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Dynamic risk management

Cover note

Objective

- 1 The objective of this session is to provide an update to EFRAG FRB and FR TEG members on the development of the DRM project in recent months and to ask for their views concerning the timing and the approach to field testing.

Project status

- 2 The project was added to the standard-setting programme in May 2022 and the IASB has since then further developed the DRM model.
- 3 From June till September 2024, the IASB has discussed and took tentative decisions related to various aspects of the DRM model as follows:
 - (a) June 2024 IASB meeting - capacity assessment, presentation requirements, disclosure requirements (discussions only, no tentative decisions were made on disclosures);
 - (b) July 2024 IASB meeting – applicable risk management activities for the DRM model, optional application of the DRM model;
 - (c) September 2024 IASB meeting – disclosure requirements, discontinuation of the DRM model.
- 4 Most of these topics have been discussed at EFRAG FIWG meeting on 2 September 2024 and at EFRAG FR TEG meeting on 7 October 2024. Also, feedback on some of these topics, notably applicable risk management activities for the DRM model was received at EFRAG IAWG meeting on 9 September 2024 where the IASB DRM team presented the DRM model and the current status of the project to EFRAG IAWG members.

- 5 One key concern which was raised during those meetings is that the DRM model as being developed now will not be applicable by insurers, whilst the insurance industry needs such a model as a solution for their accounting issues. This issue was raised by multiple stakeholders from the insurance industry. On the contrary, the IASB's approach at the moment is to focus on a narrow-scope target (interest rate risk management which reflects predominantly risk management practices of banks) and to address the needs of the insurance industry at a later stage. For this purpose, at its July 2024 meeting the IASB tentatively decided to include a specific question for insurers in the prospective DRM exposure draft to collect more information about their risk management strategies and activities.
- 6 At its October 2024 meeting, the IASB is expected to discuss the remaining issues of the DRM, including transition requirements, thus concluding its deliberations of the DRM.
- 7 The IASB is expected to publish the Exposure Draft late in H1 2025.

Field testing – timing and approach

- 8 In order to give assurance that the proposed DRM model is operationally feasible and provides acceptable mitigation of accounting volatility, field testing is essential. This was also supported by EFRAG FIWG and EFRAG FR TEG in previous discussions.
- 9 The field testing is expected to be a time-consuming process which will require significant resources from the parties involved. At this stage, given the direction of the DRM project, the DRM model should first be tested by banks.

Timing of the field testing

- 10 As previously mentioned, the Exposure Draft is currently expected to be published late in H1 2025.
- 11 One view on the timing is that the Exposure Draft is needed first before field testing can be performed because it will have the proposed draft accounting requirements rather than focusing the field test on IASB tentative decisions (and IASB staff papers). This would imply that the field testing may start shortly after the Exposure Draft is published.
- 12 However, according to the IASB discussions, all key tentative decisions concerning the current stage of the DRM have already been taken (the last ones are expected at the October 2024 IASB meeting. Therefore, as an alternative, the field testing, at least some of its preliminary stages¹, could already be launched, to the extent possible, on the basis of

¹ Such preliminary activities could include, for instance, analysis of risk management practices and data flows necessary to deal with the DRM model.

the tentative decisions taken by the IASB (they are summarised in the IASB staff paper provided for this session as background information – Agenda Paper 08-02). Such an approach could save time for the field testing and therefore, could relieve some time pressure at a later stage of the field testing, i.e. after the Exposure Draft is published.

- 13 *EFRAG Secretariat recommendation* – In order to avoid any misinterpretations or unintended consequences relating to the IASB’s tentative decisions, the EFRAG Secretariat recommends that the field testing be conducted once the Exposure Draft is published. Prior to the Exposure Draft being published, the EFRAG Secretariat may do preparatory work also considering the approach to field testing below.

Approach to the field testing

- 14 On the basis of discussions with some stakeholders, below are some of approaches to field testing which can be considered. Please see below a table which summarises the key features of these approaches.

Approach	Intensity per bank	Confidentiality concerns	Cost per bank	How simple to organise?
Single bank	High	High	Medium	Simple
Small number of banks (call for volunteers)	High	High	High	Medium
Fictive bank	Medium	Low	Low	Difficult

- 15 *Single bank* – One bank is selected to perform the field testing on their banking book.
- 16 *Small number of banks* – Similar to the extensive field test done for IFRS 17 endorsement, there was [a call for volunteer entities](#) to perform the exercise.
- 17 *Fictive bank* – a hypothetical set of data is constructed by the participants for the purpose of the exercise.
- 18 The EFRAG Secretariat considers that the best approach would be to start with a single bank, involving, where possible, further participants at a later stage, e.g. during the endorsement stage, as this will allow to demonstrate challenges of the DRM model, both accounting and operational, in a real-life environment. However, concerns regarding organisation, confidentiality and costs to the participants are to be taken into account.

- 19 On the contrary, the EFRAG Secretariat does not consider the fictive bank as a useful approach as, despite its benefits (of being less costly, simpler in organisational terms and would address confidentiality concerns), it will likely not demonstrate all of the issues which may arise later when the DRM model is actually applied by the entities to the real life banking book nor will the fictitious bank have the risk management or accounting systems to run the data.

Questions for EFRAG FRB and FR TEG

- 20 Do you have any comments or questions regarding the actual status of the DRM project?
- 21 When do you consider that field-testing should be conducted?
- 22 Referring to the table in paragraph 14, what is your preferred approach to the field testing? Please explain why.

Next steps

- 23 The EFRAG Secretariat will continue to monitor the IASB developments on the project and provide update to the EFRAG FIWG, EFRAG IAWG, EFRAG FR TEG and EFRAG FRB. Also, the EFRAG Secretariat will further communicate with the stakeholders in what concerns the field testing.

Agenda papers

- 24 In addition to this cover note, the following paper is uploaded for this session as background information:
- (a) Agenda paper 08-02 – AP4: Cover note (the IASB’s agenda paper for the September 2024 meeting – summary of the IASB’s tentative decisions to date).