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für Rückfragen zu der beigefügten Publikation „In depth“ zur Thematik
“IFRS 9: Impairment of financial assets – Questions and answers”
stehen Ihnen folgende Ansprechpartner gerne zur Verfügung:



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In depth

A look at current financial reporting issues

IFRS 9: Impairment of financial assets – Questions and answers

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At a glance

On 24 July 2014, the IASB published the complete version of IFRS 9, 'Financial instruments', which replaces most of the guidance in IAS 39. The final standard contains a new impairment model which will result in earlier recognition of impairment losses. For further guidance, see 'In depth: IFRS 9 – Expected Credit Losses'.

This publication sets out our views on some of the most common issues that have been raised by preparers and reviewers of financial statements as part of implementation of the new standard. Issues related to classification and measurement requirements and hedging requirements under IFRS 9 have been considered in separate documents.

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Expected credit losses

Measurement of expected credit losses for drawn and undrawn components of financial assets

Question:

Paragraph 5.5.20 of IFRS 9 contains an exception for certain types of financial instruments to measure expected credit losses over the period that the entity is exposed to credit risk, even if that period extends beyond the contractual period. The exception applies to some financial instruments that include both a loan and an undrawn commitment.

This seems to indicate that, in order for the exception to apply, a facility must have both drawn and undrawn components. However, in many cases, at any point in time, a facility might only have an undrawn component, such as a credit card facility.

Is it necessary for the financial instrument to have both drawn and undrawn components at the measurement date for the exception in IFRS 9 to apply?

Solution:

No. The rationale for the exception, as expressed in paragraph BC5.261 of IFRS 9, is to ensure that sufficient loss allowance is established for contracts where 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.

A financial instrument might have a nil drawn-down balance at the reporting date. However, expected credit losses should still be recognised in the same way as they would be for an undrawn loan commitment. For example, a credit card which has been originated just before reporting date, but is yet to be used, will require recognition of expected credit losses.

Paragraph B5.5.39 of IFRS 9 also gives an example of a credit card as an instrument that can be withdrawn by the lender with little notice but that, in practice, exposes the lender to credit risk for a longer period. At any point in time, a portfolio of credit cards is likely to include instruments that have drawn-down amounts and those that do not.

Measurement of expected credit losses over a period longer than the maximum contractual period

Question:

A bank issues mortgage loans to its customers which have contractual maturities of 12 months. The interest rate is fixed for each 12-month period at the beginning of the period. At maturity, if the borrower and lender do nothing, the loan is automatically rolled over for the following 12 months. The interest rate is reset to the current rate at the roll-over date. In practice, such loans roll over many times and can last for many years.

What is the period the bank should consider in measuring expected credit losses under IFRS 9 for such mortgage loans?

Solution:

Paragraph 5.5.19 of IFRS 9 clearly states that ‘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’.

Therefore, the period that the bank considers for measuring expected credit losses is the remaining period up to the 12 months to contractual maturity. The bank’s credit exposure is limited to a maximum of 12 months as, after that period, the bank can cancel the loan at its discretion. Although, in practice, the loans are rolled over for many years, the only matter of relevance is the contractual period over which the lender is exposed to credit risk.

The only exception from this principle under IFRS 9 is certain financial instruments that include both a loan and an undrawn commitment component where the entity is exposed to credit losses beyond the contractual period. This exception does not apply to the example above as, in the jurisdiction concerned, the bank has a substantive ability to demand repayment at the end of the 12 months which limits its exposure to the contractual period, irrespective of whether the loan is fully drawn or not.

Impairment accounting for purchased debt instruments in the case of a business combination

Question:

An entity acquires a business and applies IFRS 3, 'Business combination accounting'. The business being purchased has a number of loans that will be measured at amortised cost by the acquirer. Given that IFRS 3 requires the loans to be measured at their acquisition date fair values, does the entity need to recognise under IFRS 9, a separate impairment loss provision on the loans at acquisition?

Solution:

Yes, the entity needs to recognise a separate impairment loss provision for the loans under IFRS 9, after accounting first for the acquisition under IFRS 3. Paragraph C7.B41 of IFRS 9 has amended IFRS 3 to provide the following guidance: *"In the case of a business combination, the acquirer shall not recognise a separate valuation allowance as of the acquisition date for assets acquired in a business combination that are measured at their acquisition-date fair values because the effects of uncertainty about future cash flows are included in the fair value measure"*.

This means that the IFRS 9 provision should not affect the measurement of goodwill. However, no exception is provided to the general principles of IFRS 9 and IFRS 3:

- Goodwill is measured at the acquisition date as the excess of the consideration transferred and the fair value of the identifiable assets and liabilities.
- As part of this, the loans are initially recorded at their fair value and are classified at amortised cost before any IFRS 9 provision is made.
- Consistent with IFRS 9, at each reporting date following the business combination, the acquirer will have to measure a loss allowance at an amount equal to either 12-month or lifetime expected credit losses, depending on whether there has been a significant increase in credit risk since the acquisition date.

As a result, an entity will recognise an impairment provision the day after the acquisition, so as to account for expected credit losses on the acquired assets in accordance with IFRS 9.

Credit impaired assets

Purchased or originated credit impaired loans

Question:

An entity originates a loan of £1,000. The total interest charge over the term of the loan is 20% per annum, payable in quarterly instalments. The borrower has a high credit risk on origination, and the entity expects the borrower to pay late or fail to pay some of the loan instalments.

Could the loan be considered as originated credit impaired under IFRS 9?

Solution:

It is very unlikely. IFRS 9 defines a financial asset as credit impaired when one or more events that have a detrimental impact on the estimated future cash flows of that financial asset have occurred. This seems unlikely to have happened in the example above, as the loan has been originated with no such 'event' having occurred.

Paragraph BC5.216 of IFRS 9 indicates that it would be an unusual circumstance in which a financial asset could be originated as credit-impaired. It provides an example of a substantial modification of a distressed debt that results in derecognition of the original asset. It then explains that the newly originated financial asset might be credit-impaired, as the modification could constitute objective evidence that the new asset is credit-impaired at initial recognition. In the example above, no such modification has occurred.

Application of the write-off criteria to impaired assets

Question:

Before the publication of IFRS 9, neither IAS 39 nor IFRS 7 provided guidance on the criteria for writing off a financial asset (although paragraph B5(d)(ii) of IFRS 7 did require disclosure of an entity's criteria for writing off amounts charged to the allowance account against the carrying amount of impaired financial assets). IFRS 9 introduced a requirement that financial assets are written off once the entity has 'no reasonable expectation of recovering a financial asset' in its entirety or a portion thereof.

How should the term 'no reasonable expectation of recovering a financial asset' be interpreted?

Solution:

The point at which there is 'no reasonable expectation of recovering a financial asset' is a matter of judgement that will depend on the particular facts and circumstances. The table below considers some indicators that might be relevant in making this judgement. These indicators are not exhaustive and do not provide any bright lines, but serve merely as potential considerations in an entity's overall assessment.

Indicator	Application to IFRS 9's write-off criteria
Has the security/collateral been realised?	<p>To the extent that the security has not yet been realised, one would expect a reasonable expectation of future cash flows to exist based on the collateral's fair value. However, paragraph B5.4.9 of IFRS 9 would suggest that, before realisation of the collateral, if there is no reasonable expectation of cash flows from a portion of the financial asset, that portion should be derecognised.</p> <p>Post realisation of security/collateral, the entity would need to understand its ability and experience in recovering other cash flows in order to determine the amount to be written off.</p>
Is the entity currently enforcing the debt?	<p>The entity ceasing to enforce the debt could be an indicator of write-off. However, a loan could be written off while enforcement activities are continuing, because paragraph 35F(e) of IFRS 7 requires 'information about the policy for financial assets that are written off but still subject to enforcement activity'.</p>
The range of expected outcomes	<p>The wider the range of expected cash flows are, the less likely the entity can assert that it has no reasonable expectation of collecting some or all of the future cash flows.</p>



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Indicator	Application to IFRS 9's write-off criteria
Status of the debtor (for example, liquidation or sequestration proceedings)	<p>The entity only expects to receive any cash flows once formal liquidation or other proceedings are finalised. So, although it is already impaired, the entity might be unable to form a reasonable expectation of what the liquidator will pay.</p> <p>However, if it is clear that the debtor has insufficient assets to repay certain assets on liquidation, these might be written off before the liquidation is completed.</p>
Number of days past due	<p>If this is used as an indicator, it will need to be supported by objective evidence regarding the level of recoveries after the point of write-off to demonstrate that there is no reasonable expectation of future cash flows.</p> <p>It is unlikely that a single number of days past due could be used for all portfolios or that this indicator will be sufficient in isolation.</p>
Number of days since last payment received	Similar to the number of days past due above.

Question:

Should the term 'no reasonable expectations of recovering a financial asset' be applied at an individual asset level or a portfolio level?

Solution:

The assessment of whether an entity has 'no reasonable expectations of recovering a financial asset' should be made at the level of individual financial asset or a portfolio of financial assets, depending on the facts and circumstances, taking into account the nature and credit risk characteristics of the financial assets. For example, it might be appropriate to assess retail mortgage loans on a portfolio level, given that they share similar characteristics, whereas it might be appropriate to assess corporate loans at an individual loan level.

Questions?

PwC clients who have questions about this *In depth* should contact their engagement partner.

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