



**Analyst Representative
Group**

Agenda
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Date **June, 2009**

Topic **Derecognition**

This paper has been prepared for discussion at a public meeting of the Analyst Representative Group of the IASB.

The views expressed in this paper are those of the authors.

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The tentative decisions made by the IASB at its public meetings are reported in IASB Update. Official pronouncements of the IASB, including Discussion Papers, Exposure Drafts, IFRSs and Interpretations are published only after it has completed its full due process, including appropriate public consultation and formal voting procedures.

Exposure Draft *Derecognition*

Proposed amendments to IAS 39 and IFRS 7

June 2009

The views expressed in this presentation are those of the presenter,
not necessarily those of the IASC Foundation or the IASB



Agenda

- Proposed derecognition approach for financial assets
- Alternative derecognition approach for financial assets
- Examples
- Proposed disclosure requirements
- Next steps
- Questions for the ARG



Proposed approach

Derecognise a financial asset (or a specified part thereof) if...

Contractual rights to the cash flows expire

Transfer + no continuing involvement

OR

Transfer + continuing involvement, but transferee has practical ability to transfer the asset (or part) for its own benefit



Alternative approach

Derecognise a financial asset if...

no longer *present access, for own benefit*, to *all* of the cash flows or other economic benefits of the asset.

Implications

Rights to some or all
CFs are transferred



Derecognise the
entire asset

Any involvement
retained/obtained



FV (initially) as
a new asset/liability

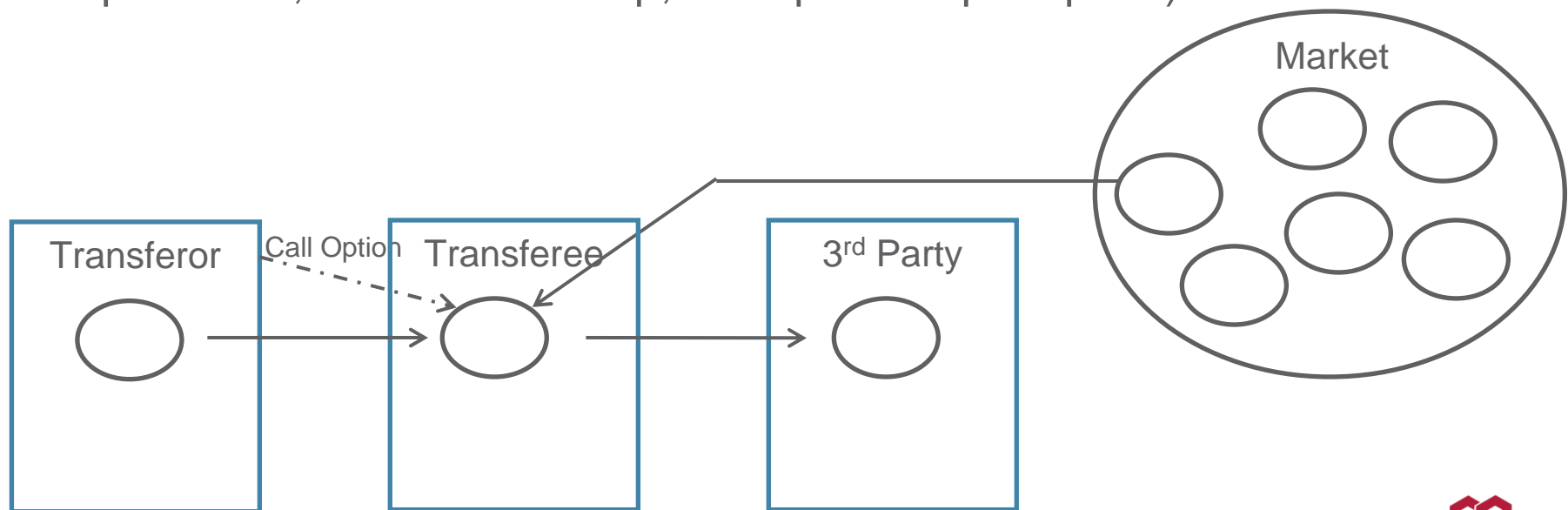


Examples: Readily-obtainable FAs

Facts

An entity:

- transfers a publicly-traded government bond and
- as part of the transfer, enters into a derivative (eg forward purchase, total return swap, call option or put option)



Examples: Readily-obtainable FAs

Analysis – PROPOSED APPROACH

The Asset?	Bond
Continuing involvement?	Yes, derivative (forward, total return swap or call/put option)
Transferee practical ability to transfer for own benefit?	Yes, derivative does not restrict transferee from selling the bond (could readily obtain a replacement bond upon settlement of the derivative). Also, transferee can keep all of sales proceeds for itself (no obligation to pass them onto transferor).
Accounting outcome?	Derecognition of bond + recognition of derivative



Examples: Readily-obtainable FAs

Analysis – ALTERNATIVE APPROACH

Present access to all CFs?	No
Accounting outcome?	Derecognition of bond + recognition of derivative

Same outcome under proposed and alternative approach if transfer involves readily-obtainable (entire) financial assets!

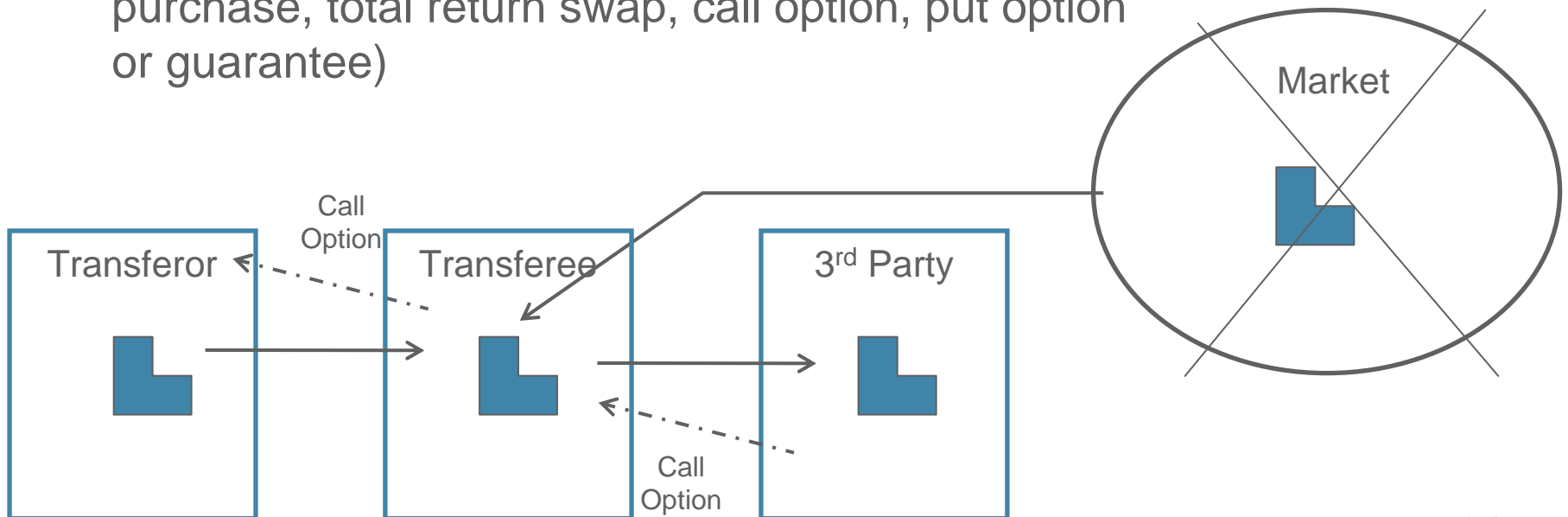


Examples: Not readily-obtainable FAs

Facts

An entity:

- transfers a loan it originated and
- as part of the transfer, enters into a derivative (eg forward purchase, total return swap, call option, put option or guarantee)



Examples: Not readily-obtainable FAs

Analysis – PROPOSED APPROACH

The Asset?	Loan
Continuing involvement?	Yes, derivative (forward, total return swap or call, put or guarantee)
Transferee practical ability to transfer for own benefit?	No, derivative restricts transferee from selling the bond (would have to default upon settlement of the derivative (forward, total return swap, call) or would forfeit the value of the derivative (put or guarantee))
Accounting outcome?	No derecognition



Examples: Not readily-obtainable FAs

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Analysis – ALTERNATIVE APPROACH

Present access to all CFs?	No
Accounting outcome?	Derecognition of loan + recognition of derivative

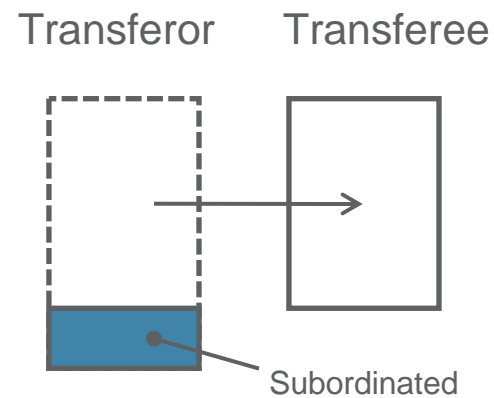
Different outcome under proposed and alternative approach if transfer involves NOT readily-obtainable (entire) financial assets!



Examples: Disproportionate interest

Facts

An entity transfers the right to the *first* 90% of cash flows from a loan portfolio



Examples: Disproportionate interest

Analysis – PROPOSED APPROACH

The Asset?	Loan portfolio (first 90% is a disproportionate interest)
Continuing involvement?	Yes, residual interest (last 10%)
Transferee practical ability to transfer for own benefit?	No, in light of transferor's residual interest, transferee cannot sell the loan portfolio
Accounting outcome?	No derecognition



Examples: Disproportionate interest

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Analysis – ALTERNATIVE APPROACH

Present access to all CFs?	No
Accounting outcome?	Derecognition of loan portfolio + recognition of residual interest

**Different outcome under
proposed and alternative
approach if transfer
involves a portion of a
financial asset!**



Examples: Residential mortgage-backed securitisation

Facts

- Originator transfers CU265mn loans to SPE
- SPE finances purchase of loans through issuance of senior, mezzanine and junior notes to unrelated third-party investors
- SPE restricted from selling the loans
- Originator services the loans for at-market fee
- Originator funds a CU4mn reserve fund for liquidity/credit support
 - Fund is replenished from excess spread of (a) CFs from loans less (b) CFs to noteholders and to pay SPE's expenses
 - CFs collected above required level go to originator (also, originator gets residual in fund upon liquidation of SPE)



Examples: Residential mortgage-backed securitisation

Analysis – PROPOSED APPROACH

Reporting entity?	Originator
The Asset?	Loan portfolio (originator has a residual interest through reserve fund)
Continuing involvement?	Yes, reserve fund
Transferee practical ability to transfer for own benefit?	No because SPE is restricted from selling the loan portfolio
Accounting outcome?	No derecognition

If reporting entity = group (originator + SPE), analyse issuance of BIs as transfer. Same acctg outcome!



Examples: Residential mortgage-backed securitisation

Analysis – ALTERNATIVE APPROACH

Reporting entity?	Originator
Present access to all CFs?	No
Accounting outcome?	Derecognition of CU265mn loans + recognition of CU4mn residual interest (reserve fund)

If reporting entity = group (originator + SPE), analyse issuance of BIs as transfer. Same acctg outcome!



Examples: Distressed debt

Facts

- Subsidiary transfers CU20bn loans to SPE
- SPE finances purchase of loans through
 - CU15bn non-recourse loan by parent of subsidiary
 - CU5bn equity investment by unrelated third-party investor (equity is at first risk of loss)
- Unrelated third party services the loans for at-market fee (investor can remove the servicer without cause)



Examples: Distressed debt

Analysis – PROPOSED APPROACH

Reporting entity?	Group (parent consolidates subsidiary, third-party investor consolidates SPE)
The Asset?	Loan portfolio (group has a net senior interest through non-recourse loan)
Continuing involvement?	Yes, non-recourse loan
Transferee practical ability to transfer for own benefit?	No because of group's senior interest through non-recourse loan
Accounting outcome?	No derecognition

**But:
Derecognition
in sub's stand-
alone f/s!**



Examples: Distressed debt

Analysis – ALTERNATIVE APPROACH

Reporting entity?	Group (Parent consolidates subsidiary, third-party investor consolidates SPE)
Present access to all CFs?	No
Accounting outcome?	Derecognition of CU20bn loans + recognition of CU15bn senior interest (nonrecourse loan)



Examples: Multi-seller conduit

Facts

- Credit card operators, retailer and leasing company each transfer (on an ongoing basis) receivables into an SPE in exchange for cash + residual interest in assets transferred
- SPE funds purchase of receivables by issuing commercial paper
- Bank acts as:
 - Administrator (eg evaluates + enters into asset purchases and hedging programs; issues, manages + repays CP)
 - Liquidity provider (stands ready if CP cannot be rolled over)
 - Credit enhancer (guarantees credit losses in excess of losses absorbed by transferor's residual interests)
- Bank has residual interest in reserve fund set up to cover credit losses



Examples: Multi-seller conduit

Analysis – PROPOSED APPROACH

Reporting entity?	Credit card operators, retailer, leasing company
The Asset?	Receivable portfolio (each transferor has a residual interest)
Continuing involvement?	Yes, residual interest
Transferee practical ability to transfer for own benefit?	No because SPE is restricted from selling the receivables
Accounting outcome?	No derecognition

Bank consolidates SPE



Examples: Multi-seller conduit

Analysis – ALTERNATIVE APPROACH

Reporting entity?	Credit card operators, retailer, leasing company
Present access to all CFs?	No
Accounting outcome?	Derecognition of receivables + recognition of residual interest

Bank consolidates SPE



ON-balance sheet transfer disclosures (¶42B)

- a) Nature of the assets
- b) Nature of the risks to which the entity remains exposed
- c) Carrying amounts of the assets and the associated liabilities
- d) Description of nature of the relationship between the assets and the associated liabilities (incl. restrictions on use of assets)
- e) FV of the assets, FV of associated liabilities and the net position, if recourse only to the assets



Proposed disclosures

Illustration for ¶42B(c)+(e)

	Class of financial asset				Available for sale financial assets
	Financial assets at fair value through profit or loss		Loans and receivables		
	Trading securities	Trading derivatives	Mortgages	Consumer loans	
CU million					Equity investments
Carrying amount of assets	X	X	X	X	X
Carrying amount of associated liabilities	(X)	(X)	(X)	(X)	(X)
For those liabilities that have recourse only to specific assets:					
Fair value of assets	X	X	X	X	X
Fair value of associated liabilities	(X)	(X)	(X)	(X)	(X)
Net position	X	X	X	X	X



OFF-balance sheet transfer disclosures (¶42D+B33)

- | | |
|--|--|
| <ul style="list-style-type: none">a) Carrying amount of the continuing involvementb) FV of the continuing involvementc) Maximum exposure to loss from continuing involvementd) FV of derecognised assets in which the entity has continuing involvemente) Cash outflows to repurchase assetsf) Maturity analysis of future cash outflowg) Sensitivity analysis | <ul style="list-style-type: none">h) Qualitative information – description of:<ul style="list-style-type: none">– Derecognised assets– Nature and purpose of retained continuing involvement– Risks to which the transferor is exposed after the transfer, incl.:<ul style="list-style-type: none">– How entity manages risk from continuing involvement– Whether entity bears losses before other parties + ranking and loss amounts borne by each category of party involved– Events/circumstances that would trigger financial support or repurchase of transferred asset |
|--|--|



Proposed disclosures

Illustration for ¶42D(a)-(e)

Continuing involvement with transferred financial assets that have been derecognised

CU million Type of continuing involvement	Fair value of transferred (derecognised) assets	Cash outflows to repurchase transferred (derecognised) assets	Carrying amount of continuing involvement in statement of financial position		Fair value of continuing involvement	Maximum exposure to loss
			Assets	Liabilities		
Repurchase agreements	X	(X)	X	(X)	X	X
Written put options	X	(X)		(X)	X	X
Purchased call options	X	(X)	X		X	X
Securities lending	X	(X)	X	(X)	X	X
Servicing	X		X	(X)	X	X
Total			X	(X)	X	X

Carrying amount of continuing involvement in the statement of financial position

CU million Class of asset or liability	Total	
	Assets	Liabilities
Held for trading	X	
Available for sale financial assets	X	
Financial liabilities at fair value through profit or loss		(X)
Total	X	(X)



Proposed disclosures

Illustration for ¶42D(f)

Undiscounted cash outflows to repurchase transferred assets

CU million Type of continuing involvement	Total	Maturity of continuing involvement					
		<1 month	<3 months	<6 months	<1 year	1-2 years	>2 years
Repurchase agreements	X	X	X	X	X	X	
Written put options	X		X	X	X	X	
Purchased call options	X			X	X	X	X
Securities lending	X	X	X				



OFF-balance sheet transfer disclosures (¶42E)

- a) Gain or loss recognised
- b) Income and expense recognised from continuing involvement
- c) If transfer activity not evenly distributed
 - Total amount of activity and related gains/losses in the period, and
 - When greatest activity took place



Next steps

- Public roundtables in June or July 2009 (together with ED10 *Consolidation*)
- Comments on this ED submitted by 31 July 2009 (Deliberation of comments with FASB)
- Final standard expected in the 1st half of 2010



Questions for ARG

- Which derecognition approach – the proposed or alternative one – do you think is more decision useful?
- Would either approach represent a significant improvement to IAS 39?
- What are your views on the proposed disclosure requirements:
 - On-balance sheet?
 - Off-balance sheet?
- What issues do you encounter in practice currently?

