International Financial Reporting Standards

IFRS 9
Financial Instruments

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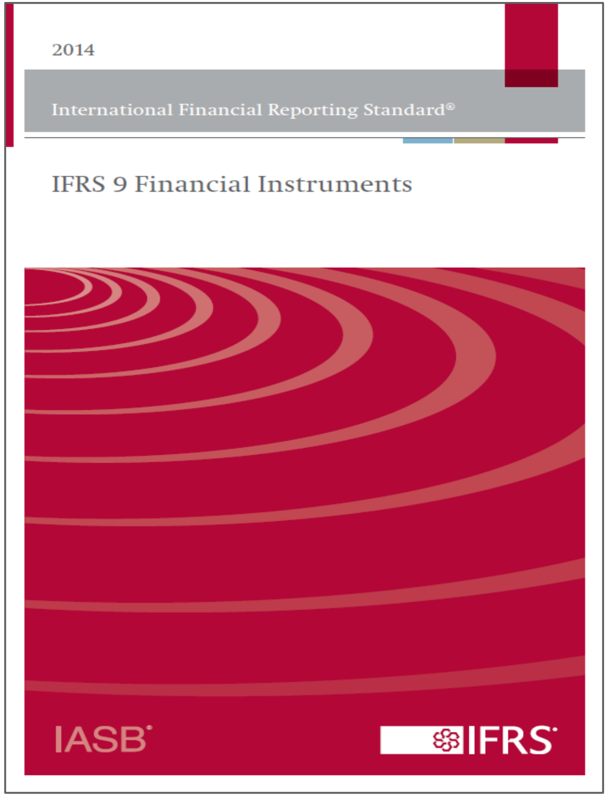
Finalisation of the IASB's response to the global financial crisis



Classification and measurement

A logical, single classification approach driven by cash flow characteristics and how it's managed

Impairment

An much needed and strongly supported forward-looking 'expected loss' model

Hedge accounting

An improved and widely welcomed model that better aligns accounting with risk management

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Classification and measurement

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The IFRS 9 classification model for assets

	Business model = hold to collect	Business model = hold to collect and sell	Other business models
Cash flows are solely payments of principal and interest (SPPI)	Amortised cost	FVOCI* NEW	FVPL
Other types of cash flows	FVPL	FVPL	FVPL

*Excludes equity investments. Can elect to present FV changes in OCI.

Clarification to business model

- Reflects how financial assets are managed to generate cash flows
- Typically observed through activities undertaken to achieve business objective(s) and manage risk
- Sales not determinative
  - However, provides source of evidence
- Business model assessment includes expectations about future
  - Don’t consider worst-case scenarios

Clarifications to cash flow characteristics

- Clarified principal and interest concept
  - More aligned with what is commonly viewed as 'simple instruments'
- Interest – not only time value and credit risk
  - Notion of a basic lending arrangement
- Exception for regulated rates
- 'Principal' = amount transferred by holder (fair value)
- Test for a modified economic relationship
  - Now 'significant' rather than 'insignificant' difference compared to benchmark
  - Qualitative or quantitative

Financial liabilities – ‘own credit’

designated under fair value option (FVO)

Financial statements – IFRS 9		
Balance sheet	*P&L*	
Financial liabilities –FVO — Full FV	Gain or loss	all FV Δ except own credit
	OCI	
	Gain or loss	FV Δ due to ‘own credit’*

* Not recycled

- Otherwise, **P&L gain when ‘own credit’ deteriorates**, loss when it improves
- ***Required* by IFRS 9** for liabilities under the FVO
- **IFRS 9** allows the ‘own credit’ requirements to be early applied in isolation

Treatment of financial liabilities is carried forward from IAS 39 essentially unchanged

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Impairment

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Overview of the requirements

Change in credit quality since initial recognition

	Stage 1 *'Performing'*	Stage 2 *'Under-performing'*	Stage 3 *'Non-performing'*
Expected credit losses ('ECL') recognised	12-month ECL	Lifetime ECL	Lifetime ECL
Interest revenue	Gross basis	Gross basis	Net basis

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Scope of the impairment requirements

- Financial assets measured at amortised cost
- Financial assets measured at FVOCI
- Lease receivables
- Trade receivables and contract assets
- Loan commitments and financial guarantee contracts not measured at FVPL

Financial assets measured at FVOCI

Financial statements – IFRS 9			
Balance sheet		*P&L*	
Financial asset - FVOCI	Full FV	Interest, impairment etc	Same as for amortised cost
		OCI	
		Gain or loss	FV Δ Other than those recognised in P&L

- Financial assets measured at FVOCI recognised in balance sheet at FV
- Loss allowance does not reduce carrying amount, but is recognised in OCI
- P&L information is the same as for financial assets measured at amortised cost

Amounts accumulated in OCI are recycled to P&L upon derecognition

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Key clarifications

- Enhanced responsiveness to changes in credit risk
  - Recognise lifetime expected credit losses on all significant increases in credit risk, whether individual or collective
- Provided solutions to noted operational concerns:
  - Don't require mechanistic approach
  - Assessment compared to initial maximum credit risk on homogeneous portfolios
  - Counterparty assessment if it meets objectives of model
- Rebuttable presumption of 90 days past due for default
- Can use an expected life for some loan commitments such as revolving credit facilities

Disclosures

Quantitative

- Reconciliation of allowance accounts showing key drivers for change
- Explanation of gross carrying amounts showing key drivers for change
- Gross carrying amount per *credit risk grade or delinquency*
- Write-offs, recoveries, modifications

Qualitative

- Inputs, assumptions and techniques used to estimate expected credit losses (and changes in techniques)
- Inputs, assumptions and techniques used to determine ‘significant increase in credit risk’ and ‘default’
- Inputs, assumptions and techniques used to determine ‘credit-impaired’
- Write off policies, modification policies, collateral

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Hedge accounting

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A better link between accounting and risk management

IFRS 9 incorporates a major overhaul of hedge accounting that more closely aligns accounting with risk management.

New requirements were first published in 2013, and are updated in the final publication for FVOCI measurement category.

- Align accounting treatment with risk management activity
- Enable **preparers** to better reflect hedging in financial statements
- Provide disclosures to help **users** understand risk management and its impact on the financial statements

Project doesn't address macro hedging

Even if apply IFRS 9 can still use specific portfolio hedge accounting requirements in IAS 39

For now entities can choose to keep using IAS 39 hedge accounting

IAS 39 hedge accounting

Accounting policy choice

IFRS 9 hedge accounting

Some banks may not make any changes to their hedge accounting at this time

- The IASB is simultaneously working on a specific project to consider accounting for macro hedges (Discussion Paper published)

Implementation of IFRS 9

Annual periods beginning on or after 1 January 2018

- Mandatory effective date consistent with stakeholder requests
- Entities permitted to early apply the completed (whole) version of IFRS 9
- Previous versions of IFRS 9 phased out:
  - Not permitted to early apply a previous version unless the relevant date of initial application is before 1 February 2015
- 'Own credit' requirements available for early application, in isolation, until the mandatory effective date
- Transition Resource Group for Impairment of Financial Instruments (ITG)

Questions and comments