

October 2009

International Financial Reporting Standards

**Analyst Representative Group
Global Preparers Forum
10 November 2009**

AGENDA PAPER 4A

IAS 39 Replacement

Proposals and timetable

IASC Foundation

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

2008 IASC Foundation | 30 Cannon Street | London EC4M 6XH | UK | www.iasb.org



Timetable

One project – three phases

Phases	Exposure Draft	Finalisation
1. Classification and Measurement	Comment period closed	In time for year end financial statements 2009 for financial assets During 2010 for financial liabilities
2. Impairment methodology	October 2009	During 2010
3. Hedge Accounting (Board deliberations ongoing)	December 2009	During 2010

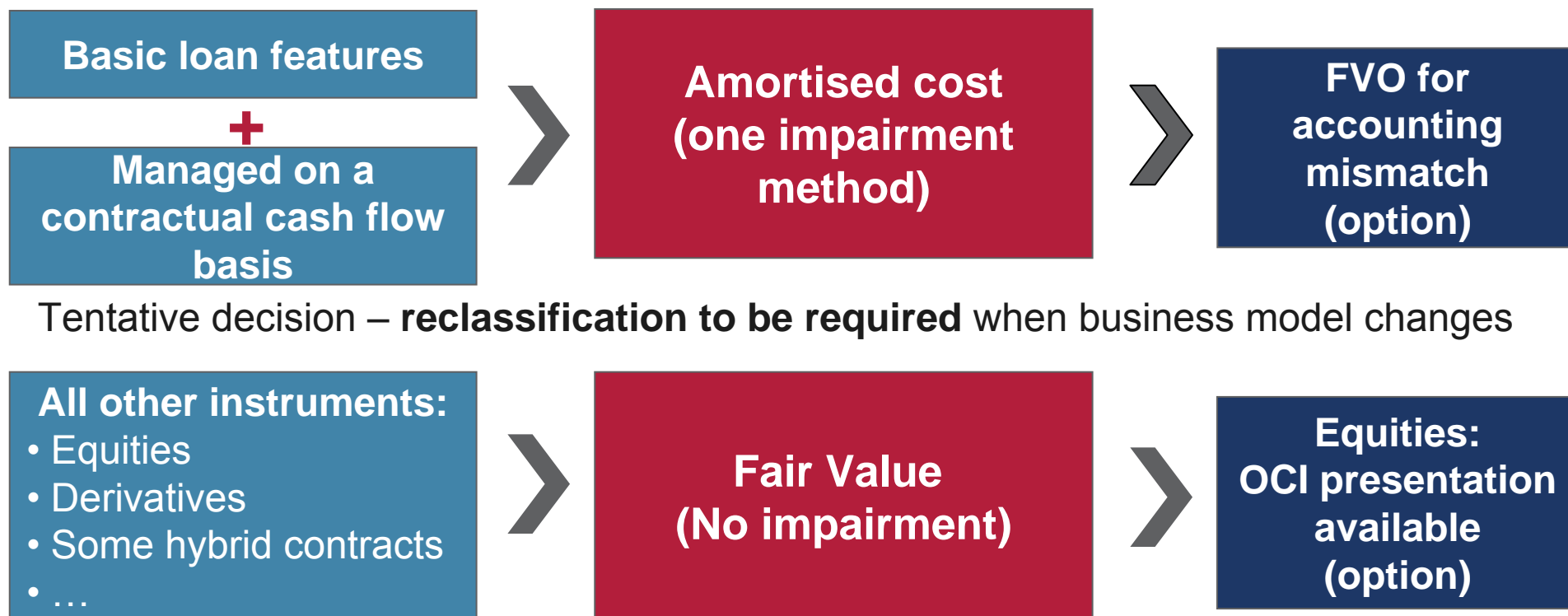


Classification and Measurement - feedback

√	X
Mixed measurement model	Alternative approaches (closer to FASB approach)
Amortised cost criteria	No reclassification
OCI presentation alternative	Restrains around OCI alternative



Overview of classification model for financial assets only



Amortised cost – Managed on a contractual cash flow basis

Basic loan features

+

Managed on a contractual cash flow basis

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- Business model
 - objective of holding instruments to collect or pay contractual cash flows rather than to sell prior to contractual maturity to realise fair value changes
 - not an instrument by instrument approach to classification
- Will only assess contractual terms of instruments within such a business model
- No ‘tainting’ rules for assets at amortised cost
 - gains or losses from derecognising such items to be presented separately with additional disclosures



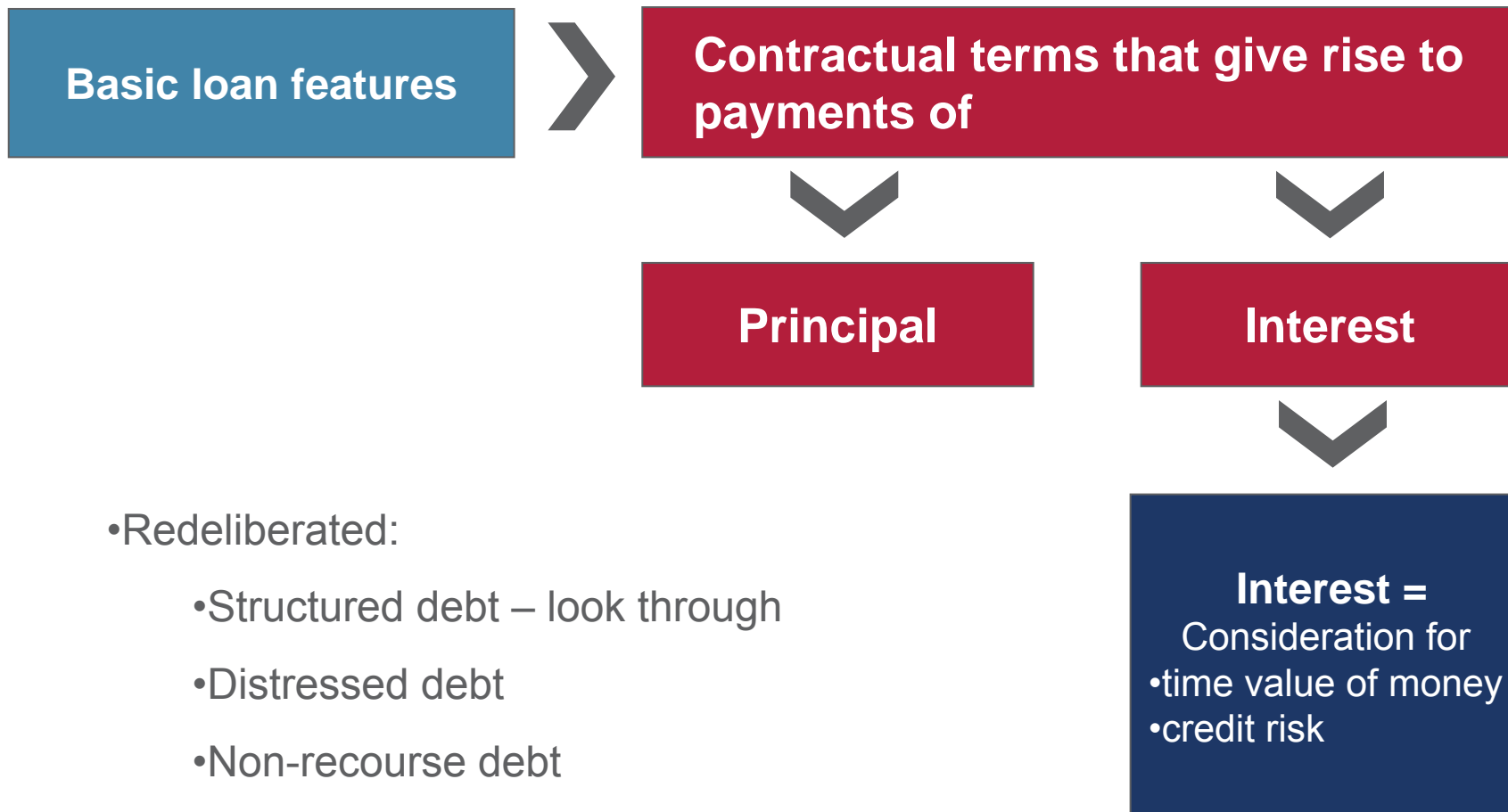
Amortised cost - Basic loan features

Basic loan features

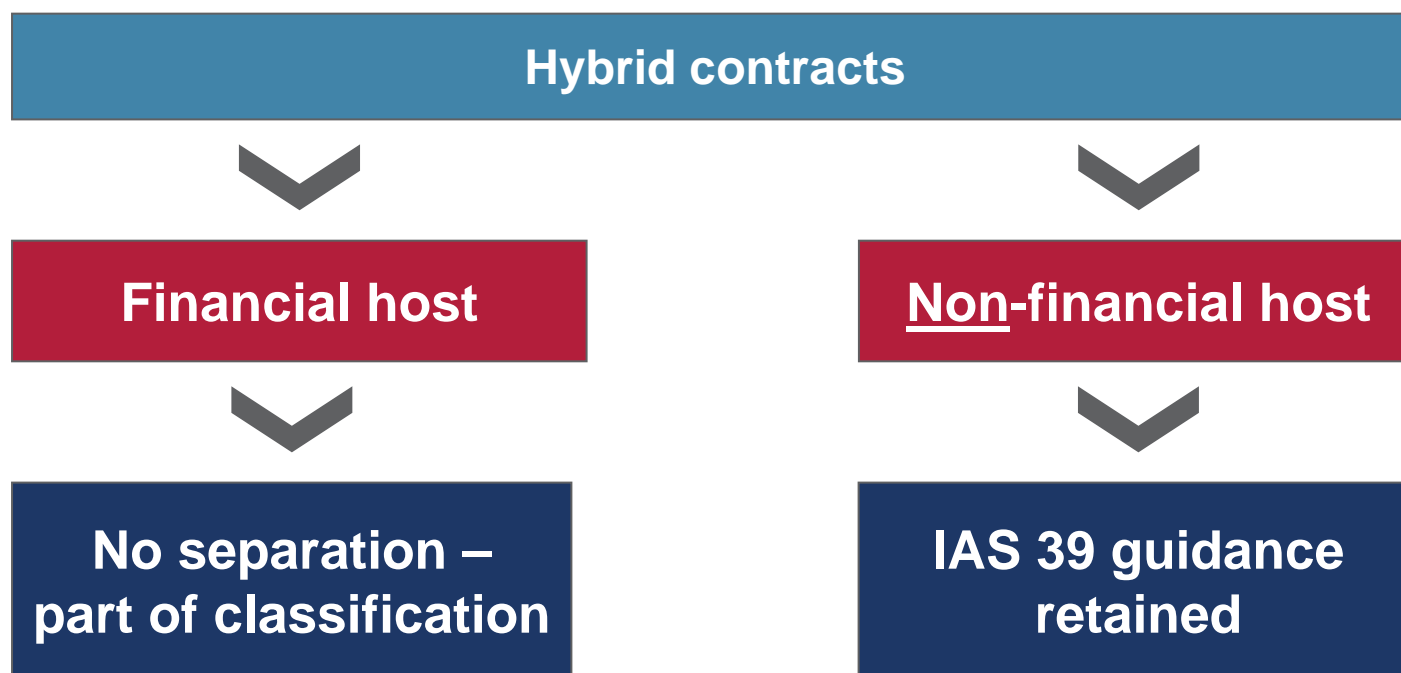
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Managed on a
contractual cash flow
basis

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Amendments to embedded derivatives (applicable only to financial assets)



Equity investments – OCI alternative

Alternative presentation of fair value changes in other comprehensive income (OCI)

- Scope – investments in equity instruments not held for trading
- Features:
 - option available instrument by instrument
 - **dividends recognised in P&L**
 - no recycling, impairment or change in presentation



Fair value option (FVO) for financial assets*



*FVO unchanged for financial liabilities at this stage



Transition

- Generally fully retrospective with some exceptions
- Comparatives only required for adopters from 1/1/12

Effective date

- Available for voluntary application in 2009 year end financial statements
- Mandatory adoption –1 January 2013
- Noted mandatory date may require subsequent reconsideration (to later date) depending on impairment and insurance Phase II



Financial liabilities – way forward

- Feedback \geq financial liabilities less urgent
- Overwhelming response to discussion paper \geq effects of own credit not decision useful
- Board wants to address the own credit issue
- Tentatively decided during redeliberations to require ‘frozen credit spread’ for some liabilities otherwise at fair value
- Reconsidered and **decided to exclude financial liabilities from scope of new IFRS for 2009 year ends**
- Allows more time to seek input on the best way to address own credit
- Objective \geq revised classification and measurement for financial liabilities during 2010



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Current state: Incurred loss impairment

IAS 39 requires an incurred loss approach for financial assets

- What does that mean?

Impairment loss only recognised when:

- Trigger (loss) event occurs
- Impact can be reliably estimated

- Consequence:

Expected losses not recognised before trigger events



Criticisms of the incurred loss approach include:

- Overstates interest revenue before trigger event (front-loading)
- Does not reflect the underlying economics of the transaction
- Triggers inconsistently applied
- Loss recognition too late



Proposed impairment method: Expected cash flow (ECF) approach

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Main outcomes of the ECF approach include:

- Earlier recognition of impairment loss
- Eliminates front loading of interest revenue
- Better reflects underlying economics (eg pricing of instruments when lending decision is made)



Expected cash flow approach

- Main features:
 - interest revenue is recognised on the basis of expected cash flows (including initial expected credit losses)
 - impairment results from an *adverse change* in credit loss expectations
 - reversal of impairment loss when expectations change *favourably*
 - re-estimation of expected cash flows each period end



Impairment Presentation

Presentation
(face of
income
statement)

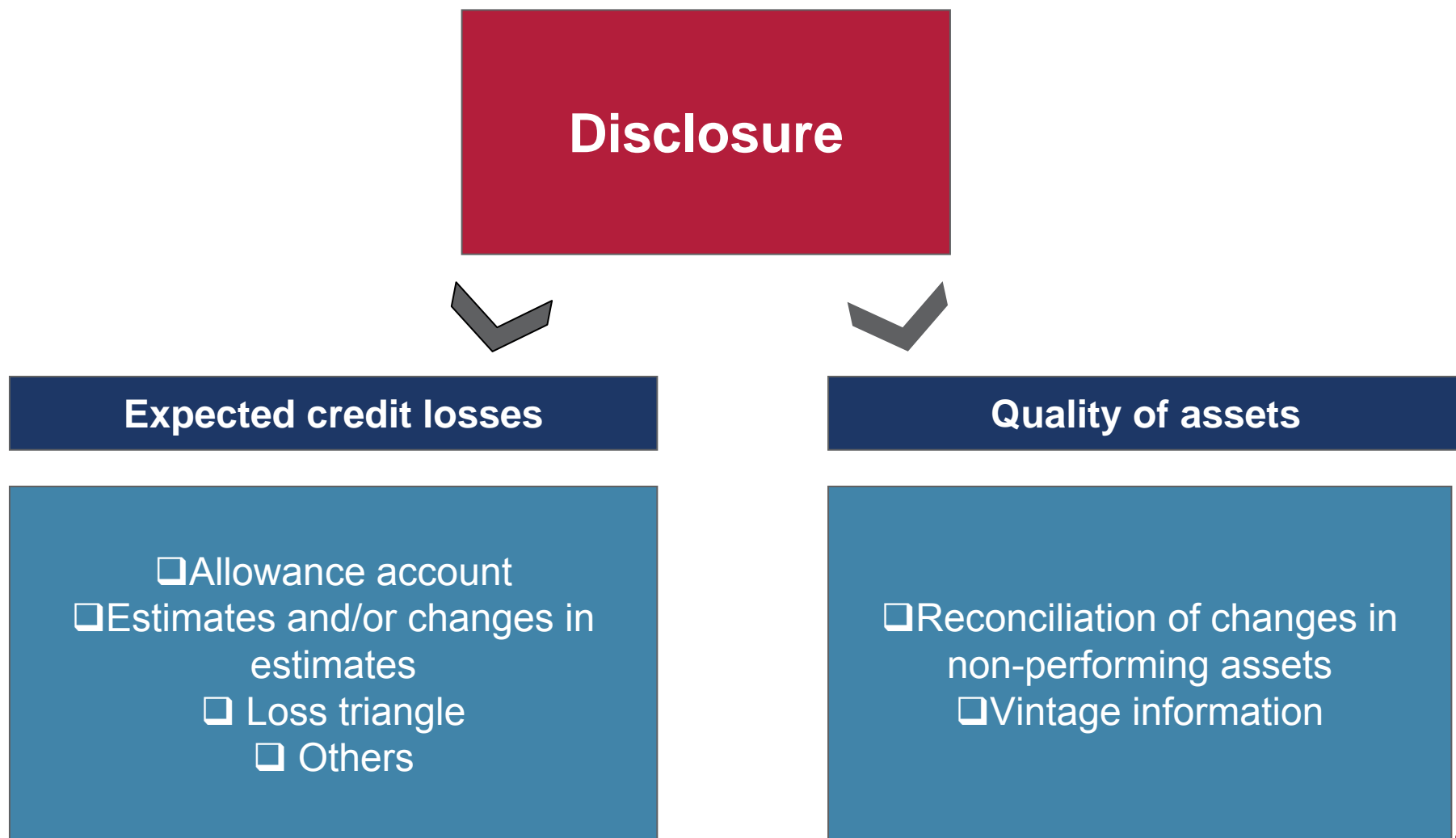
Contractual interest revenue
-- Allocation of initial expected credit losses
= Economic interest revenue (credit cost adjusted)

Effect of changes in expectations

Interest expense



Impairment Disclosure



Operational challenges

The IASB is aware of the operational challenges of the model:

- Request for Information on feasibility in June 2009
- Extensive outreach activities
- Expert advisory panel (EAP)
 - Objectives:
 - Advise the Board on how operational challenges of the ECF approach might be resolved
 - Assist in field testing



Transition and effective date

Transition

- Does not propose fully retrospective or prospective transition
- Adjust the effective interest rate to approximate the rate that would have been determined at inception using the ECF approach

Effective date

- Around 3 years after final standard with early (voluntary) application permitted



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Hedging – Broad direction

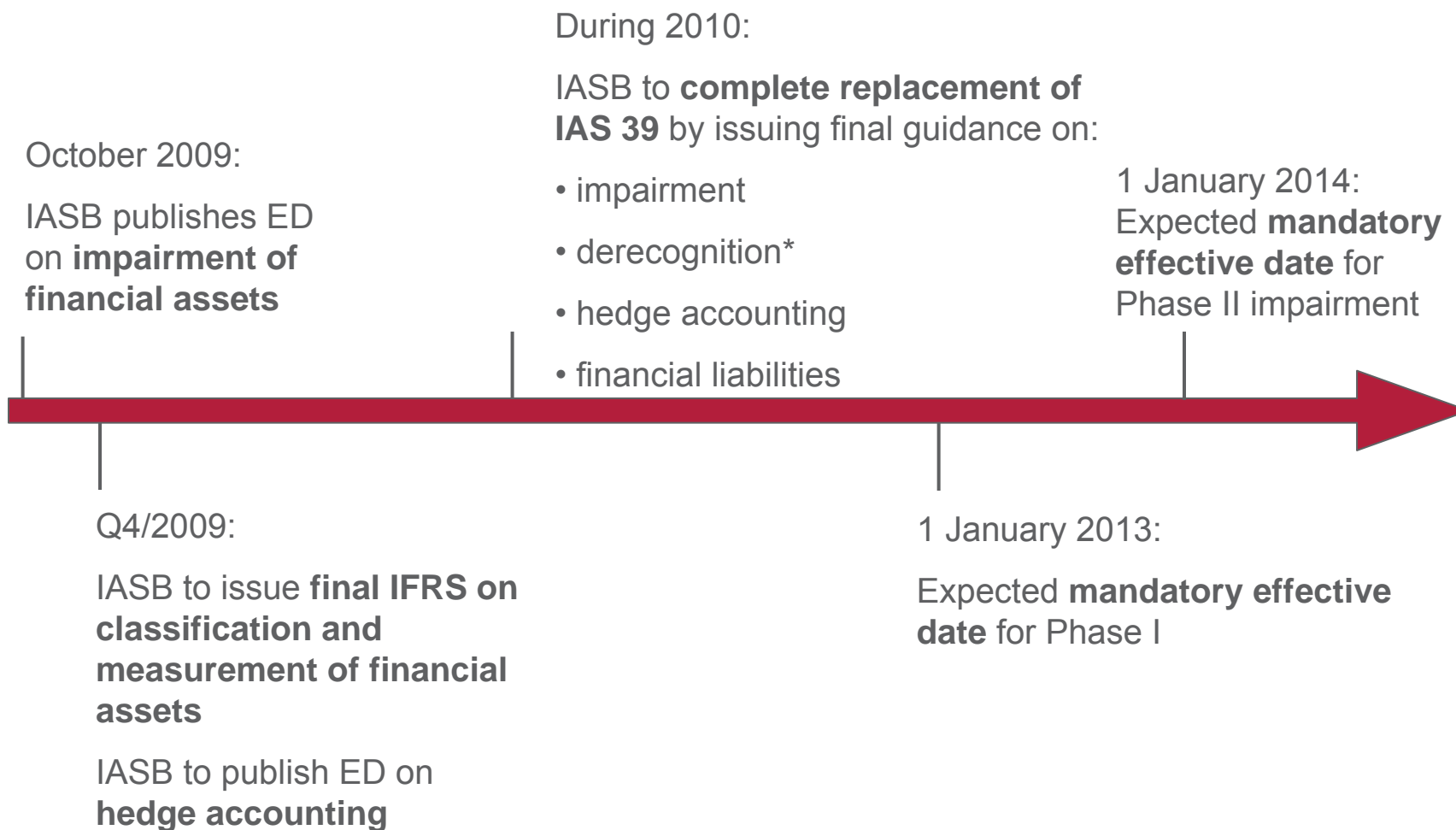
- Consider using cash flow hedge accounting mechanics for fair value hedges
 - Gains and losses on effective portion recognised in OCI
 - Hedged item not remeasured
 - ‘Lower of’ test NOT to be used for fair value hedges
- Simplify cashflow hedge accounting methodology
- Phasing:
 - broad hedging model first
 - then consider portfolio hedge accounting and net investment hedging



Project to replace IAS 39

Next steps

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*separate project



Questions or comments?

Expressions of individual views by members of the IASB and its staff are encouraged. The views expressed in this presentation are those of the presenter. Official positions of the IASB on accounting matters are determined only after extensive due process and deliberation.

