IFRS NEWSLETTER
FINANCIAL INSTRUMENTS

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cutting through complexity

“All the due process requirements for IFRS 9 have been met, and a final standard with an effective date of 1 January 2018 is expected in mid-2014.”

Chris Spall
KPMG’s global IFRS financial instruments leader

The future of IFRS financial instruments accounting

This edition of *IFRS Newsletter: Financial Instruments* highlights the IASB’s discussions in February 2014 on its financial instruments (IAS 39 replacement) project.

In its February meetings, the IASB reached a tentative decision on the mandatory effective date of IFRS 9 and agreed to prepare the ballot draft for the classification and measurement limited amendments, and the impairment chapter of IFRS 9.

Highlights

IFRS 9 (2014)

- The mandatory effective date of IFRS 9 will be 1 January 2018.
- All the due process requirements for the classification and measurement and impairment phases have been met, and so a final standard is expected in mid-2014.
- The IASB expressed disappointment that the FASB’s decisions on the classification and measurement phase meant that convergence could no longer be achieved.

Fair value measurement

- The fair value measurement amendments that clarify the unit of account for quoted investments would be initially applied by adjusting the opening retained earnings in the period of adoption.
- All the due process requirements have been met, and so an exposure draft is expected in the second quarter of 2014.

A discussion paper on macro hedge accounting is still expected in the first quarter of 2014.

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EFFECTIVE DATE AGREED

The story so far …

Since November 2008, the IASB has been working to replace its financial instruments standard (IAS 39 *Financial Instruments: Recognition and Measurement*) with an improved and simplified standard. The IASB structured its project in three phases:

- Phase 1: Classification and measurement of financial assets and financial liabilities
- Phase 2: Impairment
- Phase 3: Hedge accounting.

In December 2008, the FASB added a similar project to its agenda; however, the FASB has not followed the same phased approach as the IASB. In December 2013, the FASB tentatively decided not to pursue the same accounting model as the IASB on the classification and measurement and impairment of financial instruments.

Classification and measurement

The IASB issued IFRS 9 *Financial Instruments* (2009) and IFRS 9 (2010), which contain the requirements for the classification and measurement of financial assets and financial liabilities. In November 2012, the IASB issued an exposure draft (ED) on limited amendments to the classification and measurement requirements of IFRS 9 (the C&M ED).

The FASB issued a revised ED in February 2013 – the proposed Accounting Standards Update, *Financial Instruments—Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities* (the proposed ASU). In December 2013, the FASB decided that it would not continue to pursue the solely principal and interest ('solely P&I') model for assessing the contractual cash flow characteristics of financial assets, and would instead retain the current US GAAP guidance. In January 2014, the FASB discussed the business model assessment and decided not to continue to pursue it.

Impairment

The IASB and the FASB (the Boards) were working jointly on a model for the impairment of financial assets based on expected credit losses, which would replace the current incurred loss model in IAS 39. At the July 2012 joint meeting, the FASB expressed concern about the direction of the joint project and in December 2012 it issued an ED of its own impairment model, the current expected credit loss (CECL) model. Meanwhile, the IASB continued to develop separately its three-bucket impairment model, and issued a new ED in March 2013 (the impairment ED). In December 2013, the FASB decided to continue to refine the CECL model.

Hedge accounting

The IASB issued a new general hedging standard as part of IFRS 9 (2013) in November 2013, and is working towards issuing a discussion paper (DP) on macro hedging in the first quarter of 2014.

What happened in February 2014?

The IASB's February meetings saw the Board reach a tentative decision on the mandatory effective date of IFRS 9 – 1 January 2018.

The Board was presented with the staff analysis of the FASB's recent decisions, and an overview of the IASB's tentative expected credit losses impairment model. It was also presented with the most significant concerns raised by respondents to the impairment ED and the ways in which these were addressed.

The IASB has now concluded its redeliberations on the classification and measurement limited amendments and the impairment chapter of IFRS 9, and agreed to prepare the ballot draft for the final standard, which is expected in mid-2014.

In addition, the IASB finalised its project to clarify:

- the unit of account for measuring the fair value of financial assets that are investments in a subsidiary, joint venture or associate; and
- the interaction with the use of Level 1 inputs.

The IASB tentatively decided that the fair value measurement amendments would be applied by adjusting the opening retained earnings in the period of adoption, and agreed to prepare the ballot draft for the ED, which is expected in the second quarter of 2014.

Contents

IFRS 9 (2014)	3
Fair value measurement: Unit of account – Transition	4
Appendix A: Summary of IASB's redeliberations on the classification and measurement ED	6
Appendix B: Summary of IASB's redeliberations on the impairment ED	13
Project milestones and timeline	21
Find out more	22
KPMG contacts	23

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The mandatory effective date for IFRS 9 will be 1 January 2018.

Effective date

What's the issue?

With deliberations on the C&M and impairment EDs already substantively completed, the IASB discussed the mandatory effective date of IFRS 9 in its February meeting. It focused on:

- the interaction with the ongoing insurance contracts project, because implementing IFRS 9 and the future proposed insurance contracts standard on different dates may give rise to temporary mismatches; and
- the time required to implement the expected credit losses model part of the standard, because this aspect is likely to require the greatest lead time – in particular, for entities in the financial sector.

What did the IASB decide?

The Board tentatively decided that the mandatory effective date for IFRS 9 will be 1 January 2018.

KPMG insight

IFRS 9 has been published in stages, and a number of versions are in existence. After six months from the date of issuance of the completed version of IFRS 9, entities will no longer be able to initially adopt a previous version of IFRS 9. However, entities that have already adopted a previous version of IFRS 9 or that adopt a previous version before the six-month window expires could continue to apply that version until the mandatory effective date of 1 January 2018. Also, we expect the completed version to continue to allow an entity to early adopt the own credit requirements in IFRS 9 (2010) in isolation or to adopt the entire standard but elect to continue applying the hedge accounting requirements in IAS 39 (until the macro hedging phase is finalised). Therefore, application of the following versions of IFRS 9 may be possible until 1 January 2018:

- IFRS 9 (2009);
- IFRS 9 (2010);
- IFRS 9 (2013) – with or without an election to continue to apply IAS 39's hedge accounting requirements;
- IFRS 9 (2014) (complete version) – with or without an election to continue to apply IAS 39's hedge accounting requirements; or
- IAS 39 with adoption of the own credit requirements of IFRS 9 (2010).

The IASB expressed disappointment that the FASB's decisions on the C&M phase meant that convergence could no longer be achieved.

Interaction with FASB proposals

The Board was presented with the staff analysis of the FASB's recent decisions on both the classification and measurement and impairment phases.

For the classification and measurement phase, the IASB acknowledged that the FASB:

- tentatively decided in December 2013 not to continue to pursue the contractual cash flow characteristics assessment, but to retain the bifurcation requirements in current US GAAP; and
- decided in January 2014 not to continue the business model assessment approach, on the basis that targeted improvements to US GAAP would be a more cost-beneficial approach.

IASB members expressed disappointment that convergence could no longer be achieved and recognised that compliance with two different standards would have consequences in terms of cost and resources.

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FAIR VALUE MEASUREMENT: UNIT OF ACCOUNT – TRANSITION

The fair value measurement amendments would be applied by adjusting the opening retained earnings in the period of adoption.

What's the issue?

The IASB has conducted a project to clarify the unit of account for measuring:

- the fair value of financial assets that are investments in a subsidiary, joint venture or associate; and
- the interaction between the unit of account and the use of Level 1 inputs.

The unit of account could be either:

- the investment as a whole: in this case, the valuation may include a premium – e.g. a control premium; or
- the individual shares making up the investment: in this case, the valuation could not include a premium, due to the size of the investment.

During its previous deliberations, the IASB had tentatively decided that:

- the unit of account for investments in subsidiaries, joint ventures or associates would be the investment as a whole, rather than the individual financial instruments that make up the investment; but
- the fair value measurement of an investment composed of quoted financial instruments should be the product (P × Q) of the quoted price of the financial instrument (P) and the quantity (Q) of instruments held because quoted prices in an active market provide the most reliable evidence of fair value.

In addition, the IASB had tentatively decided that the ED that clarifies the unit of account would include a non-authoritative example illustrating the application of the portfolio measurement exception for portfolios that comprise only Level 1 financial instruments whose market risks are substantially the same. The example would clarify that the fair value of the portfolio should be measured on the basis of the Level 1 prices for the individual instruments that comprise the net risk exposure.

What did the IASB decide?

The IASB's discussion focused on transition, and it reached the following tentative decisions.

- The proposed amendments to the measurement of quoted investments at fair value would be applied by adjusting the entity's opening retained earnings for the period in which the proposed amendments are first applied. The effect of the change in measurement *during the period* would be recognised in profit or loss. Entities would be required to disclose the catch-up adjustment in their opening retained earnings.
- However, for measuring fair value less costs of disposal of quoted cash generating units for impairment purposes, the proposed amendments would be applied *prospectively.*
- Early application of the amendments would be permitted.

The proposed changes are similar to a change in accounting estimate and therefore the IASB concluded that prospective application would be consistent with:

- the requirements of IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* for changes in accounting estimates; and
- the guidance in paragraph 66 of IFRS 13 *Fair Value Measurement* on changes in valuation techniques.

However, for first-time adopters of IFRS, the IASB tentatively decided that the amended requirements would be applied *retrospectively* in the opening IFRS statement of financial position.

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An ED is expected in the second quarter of 2014.

Next steps

The IASB gave the staff permission to begin the balloting process for the ED. Therefore, the IASB expects that the ED will be published in the second quarter of 2014, with a comment period of 120 days from the date of publication.

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APPENDIX A: SUMMARY OF IASB'S REDELIBERATIONS ON THE CLASSIFICATION AND MEASUREMENT ED

What did the IASB discuss?		What did the IASB tentatively decide?	Is there an identified change to IFRS 9?	Is there an identified change to the C&M ED?
The solely principal and interest ('solely P&I') criterion	**Meaning of 'principal'**	'Principal' is the amount transferred by the current holder for the financial asset.	Yes	Yes
	Meaning of 'interest'	The IASB tentatively decided: • to clarify that *de minimis* features should be disregarded for classification; • to emphasise the underlying conceptual basis for the 'solely P&I' condition – i.e. the notion of a basic lending-type return; • to confirm that time value of money and credit risk are typically the most significant components of a basic lending-type return, but not the only possible components; • to clarify that a basic lending-type return also generally includes consideration for liquidity risk, profit margin and consideration for costs associated with holding the financial asset over time – e.g. servicing costs; • to emphasise what are not the components of a basic lending-type return and why – e.g. indexation to equity prices; and • to clarify the meaning of the time value of money – specifically: – to clarify the objective of the consideration for the time value of money – i.e. to provide consideration for *just* the passage of time, in the absence of return for other risks and costs associated with holding the financial asset over time; – to articulate the factors relevant to providing consideration for the passage of time – notably, the tenor of the interest rate and the currency of the instrument; – to clarify that both qualitative and quantitative approaches could be used to determine whether the interest rate provides consideration for just the passage of time, if the time value of money component of the interest rate is modified – e.g. by an interest rate tenor mismatch feature – but not to prescribe when each approach should be used; and – to not allow a fair value option in lieu of the quantitative assessment;	Yes	Yes

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What did the IASB discuss?		What did the IASB tentatively decide?	Is there an identified change to IFRS 9?	Is there an identified change to the C&M ED?
The solely principal and interest ('solely P&I') criterion (continued)	**Meaning of 'interest' (continued)**	• to accept regulated interest rates as a proxy for the consideration for the time value of money if those rates provide consideration that is broadly consistent with consideration for the passage of time and do not introduce exposure to risks or volatility in cash flows that are inconsistent with the basic lending-type relationship; and • to provide guidance on how the quantitative assessment of a financial asset with a modified time value of money component should be performed – i.e. by considering the contractual (undiscounted) cash flows of the instrument relative to the benchmark instrument – and to replace the 'not more than insignificant' threshold in the C&M ED with the 'not significant' threshold – i.e. a financial asset with the modified time value of money component of the interest rate would meet the 'solely P&I' condition if its contractual cash flows could not be significantly different from the benchmark instrument's cash flows.		
	Contingent features	The nature of the contingent trigger event in itself does not determine the classification of the financial asset. A contingent feature that results in contractual cash flows that are not solely P&I is inconsistent with the 'solely P&I' condition unless the feature is non-genuine.	Yes	Yes
	Prepayment and extension features	No distinction should be made between contingent prepayment and extension features and other types of contingent features. A prepayment feature that results in contractual cash flows that are not solely P&I is inconsistent with the 'solely P&I' condition unless the feature is non-genuine – with an exception for financial assets that meet the following conditions: • the financial asset is acquired or originated with a significant premium or discount; • the financial asset is prepayable at the amount that represents par and accrued and unpaid interest (and may include reasonable additional compensation for the early termination of the contract); and • the fair value of the prepayment feature on initial recognition of the financial asset is insignificant. Financial assets meeting the conditions for this exception would be eligible for classification at other than FVTPL (subject to the business model assessment).	Yes	Yes

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What did the IASB discuss?		What did the IASB tentatively decide?	Is there an identified change to IFRS 9?	Is there an identified change to the C&M ED?
Business model	**Meaning of 'business model'**	The term 'business model' should refer to the way in which financial assets are managed in order to generate cash flows and create value for the entity. The business model assessment should result in financial assets being measured in a way that would provide the most relevant and useful information about how activities and risks are managed to create value.	Yes	Yes
	Level at which a business model is assessed	The business model should be assessed at a level that reflects groups of financial assets that are managed together to achieve a particular objective. In short, this assessment should reflect the way in which the business is managed.	Yes	Yes
	Information that should be considered when assessing business model	The final standard would make the following clarifications. • The business model is often observable through particular activities that are undertaken to achieve the objectives of that business model. • These business activities usually reflect: – the way in which the performance of the business is evaluated and reported – i.e. key performance indicators; – the risks that typically impact the performance of the business model; and – how those risks are managed. • An entity should consider all relevant and objective information, but not every 'what if' or worst-case scenario.	Yes	Yes

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	What did the IASB discuss?	What did the IASB tentatively decide?	Is there an identified change to IFRS 9?	Is there an identified change to the C&M ED?
Business model (continued)	**Role of sales in the business model assessment**	The application guidance in the final standard would include the following clarifications. • Sales do not drive the business model assessment, and information about sales activity should not be considered in isolation, but as part of an holistic assessment of how the financial assets will be managed. • Historical sales information would help an entity support and verify its business model assessment. Such information should be considered in the context of: – the reasons for those sales; – the conditions that existed at that time; – the entity's expectations about future sales activities; and – the reasons for those expected future sales. • Fluctuations in sales in a particular period do not necessarily mean that the entity's business model has changed if the entity can explain: – the nature of those sales; and – why they do not indicate a fundamental change in its overall business strategy. • If cash flows are realised in a way that is different from the entity's expectations, then this would neither: – result in the restatement of prior period financial statements; nor – change the classification of the existing financial assets in the business model; as long as the entity considered all relevant and objective information that was available at the time that it made its decision.	Yes	Yes
	Change in business model	A change in business model would occur only when an entity has either stopped or started doing something on a level that is significant to its operations. This would generally be the case only when the entity has acquired or disposed of a business line.	Yes	Yes

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	What did the IASB discuss?	What did the IASB tentatively decide?	Is there an identified change to IFRS 9?	Is there an identified change to the C&M ED?
Business model (continued)	**Hold to collect business model**	The current hold to collect 'cash flows (value) realisation' concept would be reinforced by discussing, and providing examples of, the activities that are commonly associated with the hold to collect business model; and by providing guidance on the nature of information an entity should consider in assessing the hold to collect business model. Insignificant and/or infrequent sales may be consistent with the hold to collect business model, regardless of the reasons for those sales. This determination is a matter of judgment and would be based on facts and circumstances. Historical sales information and patterns could provide useful information, but that sales information would not be determinative and should not be considered in isolation. Sales to minimise potential credit risk due to credit deterioration are integral to the hold to collect objective. Sales made in managing concentration of credit risk would be assessed in the same way as any other sales made in the business model.	Yes	Yes
	A third measurement category – FVOCI	The FVTPL measurement category would be retained as the residual category.	No	No
	Clarifying the proposed application guidance for the FVTPL measurement category	The final standard would clarify the following points. • When financial assets are either held for trading or managed and evaluated on a fair value basis, the entity makes decisions – i.e. whether to hold or sell the asset – based on changes in, and with the objective of realising, the assets' fair value. • The activities that the entity undertakes are primarily focused on fair value information, and key management personnel use that information to assess the assets' performance and to make decisions accordingly. • Another indicator is that the users of the financial statements are primarily interested in fair value information on these assets to assess the entity's performance.	Yes	Yes

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	What did the IASB discuss?	What did the IASB tentatively decide?	Is there an identified change to IFRS 9?	Is there an identified change to the C&M ED?
Business model (continued)	**Clarifying the proposed application guidance for the FVOCI measurement category**	The final standard would clarify that managing financial assets both to collect contractual cash flows and for sale would reflect the way in which financial assets are managed to achieve a particular objective, rather than the objective in itself. Assets that are classified at FVOCI would be managed in order to achieve different business model objectives – e.g. liquidity management, interest rate risk management, yield management and duration mismatch management – both by collecting contractual cash flows and by selling. The application guidance should more clearly articulate that FVOCI provides relevant and useful information when both the collection of contractual cash flows and the realisation of cash flows through selling are integral to the performance of the business model. The application guidance should describe activities that are typically associated with a business model where financial assets are managed both to collect the contractual cash flows and for sale. There would be no threshold for the frequency or amounts of sales.	Yes	Yes
Other matters	**Extension of the fair value option to the FVOCI measurement category**	Entities would be permitted to apply the fair value option to a financial asset that would otherwise be mandatorily measured at FVOCI if such a designation eliminates or significantly reduces an accounting mismatch. In accordance with the existing fair value option in IFRS 9, such a designation would be performed at initial recognition and would be irrevocable.	Yes	Yes
	Extension of presentation and disclosure requirements	The disclosure and presentation requirements in IFRS 7 and IAS 1 would extend to reclassifications into and out of the FVOCI category.	Yes	No
	Disclosure of significant judgements	The judgement involved in assessing an asset's contractual cash flow characteristics would be added to IAS 1 as an example of a judgement that could have a significant effect on the amounts recognised in the financial statements.	Yes	No
	Comparative information and related disclosures for first-time adopters of IFRS	First-time adopters would be given adequate lead time to prepare for the transition to IFRS 9. They would: • not be required to present comparative information if the beginning of their first IFRS reporting period is earlier than the mandatory effective date of IFRS 9 *plus one year*; • be required to provide additional disclosures if the comparative financial information does not comply with IFRS 9; and • be required to present comparative information that complies with a previous version of IFRS 9 if they choose to apply that previous version early.	Yes	Yes

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What did the IASB discuss?		What did the IASB tentatively decide?	Is there an identified change to IFRS 9?	Is there an identified change to the C&M ED?
Other matters (continued)	**Early application of IFRS 9**	Entities would be able to apply the completed version of IFRS 9 early, but not a previous version of IFRS 9, if their date of initial application is six months or more after the completed version of IFRS 9 is issued.	Yes	No
	Transition– Modified economic relationships	If it is impracticable to assess a modified economic relationship on transition, then the contractual cash flow assessment would be made without taking into account the specific requirements for modified economic relationships.	Yes	Yes
	Transition– Prepayment features	If it is impracticable to assess the significance of prepayment features on transition, then the contractual cash flow assessment would be made without taking into account the exception for certain prepayment features.	Yes	Yes
	Transition – Fair value option	On transition, entities would reconsider their fair value option designations only to the extent that either previous accounting mismatches no longer exist or new accounting mismatches are created. Entities would be required to revoke previous fair value option elections if the accounting mismatch that formed the basis for the previous designation no longer exists at initial application of the completed version of IFRS 9 as a result of the amended C&M requirements, but would not be able to revoke previous fair value option elections if the accounting mismatch continues to exist. They may also apply the fair value option for new accounting mismatches that are created by the initial application of the amended C&M requirements, but would not be able to newly apply the fair value option for accounting mismatches that already existed before initial application.	No	No
	Early application of 'own credit' requirements	The early application guidance in IFRS 9 should be amended to permit entities to early apply only the own credit requirements in IFRS 9 when the IASB adds the hedge accounting chapter to IFRS 9.	Yes – included in IFRS 9 (2013)	No

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APPENDIX B: SUMMARY OF IASB'S REDELIBERATIONS ON THE IMPAIRMENT ED

	What did the IASB discuss?	What did the IASB tentatively decide?	Is there an identified change to the impairment ED?
The general principles	**Responsiveness of the impairment model to forward-looking information**	The objective of the model is to recognise lifetime expected credit losses on all financial instruments for which there has been a significant increase in credit risk – *whether on an individual or a portfolio basis*. All reasonable and supportable information, including forward-looking information that is available without undue cost or effort, would need to be considered. In addition, the final standard would include illustrative examples to reflect the intention of the proposals.	Yes. The final standard would clarify the objective and include application examples
	Recognition of expected credit losses for financial instruments that have not significantly deteriorated	For financial instruments for which there has not been a significant increase in credit risk since initial recognition, an entity would measure the expected credit losses at an amount equal to the 12-month expected credit losses.	No
	Timing of recognition of lifetime expected credit losses	Lifetime expected credit losses would be recognised when there is a significant increase in credit risk since initial recognition. The final standard would clarify (potentially through examples) that: • the assessment of significant increases in credit risk could be implemented more simply by establishing the initial maximum credit risk for a particular portfolio (of financial instruments with similar credit risk on initial recognition) – the 'origination' credit risk – and then comparing the credit risk of financial instruments in that portfolio at the end of the reporting period with that origination credit risk; • the assessment of significant increases in credit risk could be implemented through a counterparty assessment – provided that this assessment achieves the objectives of the proposed model; • the assessment of the timing of recognition of lifetime expected credit losses would consider only changes in the risk of a default occurring, rather than changes in the amount of expected credit losses (or the credit LGD); • an assessment based on the change in the risk of a default occurring in the next 12 months would be permitted unless circumstances indicate that a lifetime assessment is necessary; and • a loss allowance measured at an amount equal to 12-month expected credit losses would be re-established for financial instruments for which the criteria for the recognition of lifetime expected credit losses are no longer met.	Yes. The final standard would include clarifications and potentially examples to articulate how to identify a significant increase in credit risk since initial recognition

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What did the IASB discuss?		What did the IASB tentatively decide?	Is there an identified change to the impairment ED?
The general principles (continued)	**Definition of 'default'**	An entity would apply a definition of 'default' that is consistent with its credit risk management practices. Qualitative indicators of default should be considered when appropriate – e.g. for financial instruments that contain covenants. Also, the final standard would include a rebuttable presumption that default does not occur later than 90 days past due unless an entity has reasonable and supportable information to corroborate a more lagging default criterion.	Yes. The rebuttable presumption was not included in the impairment ED
Operational simplifications	**'More than 30 days past due' rebuttable presumption**	The rebuttable presumption that there is a significant increase in credit risk when contractual payments are more than 30 days past due would be retained in the final standard. However, information that is more forward-looking will typically be available and should be considered. Also, it would be clarified that: • the objective of the rebuttable presumption is to serve as a backstop or latest point at which to identify financial instruments that have experienced a significant increase in credit risk; • the presumption is rebuttable; and • the application of the rebuttable presumption is to identify significant increases in credit risk before default or objective evidence of impairment.	Yes. The final standard would provide clarifications to resolve some of the operational concerns
	'Low credit risk' operational simplification	An entity can assume that a financial instrument has not significantly increased in credit risk if it has low credit risk at the end of the reporting period. The meaning and application of the low credit risk notion would be clarified as follows: • the proposed description of low credit risk would be modified to state that: – the instrument has a low risk of default; – the borrower is considered, to have a strong capacity to meet its obligations in the near term; and – the lender expects that adverse changes in economic and business conditions in the longer term may, but will not necessarily, reduce the ability of the borrower to fulfil its obligations; • the low credit risk notion is not a bright-line trigger for the recognition of lifetime expected credit losses; and • financial instruments are not required to be externally rated; however, low credit risk equates to a global credit rating definition of 'investment grade'.	Yes. For low credit risk instruments, it seems from the IASB's tentative decision that the final standard may allow (rather than require) entities to assume that the credit risk had not significantly increased; also, clarifications on the meaning and application of low credit risk would be provided

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What did the IASB discuss?		What did the IASB tentatively decide?	Is there an identified change to the impairment ED?
Measurement of expected credit losses	**Discount rate**	The expected credit losses would be discounted at the effective interest rate (EIR) or an approximation thereof.	Yes. The final standard would explicitly require the use of EIR or its approximation
	Use of forward-looking information	The measurement of expected credit losses would incorporate the best information that is reasonably available, including information about past events, current conditions and reasonable and supportable forecasts of future events and economic conditions at the end of the reporting period.	No
	Use of regulatory models	The regulatory expected credit loss models may form a basis for expected credit loss calculations, but the measurement may need to be adjusted to meet the objectives of the proposed model.	No
	12-month expected credit losses	The final standard would clarify the measurement of 12-month expected credit losses by incorporating paragraph BC63 of the ED as part of the application guidance, namely that 12-month expected credit losses are a portion of the lifetime expected credit losses and represent the amount of expected credit losses that would result from a default in the 12 months after the reporting date. Therefore, they are neither: • the lifetime expected credit losses that an entity will incur on financial instruments that it predicts will default in the next 12 months; nor • the cash shortfalls that are predicted over the next 12 months.	Yes. The final standard would clarify that 12-month expected credit losses are a portion of the lifetime expected credit losses by incorporating the discussion in the basis for conclusions into the application guidance
	Financial assets at FVOCI	No relief from recognising 12-month expected credit losses would be introduced for financial assets measured at FVOCI. The final standard would clarify that expected credit losses reflect management's expectations of credit losses. However, when considering the 'best available information' in estimating expected credit losses, management should consider observable market information about credit risk.	Yes. The final standard would clarify that expected credit losses reflect management's expectations of credit losses
Asset modifications	**Scope of application**	The modification requirements in the ED would apply to all modifications or renegotiations of contractual cash flows, regardless of the reason for the modification.	No
	Modification gain or loss	The modification gain or loss would be recognised in profit or loss.	No
	Applicability of the general model to modified financial assets	Modified financial assets would be subject to the same 'symmetrical' treatment – i.e. could revert back to 12-month expected losses – as other financial instruments; however, clarifications would be made in paragraph B24 of the application guidance to emphasise that the credit risk on a financial asset would not automatically improve merely because the contractual cash flows have been modified.	Yes. The final standard would clarify that the application guidance in paragraph B24 applies to all modified financial assets

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	What did the IASB discuss?	What did the IASB tentatively decide?	Is there an identified change to the impairment ED?
Financial guarantee contracts and loan commitments other than revolving credit facilities	**Measurement period for expected credit losses**	The maximum period over which expected credit losses should be estimated would be the contractual period over which the entity is committed to provide credit.	No
	Discount rate	Expected credit losses on the undrawn part of the balance would be discounted using the same EIR, or an approximation thereof, as would be used to discount the drawn part, unless the EIR cannot be determined, in which case the discount rate should be determined as proposed in the impairment ED – i.e. it should reflect the current market assessment of the time value of money and the risks that are specific to the cash flows.	Yes. The final standard would require, with some exceptions, that the same EIR is used for the drawn and undrawn components
	Presentation of expected credit losses	The provision for the expected credit losses on the undrawn balance would be presented together with the loss allowance on the drawn amount if an entity cannot separately identify the expected credit losses associated with the undrawn balance.	Yes. The final standard would provide an operational simplification in certain circumstances
Revolving credit facilities	**Measurement period for expected credit losses**	Expected credit losses – including expected credit losses on the undrawn facility – would be estimated for the period over which an entity is exposed to credit risk and over which future draw-downs cannot be avoided – i.e. considering the behavioural life.	Yes. The final standard would change the measurement period
	Discount rate	Expected credit losses on the undrawn part of the revolving credit facility would be discounted using the same EIR, or an approximation thereof, as would be used to discount the drawn part, unless the EIR cannot be determined, in which case the discount rate should be determined as proposed in the impairment ED – i.e. it should reflect the current market assessment of the time value of money and the risks that are specific to the cash flows.	Yes. The final standard would require, with some exceptions, that the same EIR is used for the drawn and undrawn components
	Presentation of expected credit losses	The provision for the expected credit losses on the undrawn component of the facility would be presented together with the loss allowance for expected credit losses on the drawn facility if an entity cannot separately identify the expected credit losses associated with the undrawn facility.	Yes. The final standard would provide an operational simplification in certain circumstances
Purchased or originated credit-impaired assets	**Credit loss allowance**	In respect of POCI assets: • at initial recognition, these assets would not carry a loss allowance; instead, lifetime expected credit losses would be incorporated into the EIR calculation (resulting in a credit-adjusted EIR); and • the cumulative changes in lifetime expected credit losses since initial recognition would be recognised as an impairment gain or loss.	No
	Interest revenue	Interest revenue would be calculated by applying the credit-adjusted EIR to the amortised cost (net carrying amount) of the POCI asset.	No

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What did the IASB discuss?		What did the IASB tentatively decide?	Is there an identified change to the impairment ED?
Trade and lease receivables	**Simplified approach**	A simplified approach would be available for trade and lease receivables. • Trade receivables that do not constitute a financing transaction would be initially measured at the transaction price and would always carry a loss allowance equal to lifetime expected credit losses. • For trade receivables with a significant financing component and lease receivables, an accounting policy election could be made to either: – apply the general approach; or – recognise lifetime expected credit losses at all times.	No
	Disclosures for receivables assessed using the simplified approach	Reduced disclosure requirements in the impairment ED for trade receivables and lease receivables that are accounted for using the simplified approach would be retained.	No
Interest revenue	**Calculation basis**	Interest revenue would generally be calculated by applying the EIR to the gross carrying amount unless there is objective evidence of impairment, in which case interest would be calculated by applying the EIR to the amortised cost (net carrying amount) of an asset.	No
	Criteria for the change in calculation basis	The calculation of interest revenue would change to a net basis for financial assets that have objective evidence of impairment at the reporting date.	No
	Symmetry in calculation	The calculation of interest revenue would be symmetrical – i.e. it would revert to the gross basis if there is no longer objective evidence of impairment.	No
Presentation	**Presentation requirements**	• Interest revenue and impairment losses (including reversals) would be presented as separate line items in the statement of profit or loss and OCI. • No accumulated impairment amount would be presented in the statement of financial position for assets that are mandatorily measured at FVOCI. However, the loss allowance amount would be disclosed.	No
Disclosure objectives	**Disclosure objectives**	Disclosure objectives would be expanded to emphasise that the information provided should enable a user of the financial statements to understand: • how an entity manages credit risk; • the methods, assumptions and information used to estimate expected credit losses; • an entity's credit risk profile – i.e. the credit risk inherent in the financial instruments – including significant credit concentrations; and • changes, and the reasons for the changes, in the estimate of expected credit losses during the period.	Yes. Disclosure objectives would be expanded

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What did the IASB discuss?		What did the IASB tentatively decide?	Is there an identified change to the impairment ED?
Qualitative disclosures	**Qualitative disclosures**	• Additional disclosure requirements would be added to explain: – the entity's policy on the modification of financial instruments; and – how macroeconomic information has been incorporated in the estimates. • The requirement to disclose information about the discount rate selected would be removed.	Yes. Changes would be introduced to qualitative disclosure requirements
Quantitative disclosures	**Reconciliations**	Disclosures would be amended such that the reconciliation of the gross carrying amounts for all financial assets would focus on the key drivers for changes in the loss allowance.	Yes. Quantitative disclosure requirements for gross carrying amounts would be simplified
Quantitative disclosures	**Modifications**	• The disclosure of the gross carrying amount of modified financial assets for which the measurement for the credit loss allowance has changed from lifetime expected credit losses to 12-month expected credit losses should be required only in the period of change. • The disclosure requirement would be clarified by referring to the deterioration rate – i.e. the percentage – of financial assets, for which credit risk has subsequently increased significantly, resulting in the measurement of the loss allowance reverting to lifetime expected credit losses.	Yes. The final standard would clarify when the disclosure of the gross carrying amount for modified assets would be required and by referring to the deterioration rate
Quantitative disclosures	**Collateral and credit risk mitigation**	The following will be clarified: • qualitative information should be disclosed about how collateral and other credit enhancements have been incorporated into the measurement of expected credit losses on all financial instruments; and • quantitative information about the extent to which collateral or other credit enhancements affect the expected credit loss allowance (or provision) does not require information about the fair value of collateral. It was also suggested that the IASB clarify that entities would be required to disclose the gross carrying amount of financial assets that have an expected credit loss of zero because of collateral only in certain circumstances.	Yes. The final standard would clarify the extent of disclosures in respect of collateral and other credit enhancements
Other disclosures	**Write-offs**	The final standard would clarify the term 'nominal amount' and that: • only financial assets written off during the period would be subject to the requirement to disclose the nominal amount of assets subject to enforcement activity; and • financial assets written off in prior periods but still subject to enforcement activity would be subject to the requirement to disclose narrative information.	Yes. The term 'nominal amount' would be clarified and the disclosure of it would be required only for write-offs during the period

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	What did the IASB discuss?	What did the IASB tentatively decide?	Is there an identified change to the impairment ED?
Other disclosures (continued)	**Credit risk disaggregation**	Credit risk disaggregation requirements would be modified to permit the use of an ageing analysis for financial assets for which delinquency information is the only borrower-specific information available to assess significant increases in credit risk. The requirement for the minimum number of three credit risk grades would be removed, but instead credit risk disaggregation would be required to be aligned with the way credit risk is managed internally and to be applied consistently over time.	Yes. Credit risk disaggregation requirements would be aligned closer to risk management
	Significant effect on the loss allowance	It was suggested that the disclosure of information about significant effects on the loss allowance that are caused by a particular portfolio or geographical area would be incorporated into the qualitative disclosures. (The impairment ED proposed in addition that quantitative disclosures would be required.)	Possibly. The impairment ED contained a separate requirement to disclose quantitative and qualitative analysis of significant effects on the loss allowance caused by a particular portfolio or geographical area
	The amount of financial assets assessed on an individual basis	It was suggested that the following quantitative disclosure requirements would be removed: • the gross carrying amount of financial assets; and • the amount recognised as a provision for loan commitments and financial guarantee contracts that are evaluated on an individual basis and meet the criterion for the recognition of lifetime expected credit losses.	Possibly. Quantitative disclosure requirements on the amount of assets assessed on an individual basis may be removed
Transition	**Retrospective application**	The final requirements would be applied retrospectively in accordance with IAS 8.	No
	Low credit risk exception	When applying the proposals retrospectively, entities may use the low credit risk exception to identify financial instruments for which the credit risk has not significantly increased.	No
	Approximation of credit risk	An entity could approximate the credit risk on initial recognition by using the best information that is available without undue cost or effort.	Yes. The final standard would allow an approximation of the credit risk at initial recognition to be used
	Assets for which credit risk on initial recognition cannot be determined or approximated	If an entity is unable to approximate the credit risk at initial recognition without undue cost or effort, the loss allowance would be measured based on the credit quality at each reporting date until the financial instrument is derecognised.	Yes. If an entity is unable to approximate the credit risk at initial recognition, the loss allowance would be measured based on the credit quality at each reporting date until the financial instrument is derecognised

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	What did the IASB discuss?	What did the IASB tentatively decide?	Is there an identified change to the impairment ED?
Transition (continued)	**Application guidance or examples**	To provide, in the final standard, application guidance or examples to describe how an entity would assess whether there has been a significant increase in credit risk where it uses: • the more than 30 days past due rebuttable presumption if the entity identifies increases in credit risk according to days past due; and • a comparison of the credit risk at the date of transition to the initial maximum credit risk (by product type and/or region).	Yes. The final standard would include application guidance or examples
	First-time adoption	Transitional requirements in the final standard would apply to first-time adopters of IFRS.	Yes. The impairment ED did not include similar transition requirements for first-time adopters

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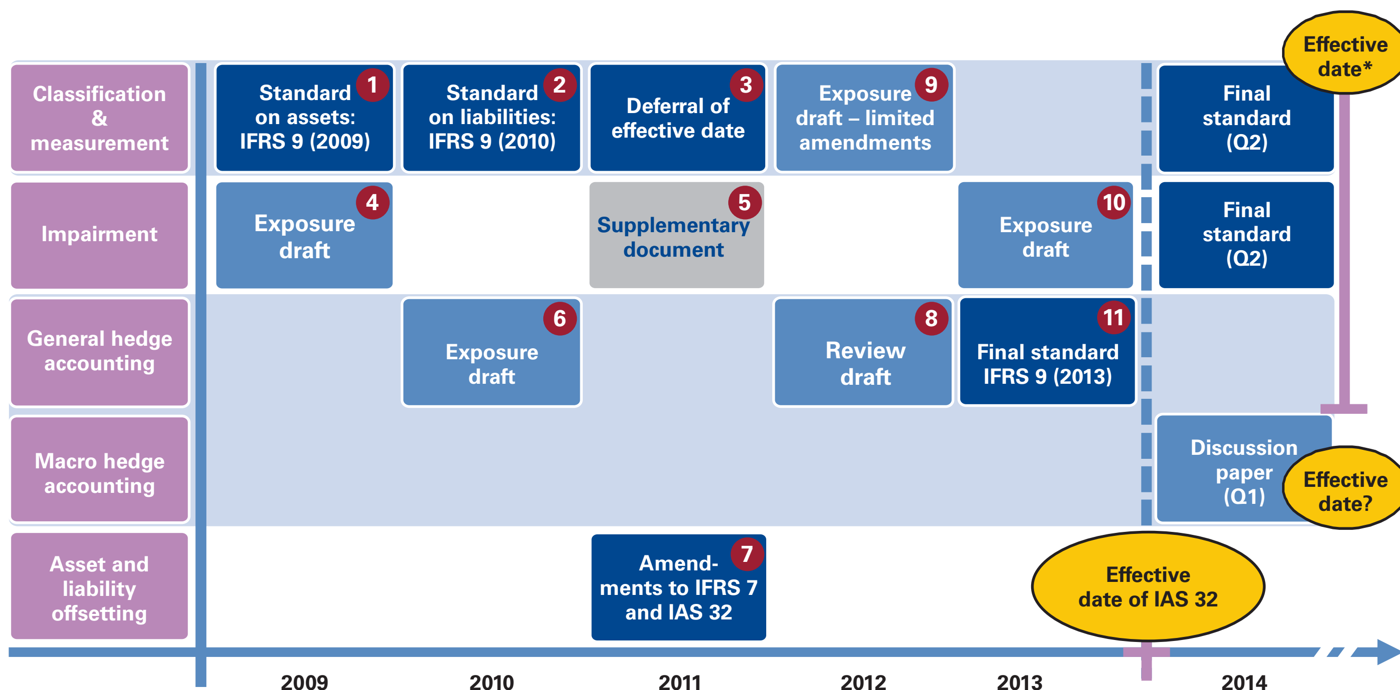
PROJECT MILESTONES AND TIMELINE



Source: IASB work plan – projected targets as at 25 February 2014

* IFRS 9 (2013) removed the previous 1 January 2015 mandatory effective date of IFRS 9. At the IASB's November 2013 meeting, the Board tentatively decided that the mandatory effective date of IFRS 9 would not be before 1 January 2017, but that the final effective date will be determined when the classification and measurement and impairment chapters of IFRS 9 are finalised. At the IASB's February 2014 meeting, the final effective date was tentatively agreed to be 1 January 2018.

Our suite of publications considers the different aspects of the work plan, and provides a comparison to IAS 39 where relevant.

	KPMG publications
1	First Impressions: IFRS 9 Financial Instruments (December 2009) • For KPMG's most recent and comprehensive views on IFRS 9, refer to *Insights into IFRS: Chapter 7A – Financial instruments: IFRS 9*.
2	First Impressions: Additions to IFRS 9 Financial Instruments (December 2010) • For KPMG's most recent and comprehensive views on IFRS 9, refer to *Insights into IFRS: Chapter 7A – Financial instruments: IFRS 9*.
3	In the Headlines: Amendments to IFRS 9 – Mandatory effective date of IFRS 9 deferred to 1 January 2015 (December 2011)
4	New on the Horizon: ED/2009/12 Financial Instruments: Amortised Cost and Impairment (November 2009)
5	New on the Horizon: Impairment of financial assets measured in an open portfolio (February 2011)
6	New on the Horizon: Hedge Accounting (January 2011)
7	First Impressions: Offsetting financial assets and financial liabilities (February 2012)
8	New on the Horizon: Hedge Accounting (September 2012)
9	New on the Horizon: Classification and Measurement – Proposed limited amendments to IFRS 9 (December 2012)
10	New on the Horizon: Financial Instruments – Expected credit losses (March 2013)
11	First Impressions: IFRS 9 (2013) – Hedge accounting and transition (December 2013)

For more information on the project, see our website.

The IASB's website and the FASB's website contain summaries of the Boards' meetings, meeting materials, project summaries and status updates.

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FIND OUT MORE

For more information on the financial instruments (IAS 39 replacement) project, please speak to your usual KPMG contact or visit the IFRS – financial instruments hot topics page, which includes line of business insights.

You can also go to the Financial Instruments page on the IASB website.

Visit KPMG's Global IFRS Institute at kpmg.com/ifrs to access KPMG's most recent publications on the IASB's major projects and other activities.

Our IFRS – revenue hot topics page brings together our materials on the revenue project, including our *IFRS Newsletter: Revenue*.

Our IFRS – leases hot topics page brings together our materials on the leases project, including our *IFRS Newsletter: Leases*.

Our IFRS – insurance hot topics page brings together our materials on the insurance project, including our *IFRS Newsletter: Insurance*.

Our IFRS Breaking News page brings you the latest need-to-know information on international standards in the accounting, audit and regulatory space.

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***IFRS Newsletter: Financial Instruments* is KPMG's update on the IASB's financial instruments project.**

If you would like further information on any of the matters discussed in this Newsletter, please talk to your usual local KPMG contact or call any of KPMG firms' offices.