

FINANCIAL INSTRUMENTS WORKSHOP PROGRAM

Session 2 IFRS 9: Financial Instruments

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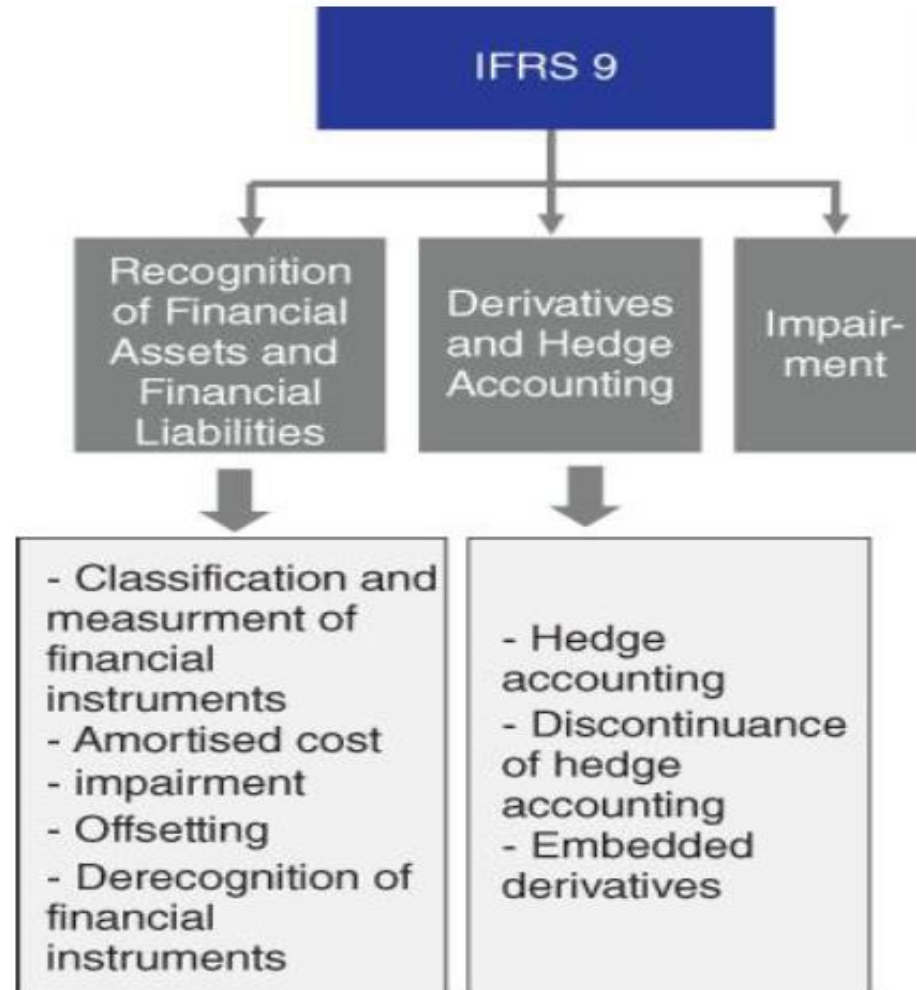


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1. Introduction



As explained before, IFRS 9 replaces IAS 39. It replaced IAS 39 in stages and the full standard now is effective commencing 2018 but early adoption is encouraged.



1. Introduction



Key Changes:

- 3 categories of financial assets instead of 4 in IAS 39
- No change for measurement of financial liabilities except for own credit risk (fair value option)
- A new impairment model based on expected losses: “day-one” provisions to be recognized on most financial assets subject to impairment
- Better alignment between hedge accounting and risk management activities
- More line items to be presented in the statement of profit or loss

2. Objective



The objective of IFRS 9 is to provide principles of reporting of financial assets and financial liabilities.

3. Scope



IFRS 9 Does not apply to

1. Subsidiaries
2. Leases (except for lease receivables and payables and embedded derivatives)
3. Employee benefits payable
4. Insurance Contracts
5. Payables under mergers
6. Provisions and contracts with customer

4. Recognition



A financial asset or a financial liability is recognized when the entity becomes a party to the contract (Except for regular way purchase of financial assets which are recognized on trade date)



5. Classification

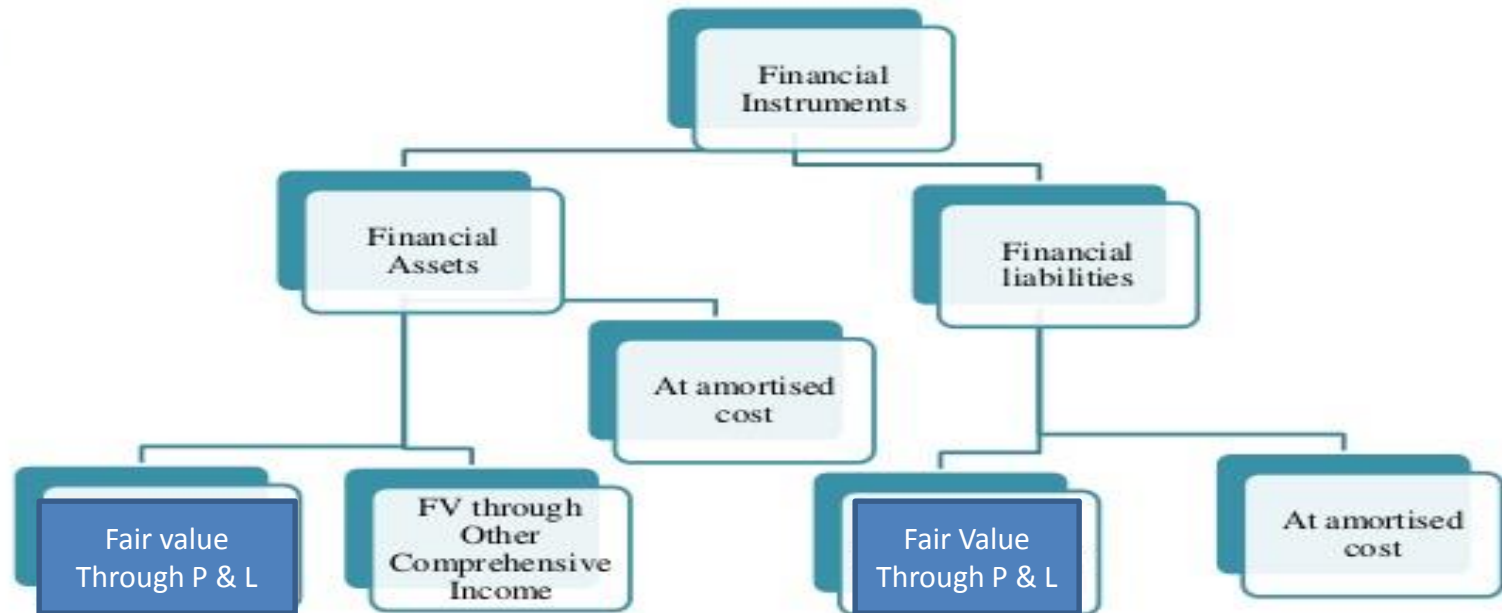


In order to classify financial instruments, IFRS 9 requires an assessment of the:

1. Business model (Is the business model for collecting/paying cash or for sale?)
2. Contractual cash flows (Are the cashflows solely for principal and interest on principal?)

5. Classification

Classification



5. Classification – Financial Assets



1. Financial Assets at Amortized Cost –(FAAC)

These two conditions must be met:

- (i) Business model objective: financial assets held in order to collect contractual cash flows
- (ii) Contractual cash flow characteristics: solely payments of principal and interest on the principal amount outstanding.

For example:

Receivables and **corporate/govt bonds** (intention to hold the bond till their maturity)

5. Classification – Financial Assets



2. Financial Assets at Fair Value through Profit or Loss (FAFVPL)

1. Financial assets that do not meet the amortised cost criteria
2. Financial assets designated at initial recognition.

Generally, if the business model is for sale in the short term
For example:

Investing in Shares/bonds held for trading. Also the appropriate category for derivatives with positive position

5. Classification – Financial Assets



3. Financial Assets at Fair Value through other comprehensive incomes (FAFVOCI)

1. Available **only** for investments in equity instruments that are **not** held for trading.
2. For debt instruments, they meet the SPPI contractual cash flow characteristics test and entity holds the instrument to collect contractual cash flows and to sell the financial assets.

For example investments in shares and bonds with a long term dimension (Please note that this can be sold to realize the cash at a future date: note that we rarely include bonds here but possible)

5. Classification – Financial Liabilities



1. Financial Liabilities at Fair Value Through Profit or Loss (FLTPL)

1. Financial liabilities held for trading
2. Derivative financial liabilities
3. Financial liabilities designated at initial recognition as at Fair Value. For example, if a company issues a bond i.e. borrows and the bond is trading on a stock market with intention to buy back. In addition derivatives with a negative position.

2. Financial Liabilities at Amortized Cost (FLAC)

All other financial liabilities. These include trade payables and loans.

5. Classification – Compare with IAS 39



4 categories in IAS 39

FVTPL

Held for trading & fair value option

HTM

Held-to-maturity investments

Loans & receivables
not held for trading

AFS

Available-for-sale



3 categories in IFRS 9

Amortized cost

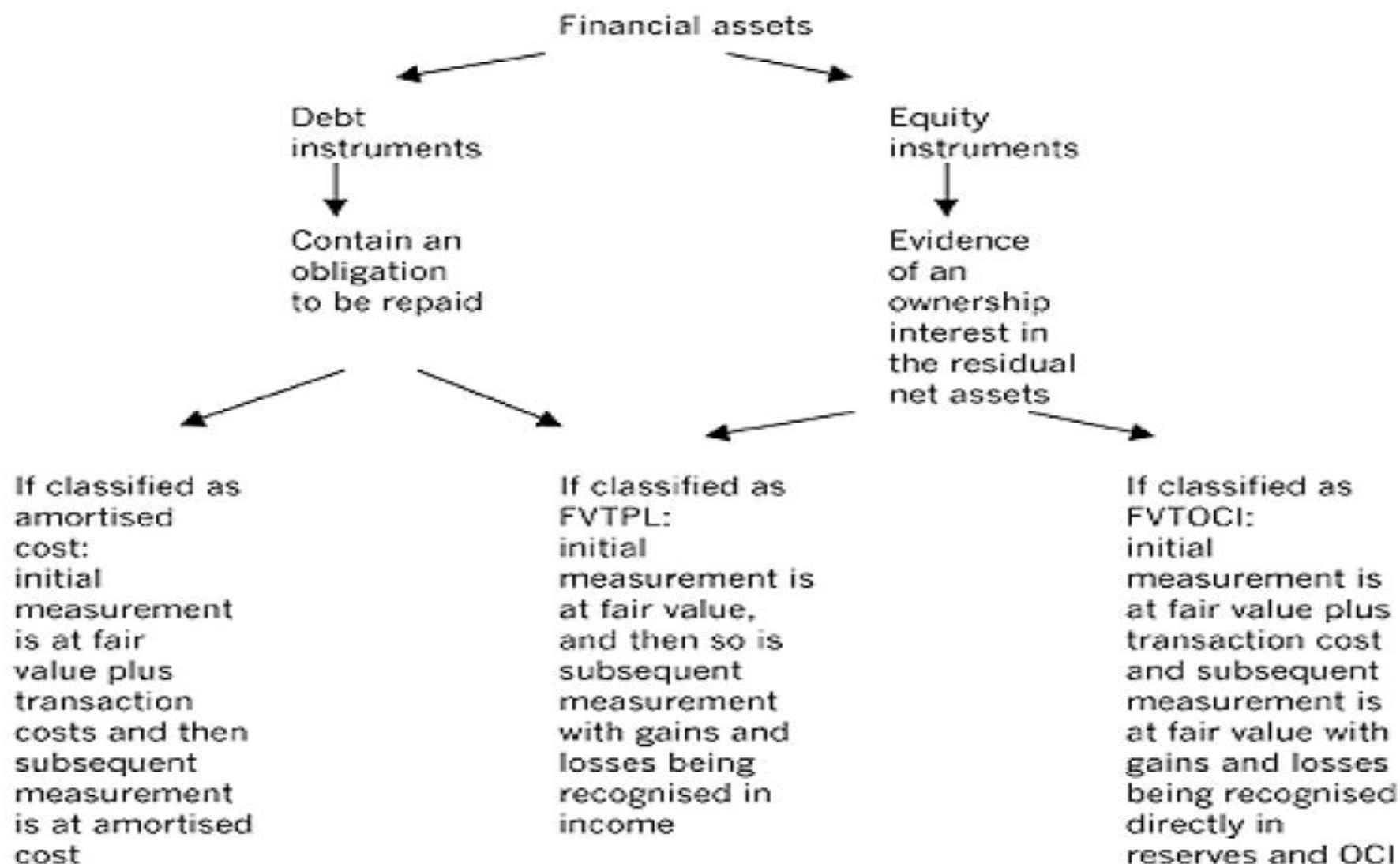
FVTOCI

FVTPL

+ 1 option

FVTOCI for equity investments

5. Measurement – Financial Assets



5. Measurement – Financial Liabilities



Financial liabilities



Contain an obligation to repay



If classified as amortised cost; initial measurement is at fair value less issue costs and then subsequent measurement is at amortised cost



If classified as FVTPL; initial measurement is at fair value, and then so is subsequent measurement with gains and losses being recognised in the income statement

6. Reclassification of financial assets



Reclassification from one category to another is possible for financial assets when and only when an entity changes its business model for managing such assets. Such changes are expected to be very infrequent. Reclassification is prohibited for financial liabilities.

1.From amortized cost to FVTPL: fair value measured at the reclassification date, any gain or loss arising from a difference between the previous amortized cost and fair value is recognized in profit or loss

6. Reclassification of financial assets



2. From **amortized cost to FVTOCI**: fair value measured at the reclassification date, any gain or loss arising from a difference between the previous amortized cost and fair value is recognized in OCI

3. From **FVTPL to amortized cost**: fair value at the reclassification date becomes the new carrying amount.

6. Reclassification of financial assets



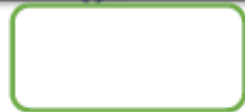
4. From **FVTPL to FVTOCI**: the financial asset continues to be measured at fair value

5. From **FVTOCI to amortized cost**: the financial asset is reclassified at its fair value at the reclassification date; the cumulative gain or loss previously recognized in OCI is removed from equity and adjusted against the fair value of the financial asset at the reclassification date.

6. From FVTOCI to FVTPL: the financial asset continues to be measured at fair value, the cumulative gain or loss previously recognized in OCI is reclassified from equity to profit or loss as a reclassification adjustment at the reclassification date.

7. De-Recognition – Financial Assets

Derecognition of financial assets



An entity should derecognize a financial asset when:

Contractual rights to the cash flows
from the financial asset expire

The entity transfers

financial asset



risks and rewards of ownership



+ transfer *qualifies* for derecognition

On derecognition of a financial asset, the difference between the fair value of consideration received if any and the value of the financial asset on date of sale should be reported in the profit or loss

7. De-Recognition – Financial Liabilities



- A financial liability is derecognised only when extinguished - i.e., when the obligation specified in the contract is discharged, cancelled or it expires
- An exchange between an existing borrower and lender of debt instruments with substantially different terms or substantial modification of the terms of an existing financial liability of part thereof is accounted for as an extinguishment
- The difference between the carrying amount of a financial liability extinguished or transferred to a 3rd party and the consideration paid is recognised in profit or loss.

Derecognition – Financial Liabilities



- Financial liability (or part thereof) is removed from the balance sheet when it is extinguished, i.e. when the obligation is discharged or cancelled or expires

IAS 1 Presentation of IFRS 9



1. Revenue, presenting separately interest revenue calculated using the effective interest method;
2. Gains or losses arising from the derecognition of financial assets measured at amortized cost;
3. Impairment losses (including reversals) determined in accordance with IFRS 9;

IAS 1 Presentation of IFRS 9



4. Gains or losses arising on reclassification of a financial asset out of the amortized cost category into the FVTPL category;
5. If a financial asset is reclassified out of the FVTOCI category into the FVTPL category, any cumulative gain or loss previously recognized in OCI that is reclassified to profit or loss.