

# Accounting for financial instruments

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## AMIS

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2 December 2009

# Agenda

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1 Current accounting

2 Future accounting

## Financial instruments

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- Accounting for financial instruments is currently governed by a series of standards:
  - IAS 32 *Financial instruments: Presentation*
  - IAS 39 *Financial instruments: Recognition and measurement*
  - IFRS 7 *Financial instruments: Disclosures*
- Definition
  - Any contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity
- Financial instruments comprise
  - Financial assets
  - Financial liabilities

## IAS 39

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- Objective
  - Establish principles for recognising and measuring financial assets, financial liabilities and some contracts to buy or sell non-financial items
- Classifies financial instruments into four categories
  - Fair value through profit and loss
  - Held-to-maturity
  - Loans and receivables
  - Available-for-sale
- Fair value option permits designation on initial recognition at fair value; no reclassification possible thereafter
- Incurred loss impairment model for assets measured under amortised cost
- Complex hedge accounting rules
- Similar to US GAAP and Canadian GAAP
  - Held-to-maturity at amortised cost
  - Held-for-trading at fair value
  - Available-for-sale at fair value

## Classification and measurement of tangible assets

Asset type	Standards	Classification	Initial measurement	Subsequent measurement	Revenue recognition
Bonds Equities	IAS 39	Held-to-maturity	Fair value plus transaction costs	Amortised cost (effective interest method)	Profit and loss
		Available-for-sale	Fair value	Fair value	Unrealised gains / losses through comprehensive income, realised sales and dividends through profit and loss
		Fair value through profit or loss	Fair value	Fair value	Profit and loss
		Loans and receivables	Fair value plus transaction costs	Amortised cost (effective interest method)	Profit and loss
Property	IAS 40	Fair value	Cost (fair value)	Fair value	Profit and Loss
	IAS 16	Depreciated cost	Cost (fair value)	Depreciated cost	Profit and Loss
Cash	IAS 39		Cost (fair value)	Fair value	Profit and Loss

# Agenda

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1 Current accounting

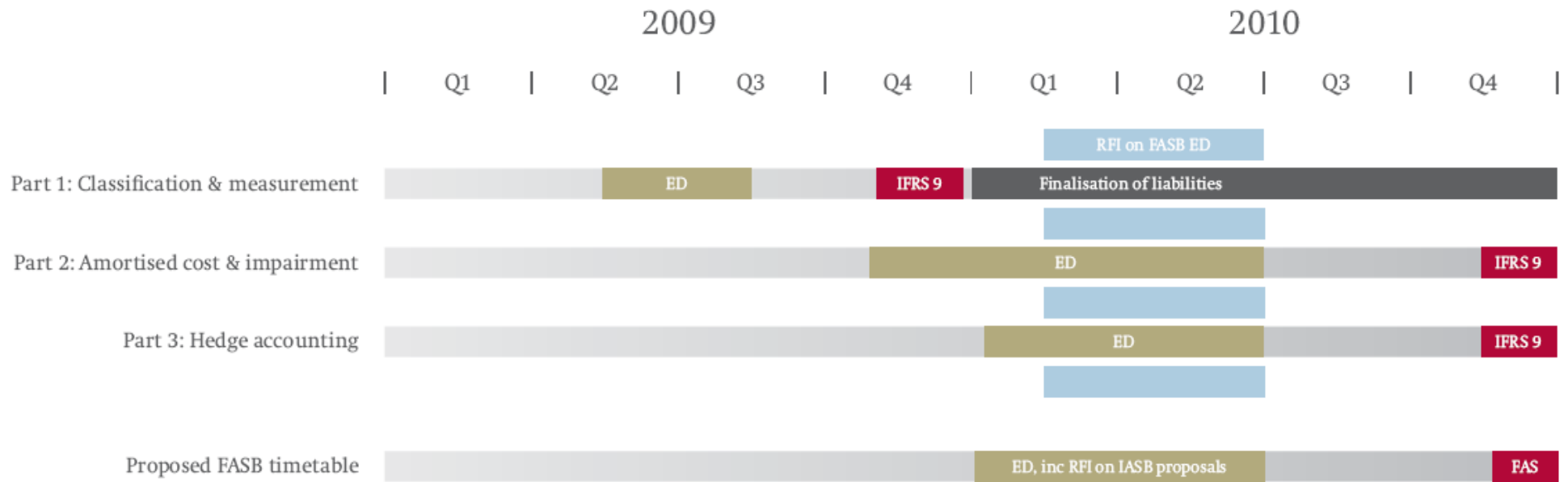
2 Future accounting

## Background

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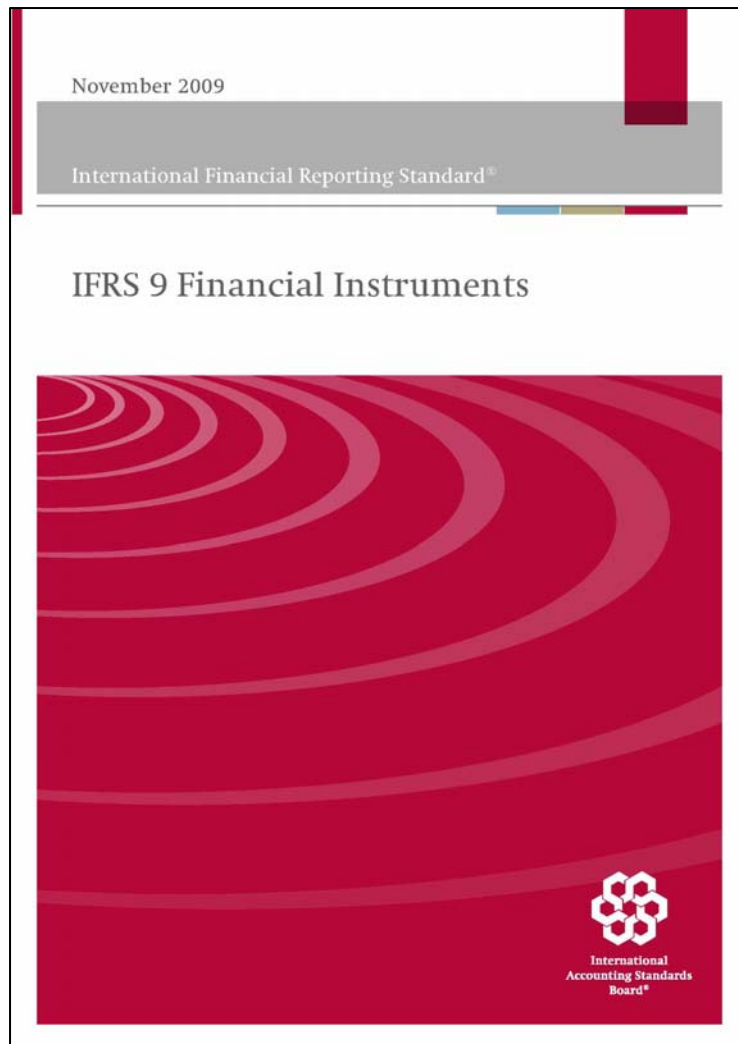
- IASB inherited IAS 39 *Financial Instruments: Recognition and Measurement* from its predecessor body IASC
- IAS 39 is one of the most complex standards – it contains a few principles with many exceptions
- The IASB has for a long time been encouraged to improve IAS 39
- As a consequence of the financial crisis, the IASB and FASB agreed at the end of 2008 to work jointly towards a globally accepted principle-based and less complex replacement for requirements on accounting for financial instruments
- IASB's project plan to replace IAS 39 consists of three main phases:
  - Classification and measurement
  - Amortised cost and impairment
  - Hedge accounting

# Timeline



Source: IASB

## IFRS 9 *Financial Instruments*



- Published November 2009
- Mandatory from 1 January 2013 with early adoption possible
- Prescribes (so far) classification and measurement of financial assets
- Financial liabilities, impairment, embedded derivatives and disclosures yet excluded
- Main improvements compared to IAS 39
  - Two measurement categories only – fair value and amortised cost
  - Tainting rules have been eliminated
  - Strategic investments at fair value through other comprehensive income
  - No cost exception for unquoted equity instruments
  - Reclassification when business model changes

Please note: Not yet adopted by EU!

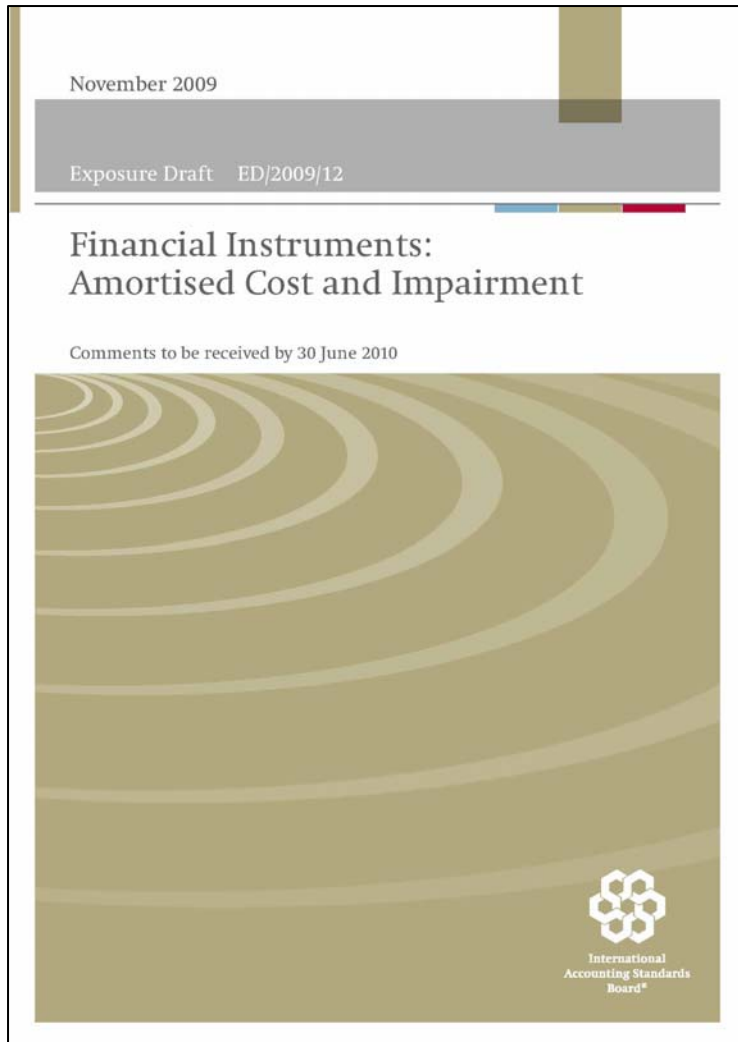
## Initial and subsequent measurement for financial assets

Asset type	Initial measurement	Subsequent measurement	Revenue recognition
Instruments with basic loan features (principal and interest) held to collect contractual cash flows	Fair value plus transaction cost	Amortised cost	Profit and loss
	Fair value <sup>1</sup>	Fair value <sup>1</sup>	Profit and loss
Equity instruments not held for trading	Fair value	Fair value	Subsequent changes in other comprehensive income <sup>2</sup>
All other financial instruments	Fair value	Fair value	Profit and loss

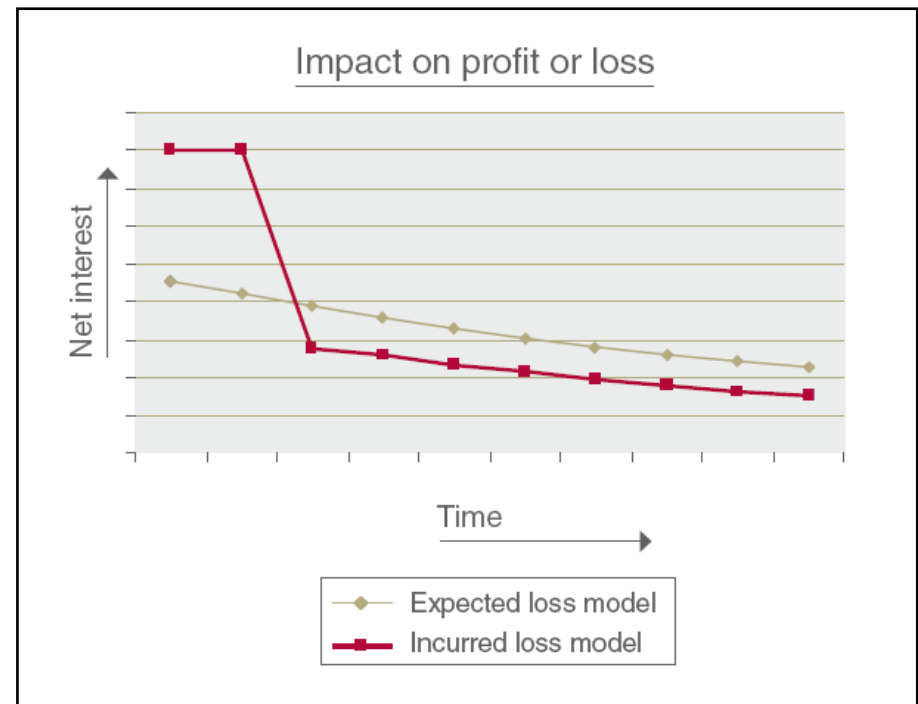
<sup>1</sup> Fair value option eligible if it eliminates or significantly reduces a measurement or recognition inconsistency (sometimes referred to as an 'accounting mismatch')

<sup>2</sup> Including realised gains/losses

## ED Amortised cost and impairment



- Published November 2009
- Open for public comment until 30 June 2010
- Proposes to move from the current incurred loss model to an expected loss impairment model



Source: IASB