This paper has been prepared by the EFRAG Secretariat for discussion at a public meeting of EFRAG FR TEG. The paper forms part of an early stage of the development of a potential EFRAG position. Consequently, the paper does not represent the official views of EFRAG or any individual member of the EFRAG FRB or EFRAG FR TEG. The paper is made available to enable the public to follow the discussions in the meeting. Tentative decisions are made in public and reported in the EFRAG Update. EFRAG positions, as approved by the EFRAG FRB, are published as comment letters, discussion or position papers, or in any other form considered appropriate in the circumstances.

Outlined Draft Comment Letter

You can submit your comments on EFRAG's draft comment letter by using the 'Express your views' page on EFRAG's website, then open the relevant news item and click on the 'Comment publication' link at the end of the news item.

Comments should be submitted by [date].

International Accounting Standards Board

7 Westferry Circus, Canary Wharf

London E14 4HD

United Kingdom

[XX Month 202X]

Dear Mr Barckow,

Re: Provisions–Targeted Improvements (Proposed amendments to IAS 37)

On behalf of the European Financial Reporting Advisory Group (EFRAG), I am writing to comment on the proposed amendments to IAS 37, *Provisions—Targeted Improvements,* issued by the IASB on [date] November 2024 (the 'ED').

This letter is intended to contribute to the IASB's due process and does not necessarily indicate the conclusions that would be reached by EFRAG in its capacity as advisor to the European Commission on endorsement of definitive IFRS Standards in the European Union and European Economic Area.

EFRAG welcomes the IASB's efforts to provide requirements on the amounts to an entity includes in estimating the future expenditure required to settle a provision and the rate an entity uses to discount the future expenditure to its present value. EFRAG generally agrees with these proposals. The proposals on the future expenditure required to settle a provision reduce diversity in practice and are aligned with the requirements on when a contract is onerous. The proposals

on the discount rate are also expected to reduce diversity in practice and EFRAG agrees with prohibiting reflecting non-performance risk in the discount rate as it could result in counterintuitive information. On the proposed amendments to IAS 37 on when an entity has a present obligation [view to be inserted].

EFRAG's detailed comments and responses to the questions in the ED are set out in the Appendix.

If you would like to discuss our comments further, please do not hesitate to contact Isabel Batista, Vasilis Dionelis, Rasmus Sommer or me.

Yours sincerely,

Wolf Klinz

President of the EFRAG FRB

Appendix - EFRAG's responses to the questions raised in the ED

Criteria on when an obligation is present

Notes to constituents – Summary of proposals in the ED

1 The ED proposes to amend the criteria for when to recognise a provision by:

(a) *Updating the definition of a liability in IAS 37 to correspond to the definition included in the Conceptual Framework for Financial Reporting ('the Conceptual Framework').*

(b) *Amending the present obligation criterion to be aligned with the guidance included in the Conceptual Framework. This criterion comprises three requirements:*

(i) ***Requirement 1 - The entity has an obligation**. This involves that there is a mechanism in place that imposes a responsibility on the entity if it obtains specified economic benefits or takes a specified action. The entity owes that responsibility to another party and has no practical ability to avoid discharging the responsibility if it obtains the specified benefits or takes the specified action. Similar to current IAS 37, a present obligation can be legal or constructive.*

- *A legal obligation would typically arise from a contract or legislation. An entity would have no practical ability to avoid discharging its responsibility in relation to a legal obligation if the other party has a legal right to take action against the entity if it fails to discharge the responsibility; and the economic consequences for the entity of not discharging the responsibility are expected to be significantly more adverse than the economic consequences of discharging it.*
- *A constructive obligation could arise when an entity establishes a valid expectation based on for examples past practice.*

(ii) ***Requirement 2 - The entity's obligation is to transfer an economic resource**. An entity can have an obligation to transfer an economic resource if an uncertain future event occurs. The likelihood of the future event does not impact whether an entity has an obligation to transfer an economic resource. However, as the current criterion in IAS 37 requiring that a provision is only recognised when an outflow is probable will be maintained. An obligation to exchange economic resources with another party is not an obligation to transfer an economic resource unless the terms are unfavourable to the entity – for example an onerous contract.*

(iii) ***Requirement 3 - The entity's obligation is a present obligation that exists as a result of a past event.*** *This criterion means, among other things, that no provision is recognised for costs that need to be incurred to operate in the future. A present obligation is only recognised when the entity has obtained economic benefits or taken an action resulting in an obligation and as a consequence, will or may have to transfer an economic resource it would not otherwise have had to transfer.*

The ED specifies that if an entity is required to transfer an economic resource only if it takes two (or more) separate actions, the entity incurs a present obligation when it takes the first action and has no practical ability to avoid taking the other action(s).

The ED also specifies that if an entity is required to transfer an economic resource only if it exceeds a specified threshold, a present obligation arises as the entity carries out the activity for which the specified threshold is related. A provision should thus be recognised for the portion of the total expected obligation before the specified threshold is met if it is also probable that an outflow of resources embodying economic benefits will be required to transfer an economic resource to settle the obligation; and a reliable estimate can be made of the amount of the obligation.

(c) *Withdrawing IFRIC 6* Liabilities arising from Participating in a Specific Market—Waste Electrical and Electronic Equipment *and IFRIC 21* Levies*.*

Question 1

Question on the proposed amendments to the requirements on when a provision exists.

EFRAG's response

[To be included]

2 EFRAG acknowledges that there could be arguments both in favour and against amending the requirements on when a provision exists in line with the proposals included in the ED (present obligation recognition criteria).

3 In favour of the proposals included in the ED, EFRAG notes that:

(a) Input received from users when IFRIC 21 was issues, was that the requirements did not result in useful information. As noted in EFRAG's endorsement advise, levies are often regarded as a charge that relates to a period of time and many believe that a progressive recognition of an expense would be better understood by users. EFRAG

accordingly supported the changes to the Conceptual Framework made in 2018, which the proposals in the ED reflect.

(b) The proposals on when a liability exists in cases where an entity is only required to transfer an economic resource if it takes two (or more) separate actions, seem more consistent with other IFRS requirements (such as the requirements in IAS 12, IAS 19, IFRS 2 and the forthcoming standard on rate-regulated activities) compared to the requirements following from IFRIC 21.

(c) The proposals on when a liability exists in cases where an entity is only required to transfer an economic resource if it takes two (or more) separate actions seem more prudent than the current requirements following from IFRIC 21.

(d) The proposals are also more consistent with the principle of recognising expenses in the same period as the related income and are likely to reduce volatility in the performance statement as the liability and corresponding expense will be recognised ‘’over time’ as the entity starts to undertake the activity on which a liability arises (such as a levy or another threshold-triggered expense rather than a point in time when the threshold is met/exceeded. This means that regardless of whether the entity’s activity (such as generating revenue on which a levy will be imposed once a threshold is met) is below or above the threshold affects the expense (levy) the entity might incur. In other words, an entity whose activity (generating revenue) is closer to the threshold might incur an expense (levy) it would not have incurred without that activity.

(e) As it appears from several academic studies, including a study sponsored by EFRAG[1], the first primary financial statement considered by users is most often the statement of profit or loss. The reported performance of an entity is used to estimate future performance (and cash flows). The performance of an entity included in this statement seems most relevant when expenses are recognised in the same period as the related income. Accordingly, if a levy, for example, depends on two factors: the revenue earned in 20X1 and whether the entity operates on 1 January 20X2, it seems to result in the most useful information for assessing the entity’s performance in 20X1 to recognise the expenses associated with the levy in 20X1 rather than in 20X2 if the entity has no practical ability not to operate on 1 January 20X2. For similar

[1] See https://www.efrag.org/en/news-and-calendar/financial-reporting-publications#23692

reasons, the proposed requirements on when to recognise a provision when an economic resource should only be transferred if the entity exceeds a specified threshold, is assessed to result in more relevant information compared to only recognising a provision when the threshold is reached.

(f) Basing the recognition of a provision for a threshold-triggered expense such as a levy that depends on the entity taking two (or more) separate actions under the requirements of IFRIC 21 could result in an arbitrary recognition of a liability that does not reflect reality. This happens when an entity has already received economic benefits or taken an action and does not have a practical ability to avoid taking the following actions that would trigger the transfer of an economic resource. For example, in the EU, it happens that Member States can decide the date in a year at which an entity should be operating to be covered by a particular levy. If that levy also depends on economic benefits the entity has received in the past year, or an action the entity has taken in the past year, and the entity does not have a practical ability not to operate in the following year, it does not result in comparable information that some entities are recognising a provision for the levy later than others.

4 Against the proposals included in the ED, EFRAG notes that:

(a) Users may now have become used to the manner in which provisions are recognised under IFRIC 21. Changing the requirements may therefore not result in benefits, but only in confusion. Furthermore, some may consider that the requirements under IFRIC 21 to recognise a liability for a levy only once an entity exceeds the specified threshold would be clearer and would represent less judgement in the measurement.

(b) Recognising a provision for a levy following the requirements of IFRIC 21 is not arbitrary as argued in paragraph 3(f) above. The requirements in IFRIC 21 reflect when a liability exists. Recognising a provision following the proposals could result in recognising a liability that would not result in any outflow of economic resources. This could happen, for example:

(i) **When the obligation depends on two or more actions of the entity**, the entity can have taken the first action and assesses that it does not have a practical ability to avoid taking the remaining actions. But then something unexpected can happen (for example, the entity can unexpectedly go bankrupt) and the actions that were once considered practical unavoidable, have been avoided.

(ii) When, for example, a levy (or other **threshold-triggered costs**) depend(s) on the amount of revenue (or other activity) earned above a certain threshold, the proposals will generally result in an entity having to recognise a provision as it earns revenue (below the threshold) if it expects to exceed the threshold. However, some argue that this liability does not really exist. If the entity, does not reach the revenue threshold, it will not have to transfer any economic resources.

(c) The requirements following from IFRIC 21 are quite clear on when to recognise a provision. The proposals, on the other hand, can result in many uncertainties related to, for example:

(i) When an entity does not have a practical ability to avoid taking specified future actions.

(ii) What affects recognition and what affects measurement. For example, if the amount an entity would have to pay under a threshold-triggered costs such as a levy would depend on a threshold such as the amount of revenue generated (the activity), under what circumstances would earning an amount of revenue trigger the recognition of a provision and under what circumstances would the amount of revenue earned affect the measurement of the provision?

5 Based on these arguments [insert EFRAG's initial position or that EFRAG seeks input from constituents on this question].

6 EFRAG appreciates that the proposed requirements on when a **provision exists** is very helpful also for understanding the guidance included in the Conceptual Framework. However, we consider that the following issues need being clarified, should the IASB move forward with the proposals:

(a) When an entity does not have a practical ability to avoid taking an action.

(b) How to distinguish between factors affecting the recognition of a provision and factors affecting measurement.

(c) [Additional issues that can only be identified when the final drafting of the ED is ready].

7 To make the new standard more understandable, we are also suggesting to:

(a) Distinguish requirements related to when the definition of a liability/provision is met (when an obligation exists) and recognition requirements (when to recognise that

obligation). This means that an entity would first assess whether an obligation exists based on the proposed criterion and then assess whether it should be recognised (for example recognise only when it can be reliably measured).

(b) Move specific requirements to the application guidance (how to consider new legislation; restructuring; and when a present obligation exists when an entity is required to transfer an economic resource only if it exceeds a specific threshold (threshold-triggered costs). This suggestion is based on the fact that specific criteria is required to be met for (1) new legislation (virtually certain to be enacted), (2) restructuring (the ED will note specific requirements to be met before a restructuring provision exists and is recognised) and some threshold-triggered costs (where there are two (or more) separate actions.

(c) [issues that can only be identified when seeing the final drafting of the ED]

Costs included in the estimation of the expenditure required to settle a provision

Notes to constituents – Summary of proposals in the ED

8 *The IASB has tentatively decided that the expenditure required to settle the entity's present obligation should be the costs that relate directly to settling that obligation, which consist of both:*

(a) *the incremental costs of settling the obligation; and*

(b) *an allocation of other costs that relate directly to settling obligations of that type.*

9 *A similar requirement was recently included in IAS 37 for the assessment of whether a contract is onerous (when the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received under it, i.e., onerous contract).*

Question 2
Question to the proposed amendments to requirements on costs included in the estimation of the expenditure required to settle a provision.

EFRAG's response

EFRAG generally supports the proposals.

10 EFRAG is generally supportive of the proposed amendments. However, EFRAG considers that it would be useful to include additional application guidance and illustrative examples

on what is considered incremental costs included in the estimation of expenditures required to settle provisions.

The rate to be used to discount future expenditure to their present value and related disclosure requirements

Notes to constituents – Summary of proposals in the ED

Discount rates to be used to discount future expenditure to their present values

11 *The IASB tentatively decided that an entity should discount the estimated future expenditure at a rate that reflects:*

(a) *the time value of money—represented by a risk-free rate—with no adjustment for non-performance risk (i.e., the risk that the entity will not settle the obligation); and*

(b) *risks surrounding the amount or timing of the expenditure required to settle the obligation if those risks are not reflected in the estimates of the cash flows.*

12 *However, the IASB tentatively decided not providing further application guidance on estimating the time value of money for the following reasons:*

(a) *practice is already well-established without any guidance in IAS 37 (e.g., policy of discounting at a risk-free rate or as the starting point for estimating a credit-adjusted rate);*

(b) *provisions within the scope of IAS 37 vary widely in their terms and the circumstances of their settlement; and*

(c) *risk of unintended consequences because several other IFRS Accounting Standards already require assets or liabilities to be measured by reference to risk-free rates.*

13 *This approach would allow/require entities to apply judgement in estimating an appropriate rate. The rate might be determined by reference to the current market yield on a very low risk market investment (for example, a low-risk government bond) in a currency consistent with that of the provision. But adjustments might be required, for example if the provision is of longer duration, or less liquid, than the closest available market investment.*

Disclosure requirements

14 *Furthermore, the IASB tentatively decided to propose requiring an entity to disclose, for each class of provision:*

(a) *the rate or rates used in measuring the provision; and*

(b) *the approach used to determine those rates.*

15 *The IASB reached this proposal as a compromise between:*

(a) *the feedback received from preparers, which mainly highlighted the high level of uncertainty related to very long-term provisions, the costs associated to any additional disclosure and the disclosure overloading risk;*

(b) *the suggestions received by users, which also proposed to require information about the undiscounted amount and timing of the cash flows and a sensitivity analysis to allow them adjusting provisions amount by using other entities' rates; and*

(c) *the fact that this project is limited in the scope (i.e., it only aims to targeted amendments to IAS 37 and to not introduce disclosure requirements besides those already required by other IFRS Accounting Standards).*

Question 3

Question on the proposed amendments to the rate to be used to discount future expenditure to their present value and related disclosure requirements.

EFRAG's response

EFRAG generally supports the proposals.

16 EFRAG expresses overall support for the proposals as they specify that an entity should apply a discount rate that excludes non-performance risk.

17 EFRAG acknowledges that the proposals will remove some of the diversity in practice in relation to discounting provisions. At the same time, diversity in practice will continue to exist with respect to estimating the discount rate.

18 However, as the proposals will also require disclosures on the discount rate used, EFRAG assesses that users will receive sufficient information to be able to compare the provisions of different entities and make any adjustments they consider necessary for their own analysis.

19 EFRAG notes that the [indicative drafting of] the ED only states that non-performance risk should not be reflected in the discount rate. To avoid confusion, EFRAG suggests the ED also states that non-performance risk is not to be included in the expected cash flows of the related provisions either.

20 Moreover, EFRAG notes that some types of rate-regulated entities could be significantly affected by the proposals as they have long-term provisions. Some of these entities are required to set aside funds for the amounts of provisions. Sometimes other regulation describes how the discount rate should be determined for this purpose. When this is the

case, EFRAG considers that these entities should be allowed to use that discount rate also used for other regulatory purposes which has a real economic impact on the entity.

21 Lastly, EFRAG considers the IASB should specify whether inflation should be reflected in the discount rate. Whether or not inflation is reflected in the discount rate has implications for whether the expenses related to the unwinding of the discounting are considered operating expenses.

Implementation guidance

Notes to constituents – Summary of proposals in the ED

22 It is expected that the IASB will provide implementation guidance in the form of examples.

Question 4

Question on the proposed amendments to implementation guidance.

EFRAG's response

[EFRAG generally supports the proposed amendments to the implementation guidance. However, this is subject to our position in response to Question 1 and to seeing the drafting in the ED]

23 [General support, however, subject to answer to Question 1 and to seeing the ED].

Transition requirements

Notes to constituents – Summary of proposals in the ED

24 [Note to EFRAG FR TEG members: Please note that this section will be shortened for the draft comment letter. It is extensive because it is the first time these specific proposals are brought for discussion in an EFRAG FR TEG meeting.]

25 The IASB tentatively decided to not propose in the ED specific transition requirements for the amendments to the requirements supporting the present obligation recognition criterion. The IASB considered that retrospective application of those amendments is likely to be practicable for most entities, and that the benefits of retrospective application are likely to exceed the costs. This view was based on the IASB's understanding that:

(a) *the types of costs for which a change in accounting policy is most likely to be required (levies and similar costs) are typically recurring charges—often recurring annually. With prospective application, an entity might recognise two annual charges as expenses the period of initial application of the amended requirements, and no charges as expenses in the comparative period. The income statements for the*

current and comparative periods would not be comparable and would not provide a faithful representation of the entity's financial performance in either period.

(b) *the types of costs for which a change in accounting policy would be required are typically recognised as expenses when the provision is recognised, or included in the cost of inventory—they are typically not added to the costs of property, plant and equipment or other long-term assets. So retrospective application would not require an entity to gather information about transactions occurring long before the start of the comparative period.*

26 *The IASB tentatively decided to propose in the ED that an entity apply the proposed amendments retrospectively in accordance with IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors, with two exceptions.*

27 *With respect to the amendments to the discount rate, the IASB noted that, at present, some entities discount asset decommissioning and environmental rehabilitation provisions at rates that reflect some degree of non-performance risk. Such entities would need to change their accounting policy to use a lower rate than they have used in previous periods.*

28 *The change in accounting policy would result in those entities recognising a larger provision. In some cases, the entity would recognise the corresponding debit as an expense. But in many cases, they would recognise it as an addition to the cost of the property, plant or equipment (PPE) to which the decommissioning or rehabilitation obligation relates.*

29 *The IASB further considered that where the cost of fulfilling an asset decommissioning or environmental rehabilitation obligation is added to the cost of the related PPE, applying a change in the basis for determining the discount rate fully retrospectively could be difficult. It would require the entity to gather or reconstruct information generated from the time of initial recognition of the provision—which could be decades in the past if the provision relates to the decommissioning of long-lived assets.*

30 *A particular complication arose because IAS 37 requires an entity to measure a provision using current estimates of the cash outflows required to settle the provision and a current market assessment of the time value of money:*

(a) *the measure of an asset decommissioning or environmental rehabilitation provision can therefore fluctuate from one reporting date to the next because of changes in estimates of the cash outflows or of current market interest rates; and*

(b) *IFRIC 1 Changes in Existing Decommissioning, Restoration and Similar Liabilities requires such changes to be added to, or deducted from, the cost of the related PPE—*

and recognised in the income statement prospectively as that PPE is depreciated over its useful life or when it is judged to be impaired. Consequently, the amount of decommissioning costs recognised in the carrying amount of PPE at the date of transition would depend on when and how estimates of the future cash outflows and market interest rates had fluctuated from the date the decommissioning obligation arose.

31 *This means that pure retrospective application of a change in the basis for determining the discount rate for the provision would require an entity to construct a historical record of all the adjustments that would have been made to PPE at each reporting date between initial recognition of the provision and the date of transition—applying the new-basis discount rate current at each reporting date to the estimates of the cash outflows current at that date. The entity would need to determine the historical discount rates from historical records of market interest rates. And if it had not kept a record of its estimates of the cash outflows and amounts of impairment losses recognised, from the date of initial recognition of the provision, it would need to reconstruct those estimates and amounts on the basis of the information it would have had at the time (that is, without the use of hindsight).*

32 *Therefore, as the IASB considered that full retrospective application would be impractical, the IASB tentatively decided to propose in the ED an exception to the retrospective application, to the discount rate requirements affecting provisions for asset decommissioning, restoration or similar costs that are added to the cost of the related asset. The exception would permit an entity to apply a simplified retrospective approach, whereby in the year of transition the entity would:*

(a) *apply the amended requirements in IAS 37 to restate the provision at the start of the first period for which it provides comparative information; and*

(b) *apportion the amount by which it adjusts the provision at that date between the related asset and retained earnings:*

(i) assuming the current discount rate(s) and estimates of cash flows used in measuring the provision have not changed since the provision was first recognised; and

(ii) using current estimates of the useful life of the related asset.

33 *When it comes to costs included in the measurement of the expenditure required to settle a provision, the IASB tentatively decided to propose a second exception. This exception would require an entity to apply the proposed amendment:*

(a) *only to obligations that exist on, or arise after, the beginning of the annual reporting period in which the entity first applies that amendment.*

(b) *without restating comparative information. Instead, the entity would recognise the cumulative effect of applying the amendment as an adjustment to the opening balance of retained earnings or other component of equity, as appropriate, at the date of initial application.*

34 This exception is based on the modified retrospective application introduced in the 2020 amendments to IAS 37 on onerous contracts.

35 *Lastly, the IASB tentatively decided to propose in the ED to make no amendments to IFRS 1 First-time adoption of International Financial Reporting Standards as a result of the amendments proposed in this project and not introduce any transition requirements for the proposed amendments to IFRS 3.*

Question 5

Question on the transition requirements included in the proposals.

EFRAG's response

[To be included]

36 EFRAG agrees with not proposing transition requirements for the amendments to the present obligation recognition criterion, and with the proposed transition requirements for the proposed amendments to the discount rate and costs included in the measurement of a provision.

37 In addition, EFRAG highlights that the illustrative example provided in the Appendix of IASB staff paper 22b (June 2024) should constitute part of the proposed amendments, to further clarify the proposed simplified retrospective approach.

38 EFRAG also agrees with the proposal to make no amendments to IFRS 1 as a result of the amendments proposed in this project and to not propose any transition requirements for the amendments to IFRS 3.

Proposed amendments to IFRS 19 Subsidiaries without Public Accountability: Disclosures

Notes to constituents – Summary of proposals in the ED

39 [Note to EFRAG FR TEG members: Please note that this section will be shortened for the draft comment letter. It is extensive because it is the first time these specific proposals are brought for discussion in an EFRAG FR TEG meeting.]

40 *The IASB tentatively decided to propose in the ED to add to IFRS 19 Subsidiaries without Public Accountability: Disclosures a requirement for an entity to disclose the discount rate(s) used in measuring a provision, but not to add to IFRS 19 a requirement for an entity to disclose the approach used to determine the rate(s).*

41 *Moreover, information about the rates used to discount estimates of future cash flows are consistent with the principle for measurement uncertainty which is one of the principles the IASB is expected to apply when considering whether new or amended disclosure requirements in IFRS Accounting Standards should be included in IFRS 19.*

42 *It is also noted that IFRS 19 includes most of the requirements in other accounting standards to disclose discount rates, for example the requirements in IAS 36, IFRS 17 are directly required, whereas the requirements in IAS 19 and IFRS 2 are indirectly required through the disclosure of actuarial assumptions or inputs. In addition, IFRS 19 includes all the other disclosure requirements in IAS 37.*

43 *The IASB considered that it would therefore be consistent with the current requirements in IFRS 19 to require disclosure of the discount rate used in measuring provisions. The IASB further considered whether to include the proposed requirement to disclose the approach used to determine the discount rate. When deciding to propose requiring an entity to disclose the approach used, the IASB considered that even in estimating a risk-free rate, there is scope for varying approaches to be used and, especially for large long-term provisions, information about the rates an entity has used and the approach it has used to determine these rates is likely to be material.*

44 *Although it could be argued that information about the approach used to determine the discount rate is equally relevant for entities in the scope of IFRS 19, the IASB noted that with the exception of IFRS 17, none of the other requirements in IFRS 19 require disclosure of the approach used to determine the discount rate. The IASB therefore proposed not to include this proposed requirement in IFRS 19.*

Question 6

Question on the proposed amendments to IFRS 19 *Subsidiaries without Public Accountability: Disclosures*

EFRAG's response

[To be included]

45 EFRAG understands that barring IFRS 17, none of the other requirements in IFRS 19 require disclosure of the approach used to determine the discount rate. EFRAG also considers that as provisions can often be very large and long-term (e.g., decommissioning provisions), information about the approach an entity has used to determine the discount rate of provisions is likely to be material. As such, EFRAG also sees merit in the proposal to require information about the approach used to determine the discount rate for entities in the scope of IFRS 19.

46 On the other hand, EFRAG notes that for most entities, the manner in which provisions are discounted may not be particularly significant and allowing entities under IFRS 19 not to provide information on the estimation of discount rate could reduce costs for preparers.

47 Taking the above into consideration, EFRAG, on balance, supports the proposed amendments to IFRS 19.

Proposed amendments to IFRS 3 Business Combinations

Notes to constituents – Summary of proposals in the ED

48 [Note to EFRAG FR TEG members: Please note that this section will be shortened for the draft comment letter. It is extensive because it is the first time these specific proposals are brought for discussion in an EFRAG FR TEG meeting.]

49 Until 2020, IFRS 3 referred to an old version of the Conceptual Framework, which the International Accounting Standards Committee had issued in 1989. However, in 2020, the IASB updated the reference so that IFRS 3 now refers to 2018 Conceptual Framework.

50 The recognition requirements in IAS 37 and IFRIC 21 are not consistent with those of the 2018 Conceptual Framework. Specifically, some items that satisfy the present obligation recognition criterion as it is described in the 2018 Conceptual Framework do not meet that criterion as described in IAS 37. Consequently, updating the IFRS 3 reference to the Conceptual Framework could have required acquirers to recognise on the acquisition of a business liabilities that they would be required to derecognise subsequently (resulting in 'day 2' gains).

51 To avoid this outcome, the IASB made a second amendment to IFRS 3 when it updated the reference. It added to IFRS 3 an exception to the initial recognition principle. The exception applies to liabilities and contingent liabilities that would be within the scope of IAS 37 or IFRIC 21 if they were incurred separately rather than assumed in a business combination. It specifies that an entity applies IAS 37 or IFRIC 21 (not the 2018 Conceptual Framework) to determine whether to recognise a liability for those items at the acquisition date.

52 The exception is set out in paragraphs 21A–21C in IFRS 3:

(a) *Paragraph 21A: Paragraph 21B applies to liabilities and contingent liabilities that would be within the scope of IAS 37 Provisions, Contingent Liabilities and Contingent Assets or IFRIC 21 Levies if they were incurred separately rather than assumed in a business combination.*

(b) *Paragraph 21B: The Conceptual Framework for Financial Reporting defines a liability as 'a present obligation of the entity to transfer an economic resource as a result of past events'. For a provision or contingent liability that would be within the scope of IAS 37, the acquirer shall apply paragraphs 15–22 of IAS 37 to determine whether at the acquisition date a present obligation exists as a result of past events. For a levy that would be within the scope of IFRIC 21, the acquirer shall apply IFRIC 21 to determine whether the obligating event that gives rise to a liability to pay the levy has occurred by the acquisition date.*

(c) *Paragraph 21C: A present obligation identified in accordance with paragraph 21B might meet the definition of a contingent liability set out in paragraph 22(b). If so, paragraph 23 applies to that contingent liability.*

53 The IASB considers that the proposed amendments would eliminate the inconsistency between the IFRS 3 recognition principle and IAS 37 recognition criteria, rendering the exception in IFRS 3 redundant. Therefore, the IASB tentatively decided to delete paragraphs 21A–21C from IFRS 3 Business Combinations, thereby removing the exception to the recognition principle in IFRS 3.

Question 7

Question on proposed amendments to IFRS 3 *Business Combinations*.

EFRAG's response

EFRAG agrees with the proposed amendments to IFRS 3 *Business Combinations*.

54 EFRAG agrees with the proposed amendments to IFRS 3 as the exception in IFRS 3 is rendered redundant due to the proposed amendments to IAS 37.