

IFRS

The Complex Issues Banks Face*

8 June 2006

*connectedthinking

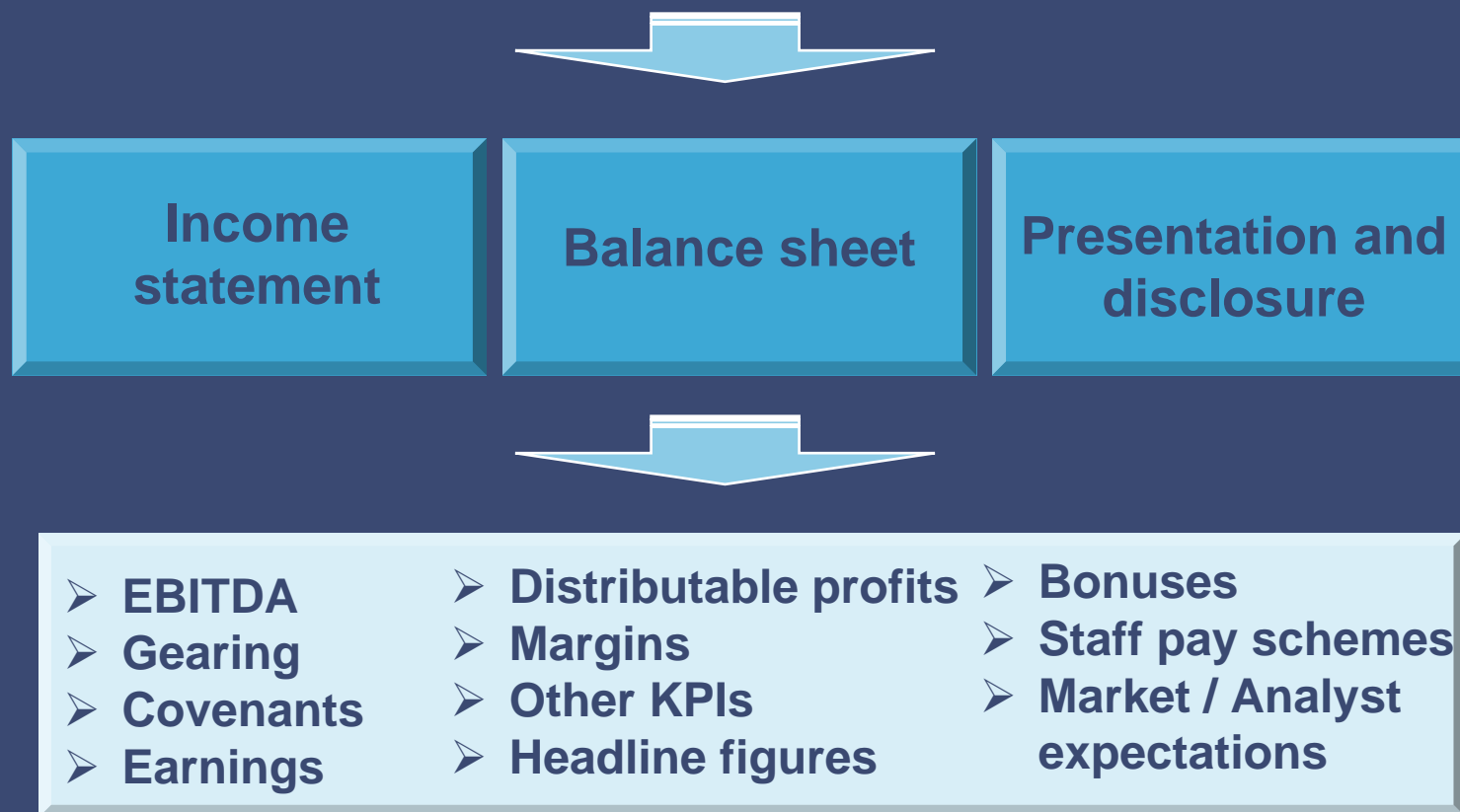


Background

- Why is IFRS an issue? PSAK is converging with IFRS
- Growing need for one international set of accounting standards
 - ✓ due to mergers & acquisitions, marketability, cross border trading, raising finance, shareholder / analyst dialogue
- Dealing with IFRS in the organisation is a major business challenge
- Success enhanced on clear commitment and active sponsorship from the board and from management at all levels (not just the finance function)

Financial implications

Financial implications of IFRS transition



Business implications

Business implications of IFRS transition



Top accounting issues for banks

Revenue Recognition

- Interest income should be calculated on an effective yield basis
- More difficult to realise 'day 1' profits on structured deals

Derivatives and Hedging

- All derivatives to be held at Fair value with limited flexibility in valuation methods.
- Stringent Hedge Accounting Requirements
- Requirement to split out and fair value "Embedded Derivatives"

Provisioning and Impairment

- Likely change in provisioning methodology
- More scientific approach using discounted expected future cash flows.
- Significant data and systems requirements although linkages with Basel II requirements

Revenue Recognition

Derivatives & Hedging

Provisioning and Impairment

IFRS

SPEs

SPEs / Securitization

- Changes in treatment of SPEs make it more difficult to get off-balance sheet treatment

First-time adoption

- Several options are available to avoid full retrospective application of IFRS

Business Combinations

- No merger accounting, new goodwill rules

Disclosures

- Significantly increased requirements, e.g. financial instruments fair value, pensions, segment reporting, risk management

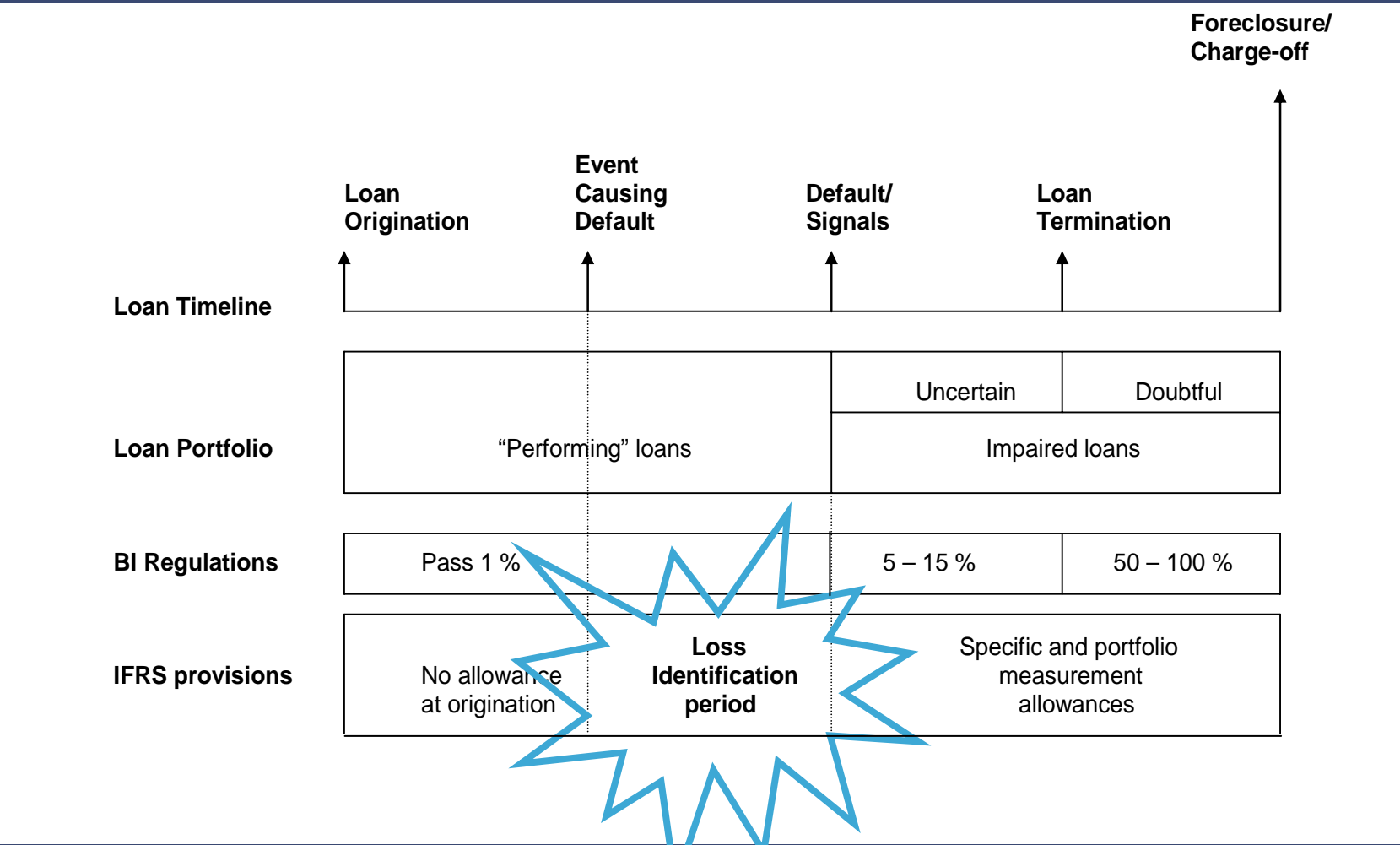
Other Issues

Asset Classification

Asset Classification

- IAS requires financial assets to be allocated into one of four categories:
 - Held for Trading
 - Available for Sale
 - Originated loans and receivables
 - Held to Maturity
- Accounting treatments vary by classification with generally a greater need for fair values
- Financial Assets and Liabilities initially recognised at fair value

Loan loss provisions



Loan loss provisions – in practice

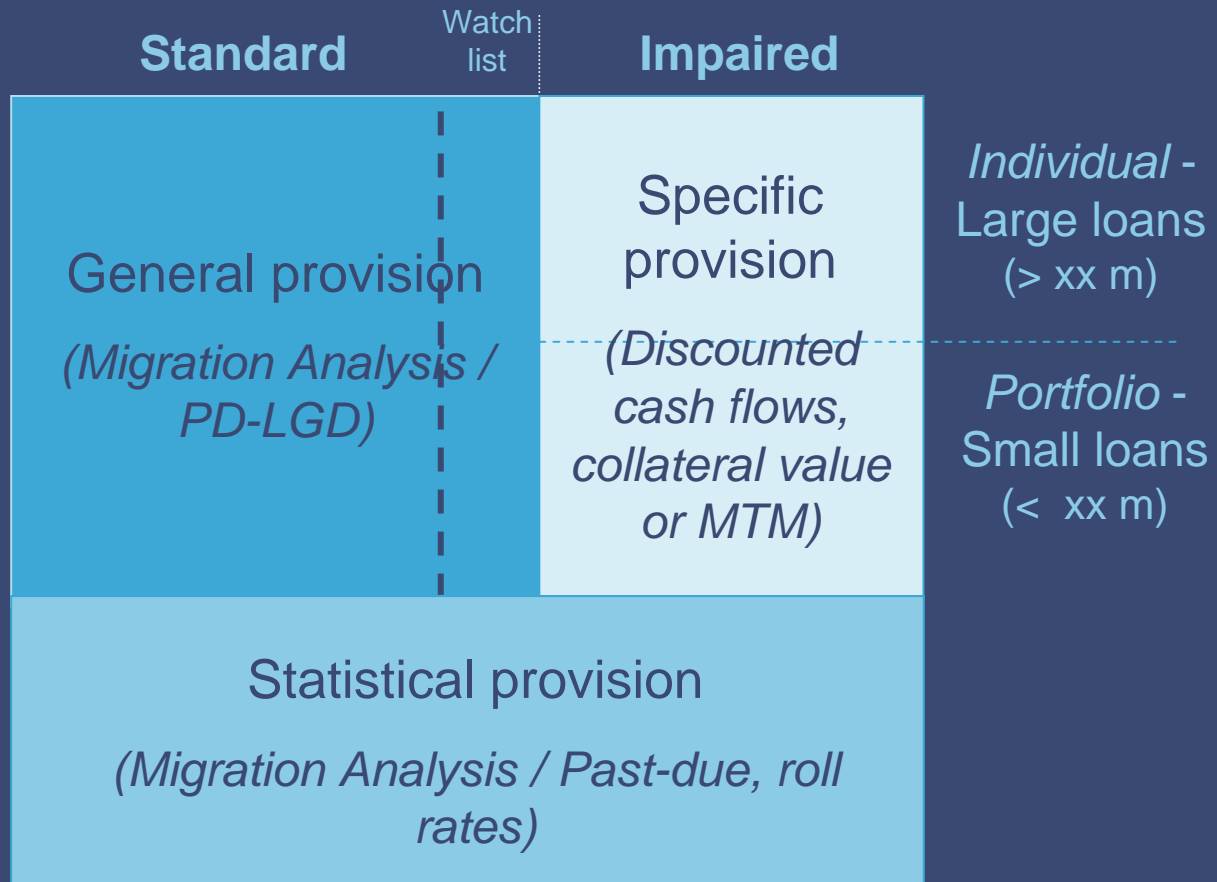
$$LLP = EAD \times PD \times LGD$$

Commercial / SME

- Public sector
- Large corporate
- Commercial
- Foreign

Retail

- Small businesses
- Consumer/auto
- Residential mortgages



Other accounting issues

- Joint financing arrangements
- Stock compensation
- Insurance
- Income taxes
- Leasing
- Financial asset / liability derecognition
- Impairment
- Business combinations
- Fixed assets and investment property

Questions?

