# IFRS 9

# **REVISIONS TO THE ACCOUNTING OF FINANCIAL INSTRUMENTS**

#### MAIN ASPECT

#### IAS 39–categorization:

There are four different categories and generous options for reclassification.

The aim of IFRS 9 is to reduce complexity and to improve the decision-making benefits for the addressee of the annual accounts.

#### IFRS 9—categorization:

- Financial assets are classified according to
- The business model
- The characteristics of the receivable cash flows
- There are two basic categories
- Amortized cost
- Fair value (through OCI and P/L)

#### RECLASSIFICATION

**CORE ASPECT** 

accounting

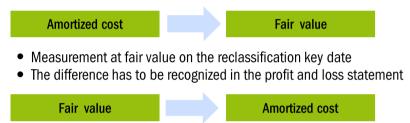
accounting instead

FVHA still allowed

IAS 39–Hedge accounting:

IFRS 9—Hedge accounting:

Only valid reason: changes in the business model



• Fair value on the reclassification key date is the new book value • The reclassification key date is always the first day of the accounting period starting after the change of the business model

Focus on balance sheet, only limited coverage of

economic risk hedging under IAS 39 provisions

Economic focus, aimed at an integrated view on

risk management up to financial reporting hedge

On effective date of first application of IFRS 9, an

Application of IAS 39 interest rate risk portfolio

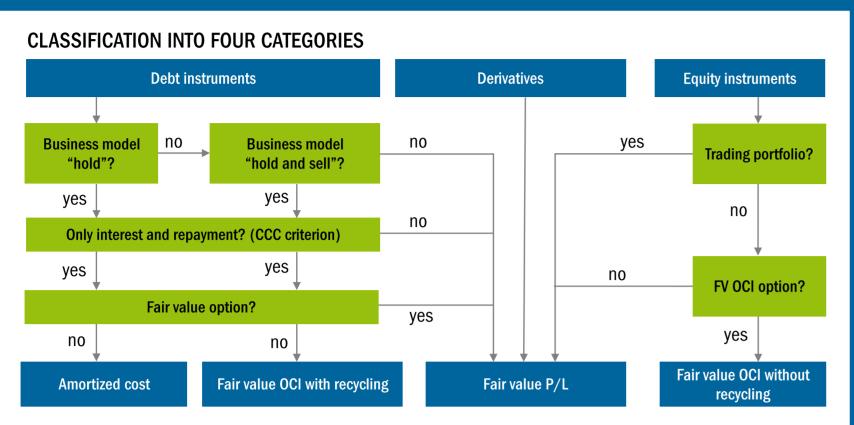
**BETTER REPRESENTATION OF RM-STRATEGIES** 

Designation of aggregated risk positions Designation of net positions

BY EXTENDING THE SET OF ELIGIBLE HEDGED ITEMS

entity may choose to apply IAS 39 hedge

# CATEGORIZATION



#### EMBEDDED DERIVATIVES

Embedded derivatives are components of a structured instrument consisting of a non-derivative host contract and a derivative. Contrary to IAS 39, the derivative is not recognized separately from its financial asset host. Instead, under IFRS 9, the overall contract is recognized. In most cases this will lead to a measurement at fair value through profit or loss. In case of a non-financial host contract or financial liability, the accounting of the embedded derivative is still effected in accordance with IAS 39.

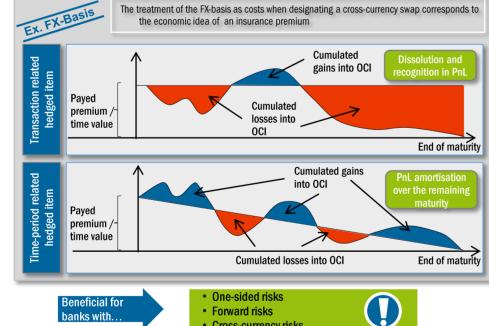
#### **OUR SOFTWARE SOLUTION**

- Allocation of financial instruments to the defined IFRS categories
- Definition of the categorization rules through a graphical user interface
- Identification of conflicts and discrepancies in the categorization rules
- Audit-proof recording of all settings

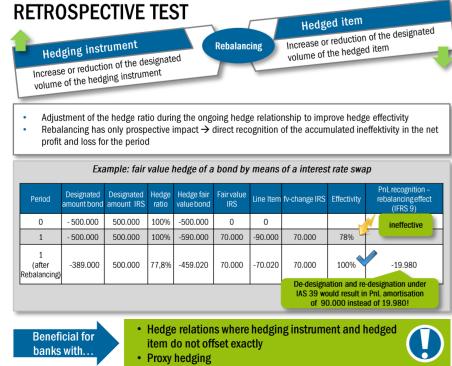
Gabale Destellangen			
R Chickele Gesandkal			
♥ () States Exceletaryen ♥ () States Exceletaryen ♥ () States ♥ () Independence ↓ D Endependenceg	Avalance to Sale     Ara Visa Rough Part and Line     Reptor Theory     Lowers     Lowers     Lowers	Confliction         Confliction           [15] (160)         [15] (160)           [16] (160)         [16] (160)           [16] (160)         [16] (160)           [16] (160)         [16] (160)           [16] (160)         [16] (160)           [16] (160)         [16] (160)           [16] (160)         [16] (160)           [16] (160)         [16] (160)           [16] (160)         [16] (160)           [16] (160)         [16] (160)           [16] (160)         [16] (160)           [16] (160)         [16] (160)           [16] (160)         [16] (160)           [16] (160)         [16] (160)           [16] (160)         [16] (160)           [16] (160)         [16] (160)           [16] (160)         [16] (160)           [16] (160)         [16] (160)           [16] (160)         [16] (160)           [16] (160)         [16] (160)           [16] (160)         [16] (160)           [16] (160)         [16] (160)           [16] (160)         [16] (160)           [16] (160)         [16] (160)           [16] (160)         [16] (160)           [16] (160)         [16] (160)	[Dept] Trablock. Accord
	New Houritigen Entimes Kalogatebegeichnung Lours and Parahastiks werz	Analyse vice Kalls	datawan Dima Gast Ingstein Produkte
	Liters and Receivables week	und	Gastipplan Probate
	Loans and Pacahables		Gaellopten Produkte Gaellopten
	Loare and Receivables were		Produkte Grad Torotern Produkte
	Loans and Receivables		Gue leyden. Profule

# HEDGE ACCOUNTING

#### SEPARATION OF TIME VALUE OF OPTIONS. SPOT LEG OF FORWARDS AND FX-BASIS OF CROSS-CURRENCY SWAPS



## **REBALANCING AND OMISSION OT THE**

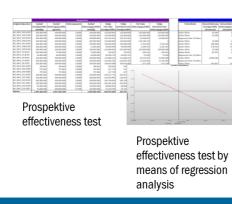


#### **DESIGNATION OF RISK COMPONENTS OF NON-FINANACIALS** Example: A wholesalar people discal fuel a

Example: A wholesal		ls diesel fu dge agains		
1 Suppositions: • the risk compo • the fair value be reliably meas	change			-
price diesel fuel	x	tax	х	F
2 Designation hee Hedging of sing therefore reduc	le risk o	omponents	inci	reas
price diesel fuel	x	tax	x	F
Hedge relation		_ Hedging of diesel fuel price		
Commodity swap on diesel fuel	fluctuations			FX
Beneficial for		Busines		

#### **OUR SOFTWARE SOLUTION**

- Implementation of all variants under IFRS 9 general hedge accounting
- Integrated simulation and decision-making model for ALM and hedge accounting
- Process support and extensive reporting functions



#### Inflows Outflows Inflows Outflows Forward USD100 USD80 Image: Control of the second seco Hedging of cross-currency risk and interest rate risk esignation of credit exposure at FVTPL nation of layers components Credit Defau Credit Default Swap presentation of credit risk hedging in accounting, provide that name und seniority of hedged item nd hedging instrument match ·(Partial) designation of the hedged item as F Full fair value accounting of the hedged item during the hedge period Beneficial for Hedging of combined risk positions banks with.. Many-sided hedging strategies in risk management

## Your contacts:

**Detlev Ahrens** Senior Manager

Lars Meyer Senior Manager Dr. Thomas Pöhlmann Senior Manager

Frank Kathage Head of Sales zeb.control



regular basis and therefore

of the risk component must

X spot rate + margin

s hedge effectiveness and

X spot rate + margin

depending on materials

Hedging of

fluctuations

- currency

relation

swap

sing prices

lentifiable

#### MAIN ASPECT

#### IAS 39-measurement:

Assets and liabilities are to be valued according to their categorization.

#### **IFRS 9**—measurement:

Financial instruments are also to be valued according to their categorization.

In general, measurement is at (amortized) cost or as "other liability" (through effective interest, if applicable) or at fair value.

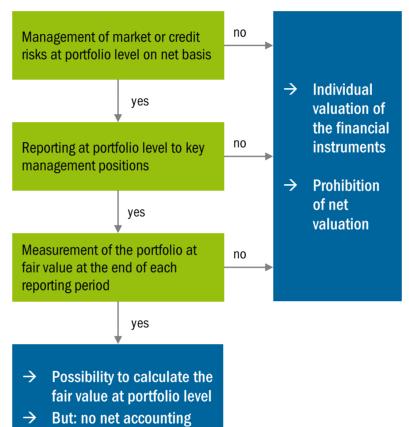
### MANAGED PORTFOLIOS

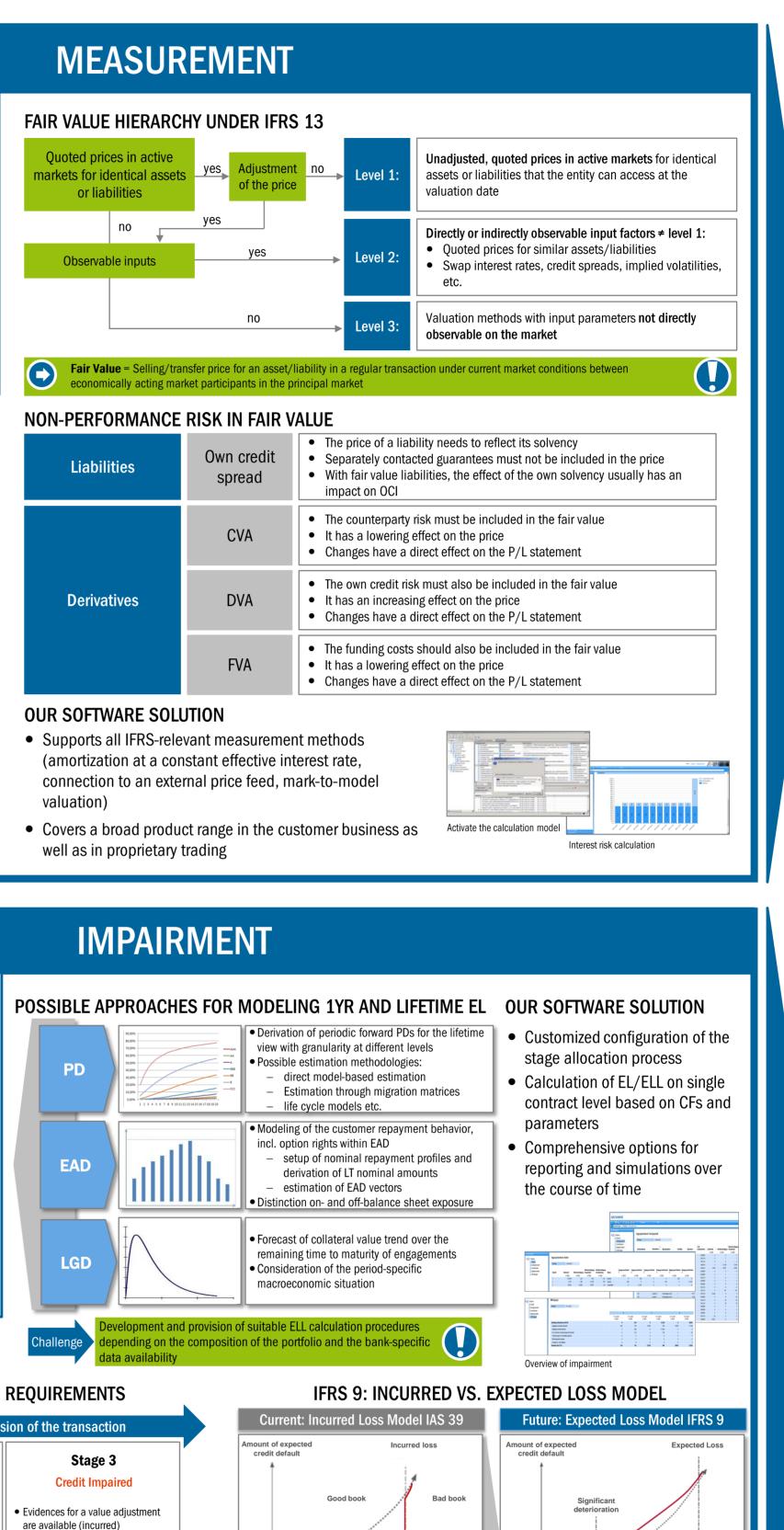
**CORE ASPECT** 

actually been incurred

insufficient extent

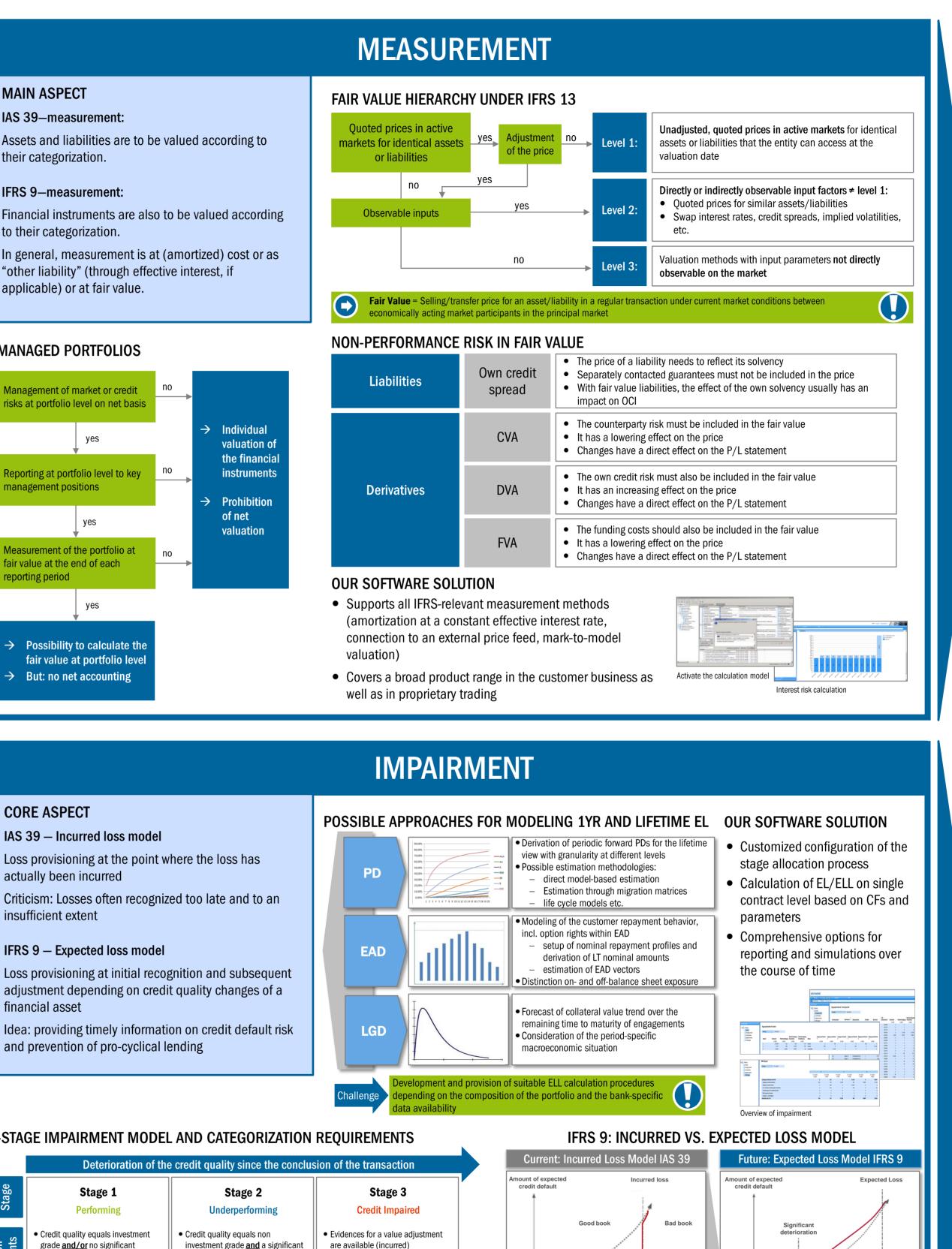
financial asset





Liabilities	Own credit spread	<ul> <li>The price of a liability needs to reflect its</li> <li>Separately contacted guarantees must n</li> <li>With fair value liabilities, the effect of the impact on OCI</li> </ul>
Derivatives	CVA	<ul> <li>The counterparty risk must be included in</li> <li>It has a lowering effect on the price</li> <li>Changes have a direct effect on the P/L</li> </ul>
	DVA	<ul> <li>The own credit risk must also be included</li> <li>It has an increasing effect on the price</li> <li>Changes have a direct effect on the P/L</li> </ul>
	FVA	<ul> <li>The funding costs should also be include</li> <li>It has a lowering effect on the price</li> <li>Changes have a direct effect on the P/L</li> </ul>





## 3-STAGE IMPAIRMENT MODEL AND CATEGORIZATION REQUIREMENTS

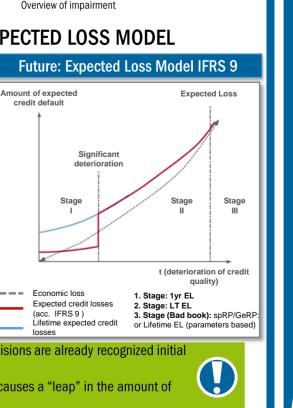
#### Deterioration of the credit quality since the conclusion of the transaction Stage 1 Performing redit quality equals investment grade and/or no significant investment grade **and** a significant aggravation of the credit risk deterioration of the credit quality (not impaired) Lifetime expected credit losses 12-month expected credit losses Lifetime expected credit losses (ELL) (ELL) t (deterioration of credit quality) Good Book: GeRP (1yr param) Economic loss EAD x PD x LGD x LIP Effective interest rate on gross book Effective interest rate on gross book ncurred credit losses (acc Bad Book: spRP/GeRP IAS 39) Lifetime EL (DCF) value • Setup of a categorization logic for the allocation of transactions to the corresponding stage • With the new impairment model, loss provisions are already recognized initial and definition of the required valuation (EL or ELL)? recognition of the asset ullet Comparison of the categorization between the previous and the current period in order to $\bullet$ ransition to expected lifetime credit loss causes a "leap" in the amount of dentify shifts between stages (deteriorations and improvements possible) 1) Risk provision

#### Hammer Str. 165 D-48153 Münster, GERMANY

Phone +49 251 97128 0 E-mail accounting@zeb.de







# CONSEQUENCES

## **CHALLENGES**

- Analysis of business models and portfolios as to the necessity of using the fair value approach and of the discretion available for AC measurement
- The classification is usually carried out at portfolio level - this mostly being the financial & risk management level of credit institutions. The aggregation of portfolios is possible, as long as this is compliant with the financial and risk management.
- Analysis of contractual CF characteristics

### **APPROACH**

- Flexible simulation and pricing of the product portfolio to be calculated
- Identification of conflicts and discrepancies in the categorization rules

•••

### CHALLENGES

- Analysis of existing loan contracts for the determination of fair value using the DCF method or a suitable model
- In the FV measurement, the solvency of the parties involved in the contract of a financial instrument has to be taken into account

#### APPROACH

Re-usable standard valuation algorithms (functional modules) of zeb or specific ones of the client

#### $\bullet \bullet \bullet$

#### CHALLENGES

- The closer relation to risk management / treasury leads to improved realization capacities in hedge accounting, i.e. a stronger link to economic management possible
- Examination of the applicability of methods and parameters from risk controlling

#### **APPROACH**

Early analysis and simulation to assess the possible impact (positive / negative) of hedge accounting when changing to IFRS 9 general hedge accounting

 $\bullet \bullet \bullet$ 

## **CHALLENGES**

- Early conception and implementation of the EL/ELL-based impairment model, perform impairment simulations for managing future P&L volatility & creation of transparency about the first-time adoption effect
- Review and follow-up checks of periodic changes of the credit quality for purposes of (re-)allocation via the three-stage logic

### **APPROACH**

- Institution-specific definition of stagetransfer criteria depending on borrower groups, volumes, days in arrears, etc.
- Development of appropriate calculation models for EL/ELL and analysis of quantitative impacts

zeb control.accounting



# control.zeb.eu/ifrs