

IFRS Interpretations Committee
Columbus Building, 7 Westferry Circus
Canary Wharf, London E14 4HD, UK

6 March 2025

Dear Members of the IFRS Interpretations Committee,

I am writing to submit an enquiry regarding the interpretation of transaction costs under IFRS 9.

Appendix A to IFRS 9 defines transaction costs as “incremental costs that are directly attributable to the acquisition, issue or disposal of a financial asset or financial liability.” It further clarifies that “an incremental cost is one that would not have been incurred if the entity had not acquired, issued or disposed of the financial instrument.”

A key source of ambiguity lies in the interpretation of the term *incremental*. Specifically, the uncertainty arises as to whether:

- **Transaction costs must be directly triggered by the signing of the contract (View 1):**

Should incremental costs be interpreted strictly as those arising solely as a result of the signing of the contract that establishes the financial instrument? Under this view, costs would only qualify as "incremental" if they were directly triggered by the contract's execution and would not have been incurred otherwise.

- **Preparatory costs incurred prior to contract signing also qualify as “incremental” (View 2):**

Alternatively, does the definition extend to preparatory costs incurred prior to contract signing, provided these costs are directly attributable to the prospective financial instrument? This interpretation would allow for the inclusion of such costs even if they would have been incurred regardless of whether the financial instrument was ultimately acquired or issued.

The implementation guidance to IFRS 9 briefly states that transaction costs include fees and commissions paid to third parties as well as various levies (IFRS 9.B5.4.8). However, it provides no further clarification on the meaning of *incremental*, leaving the question of which of the two views is correct unresolved.

Separately, another section of the implementation guidance (IFRS 9.B5.4.1–B5.4.3) provides extensive discussion on fees exchanged between parties to a financial instrument. However, it is important to note that such fees are distinct from transaction costs. As indicated in the definition of the effective interest rate in Appendix A to IFRS 9, fees are exchanged between the parties to a financial instrument. Conversely, transaction costs are incurred to third parties who are not part of the contractual relationship giving rise to the financial instrument.

Furthermore, if View 2 is deemed appropriate, an additional question arises concerning the treatment of costs incurred in a reporting period that precedes the origination of a financial instrument.

To illustrate this issue, consider the following scenario:

An entity (a borrower) intends to enter into a loan agreement with a bank in 20X2. Both the borrower and the bank have a 31 December year-end.

In 20X1, the borrower incurs legal and advisory fees while analysing the terms and conditions of the proposed loan. The borrower intends to proceed with the agreement, but the loan contract has not been signed as of the authorisation date of the 20X1 financial statements.

Similarly, in 20X1, the bank incurs professional fees for valuing a property that would serve as collateral for the loan. These costs are incurred during the process of preparing a loan quote. However, as with the borrower, the loan contract remains unsigned by the reporting date.

The question arises: how should the costs incurred in 20X1 be accounted for in the financial statements of the respective parties, given that the loan contract has not been signed and may never be executed? Specifically, should the 20X1 costs be:

- **Option A:** Expensed in profit or loss in 20X1 as incurred, without subsequent reinstatement as part of the amortised cost of the loan, even if the loan is eventually signed.
- **Option B:** Expensed in profit or loss in 20X1 as incurred, but later reinstated as part of the amortised cost of the loan if the loan is ultimately signed.
- **Option C:** Recognised as an intangible asset in 20X1. They would later be included in the amortised cost of the loan or expensed in profit or loss if it becomes unlikely that the loan contract will be signed. (Alternatively, should a different probability threshold be applied in determining the treatment?).
- **Option D:** Treated in another manner entirely?

This issue has been frequently raised in queries on the IFRS Community forums ([example](#)). During my research, I found that the IFRS Staff have also identified diversity in practical application as part of the “Primary Financial Statements” project ([source](#)). Specifically:

Many of those respondents said that there is diversity in practice in how entities identify incremental expenses and similar concepts applying existing Accounting Standards. A few respondents asked the IASB to clarify [...] whether legal and advisory fees incurred in purchasing an investment are incremental, considering that often (part of) these fees would still be due even when the transaction does not go ahead.

It's worth noting that, in the EU alone, total outstanding loans to non-financial corporations and households amounted to EUR 13.6 trillion as of the 2023 year-end ([source](#)). If we assume, conservatively, that transaction costs represent approximately 0.1% of loan amounts, then the transaction costs associated with outstanding loans at any given time would amount to approximately EUR 14 billion in the EU alone.

Given the extensive use of financial instruments globally, this issue has significant and widespread implications, with the potential to materially impact affected parties. Nevertheless, I believe the matter can be resolved effectively within the framework of existing IFRS Accounting Standards and the Conceptual Framework for Financial Reporting.

Thank you for your attention to this matter.

Yours sincerely,

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