board's (IASB) Exposure Draft, "Interest Rate Benchmark Reform—Phase 2" (Proposed amendments to IFRS 9, IAS 39, IFRS 7, IFRS 4 and IFRS 16)", issued in April 2020.

Our process

As part of our due process for these proposals, we consulted with members of our IFRS® Discussion Group and the Canadian Bankers Association. We considered the results of these discussions when developing this letter.

Our views

We commend the IASB for its continuing efforts to address accounting issues arising from entities transitioning to alternative risk-free benchmark rates. Furthermore, we support the IASB providing temporary relief from existing IFRS requirements for replacement issues[1] while entities transition to these rates. We think this relief will reduce operational complexities faced by financial statement preparers while still providing useful and relevant information to the financial statement users.

While we support the proposed amendments, we think certain principles underpinning them should be clarified both in the final amendments and in the basis for conclusions. Specifically, we encourage the IASB to provide more context and guidance on how the term "economically equivalent" will be applied in practice. We think that entities should be permitted to exercise judgement when applying this principle to

[1] For the purposes of this response letter, the term "replacement issues" includes changes made to contractual cash flows or hedging relationships, as a result of an entity transitioning to alternative benchmark rates.

determine whether a qualitative or quantitative analysis is most appropriate, based on the circumstances of the modification. We also think that not clarifying this term may lead to diversity in practice with some stakeholders interpreting it to mean that two values need to be exactly equal, therefore requiring a quantitative assessment to validate that the modification qualifies for relief. Furthermore, we understand, based on our discussions with stakeholders, that this quantitative assessment may be extremely challenging in certain circumstances.

We also think the IASB should clarify how the proposed reliefs will work in multi-rate jurisdictions. In Canada, the Canadian Overnight Repo Rate Average (CORRA) is not expected to replace the Canadian Dollar Offered Rate (CDOR), Canada's version of LIBOR, in the near term. However, many market participants are of the view that CORRA will eventually replace CDOR and, therefore, have started the transition from CDOR to CORRA. As such, we think these proposals should be applicable when there is a general expectation that an IBOR rate will be replaced by a risk-free rate, even if such replacement has not been mandated.

Finally, given the urgency and the impact of the project, we support the effective date as proposed. We also encourage the IASB to issue the final amendments as soon as possible to allow stakeholders to avail themselves of these proposals. In finalizing the proposals, the IASB should consider the robust endorsement processes in jurisdictions like Canada. In Canada, the proposals need to be translated and endorsed by the AcSB before they are incorporated into the Canadian Handbook and applied by our stakeholders. The IASB's timely issuance of these amendments will help jurisdictions expedite finalizing and incorporating these amendments into their local accounting frameworks.

Our response to your questions

Appendix 1 to this letter responds to the questions posted in the Exposure Draft and expands on the points raised above.

We would be pleased to elaborate on our comments in more detail if you require. If so, please contact me or, alternatively Kelly Khalilieh, Director, Accounting Standards (+1 416 204-3453 or email kkhalilieh@acsbcanada.ca), or Sean Wang, Principal, Accounting Standards (+1 416 204-2969 or email swang@acsbcanada.ca).

Yours truly,

Linda F. Mezon, FCPA, FCA
CPA (MI), CGMA
Chair, Canadian Accounting Standards Board
lmezon@acsbcanada.ca
+1 416 204-3490

About the Canadian Accounting Standards Board

We are an independent body with the legal authority to establish accounting standards for use by all Canadian publicly accountable enterprises, private enterprises, not-for-profit organizations and pension plans in the private sector. We are comprised of a full-time Chair and volunteer members from a variety of backgrounds, including financial statement users, preparers, auditors and academics; a full-time staff complement supports our work.

Our standards

We have adopted IFRS® Standards as issued by the IASB for publicly accountable enterprises. Canadian securities legislation permits the use of U.S. GAAP in place of IFRS Standards in certain circumstances. We support a shared goal among global standard setters of high-quality accounting standards that result in comparable financial reporting outcomes regardless of the GAAP framework applied.

We developed separate sets of accounting standards for private enterprises, not-for-profit organizations and pension plans. Pension plans are required to use the applicable set of standards. Private enterprises and not-for-profit organizations can elect to apply either the set of standards developed for them, or IFRS Standards as applied by publicly accountable enterprises.

Our role vis-à-vis IFRS Standards

Our responsibility to establish Canadian GAAP necessitates an endorsement process for IFRS Standards. We evaluate and rely on the integrity of the IASB's due process as a whole, and monitor its application in practice. In addition, we perform our own due process activities for each new or amended IFRS Standard to ensure that the standard is appropriate for application in Canada. We reach out to Canadians on the IASB's proposals to understand and consider their views before deciding whether to endorse a final IFRS Standard. A final standard is available for use in Canada only after we have endorsed it as Canadian GAAP.

APPENDIX 1

Question 1—Modifications of financial assets and financial liabilities (paragraphs 6.9.1–6.9.6 of the [Draft] amendments to IFRS 9, paragraphs 20R–20S and 50–51 of the [Draft] amendments to IFRS 4 and paragraphs 104–106 and C1A–C1B of the [Draft] amendments to IFRS 16)
Paragraphs 6.9.2–6.9.6 of the draft amendments to IFRS 9 propose that: (a) a financial asset or financial liability would be modified if the basis for determining the contractual cash flows is changed after the initial recognition of the financial instrument. In this context, a modification can arise even if the contractual terms of the financial instrument are not amended. (b) an entity would apply paragraph B5.4.5 of IFRS 9 as a practical expedient to account for a modification of a financial asset or financial liability that is required by interest rate benchmark reform. (c) a modification is required by interest rate benchmark reform if and only if (i) it is required as a direct consequence of interest rate benchmark reform; and (ii) the new basis for determining the contractual cash flows is economically equivalent to the previous basis (ie the basis immediately preceding the modification). (d) an entity would also apply the practical expedient proposed in paragraph 6.9.3 if an existing contractual term is activated that results in a change in the basis for determining the contractual cash flows of a financial asset or a financial liability, and particular other conditions are met. Paragraphs BC10–BC36 of the Basis for Conclusions describe the Board’s reasons for these proposals. (e) The Exposure Draft proposes to make corresponding amendments to IFRS 4 that would require insurers applying the temporary exemption from IFRS 9 to apply the same practical expedient as described above. (f) The Exposure Draft proposes amendments to IFRS 16 that would require entities to apply paragraph 42 of IFRS 16 to account for a lease modification that is required by interest rate benchmark reform. Paragraphs BC39–BC41 and paragraphs BC118–BC125 of the Basis for Conclusions describe the Board’s reasons for these proposals. Do you agree with these proposals? Why or why not? If you agree with only parts of the proposals, please specify what you agree and disagree with. If you disagree with the proposals, please explain what you propose and why.

1. We agree with the proposed amendments in paragraphs 6.9.2–6.9.6 of the draft amendments to IFRS 9 for the reasons set out in paragraphs BC10–BC36 of the Basis for Conclusions. We also

agree with the amendments to IFRS 4 and paragraph 42 of IFRS 16 for the reasons set out in paragraphs BC39–BC41 and paragraphs BC118–BC125 of the Basis for Conclusions.

2. The term “economically equivalent” is prevalent throughout the proposed amendments and is an essential element to determine whether a modification qualifies for relief. However, we note that this principle is not explained in the proposed amendments. We think that without clarification of this principle, financial statement preparers will need to apply their own judgment to determine whether a change is done on an economically equivalent basis, which may lead to diversity in practice. For example, some stakeholders we have consulted interpret this term to mean that two values need to be exactly equal. These stakeholders think that a quantitative assessment must be performed to prove that the value of the modified financial instrument equals to the value of the original instrument and qualify for the relief. We think that such precision may not be possible considering the significant judgement used to value the modified financial instrument. Furthermore, for entities with contracts based on various IBOR benchmarks across many governing frameworks, it may be impractical to perform quantitative tests on each modified contract to prove economic equivalence. As such, we recommend the IASB provide more context and guidance on how to apply the economic equivalence principle in practice. Specifically, we think that entities should be permitted to exercise judgement when applying this principle to determine whether a qualitative or quantitative analysis is most appropriate based on the circumstances of the modification. For example, a modification replacing the existing IBOR rate to its alternative benchmark and adding a fixed spread to reflect the basis difference between them may be considered as meeting the economically equivalent principle without a quantitative assessment.
3. We note that under U.S. GAAP, the addition of an interest rate floor or cap that is out of the money is explicitly noted as one example of changes to terms of an instrument that are related to the interest rate benchmark reform[2]. However, such example is not included in proposed paragraph 6.9.4 in IFRS 9. In this current interest rate environment, insertions of an interest rate floor to contracts are becoming more common in practice. Therefore, we think the IASB should provide additional clarification as to whether these types of amendments to the contracts are intended to be in the scope of the relief.
4. We think that proposed paragraphs 6.9.1 to 6.9.6 of IFRS 9 are related to modifications of financial assets and liabilities, not hedge accounting, and therefore should be moved to Chapter 5, Measurement of IFRS 9. Furthermore, we think that moving this guidance from the hedge accounting section of IFRS 9 also clarifies that entities applying the hedge accounting requirements in IAS 39 can also apply these amendments.
5. We also think proposed paragraph 6.9.3 in IFRS 9 is difficult to understand. Specifically, the phrase “required by interest rate benchmark reform” is repeated multiple times in this paragraph. Therefore, we propose the following changes:

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[2] Paragraph ASC 848-20-15-5 (e) states that the “addition of an interest rate floor or cap that is out of money on the basis of the spot rate at the time of the amendment of the contract” is an example of changes to terms that are related to the replacement of a reference rate.

6.9.3 As a practical expedient, an entity shall apply paragraph B5.4.5 to account for a modification of a financial asset or financial liability that is required by interest rate benchmark reform. This practical expedient applies only to such modifications (~~but~~ see also paragraphs 6.9.5 and 6.9.6) ~~and only to the extent the modification is required by interest rate benchmark reform (see also paragraph 6.9.6)~~

Question 2—Amendments to hedging relationships (paragraphs 6.9.7–6.9.10 of the [Draft] amendments to IFRS 9 and paragraphs 102O–102R of the [Draft] amendments to IAS 39)

Paragraphs 6.9.7–6.9.10 of the draft amendments to IFRS 9 and paragraphs 102O–102R of the draft amendment to IAS 39 propose that an entity would amend the formal designation of the hedging relationship only to make one or more of the changes specified in paragraph 6.9.7 and paragraph 102O as and when uncertainty arising from interest rate benchmark reform is no longer present with respect to the hedged risk and/or the timing and the amount of interest rate benchmark-based cash flows of the hedged item or of the hedging instrument.

Paragraphs BC42–BC50 of the Basis for Conclusions describe the Board's reasons for these proposals.

Do you agree with these proposals? Why or why not? If you agree with only parts of the proposals, please specify what you agree and disagree with. If you disagree with the proposals, please explain what you propose and why.

6. We agree with these proposals to IFRS 9 and IAS 39 for the reasons set out in paragraphs BC42–BC50 of the Basis for Conclusions.
7. We note that proposed paragraphs 6.9.7-6.9.8 in IFRS 9 and 102O-102P in IAS 39 appear to limit relief to contractual amendments to hedging instruments. However, we observe that in practice, it is common for entities to modify a hedging relationship without amending existing contracts. A transition to the alternative benchmark rates can be achieved either by unwinding the IBOR-based derivative and entering a new RFR-based derivative or by layering a new RFR-based derivative onto the existing hedging relationship. Both methods will achieve a similar economic outcome to modifying the original contract, but it is unclear whether these scenarios are contemplated in the proposed amendments or whether they will qualify for the proposed relief. We think such arrangements should qualify for relief as they are only variations of the form of the arrangements and will have the same economic consequences as amending the original contract. Therefore, we encourage the IASB to update the amendments to allow these scenarios to qualify for relief.

Question 3—Accounting for qualifying hedging relationships and groups of items (paragraphs 6.9.11–6.9.15 of the [Draft] amendments to IFRS 9 and paragraphs 102S–102X of the [Draft] amendments to IAS 39)

Paragraphs 6.9.11–6.9.15 of the draft amendments to IFRS 9 and paragraphs 102S-102X of the draft amendments to IAS 39 propose that:

(a) the requirements in IFRS 9 and IAS 39 would be applied when the designation of a hedging relationship is amended to remeasure the hedging instrument and the hedged item based on the alternative benchmark rate and recognise any resulting ineffectiveness in profit or loss.

(b) the amount accumulated in the cash flow hedge reserve at the date the entity amends the description of the hedged item would be deemed to be based on the alternative benchmark rate on which the hedged future cash flows are determined.

(c) when there is a change in the basis for determining the contractual cash flows of a financial asset or a financial liability previously designated as a hedged item in a hedging relationship that has been discontinued, the amount accumulated in the cash flow hedge reserve for the discontinued hedging relationship would be deemed to be based on the alternative benchmark rate on which the hedged future cash flows will be based.

(d) when applying paragraph 6.9.7 or paragraph 102O to groups of items designated as hedged items, the hedged items would be allocated to sub-groups within the same hedging relationship based on the benchmark rate to which they are referenced and that the proportionality test would be applied to each sub-group separately.

(e) for the purpose of assessing retrospective effectiveness as required by IAS 39, the cumulative fair value changes of the hedged item and hedging instrument would be reset to zero when paragraph 102G of IAS 39 ceases to apply.

Paragraphs BC51–BC79 of the Basis for Conclusions describe the Board's reasons for these proposals.

Do you agree with these proposals? Why or why not? If you agree with only parts of the proposals, please specify what you agree and disagree with. If you disagree with the proposals, please explain what you propose and why.

8. We agree with the proposed amendments illustrated in paragraphs 6.9.11 – 6.9.15 of IFRS 9 and paragraphs 102S – 102X of IAS 39 for the reasons highlighted in paragraphs BC51-BC79 of the Basis for Conclusions. We think immediately reclassifying a cash flow hedge reserve to profit or loss does not reflect the economic effect of an entity transitioning to an alternative RFR. We also think that the proposal in paragraph 102S of IAS 39 will not change the current requirement to measure

ineffectiveness and thus will continue to reflect the actual results of the hedging relationship in the financial statements.

Question 4—Designation of risk components and portions (paragraphs 6.9.16–6.9.18 of the [Draft] amendments to IFRS 9 and paragraphs 102Y–102Z1 of the [Draft] amendments to IAS 39)

Paragraphs 6.9.16–6.9.18 of the draft amendments to IFRS 9 and paragraphs 102Y–102Z1 of the draft amendments to IAS 39 propose that:

(a) an alternative benchmark rate designated as a non-contractually specified risk component that is not separately identifiable at the date it is designated, would be deemed to have met that requirement at that date, if and only if, the entity reasonably expects the alternative benchmark rate will be separately identifiable within a period of 24 months from the date the alternative benchmark rate is designated as a risk component.

(b) if subsequently, an entity reasonably expects that the alternative benchmark rate will not be separately identifiable within 24 months from the date it was designated as a risk component, an entity would cease applying the requirement in paragraph 6.9.16 and paragraph 102Y and discontinue hedge accounting prospectively from the date of that reassessment.

Paragraphs BC87–BC97 of the Basis for Conclusions describe the Board’s reasons for these proposals.

Do you agree with these proposals? Why or why not? If you agree with only parts of the proposals, please specify what you agree and disagree with. If you disagree with the proposals, please explain what you propose and why.

9. We agree with the proposal to provide relief on the separately identifiable criterion for the reasons summarized in paragraphs BC87-BC97 of the Basis for Conclusions.

Question 5—Effective date and transition (paragraphs 7.1.9 and 7.2.36–7.2.38 of the [Draft] amendments to IFRS 9 and paragraphs 108H–108J of the [Draft] amendments to IAS 39)

(a) The Exposure Draft proposes that the amendments would have an effective date of annual periods beginning on or after 1 January 2021. Earlier application would be permitted.

(b) The Exposure Draft proposes that the amendments would be applied retrospectively in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*, except as specified in (ii) below. An entity would:

(i) reinstate a discontinued hedging relationship if and only if the entity discontinued that hedging relationship solely due to changes required by interest rate benchmark reform and, therefore,

> the entity would not have been required to discontinue that hedging relationship if the amendments had been applied at that time.
>
> (ii) not be required to restate prior periods to reflect the application of these amendments. However, the entity may restate prior periods if, and only if, it is possible without the use of hindsight.
>
> Paragraphs BC110–BC115 of the Basis for Conclusions describe the Board's reasons for these proposals.
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> Do you agree with these proposals? Why or why not? If you agree with only parts of the proposals, please specify what you agree and disagree with. If you disagree with the proposals, please explain what alternative you propose and why.

10. Given the urgency and the impact of the project, we support the proposal to have an effective date of beginning on or after 1 January 2021 with early adoption permitted. We also agree with the proposed amendments being applied retrospectively for the reasons summarized in paragraphs BC110-BC115 of the Basis for Conclusions.
11. Paragraph 7.2.37 of IFRS 9 and paragraph 108I of IAS 39 require an entity to reinstate a discontinued hedging relationship when the entity discontinued that relationship solely due to the IBOR reform. In practice, reinstating a discontinued hedging relationship may not be possible if the hedging instrument has been terminated or designated in a new hedging relationship. Therefore, we recommend the IASB change the words from "an entity shall" to "an entity may" in those paragraphs so that an entity is not required to reinstate a discontinued hedging relationship in circumstances where it is impractical to do so.
12. We think that the IASB should clarify how the proposed relief will work in multi-rate jurisdictions. In Canada, CORRA will act as a complementary reference rate for the Canadian market and will operate alongside CDOR, Canada's version of LIBOR. Many market participants think that the coexistence of CORRA and CDOR will be definite-lived and that CDOR will eventually cease to exist[3]. With this expectation, some stakeholders have started to transition from CDOR to CORRA. Paragraph BC2 of the Basis for Conclusions and paragraph 6.8.2 of IFRS 9 refer to the replacement of interest rate benchmarks. We think that it is unclear whether the related reliefs are applicable when an IBOR rate is not being replaced in the near term (i.e. before 2022). Considering the importance of these proposals in Canada, we recommend that the IASB clarify that relief is available even when the replacement of an interest rate benchmark has not been mandated.
13. We encourage the IASB to issue the final amendments as soon as possible to allow stakeholders to avail themselves of these proposals. In finalizing the proposals, the IASB should consider the robust endorsement processes in jurisdictions like Canada. In Canada, the proposals need to be translated

[3] TMX Montreal Exchange presentation- North American Interest Rate Benchmark Transition and CORRA Futures: https://www.m-x.ca/f_publications_en/north_american_interest_rate_benchmark_transition_and_CORRA_futures.pdf

and endorsed by the AcSB before they are incorporated into the Canadian Handbook and applied by our stakeholders. The proposed amendments will have significant impacts on our financial institutions. In Canada, major financial institutions have October 31 year end dates. Considering the time required for translation and our endorsement process, getting these done by October 31, 2020 will be challenging, but it won't be possible if there is any delay at all in issuing the final amendments.

Question 6—Disclosures (paragraphs 24I–24J and paragraphs 44HH–44II of [Draft] amendments to IFRS 7)
The Exposure Draft proposes that entities provide specific disclosures in order to provide information about: (a) the nature and extent of risks arising from interest rate benchmark reform to which the entity is exposed, and how it manages those risks; and (b) the entity's progress in completing the transition from interest rate benchmarks to alternative benchmark rates, and how the entity is managing that transition. Paragraphs BC105–BC109 of the Basis for Conclusions describe the Board's reasons for this proposal. Do you agree with this proposal? Why or why not? If you disagree with the proposals, please explain what you propose instead and why.

14. We agree with the proposed disclosures for the reasons set out in paragraphs BC105 to BC109 of the Basis for Conclusions.