IFRS 9/ IPSAS 41: Exposure Draft Classification, Measurement and Recognition

Transition from IAS 39

Jim McFie
Convenor, Membership & Quality Assurance Committee, ICPAK

Thursday, 12th September 2018

Effective date & purpose

- IFRS 9 (issued in 2014) is mandatorily effective for periods beginning on or after 1 January 2018
- The objective of the Standard is to establish principles for the financial reporting of *financial assets* and *financial liabilities* that will present relevant and useful information to users of financial statements for their assessment of the amounts, timing and uncertainty of an entity's future cash flows.

Applies to?

To all types of financial instruments: except

- interests in subsidiaries, associates and joint ventures;
- rights and obligations under leases to which IFRS 16 Leases applies;
- employers' rights and obligations under employee benefit plans;
- financial instruments issued by the entity that meet the definition of an equity instrument in IAS 32 (including options and warrants);
- rights and obligations arising under an insurance contract as defined in IFRS 4 Insurance Contracts.

Not within the scope of IFRS 9

- Loan commitments that the entity designates as financial liabilities at fair value through profit or loss;
- Loan commitments that can be settled net in cash or by delivering or issuing another financial instrument: these loan commitments are derivates;
- Commitments to provide a loan at a below-market interest rate.

Recognition

3.1.1 An entity recognises a financial asset or a financial liability in its statement of financial position when, and only when, the entity becomes party to the contractual provisions of the instrument. When an entity first recognises a financial asset, it classifies it in accordance with paragraphs 4.1.1 – 4.1.5 and measures it in accordance with paragraphs 5.1.1 – 5.1.3. When an entity first recognises a financial liability, it classifies it in accordance with paragraphs 4.2.1 and 4.2.2 and measures it in accordance with paragraph 5.1.1.

Derecognition

3.2.3 An entity derecognises a financial asset when, and only when: (a) the contractual rights to the cash flows from the financial asset expire, or (b) it transfers the financial asset and the transfer qualifies
for derecognition in accordance
with paragraph 3.2.6.

Transfer a financial asset?

3.2.4 An entity transfers a financial asset if, and only if, it either: (a) transfers the contractual rights to receive the cash flows of the financial asset, or (b) retains the contractual rights to receive the cash flows of the financial asset, but assumes a contractual obligation to pay the cash flows to one or more recipients in an arrangement that meets the conditions in paragraph 3.2.5.

Conditions (1)

3.2.5 When an entity retains the contractual rights to receive the cash flows of a financial asset (the 'original asset'), but assumes a contractual obligation to pay those cash flows to one or more entities (the 'eventual recipients'), the entity treats the transaction as a transfer of a financial asset if, and only if: (1) The entity has no obligation to pay amounts to the eventual recipients unless it collects equivalent amounts from the original asset. Short-term advances by the entity with the right of full recovery of the amount lent plus accrued interest at market rates do not violate this condition; and (2) The entity is prohibited by the terms of the transfer contract from selling or pledging the original asset other than as security to the eventual recipients for the obligation to pay them cash flows; and

Conditions (2)

(3) The entity has an obligation to remit any cash flows it collects on behalf of the eventual recipients without material delay. In addition, the entity is not entitled to reinvest such cash flows, except for investments in cash or cash equivalents (as defined in IAS 7 Statement of Cash Flows) during the short settlement period from the collection date to the date of required remittance to the eventual recipients, and interest earned on such investments is passed to the eventual recipients

Profit/loss on disposal

3.2 12 On derecognition of a financial asset in its entirety, the difference between: (1) the carrying amount (measured at the date of derecognition) and (2) the consideration received (including any new asset obtained less any new liability assumed) shall be recognised in profit or loss

De-recognition of financial liabilities

3.3.1 An entity removes a financial liability (or a part of a financial liability) from its statement of financial position when, and only when, it is extinguished—i.e. when the obligation specified in the contract is discharged or cancelled or expires. An exchange between an existing borrower and lender of debt instruments with substantially different terms shall be accounted for as an extinguishment of the original financial liability and the recognition of a new financial liability

De-recognition

3.3.2 Similarly, a substantial modification of the terms of an existing financial liability or a part of it (whether or not attributable to the financial difficulty of the debtor) shall be accounted for as an extinguishment of the original financial liability and the recognition of a new financial liability. The difference between the carrying amount of a financial liability extinguished or transferred to another party and the consideration paid, including any non-cash assets transferred or liabilities assumed, shall be recognised in profit or loss.

Classification of financial assets (1)

4.1.1 An entity classifies financial assets as subsequently measured at

(a) amortised cost,

(b) fair value through other comprehensive income or

(c) fair value through profit or loss on the basis of both:

(1) the entity's business model for managing the financial assets and

(2) the contractual cash flow characteristics of the financial asset.

Classification of financial assets (1a)

Definition: The amortised cost of a financial asset or financial liability is the amount at which the financial asset or financial liability is measured at initial recognition minus the principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between that initial amount and the maturity amount and, for financial assets, adjusted for any loss allowance.

The gross carrying amount of a financial asset is the amortised cost of a financial asset, before adjusting for any loss allowance

Classification of financial assets (1b)

A loss allowance is the allowance for expected credit losses on financial assets measured in accordance with paragraph 4.1.2, lease receivables and contract assets, the accumulated impairment amount for financial assets measured in accordance with paragraph 4.1.2A and the provision for expected credit losses on loan commitments and financial guarantee contracts.

A financial guarantee contract is one that requires the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the original or modified terms of a debt instrument.

Effective interest rate

The rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial asset or financial liability to the gross carrying amount of a financial asset or to the amortised cost of a financial liability. When calculating the effective interest rate, an entity shall estimate the expected cash flows by considering all the contractual terms of the financial instrument (for example, prepayment, extension) but shall not consider the expected credit losses. The calculation includes all fees and points paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs, and all other premiums or discounts.

Amortised cost

The amount at which the financial asset or financial liability is measured at initial recognition minus the principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between that initial amount and the maturity amount and, for financial assets, adjusted for any loss allowance

Classification of financial assets (a)

4.1.2 A financial asset shall be measured at amortised cost if both of the following conditions are met:

(a) the financial asset is held within a business model whose objective is to hold financial assets in order to collect contractual cash flows and

(b) the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

Measurement of financial assets (b)

4.1.2A A financial asset shall be measured at fair value through other comprehensive income if both of the following conditions are met:
(a) the financial asset is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets and (b) the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

Measurement of financial assets (c)

4.1.2A A financial asset shall be measured at fair value through other comprehensive income if both of the following conditions are met:
(a) the financial asset is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets and (b) the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

Measurement of financial assets (b & c)

4.1.3 For the purpose of applying paragraphs 4.1.2(b) and 4.1.2A(b): (a) principal is the fair value of the financial asset at initial recognition; (b) interest consists of consideration for the time value of money, for the credit risk associated with the principal amount outstanding during a particular period of time and for other basic lending risks and costs, as well as a profit margin.

Measurement of financial assets (c)

4.1.4 A financial asset is measured at fair value through profit or loss unless it is measured at amortised cost in accordance with paragraph 4.1.2 or at fair value through other comprehensive income in accordance with paragraph 4.1.2A.

However an entity may make an irrevocable election at initial recognition for particular investments in equity instruments that would otherwise be measured at fair value through profit or loss to present subsequent changes in fair value in other comprehensive income.

Measurement of financial assets option

4.1.5 Despite paragraphs 4.1.1 – 4.1.4, an entity may, at initial recognition, irrevocably designate a financial asset as measured at fair value through profit or loss if doing so eliminates or significantly reduces a measurement or recognition inconsistency (sometimes referred to as an 'accounting mismatch') that would otherwise arise from measuring assets or liabilities or recognising the gains and losses on them on different bases.

Classification of financial liabilities (1)

4.2.1 An entity shall classify all financial liabilities as subsequently measured at amortised cost, except for:

(a) *financial liabilities at fair value through profit or loss*. Such liabilities, including derivatives that are liabilities, shall be subsequently measured at fair value;

(b) financial liabilities that arise when a transfer of a financial asset does not qualify for derecognition or when the continuing involvement approach applies: paragraphs 3.2.15 and 3.2.17 apply to the measurement of such financial liabilities

Classification of financial liabilities (2)

(c) financial guarantee contracts: after initial recognition, an issuer of such a contract shall (unless paragraph 4.2.1(a) or (b) applies) subsequently measure it at the higher of (i) the amount of the loss allowance determined in accordance with Section 5.5 and (ii)the amount initially recognised (see paragraph 5.1.1) less, when appropriate, the cumulative amount of income recognised in accordance with the principles of IFRS 15.

Classification of financial liabilities (3)

(d) commitments to provide a loan at a below-market interest rate. An issuer of such a commitment shall (unless paragraph 4.2.1(a) applies) subsequently measure it at the higher of: (i) the amount of the loss allowance determined in accordance with Section 5.5 and (ii) the amount initially recognised (see paragraph 5.1.1) less, when appropriate, the cumulative amount of income recognised in accordance with the principles of IFRS 15.

Classification of financial liabilities (4)

(d) contingent consideration recognised by an acquirer in a business combination to which IFRS 3 applies. Such contingent consideration shall subsequently be measured at fair value with changes recognised in profit or loss.

Option to designate (1)

4.2.2 An entity may, at initial recognition, irrevocably designate a financial liability as measured at fair value through profit or loss when permitted by paragraph 4.3.5, or when doing so results in more relevant information, because either: (a) it eliminates or significantly reduces a measurement or recognition inconsistency (sometimes referred to as 'an accounting mismatch') that would otherwise arise from measuring assets or liabilities or recognising the gains and losses on them on different bases; or

Option to designate (2)

(b) a group of financial liabilities or financial assets and financial liabilities is managed and its performance is evaluated on a fair value basis, in accordance with a documented risk management or investment strategy, and information about the group is provided internally on that basis to the entity's key management personnel (as defined in IAS 24 Related Party Disclosures), for example, the entity's board of directors and chief executive officer

Reclassification (1)

4.4.1 When, and only when, an entity changes its business model for managing financial assets it reclassifies all affected financial assets in accordance with paragraphs 4.1.1 -4.1.4.

4.4.2 An entity must not reclassify any financial liability.

4.4.3 The following changes in circumstances are not reclassifications for the purposes of paragraphs 4.4.1 – 4.4.2:

Reclassification (2)

(a) an item that was previously a designated and effective hedging instrument in a cash flow hedge or net investment hedge no longer qualifies as such;
(b) an item becomes a designated and effective hedging instrument in a cash flow hedge or net investment hedge;
(c) changes in measurement in accordance with Section 6.7.

Initial measurement (1)

5.1.1 Except for trade receivables within the scope of paragraph 5.1.3, at initial recognition, an entity measures a financial asset or financial liability at its fair value plus or minus, in the case of a financial asset or financial liability not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue of the financial asset or financial liability

Initial measurement (2)

5.1.1A However, if the fair value of the financial asset or financial liability at initial recognition differs from the transaction price, an entity shall apply paragraph B5.1.2A.

Subsequent measurement (1)

5.2.1 After initial recognition, an entity measures a financial asset in accordance with paragraphs 4.1.1 - 4.1.5 at: (a) amortised cost; (b) fair value through other comprehensive income; or (c) fair value through profit or loss.

5.2.2 An entity applies the impairment requirements in Section 5.5 to financial assets that are measured at amortised cost in accordance with para 4.1.2 and to financial assets that are measured at fair value through other comprehensive income in accordance with para 4.1.2A.

Subsequent measurement (2)

5.3.1 After initial recognition, an entity shall measure a financial liability in accordance with paragraphs 4.2.1 – 4.2.2.

5.4.1 Calculate interest revenue using the effective interest method by applying the effective interest rate to the gross carrying amount of a financial asset except for: (a) purchased or originated credit-impaired financial assets. For those financial assets, the entity shall apply the credit-adjusted effective interest rate to the amortised cost of the financial asset from initial recognition.

Definitions (1)

Expected credit losses are the weighted average of credit losses with the respective risks of a default occurring as the weights.
Lifetime expected credit losses are the expected credit losses that result from all possible default events over the expected life of a financial instrument.

Definitions (2)

12-month expected credit losses are the portion of lifetime expected credit losses that represent the expected credit losses that result from default events on a financial instrument that are possible within the 12 months after the reporting date.

A loss allowance is the allowance for expected credit losses on financial assets measured in accordance with paragraph 4.1.2, lease receivables and contract assets, the accumulated impairment amount for financial assets measured in accordance with paragraph 4.1.2A and the provision for expected credit losses on loan commitments and financial guarantee contracts.

Definitions (3)

Credit-adjusted effective interest rate is the rate that exactly discounts the estimated future cash payments or receipts through the expected life of the financial asset to the amortised cost of a financial asset that is a purchased or originated credit-impaired financial asset. When calculating the credit-adjusted effective interest rate, an entity estimates the expected cash flows by considering all contractual terms of the financial asset (for example, prepayment, extension, call and similar options) and expected credit losses. The calculation includes all fees and points paid or received between parties to the contract that are an integral part of the effective interest rate (see paragraphs B5.4.1–B5.4.3), transaction costs, and all other premiums or discounts. There is a presumption that the cash flows and the expected life of a group of similar financial instruments can be estimated reliably. However, in those rare cases when it is not possible to reliably estimate the cash flows or the remaining life of a financial instrument (or group of financial instruments), the entity shall use the contractual cash flows over the full contractual term of the financial instrument (or group of financial instruments)

Subsequent measurement (3)

(b) financial assets that are not purchased or originated credit-impaired financial assets but subsequently have become credit impaired financial assets. For those financial assets, the entity shall apply the effective interest rate to the amortised cost of the financial asset in subsequent reporting periods

Subsequent measurement (4)

5.4.3 When the contractual cash flows of a financial asset are renegotiated or otherwise modified and the renegotiation or modification does not result in the derecognition of that financial asset in accordance with this Standard, an entity shall recalculate the gross carrying amount of the financial asset and shall recognise a modification gain or loss in profit or loss.

Subsequent measurement (5)

Recalculate the gross carrying amount of the financial asset as the present value of the renegotiated or modified contractual cash flows that are discounted at the financial asset's original effective interest rate (or credit-adjusted effective interest rate for purchased or originated credit-impaired financial assets) or, when applicable, the revised effective interest rate calculated in accordance with paragraph 6.5.10. Any costs or fees incurred adjust the carrying amount of the modified financial asset and are amortised over the remaining term of the modified financial asset

Write-off

5.4.4 An entity shall directly reduce the gross carrying amount of a financial asset when the entity has no reasonable expectations of recovering a financial asset in its entirety or a portion thereof. A write-off constitutes a derecognition event.

Expected credit losses

5.5.1 An entity recognises a loss allowance for expected credit losses on a financial asset that is measured in accordance with paragraphs 4.1.2 or 4.1.2A, a lease receivable, a contract asset or a loan commitment and a financial guarantee contract to which the impairment requirements apply in accordance with paragraphs 2.1 (g), 4.2.1 (c) or 4.2.1 (d).

Expected credit losses (1)

5.5.3 Subject to paragraphs 5.5.13 – 5.5.16, at each reporting date, an entity shall measure the loss allowance for a financial instrument at an amount equal to the lifetime expected credit losses if the credit risk on that financial instrument has increased significantly since initial recognition

Expected credit losses (2)

5.5.4 The objective of the impairment requirements is to recognise lifetime expected credit losses for all financial instruments for which there have been significant increases in credit risk since initial recognition — whether assessed on an individual or collective basis — considering all reasonable and supportable information, including that which is forward-looking.

Expected credit losses (3)

5.5.5 Subject to paragraphs 5.5.13 – 5.5.16, if, at the reporting date, the credit risk on a financial instrument has not increased significantly since initial recognition, an entity shall measure the loss allowance for that financial instrument at an amount equal to the 12-month expected credit losses.

Expected credit losses (4)

5.5.6 For loan commitments and financial guarantee contracts, the date that the entity becomes a party to the irrevocable commitment is considered to be the date of initial recognition for the purposes of applying the impairment requirements..

Expected credit losses (5)

5.5.7 If an entity has measured the loss allowance for a financial instrument at an amount equal to lifetime expected credit losses in the previous reporting period, but determines at the current reporting date that paragraph 5.5.3 is no longer met, the entity shall measure the loss allowance at an amount equal to 12-month credit losses at the current reporting date.

Expected credit losses (6)

5.5.8 An entity recognises in profit or loss, as an impairment gain or loss, the amount of expected credit losses (or reversal) that is required to adjust the loss allowance at the reporting date to the amount that is required to be recognised in accordance with this Standard.

Increases in credit risk (1)

5.5.8 At each reporting date, an entity assesses whether the credit risk on a financial instrument has increased significantly since initial recognition. When making the assessment, an entity uses the change in the risk of a default occurring over the expected life of the financial instrument instead of the change in the amount of expected credit losses. To make that assessment, an entity compares the risk of a default occurring on the financial instrument as at the reporting date with the risk of a default occurring on the financial instrument as at the date of initial recognition and considers reasonable and supportable information, that is available without undue cost or effort, that is indicative of significant increases in credit risk since initial recognition.

Increases in credit risk(2)

5.5.10 An entity may assume that the credit risk on a financial instrument has not increased significantly since initial recognition if the financial instrument is determined to have low credit risk at the reporting date.

5.5.11 If reasonable and supportable forward-looking information is available without undue cost or effort, an entity cannot rely solely on past due information when determining whether credit risk has increased significantly since initial recognition.

A financial asset is past due when a counterparty has failed to make a payment when that payment was contractually due.

Increases in credit risk(3)

5.5.11 However, when information that is more forward-looking than past due status (either on an individual or a collective basis) is not available without **undue cost or effort**, an entity may use past due information to determine whether there have been significant increases in credit risk since initial recognition. Regardless of the way in which an entity assesses significant increases in credit risk, there is a rebuttable presumption that the credit risk on a financial asset has increased significantly since initial recognition when contractual payments are more than 30 days past due.

Increases in credit risk(4)

5.5.11 An entity can rebut this presumption if the entity has reasonable and supportable information that is available without undue cost or effort, that demonstrates that the credit risk has not increased significantly since initial recognition even though the contractual payments are more than 30 days past due. When an entity determines that there have been significant increases in credit risk before contractual payments are more than 30 days past due, the rebuttable presumption does not apply.

Increases in credit risk(5)

5.5.12 If the contractual cash flows on a financial asset have been renegotiated or modified and the financial asset was not derecognised, an entity assesses whether there has been a significant increase in the credit risk of the financial instrument in accordance with paragraph 5.5.3 by comparing: (a) the risk of a default occurring at the reporting date (based on the modified contractual terms); and (b) the risk of a default occurring at initial recognition (based on the original, unmodified contractual terms)

Purchased or originated credit-impaired financial assets (1)

5.5.13 Despite paragraphs 5.5.3 and 5.5.5, at the reporting date, an entity recognises the cumulative changes in lifetime expected credit losses since initial recognition as a loss allowance for purchased or originated credit-impaired financial assets.

Purchased or originated credit-impaired financial assets (2)

5.5.14 At each reporting date, an entity recognises in profit or loss the amount of the change in lifetime expected credit losses as an impairment gain or loss. An entity recognises favourable changes in lifetime expected credit losses as an impairment gain, even if the lifetime expected credit losses are less than the amount of expected credit losses that were included in the estimated cash flows on initial recognition.

Simplified approach (1)

5.5.15 Despite paragraphs 5.5.3 and 5.5.5, an entity shall always measure the loss allowance at an amount equal to lifetime expected credit losses for: (a) trade receivables or contract assets that result from transactions that are within the scope of IFRS 15, and that (i) do not contain a significant financing component in accordance with IFRS 15; (ii) contain a significant financing component in accordance with IFRS 15, if the entity chooses as its accounting policy to measure the loss allowance at an amount equal to lifetime expected credit losses. That accounting policy is applied to all such trade receivables or contract assets but may be applied separately to trade receivables and contract assets.

Simplified approach (2)

5.5.15 (b) lease receivables that result from transactions that are within the scope of IFRS 16, if the entity chooses as its accounting policy to measure the loss allowance at an amount equal to lifetime expected credit losses. That accounting policy must be applied to all lease receivables but may be applied separately to finance and operating lease receivables.

5.5.16 An entity may select its accounting policy for trade receivables, lease receivables and contract independently of each other.

Measurement of expected credit losses (1)

5.5.17 An entity measures expected credit losses of a financial instrument in a way that reflects: (a) an unbiased and probability-weighted amount that is determined by evaluating a range of possible outcomes; (b) the time value of money; and (c) reasonable and supportable information that is available without undue cost or effort at the reporting date about past events, current conditions and forecasts of future economic conditions.

Measurement of expected credit losses (2)

5.5.18 When measuring expected credit losses, an entity need not necessarily identify every possible scenario. However, it considers the risk or probability that a credit loss occurs by reflecting the possibility that a credit loss occurs and the possibility that no credit loss occurs, even if the possibility of a credit loss occurring is very low.

5.5.19 The maximum period to consider when measuring expected credit losses is the maximum contractual period (including extension options) over which the entity is exposed to credit risk and not a longer period, even if that longer period is consistent with business practice.

Measurement of expected credit losses (3)

5.5.20 However, some financial instruments include both a loan and an undrawn commitment component and the entity's contractual ability to demand repayment and cancel the undrawn commitment does not limit the entity's exposure to credit losses to the contractual notice period. For such financial instruments, and only those financial instruments, the entity shall measure expected credit losses over the period that the entity is exposed to credit risk and expected credit losses would not be mitigated by credit risk management actions, even if that period extends beyond the maximum contractual period.

Reclassification of financial assets (1)

5.6.1 If an entity reclassifies financial assets in accordance with paragraph 4.4.1, it applies the reclassification prospectively from the reclassification date. The entity does not restate any previously recognised gains, losses (including impairment gains or losses) or interest.

Reclassification of financial assets (2)

5.6.2 If an entity reclassifies a financial asset out of the amortised cost measurement category and into the fair value through profit or loss measurement category, its fair value is measured at the reclassification date. Any gain or loss arising from a difference between the previous amortised cost of the financial asset and fair value is recognised in profit or loss.

Reclassification of financial assets (3)

5.6.3 If an entity reclassifies a financial asset out of the fair value through profit or loss measurement category and into the amortised cost measurement category, its fair value at the reclassification date becomes its new gross carrying amount.

Reclassification of financial assets (4)

5.6.4 If an entity reclassifies a financial asset out of the amortised cost measurement category and into the fair value through other comprehensive income measurement category, its fair value is measured at the reclassification date. Any gain or loss arising from a difference between the previous amortised cost of the financial asset and fair value is recognised in other comprehensive income. The effective interest rate and the measurement of expected credit losses are not adjusted as a result of the reclassification.

Reclassification of financial assets (5)

5.6.5 If an entity reclassifies a financial asset out of the fair value through other comprehensive income measurement category and into the amortised cost measurement category, the financial asset is reclassified at its fair value at the reclassification date. However, the cumulative gain or loss previously recognised in other comprehensive income is removed from equity and adjusted against the fair value of the financial asset at the reclassification date.

Reclassification of financial assets (6)

5.6.5 (contd) As a result, the financial asset is measured at the reclassification date as if it had always been measured at amortised cost. This adjustment affects other comprehensive income but does not affect profit or loss and therefore is not a reclassification adjustment. The effective interest rate and the measurement of expected credit losses are not adjusted as a result of the reclassification.

Reclassification of financial assets (7)

5.6.6 If an entity reclassifies a financial asset out of the fair value through profit or loss measurement category and into the fair value through other comprehensive income measurement category, the financial asset continues to be measured at fair value.

Reclassification of financial assets (8)

5.6.7 If an entity reclassifies a financial asset out of the fair value through other comprehensive income measurement category and into the fair value through profit or loss measurement category, the financial asset continues to be measured at fair value. The cumulative gain or loss previously recognised in other comprehensive income is reclassified from equity to profit or loss as a reclassification adjustment at the reclassification date.

Gains and losses (1)

5.7.1 A gain or loss on a financial asset or financial liability that is measured at fair value shall be recognised in profit or loss unless: (b) it is an investment in an equity instrument and the entity has elected to present gains and losses on that investment in other comprehensive income in accordance with paragraph 5.7.5; (c) it is a financial liability designated as at fair value through profit or loss and the entity is required to present the effects of changes in the liability's credit risk in other comprehensive income in accordance with paragraph 5.7.7;

Gains and losses (2)

5.7.1 (d) it is a financial asset measured at fair value through other comprehensive income in accordance with paragraph 4.1.2A and the entity is required to recognise some changes in fair value in other comprehensive income in accordance with paragraph 5.7.10.

Gains and losses (3)

5.7.1A Dividends are recognised in profit or loss only when: (a) the entity's right to receive payment of the dividend is established; (b) it is probable that the economic benefits associated with the dividend will flow to the entity; and (c) the amount of the dividend can be measured reliably.

Gains and losses (4)

5.7.2 A gain or loss on a financial asset that is measured at amortised cost and is not part of a hedging relationship is recognised in profit or loss when the financial asset is derecognised, reclassified in accordance with paragraph 5.6.2, through the amortisation process or in order to recognise impairment gains or losses. An entity shall apply paragraphs 5.6.2 and 5,6,4 if it reclassifies financial assets out of the amortised cost measurement category. A gain or loss on a financial liability that is measured at amortised cost and is not part of a hedging relationship is recognised in profit or loss when the financial liability is derecognised and through the amortisation process.

Investments in equity instruments (1)

5.7.5 At initial recognition, an entity may make an irrevocable election to present in other comprehensive income subsequent changes in the fair value of an investment in an equity instrument within the scope of this Standard that is neither held for trading nor contingent consideration recognised by an acquirer in a business combination to which IFRS 3 applies.

Investments in equity instruments (2)

5.7.6 If an entity makes the election in paragraph 5.7.5, it recognises in profit or loss dividends from that investment in accordance with paragraph 5.7.1A.

Liabilities at fair value through profit or loss (1)

5.7.7 An entity present a gain or loss on a financial liability that is designated as at fair value through profit or loss in accordance with paragraph 4.2.2 or paragraph 4.3.5 as follows: (a) The amount of change in the fair value of the financial liability that is attributable to changes in the credit risk of that liability shall be presented in other comprehensive income, and (b)

Liabilities at fair value through profit or loss (2)

5.7.7 (b) the remaining amount of change in the fair value of the liability is presented in profit or loss unless the treatment of the effects of changes in the liability's credit risk described in (a) would create or enlarge an accounting mismatch in profit or loss (in which case paragraph 5.7.8 applies)

Liabilities at fair value through profit or loss (3)

5.7.7 (b) the remaining amount of change in the fair value of the liability is presented in profit or loss unless the treatment of the effects of changes in the liability's credit risk described in (a) would create or enlarge an accounting mismatch in profit or loss (in which case paragraph 5.7.8 applies)

Liabilities at fair value through profit or loss (4)

5.7.8 If the requirements in paragraph 5.7.7 would create or enlarge an accounting mismatch in profit or loss, an entity shall present all gains or losses on that liability (including the effects of changes in the credit risk of that liability) in profit or loss.

5.7.9 Despite the requirements in paragraphs 5.7.7 and 5.7.8, an entity presents in profit or loss all gains and losses on loan commitments and financial guarantee contracts that are designated as at fair value through profit or loss.

Assets at fair value through OCI (1)

5.7.10 A gain or loss on a financial asset measured at fair value through other comprehensive income in accordance with paragraph 4.1.2 is recognised in other comprehensive income, except for impairment gains or losses and foreign exchange gains and losses, until the financial asset is derecognised or reclassified. When the financial asset is derecognised the cumulative gain or loss previously recognised in other comprehensive income is reclassified from equity to profit or loss as a reclassification adjustment.

Assets at fair value through OCI (2)

5.7.10 If the financial asset is reclassified out of the fair value through other comprehensive income measurement category, the entity accounts for the cumulative gain or loss that was previously recognised in other comprehensive income in accordance with paragraphs 5.6.5 and 5.6.7. Interest calculated using the effective interest method is recognised in profit or loss.

Assets at fair value through OCI (3)

5.7.11 As described in paragraph 5.7.10, if a financial asset is measured at fair value through other comprehensive income in accordance with paragraph 4.1.2A, the amounts that are recognised in profit or loss are the same as the amounts that would have been recognised in profit or loss if the financial asset had been measured at amortised cost.

Transition (1)

7.2.1 An entity shall apply this Standard retrospectively, in accordance with IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors.

This Standard is not applied to items that have already been derecognised at the date of initial application.

Transition (2)

7.2.2 For the purposes of the transition provisions, the date of initial application is the date when an entity first applies those requirements of this Standard and must be the beginning of a reporting period after the issue of this Standard. Depending on the entity's chosen approach to applying IFRS 9, the transition can involve one or more than one date of initial application for different requirements.

Transition (3)

7.2.3 At the date of initial application, an entity shall assess whether a financial asset meets the condition in paragraphs 4.1.2(a) or 4.1.2A(a) on the basis of the facts and circumstances that exist at that date. The resulting classification is applied retrospectively irrespective of the entity's business model in prior reporting periods.

The effect on Barclays (1)

- The period reported on is the 9 months to 30 September 2017.
- Barclays Africa has been sold already.
- Barclays estimates that the IFRS 9 impact, based on its portfolio as at 30 September 2017, is a decrease in shareholders' equity of approximately £2.0bn post tax. Its market capitalization as at 30 September 2017 was £43.58 bn (on 29 January 2018 it was £49.86 bn).
- The estimated decrease in shareholders' equity includes the impact of both balance sheet classification and measurement changes and the increase in credit impairment provisions compared to those applied at 30 September 2017 under IAS 39.

The effect on Barclays (2)

- The adoption of certain classification and measurement accounting changes remain subject to endorsement by the European Union.
- This assessment is a point of time estimate and is not a forecast.
- The actual effect of the implementation of IFRS 9 on Barclays PLC could vary significantly from this estimate.
- Barclays continues to refine models, methodologies and controls, and monitor developments in regulatory rule-making in advance of IFRS 9 adoption on 1 January 2018.
- All estimates are based on Barclays' current interpretation of the requirements of IFRS 9, reflecting industry guidance and discussions to date.

The effect on Barclays (3)

- The Group's CET1 ratio will be impacted by IFRS 9 primarily from an increase in credit impairment provisions net of tax and any deduction of deferred tax assets arising from temporary differences being in excess of the allowable regulatory allowable threshold.
- This is partially offset by a reduction in the regulatory expected loss over impairment deductions and reduced RWAs (Rise Weighted Assets)
- Based on figures as at 30 September 2017, the expected CET1 impact without transitional arrangements would be an estimated reduction of approximately 40 bps.

The effect on Barclays (4)

- Barclays expects to implement transitional arrangements for capital purposes, currently being finalized by European Regulators, which would result in only a proportion of the estimated reduction impacting the CET1 ratio during 2018.
- The final impact of IFRS 9 is estimated to be approximately 20 bps lower than the point in time impact as deferred tax assets are expected to fall below the allowable threshold over time.
- Barclays plans to publish transitional disclosures during the first quarter of 2018 describing the 1 January 2018 impact of adoption of IFRS 9.

Lloyds Banking Group

- IFRS 9 : The Group's IFRS 9 implementation is nearing completion, including embedding of the new systems and processes.
- It is currently expected that the CET1 capital impact before any transitional relief will be a reduction of between 10 to 30 basis points after taking account of any offset against regulatory expected losses, mainly as a result of additional impairment provisions.
- As a consequence, on transition IFRS 9 is not expected to have a material impact on the Group's capital position.

Royal Bank of Canada(1)

In January 2015, the Office of the Superintendent of Financial Institutions Canada (OSFI) issued an advisory with respect to the early adoption of IFRS 9 for Domestic Systemically Important Banks (D-SIBs), requiring D-SIBs to adopt IFRS 9 for the annual period beginning on November 1, 2017. As a result, we are required to adopt IFRS 9 on November 1, 2017, with the exception of the own credit provisions of IFRS 9, which we adopted in the second quarter of 2014. In June 2016, OSFI issued its final guideline on IFRS 9 Financial Instruments and Disclosures. The guideline provides guidance to Federally Regulated Entities on the application of IFRS 9, including the implementation of the expected credit loss framework under IFRS 9.

Royal Bank of Canada(2)

The OSFI guideline is effective for us on November 1, 2017, consistent with the adoption of IFRS 9. The new classification and measurement and impairment requirements will be applied by adjusting our Consolidated Balance Sheet on November 1, 2017, the date of initial application, with no restatement of comparative period financial information. Based on current estimates, the adoption of IFRS 9 is expected to result in a reduction to retained earnings as at November 1, 2017 of approximately $600 million, net of taxes. The impact is primarily attributable to increases in the allowance for credit losses under the new impairment requirements. We do not expect the adoption of IFRS 9 to have a significant impact on our CET1 capital. We continue to monitor and refine certain elements of our impairment process in advance of Q1 2018 reporting.

Royal Bank of Canada(3)

Equity attributable to shareholders (Note 21)	2017	2016
	\$m	\$m
Preferred shares	6,413	6,713
Common shares (shares issued – 1,452,534,303 and 1,484,234,375)	17,703	17,859
Retained earnings	45,359	41,519
Other components of equity	4,354	4,926
	73,829	71,017

Royal Bank of Canada(4)

	2017	2016
Consolidated Statement of Income	$m	$m
Provision for credit losses (Note 5)	1,150	1,546
Consolidated Balance Sheet		
Loans (Note 5)		
Retail	385,170	369,470
Wholesale	159,606	154,369
	544,776	523,839
Allowance for loan losses (Note 5)	(2,159)	(2,235)
	542,617	521,604

Royal Bank of Canada(4)

October 31, 2017 (Millions of Canadian dollars)	Canada	United States	Other International	Total
Retail: Residential mortgages	$255,799	$11,449	$3,100	$270,348
Personal	82,022	6,357	3,915	92,294
Credit cards	17,491	294	250	18,035
Small business	4,493	–	–	4,493
	359,805	18,100	7,265	385,170
Wholesale: Business	74,425	51,556	20,310	146,291
Banks	1,027	2,498	437	3,962
Sovereign	7,370	934	1,049	9,353
	82,822	54,988	21,796	159,606
Total loans	442,627	73,088	29,061	544,776
Allowance for loan losses	(1,406)	(234)	(519)	(2,159)
Total loans net of allowance for loan losses	$441,221	$72,854	$28,542	$542,617

RBC: Classification & measurement (1)

- IFRS 9 introduces a principles-based approach to the classification of financial assets.
- Debt instruments, including hybrid contracts, are measured at fair value through profit or loss (FVTPL), FVOCI or amortized cost based on the nature of the cash flows of the assets and an entity's business model.
- These categories replace the existing IAS 39 classifications of FVTPL, AFS (available for sale), loans and receivables, and held-to-maturity.
- Equity instruments are measured at FVTPL, unless they are not held for trading purposes, in which case an irrevocable election can be made on initial recognition to measure them at FVOCI with no subsequent reclassification to profit or loss.

RBC: Classification & measurement (2)

- For financial liabilities, most of the pre-existing requirements for classification and measurement previously included in IAS 39 were carried forward unchanged into IFRS 9.
- The requirements related to the fair value option for financial liabilities, which were adopted in 2014, were changed to address the treatment of own credit risk.

RBC: Classification & measurement (3)

The combined application of the contractual cash flow characteristics and business model tests as at November 1, 2017 is expected to result in certain differences in the classification of financial assets when compared to our classification under IAS 39. The most significant changes include the following:

- Approximately $25 billion debt securities previously classified as AFS are expected to be classified as amortized cost based on a held-to-collect business model.
- Approximately $2.5 billion securities previously classified as AFS are expected to be classified as FVTPL, primarily representing equities and debt securities whose cash flows do not represent solely payments of principal and interest.

RBC: Impairment (1)

- IFRS 9 introduces an expected credit loss impairment model that differs significantly from the incurred loss model under IAS 39 and is expected to result in earlier recognition of credit losses. Additional details on the key elements of the new expected credit loss model are described below.
- Scope: Under IFRS 9, the same impairment model is applied to all financial assets, except for financial assets classified or designated as at FVTPL and equity securities designated as at FVOCI, which are not subject to impairment assessment.

RBC: Impairment (2)

- The scope of the IFRS 9 expected credit loss impairment model includes amortized cost financial assets, debt securities classified as at FVOCI, and off balance sheet loan commitments and financial guarantees which were previously provided for under IAS 37 Provisions, Contingent Liabilities and Contingent Assets (IAS 37).
- The above-mentioned reclassifications into or out of these categories under IFRS 9 and items that previously fell under the IAS 37 framework were considered in determining the scope of our application of the new expected credit loss impairment model.

RBC: Impairment (3)

- The scope of the IFRS 9 expected credit loss impairment model includes amortized cost financial assets, debt securities classified as at FVOCI, and off balance sheet loan commitments and financial guarantees which were previously provided for under IAS 37 Provisions, Contingent Liabilities and Contingent Assets (IAS 37).
- The above-mentioned reclassifications into or out of these categories under IFRS 9 and items that previously fell under the IAS 37 framework were considered in determining the scope of our application of the new expected credit loss impairment model.

Expected credit loss impairment model (1)

Under IFRS 9, credit loss allowances will be measured on each reporting date according to a three-stage expected credit loss impairment model:

- Stage 1 – From initial recognition of a financial asset to the date on which the asset has experienced a significant increase in credit risk relative to its initial recognition, a loss allowance is recognized equal to the credit losses expected to result from defaults occurring over the next 12 months.
- Stage 2 – Following a significant increase in credit risk relative to the initial recognition of the financial asset, a loss allowance is recognized equal to the credit losses expected over the remaining lifetime of the asset.

Expected credit loss impairment model (2)

- • Stage 3 – When a financial asset is considered to be credit-impaired, a loss allowance equal to full lifetime expected credit losses will be recognized. Interest revenue is calculated based on the carrying amount of the asset, net of the loss allowance, rather than on its gross carrying amount.
- Stage 1 and Stage 2 credit loss allowances effectively replace the collectively-assessed allowance for loans not yet identified as impaired recorded under IAS 39, while Stage 3 credit loss allowances effectively replace the individually and collectively assessed allowances for impaired loans.

Expected credit loss impairment model (2)

- Stage 3 – When a financial asset is considered to be credit-impaired, a loss allowance equal to full lifetime expected credit losses will be recognized. Interest revenue is calculated based on the carrying amount of the asset, net of the loss allowance, rather than on its gross carrying amount.
- Stage 1 and Stage 2 credit loss allowances effectively replace the collectively-assessed allowance for loans not yet identified as impaired recorded under IAS 39, while Stage 3 credit loss allowances effectively replace the individually and collectively assessed allowances for impaired loans.

Expected credit loss impairment model (3)

- Under IFRS 9, the population of financial assets and corresponding allowances disclosed as Stage 3 will not necessarily correspond to the amounts of financial assets currently disclosed as impaired in accordance with IAS 39.
- Consistent with IAS 39, loans are written off when there is no realistic probability of recovery.
- Accordingly, our policy on when financial assets are written-off will not significantly change on adoption of IFRS 9.

Expected credit loss impairment model (4)

Under IFRS 9, the population of financial assets and corresponding allowances disclosed as Stage 3 will not necessarily correspond to the amounts of financial assets currently disclosed as impaired in accordance with IAS 39. Consistent with IAS 39, loans are written off when there is no realistic probability of recovery. Accordingly, our policy on when financial assets are written-off will not significantly change on adoption of IFRS 9. Because all financial assets within the scope of the IFRS 9 impairment model will be assessed for at least 12-months of expected credit losses, and the population of financial assets to which full lifetime expected credit losses applies is larger than the population of impaired loans for which there is objective evidence of impairment in accordance with IAS 39, loss allowances are generally expected to be higher under IFRS 9 relative to IAS 39.

Expected credit loss impairment model (5)

- Changes in the required credit loss allowance, including the impact of movements between Stage 1 (12 month expected credit losses) and Stage 2 (lifetime expected credit losses), will be recorded in profit or loss. Because of the impact of moving between 12 month and lifetime expected credit losses and the application of forward looking information, provisions are expected to be more volatile under IFRS 9 than IAS 39.
- Measurement: The measurement of expected credit losses will primarily be based on the product of the instrument's probability of default (PD), loss given default (LGD), and exposure at default (EAD), discounted to the reporting date. The main difference between Stage 1 and Stage 2 expected credit losses is the respective PD horizon.

Expected credit loss impairment model (6)

- Stage 1 estimates will use a maximum of a 12-month PD while Stage 2 estimates will use a lifetime PD.
- Stage 3 estimates will continue to leverage existing processes for estimating losses on impaired loans, however, these processes will be updated to reflect the requirements of IFRS 9, including the requirement to consider multiple forward-looking scenarios.
- An expected credit loss estimate will be produced for each individual exposure, including amounts which are subject to a more simplified model for estimating expected credit losses; however the relevant parameters will be modeled on a collective basis using largely the same underlying data pool supporting our stress testing and regulatory capital expected loss processes.
- Models have been developed, primarily leveraging our existing models for enterprise-wide stress testing.

Expected credit loss impairment model (7)

- For the small percentage of our portfolios that lack detailed historical information and/or loss experience, we will apply simplified measurement approaches that may differ from what is described above. These approaches have been designed to maximize the available information that is reliable and supportable for each portfolio and may be collective in nature.
- Expected credit losses must be discounted to the reporting period using the effective interest rate, or an approximation thereof.

Transition (1)

To manage our transition to IFRS 9, we implemented a comprehensive enterprise-wide program led jointly by Finance and Risk Management that focuses on key areas of impact, including financial reporting, data, systems and processes, as well as communications and training. Throughout the project, we have provided regular updates to the Audit Committee, Risk Committee and senior management to ensure escalation of key issues and risks. During fiscal 2015 and 2016, we completed initial assessments of the scope of IFRS 9, differences from IAS 39, classification of financial assets, financial and economic impacts, system and resource requirements, and key accounting inter-pretations. We also designed and began building the systems, models, controls and processes required to implement IFRS 9.

Transition (2)

During fiscal 2017, we completed the following steps:

- Completed a parallel run of the full end to end process during the fourth quarter of 2017, the results of which were used to test our

models and methodologies against our key performance indicators;

- Validated significant new impairment models;
- Completed documentation of updated bank-wide accounting and risk policies;

Transition (3)

- Finalized governance and control frameworks over new processes and testing of internal controls;
- Documented the roll-out and implementation of the IFRS 9 project and governance structure including key controls;
- Continued to provide training and educational seminars to impacted internal stakeholders; and
- Prepared external disclosures to be provided on transition to IFRS 9 and going forward on a quarterly or annual basis.

Nimesh Verma, BNP Paribas (1)

- Under IFRS 9, the carrying value of loan assets – which has been at amortised cost for hundreds of years – will change to incorporate modelled, forward-looking, volatile expected losses. As the accounting value of loans forms a key input to regulatory solvency, banks face immediate one-off hits to regulatory solvency when expected losses and lifetime expected losses increase significantly, relative to current provisioning and regulatory deductions. Interestingly, recent bank disclosure shows one-off hits to solvency to be manageable – a fall of 45 basis points in Common Equity Tier 1 ratio in the recent European Banking Authority (EBA) impact assessment, for example.

Nimesh Verma, BNP Paribas (2)

This is lower than initially expected because of continued heavy provisioning and improved economic outlooks. More importantly, IFRS 9 significantly increases volatility and procyclicality. It amplifies provision levels and drives large shifts in regulatory capital on an ongoing basis, as changes in economic outlook mean swaths of assets move between stages 1 and 2. At the same time, given amplified provisioning, we expect stress scenario impacts to swing wildly – with much higher impact for the same stress scenarios under IFRS 9 than under current standards.

Credit funds (1)

- Under IAS 39, financial assets were classified into several disjointed categories, which were arguably misaligned with the requirements of financial statement users.
- This classification system was subject to criticism due to its complexity.
- The purpose of IFRS 9 has therefore been to simplify and improve the accounting for investments.
- Importantly, the new standard makes a clear distinction between accounting for investments at Fair Value and amortized cost. These changes are expected to be widely welcomed by institutional investors in alternative investment funds, which almost universally require NAV statements to be prepared based on Fair Value.

Credit funds (2)

- Fair Value is typically required by institutional investors for their own financial reporting purposes.
- Pension funds and funds of funds often use Fair Value as a common basis to make asset allocation and investment manager selection decisions.
- Fair Value is also used in the performance evaluation process and can therefore inform incentive compensation decisions. In the absence of consistent and transparent information concerning the Fair Value of underlying investments, institutional investors may face challenges in exercising their fiduciary responsibilities, including the need to measure and control risk.

Credit funds (3)

- These drivers have led institutional investors in alternative investment funds to become increasingly insistent on Fair Value measurement and these investors have become more sophisticated in communicating this to general partners in recent years.
- In certain circumstances, IFRS 9 allows banks and other financial institutions to hold loan books at amortized cost. This is not a path, however, that will be acceptable to institutional investors in the alternative investment (private equity, hedge funds, managed futures, real estate, commodities and derivatives contracts) funds sector.
- To measure and report fund investments at amortized cost is now seen by many as a disservice, given the overwhelming need of these investors for Fair Value.

Credit funds (4)

If satisfying investor requirements were not enough to convince CFOs to apply Fair Value measurement, following the 'cash flow characteristics' and 'business model' tests under IFRS 9 will inevitably lead sophisticated general partners to conclude that Fair Value is the only viable option for private debt investments.

Credit funds (5)

- A private debt investment may be accounted for at amortized cost only if, firstly, the investment gives rise on specified dates to cash flows that are solely payments of principal and interest and, secondly, the investment is held within a business whose sole objective is to hold financial assets to maturity to collect contractual cash flows.
- Applying these tests, the use of amortized cost would preclude many of the unique strategies and terms used by alternative investment funds to enable them to target excess returns. The preference for most general partners for strategies with sufficient flexibility to enable them to generate returns for investors should naturally lead most alternative investment funds towards Fair Value measurement.

Credit funds (6)

While there may be a temptation for some alternative investment funds to see amortized cost as an "easy option" for private debt investments, this would be counterintuitive to fund business models, as any perceived failure to report Fair Value can be discouraging for institutional investors. There can be no more hiding under the new standard, since IFRS 9 makes clear that historical cost and amortized cost are not proxies for Fair Value.

Credit funds (7)

In the rare circumstances that a fund chooses to measure private debt investments at amortized cost, they will now be required to perform more onerous impairment testing under IFRS 9, which must include a forward-looking assessment of expected credit losses. This will be similar to the analysis performed by banks and other financial institutions.

Alternative investment funds should carefully consider the needs of investors when applying IFRS 9 for the first time. Investors and audit firms are becoming more aware of the issues and the choices that CFOs have in this regard. Given the introduction of IFRS 9 and the ongoing needs of investors, it is becoming increasingly clear that when it comes to measuring and reporting private debt investments, all roads lead to Fair Value.

Historical default rates for Nairobi

Period	Businesses	Retail
Current	0.50%	1.30%
1-30 days past due	1.90%	2.80%
31-60 days past due	3.10%	5.25%
>61 days past d	7.50%	8.45%