

FS Business Update

PwC Indonesia Financial Services

13 October 2010

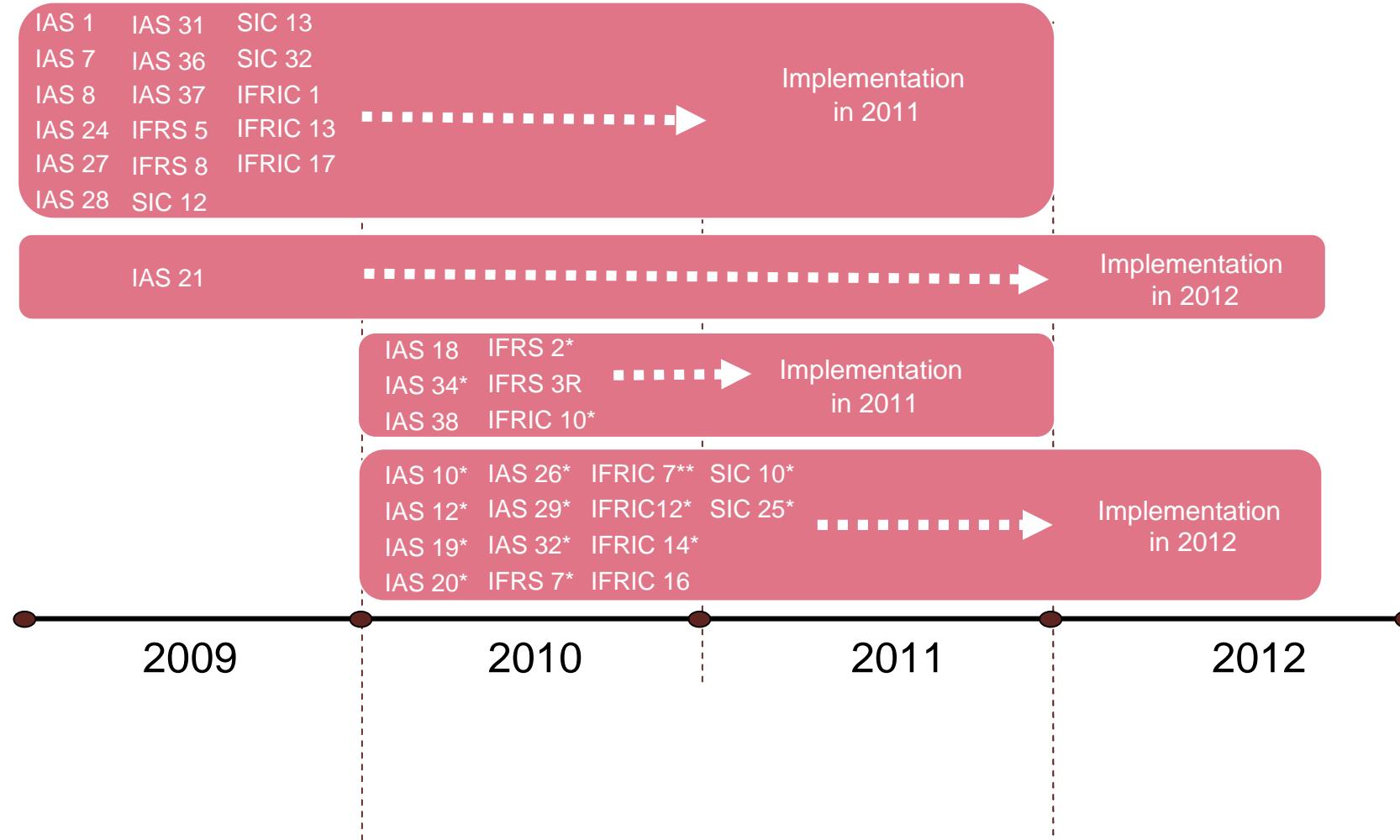


Jusuf M Wibisana
Partner
Assurance Services

Agenda

- Path to adoption of IFRS in Indonesia
- New PSAKs
- Tax Session
- Islamic Finance
- IT- How do you prepare for PSAK Implementation

Path to adoption of IFRS in Indonesia



* Still in exposure draft

** Tentatively proposed to be effective in 2012



Dudi M. Kurniawan
Associate Partner
Assurance Services

Agenda

- Path to adoption of IFRS in Indonesia
- New PSAKs
- Tax Session
- Islamic Finance
- IT- How do you prepare for PSAK Implementation

New PSAKs

- PSAK 4 (Revised 2009) - Consolidated and separate financial statements (IAS 27R)
- PSAK 5 (Revised 2009) - Operating segment (IFRS 8)
- ISAK 10 - Customer loyalty programs (IFRIC 13)
- PSAK 25 (Revised 2009) - Accounting policies, changes in estimates and errors) (IAS 8)

PSAK 4 (Revised 2009) - Consolidated & Separate F/S Comparison with previous standard

Differences with the previous version of PSAK 4, among others:

- Potential voting rights considered in determining control
- A subsidiary is not excluded from consolidation just because the investor is a venture capitalist or mutual fund
- Guidance when reporting date of the parent is different from that of the subsidiary
- Non-controlling interest can be negative
- Disposal of interests in a subsidiary that does not result in loss of control -> equity transaction
- Separate financial statements of the parent:
 - as a supplementary information to the consolidated F/S
 - investment in subsidiary at cost or in accordance with PSAK 55

PSAK 5 (Revised 2009) - Operating Segments

- An entity shall disclose information to enable users of its financial statements to evaluate the nature and financial effects of the business activities in which it engages and the economic environments in which it operates
- Operating segments are “components of an entity about which separate financial information is available that is evaluated regularly by the chief operating decision maker in deciding how to allocate resources and in assessing performance”

PSAK 5 (Revised 2009) - Operating Segments

What are the key features of an operating segment?

- a. Engages in business activities
- b. Operating results are regularly reviewed by CODM to assess performance and make decisions
- c. Discrete financial information available

PSAK 5 (Revised 2009) - Operating Segments

Determining reportable segment

Identify each operating segment that exceeds 10% threshold

Aggregate any operating segments that meet all aggregation criteria

For the remaining operating segments below 10% threshold, aggregate with each other if majority of aggregation criteria met

**If reportable segments are less than 75% of revenue
add more reportable segments**

Optional

Optional

PSAK 5 (Revised 2009) - Operating Segments

Determining reportable segments

Aggregation criteria:

Aggregation is consistent with core principle



Segments have similar economic characteristics

Segments similar on each of five specified criteria***

PSAK 5 (Revised 2009) - Operating Segments Disclosure considerations

Disclosure of certain minimal information

Non-GAAP Measures

Must disclose

Measure of assets

Measure of profit

Reconciliation of totals to primary
financial statements

Disclose if provided in some manner to CODM

Segment liabilities

Significant items like depreciation,
interest, revenue

Associates and capex

PSAK 5 (Revised 2009) - Operating Segments

Reportable segment

| Operating segment | Segment reporting |
|--------------------------|--------------------------|
| Corporate banking | |
| Retail banking | Banking |
| Investment banking | |
| Sharia banking | Sharia banking |
| Securities | Securities |
| Others | Others |

ISAK 10 - Customer Loyalty Program

How to treat an entity's obligation to provide free or discounted goods or services ("awards") in the future:

- Allocate some of the consideration received or receivable to award credits and defer revenue
- Amount of consideration allocated based on Fair Value of the award credit

Reward points
programmes

Miles credit
cards

PSAK 25 (Revised 2009) - Accounting Policies, Changes in Estimates and Errors

- Terminology: fundamental errors → errors
- Hierarchy of accounting policies
 - Specifically applicable PSAK
 - Accounting policies to produce information that is relevant and reliable
 - PSAKs applicable for similar items
 - Framework for the Preparation and Presentation of Financial Statements
 - Pronouncements by other standards-setter
- Mandatory disclosure of new PSAKs not yet effective & potential impact

PSAK 7 (R 2009) – Disclosures of Related Parties

- Related parties include, among others:
 - parent
 - subsidiaries
 - fellow subsidiaries
 - associates
 - key management personnel of the entity or its parent (or close family members of their families)
 - post-employment benefit plans

PSAK 7 (R 2009) – Disclosures of Related Parties

- Transactions with related parties require certain disclosures, such as:
 - the nature of relationships
 - the amounts of transactions
 - outstanding balances
 - doubtful debt expenses
 - other matters necessary for a clear understanding of the financial statements

PSAK 7 (R 2009) – Disclosures of Related Parties

What is new?

- Definition of related parties
- Clarifies that an entity is required to disclose whether the terms of a related party transactions are at arm's length only when the terms can be substantiated

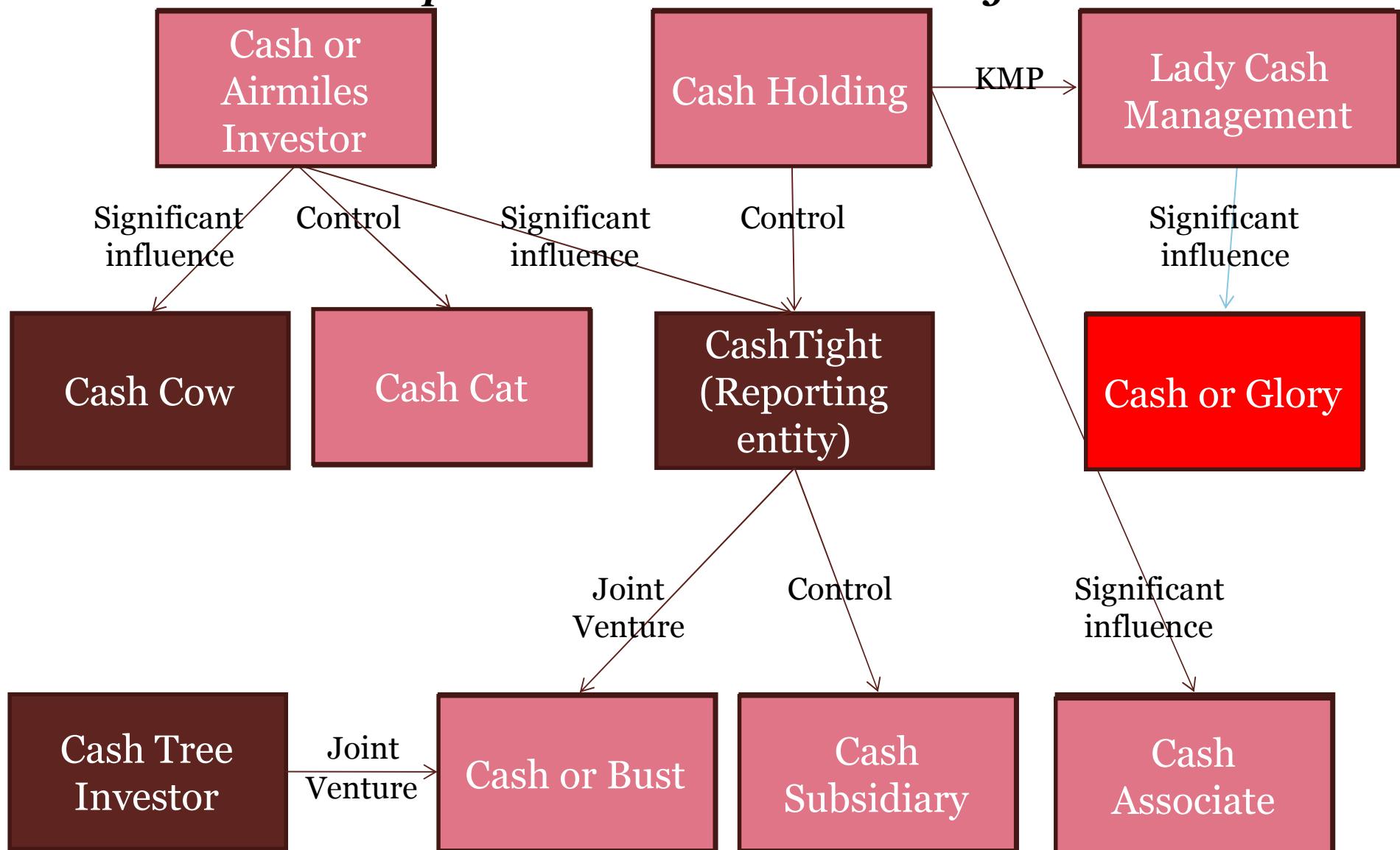
PSAK 7 (R 2009) – Disclosures of Related Parties

What is new?

- Relationships between parents and subsidiaries are disclosed irrespective of whether there have been transactions between them
- New disclosures, among others:
 - Total compensation of key management personnel by types of employee benefits
 - Classification of transactions with related parties into different categories of related parties
- Simplified disclosures for government-related entities

PSAK 7 (R 2009) – Disclosures of Related Parties

Example – Who is related to Cash Tight?





Angelique Daryanto
Partner,
Assurance Services



Samuel Ong
Technical Advisor,
Assurance Services



Triono Soedirdjo
Director,
Advisory Services



Hendra Lie
Director,
Tax Services

New PSAKs

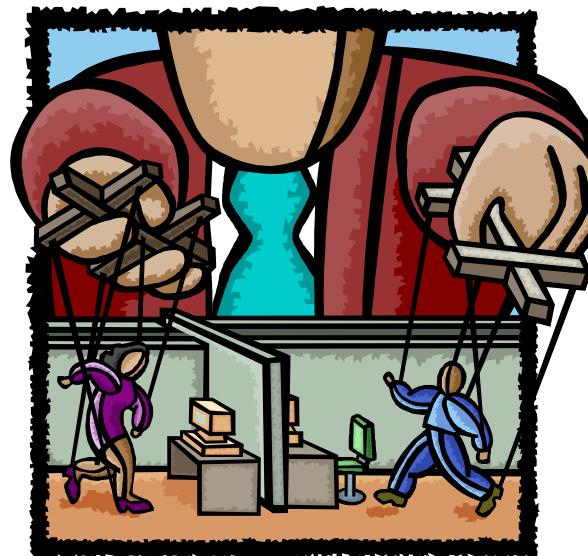
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- PSAK 22R – Business Combinations (IFRS 3R)
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New PSAKs

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What is control?

Control is the power to govern the financial and operating policies of an entity so as to obtain benefit from its activities.



Factors influencing control

Equity
shareholding

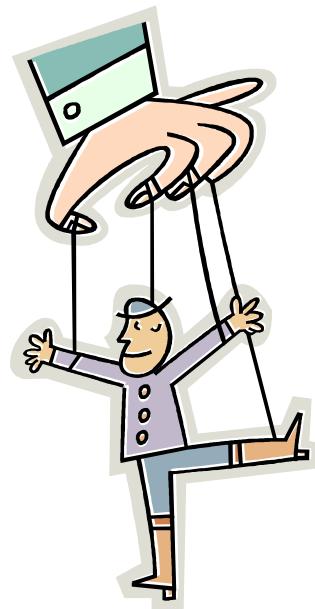
Control
agreement

Ability to appoint
directors to the
board

Potential voting
rights

De facto control

Special purpose
entities (SPEs)



A combination of all these factors needs to be considered

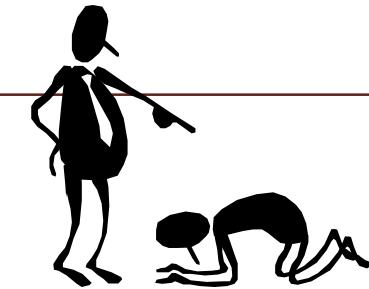
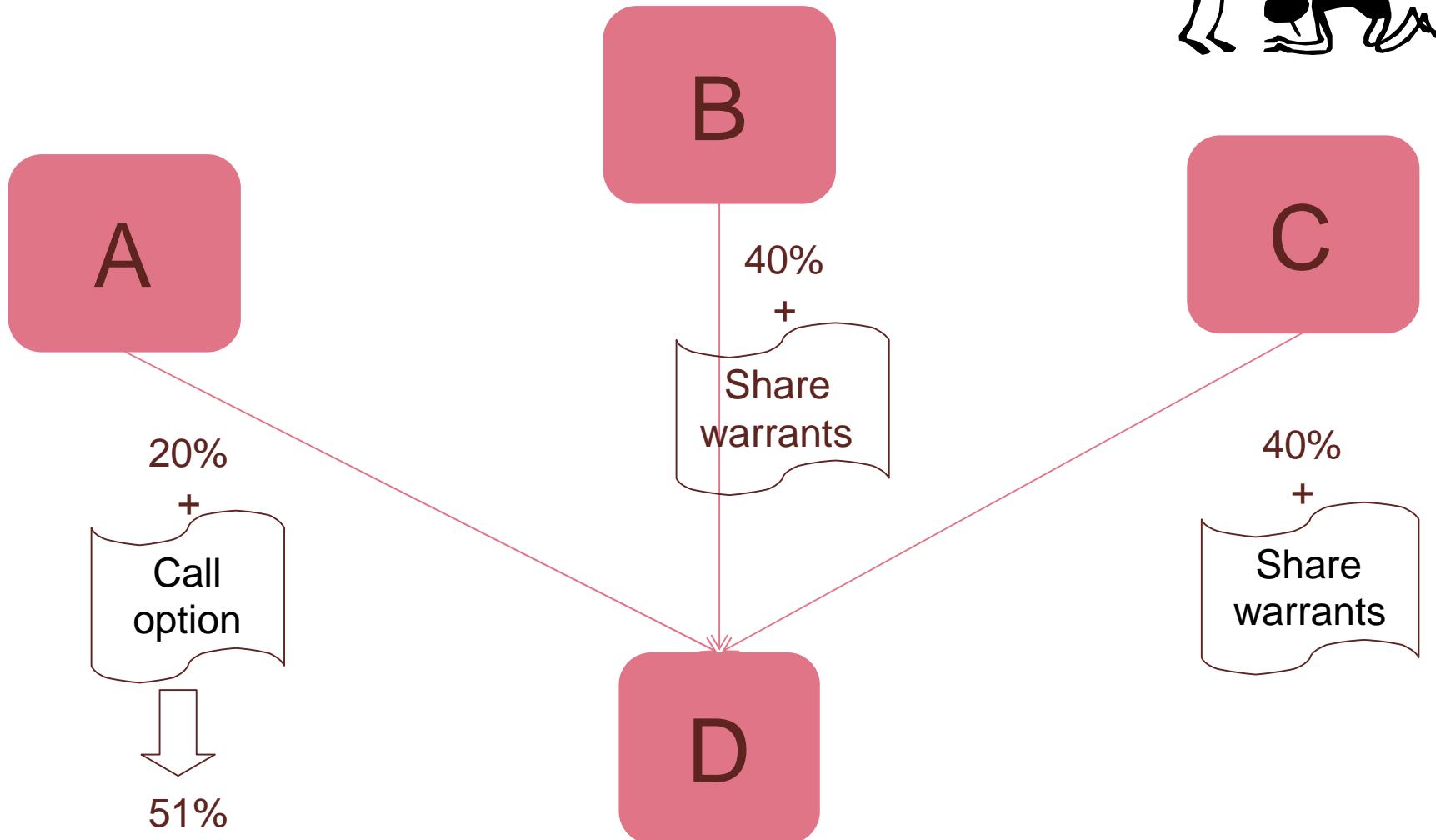
Potential voting rights

This is when an entity owns instruments that, if exercised or converted, give the entity power over the financial and operating policies of another entity e.g. share warrants, share call options, debt or equity instruments etc.

ALL FACTS AND CIRCUMSTANCES SHOULD BE EXAMINED

PSAK 4 (revised) requires all potential voting rights that are CURRENTLY exercisable or CURRENTLY convertible be considered.

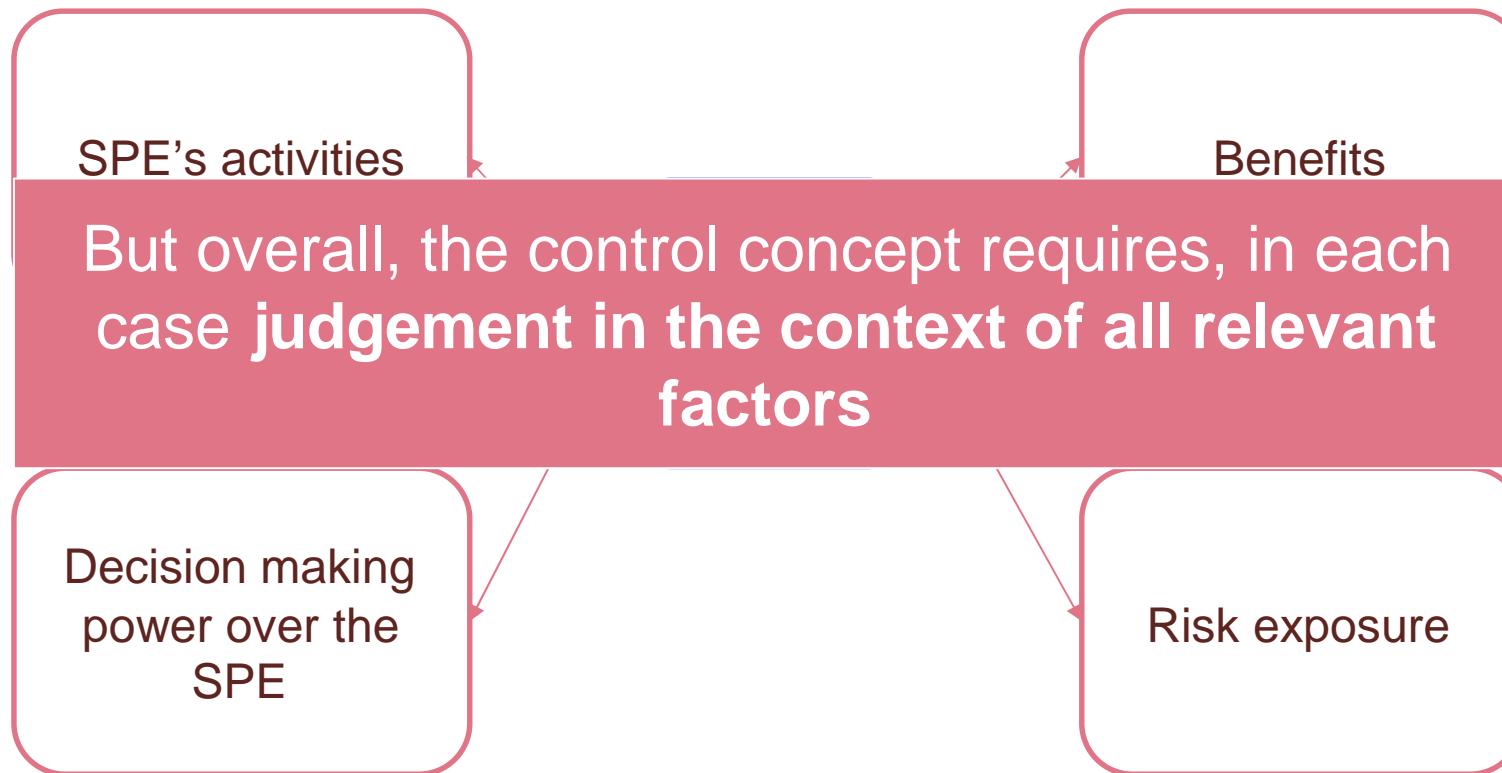
Potential voting rights



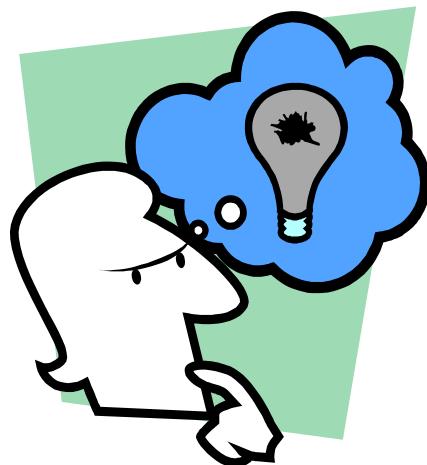
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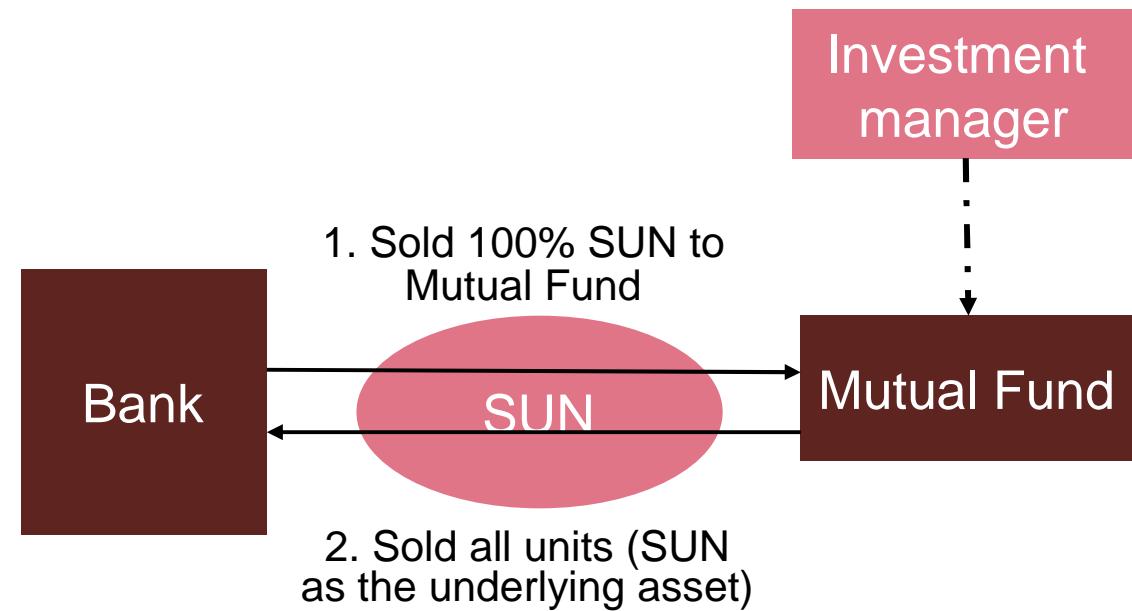
Special purpose entities (SPEs)



Special purpose entities (SPEs)

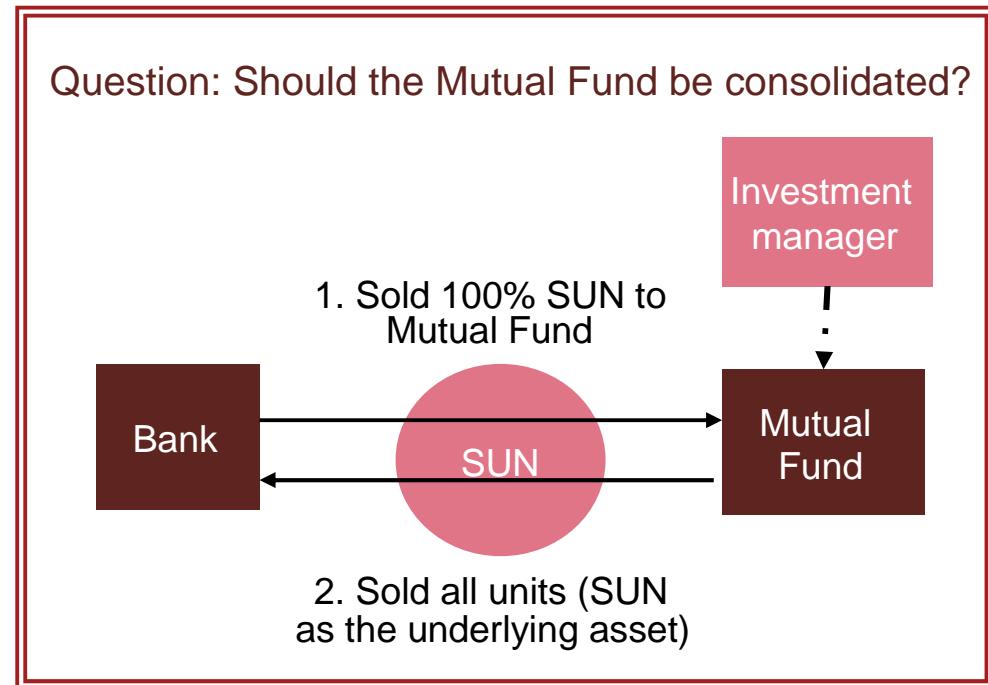


Question: Should the Mutual Fund be consolidated?



Special purpose entities (SPEs)

1. SPE's activities
2. Benefits
3. Risk exposure
4. Decision making power over the SPE



New PSAKs

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Purchase Price Allocation

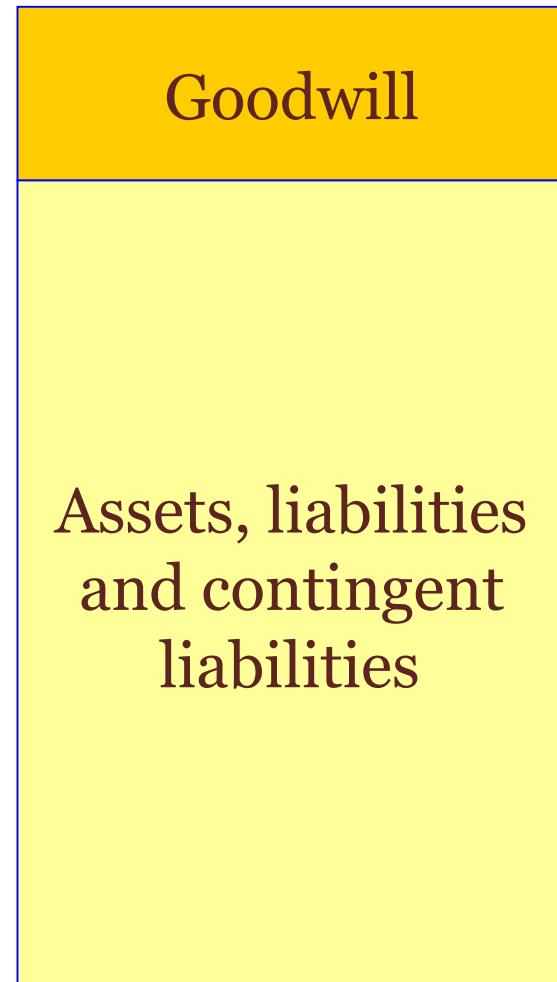
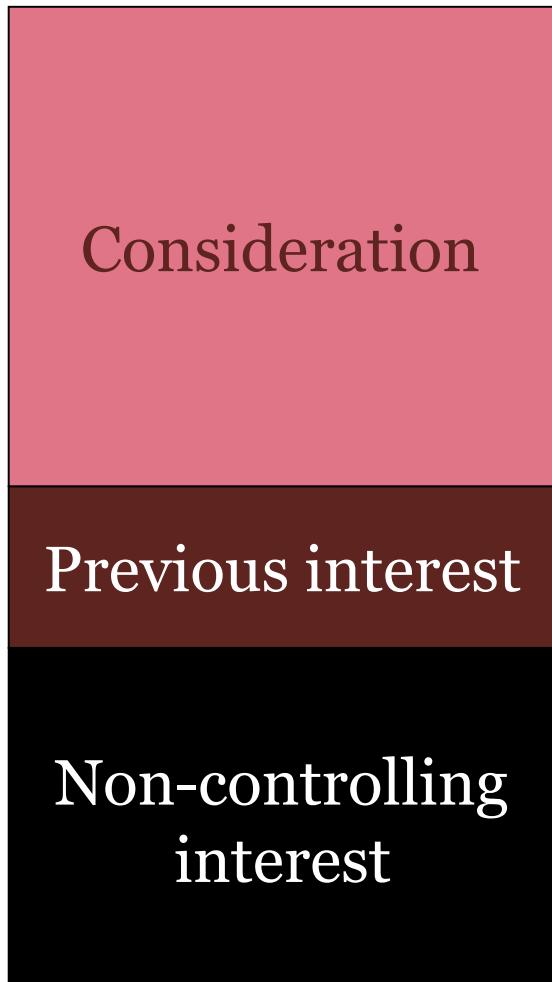
Principles

Example

almost
Fair value everything!



Principles – PSAK 22 (R 2010)



almost Fair value everything!

- Identifiable assets, liabilities and contingent liabilities recognised at fair value (FV).
- Identify and recognise intangible assets at FV: brands, customer list, etc.
- Difference between cost and net FV of identifiable assets, liabilities and contingent liabilities is goodwill.

Example of business combinations

Case 1
Consolidated

Bank A



100%



Bank B

Case 2
Stand alone

Bank A



Purchase group of
assets/business

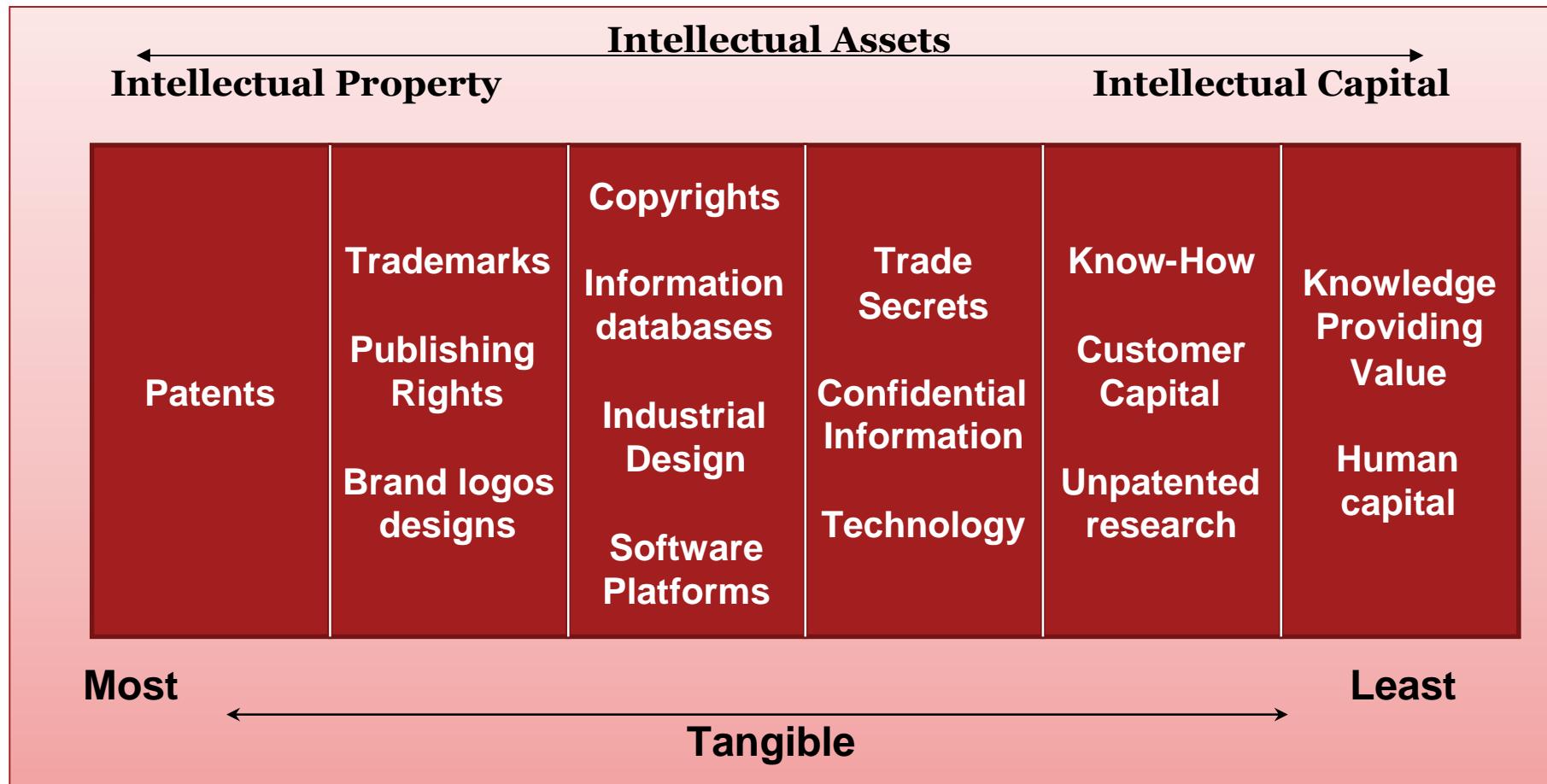


Division of Bank B
(commercial
banking)

Example of business combinations

| | Book value | Fair value |
|--------------------------|-------------------|-------------------|
| Assets | | |
| Intangible assets | 0 | 162 |
| Fixed assets | 3 | 2 |
| Financial investments | 5 | 5 |
| All other assets | 260 | 262 |
| | 268 | 431 |
| Liabilities | | |
| Provisions | 5 | 24 |
| Deferred tax liabilities | 0 | 54 |
| All other liabilities | 178 | 178 |
| | 183 | 256 |
| Net assets | 85 | 175 |
| Purchase price | | 696 |
| Goodwill | | 521 |

What are Intangible Assets?



Typical intangibles by Industries

Financial Institutions

Customer Relationships
Internet-Platform
Core Deposit Intangibles
Core Overdraft Intangibles

Brands
Software
Call Center

Pharmaceutical Industry

IPR&D
Brands
Patents
Licenses
Backlog
Technology

Trade Secrets
Order

Telecommunication

Licenses (eg UMTS/GSM)
Customer Relationships
Brands
Software (eg Billing)
Roaming Agreements (Inbound, Outbound)
Interconnection Agreements
Infrastructural Rights

Retail & Consumer Industry

Customer Relationships
Brands
Technologies
Favorable Contracts

The Intangible Assets mentioned above are examples. In performing a PPA facts and circumstances must be considered!

Typical intangibles by Industries

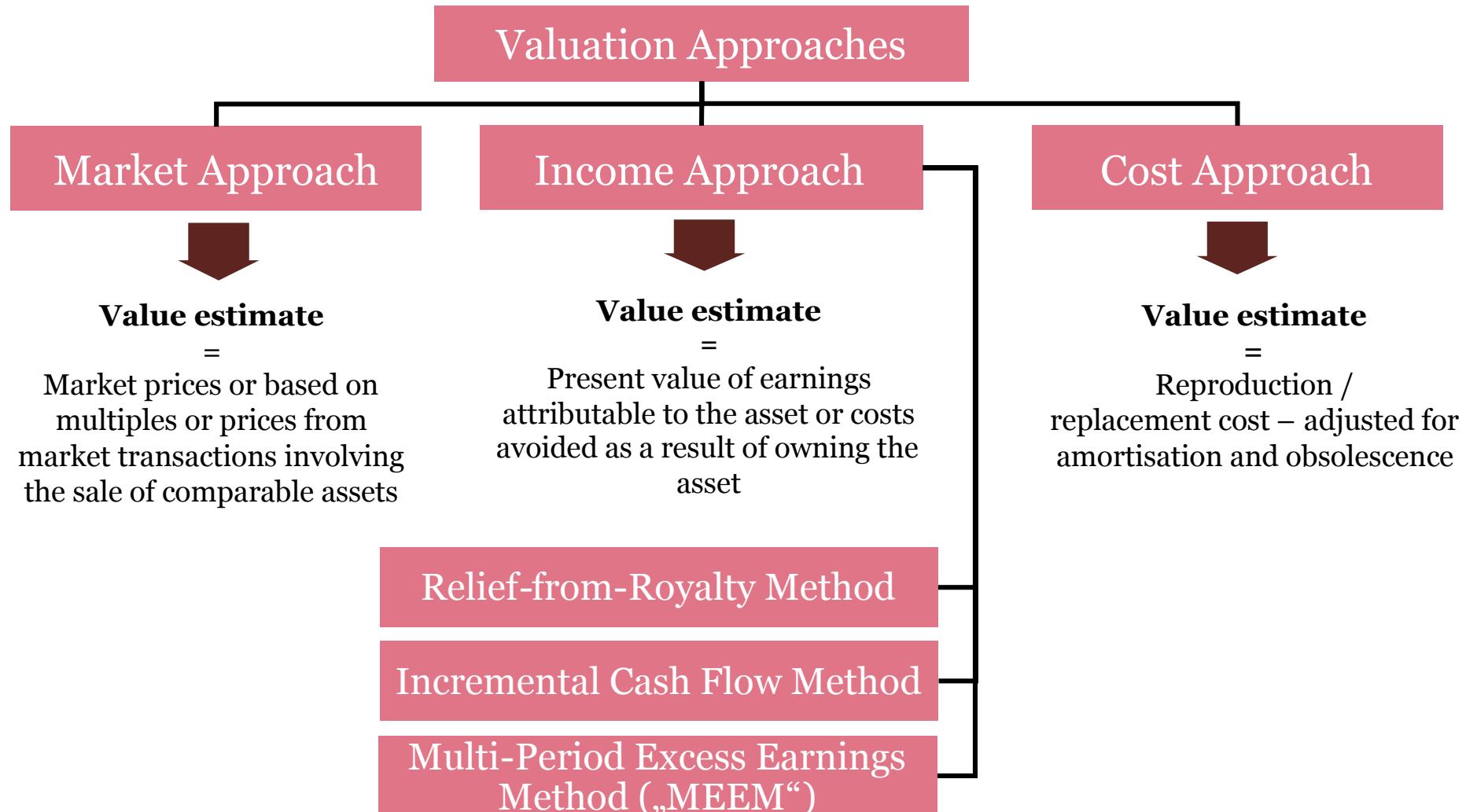
Financial Institutions

Customer Relationships
Internet-Platform
Core Deposit Intangibles
Core Overdraft Intangibles

Brands
Software
Call Center

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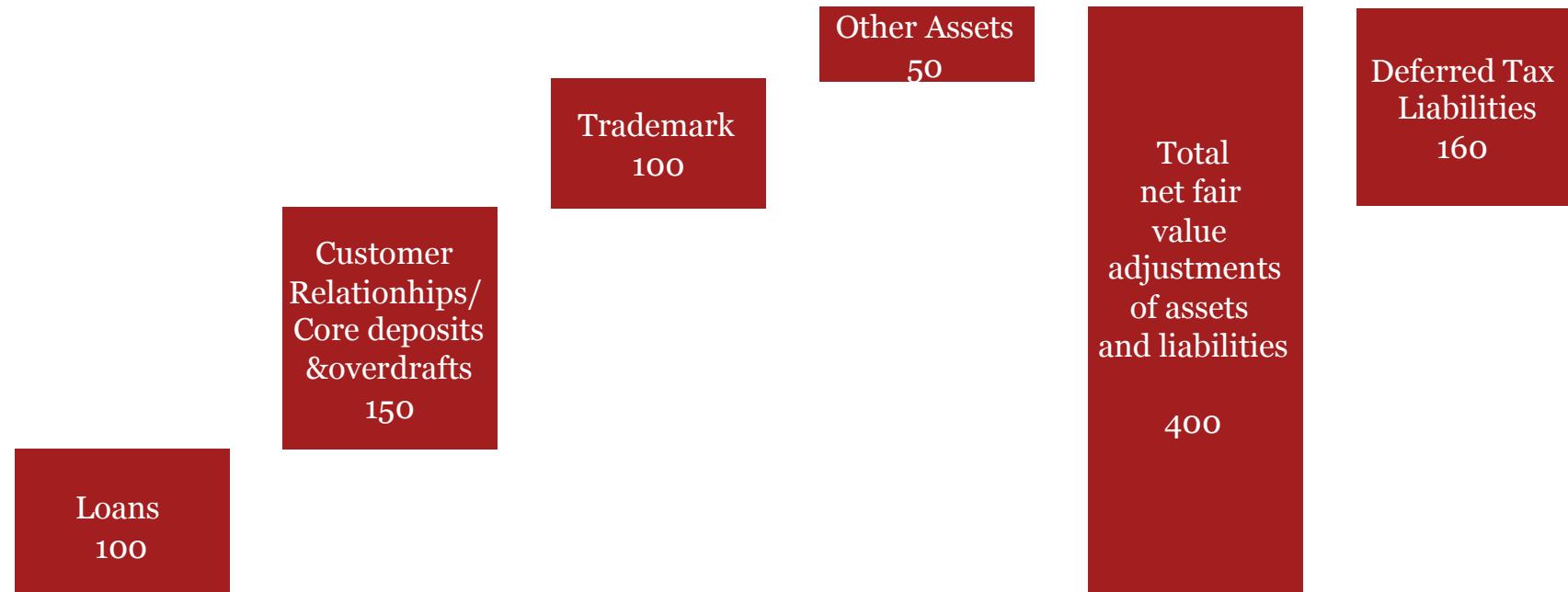
Valuation Approaches



Relief-from-Royalty Method

| Valuation of brand Valuation date: 1 January 2008 | |
|---|----------------------|
| Brand valuation | from 2008 |
| Fair value | |
| Brand-specific sales | 2000 |
| Royalty rate @ | 4% |
| Pre-tax royalty savings | 80.0 |
| Corporate taxes @ | 40% |
| After-tax royalty savings | 48.0 |
| Discount rate @ | 10% |
| Growth rate @ | 2% |
| Residual multiple | 11.918 |
| Discount factor | |
| Present value after-tax royalty savings | 572 |
| Tax amortisation benefit | 114 |
| Fair value | 686 |
| Step-up factor TAB | 1.2 |

Fair value adjustments – an example



Share Deal, Purchase Price USD 550 Mio. for 100% of shares, Net Book Value USD 100 Mio
Corporate Tax Rate 40%

How tax treats the intangible assets ?

- Amortisable?
- VAT-able?

| | Book value | Fair value |
|--------------------------|-----------------------|-------------------|
| Assets | | |
| Intangible assets | 0 | 162 |
| Fixed assets | 3 | 2 |
| Financial investments | 5 | 5 |
| All other assets | 260 | 262 |
| | 268 | 431 |
| Liabilities | | |
| Provisions | 5 | 24 |
| Deferred tax liabilities | 0 | 54 |
| All other liabilities | 178 | 178 |
| | 183 | 256 |
| Net assets | 85 | 175 |
| Purchase price | | 696 |
| Goodwill | | 521 |

Amortisation of intangible assets based on Income Tax Law

Amortisation upon expenditures to acquire intangible assets ..., including goodwill that has useful life of more than 1 year which is utilised to obtain, collect, and maintain income shall be calculated using a straight-line or declining balance method ...

VAT Imposition on intangible assets

VAT Law reference:

- Article 4(1)(a):
The delivery of taxable goods within the Indonesia customs area.
- Article 16D:
The delivery of taxable goods in the form of asset initially not for sale.

Subsequent measurement

Goodwill

CGU & impairment



New PSAKs

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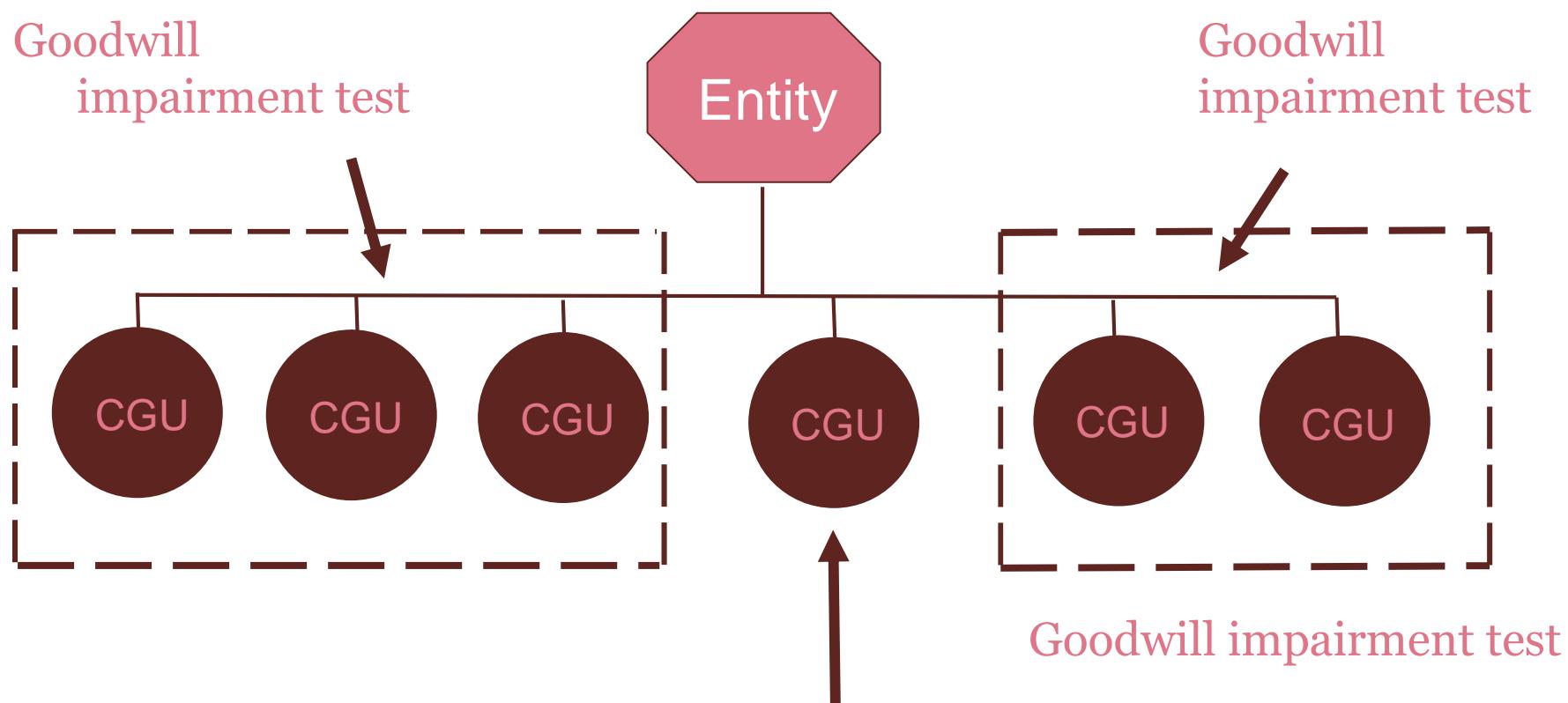
Goodwill

- Not amortised
- Test annually for impairment and when indicators arise
- Goodwill allocated to cash generating units (“CGUs”) or groups of CGUs

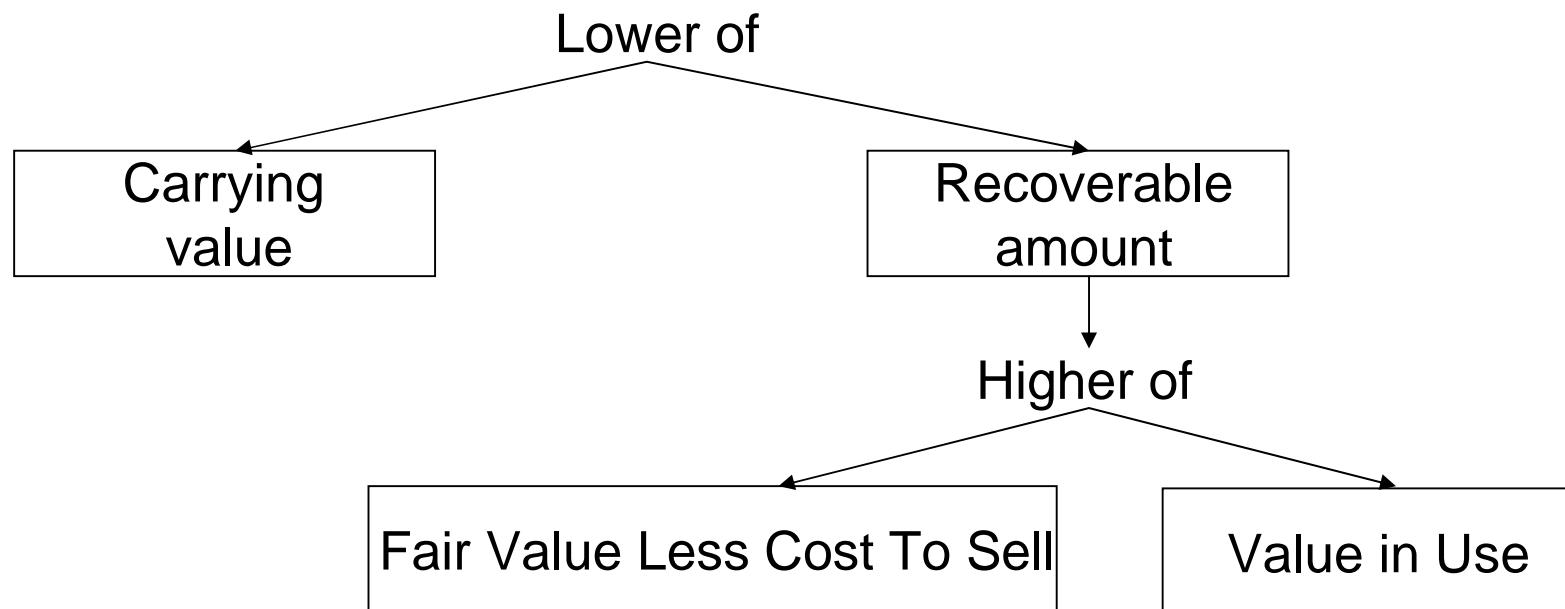


Cash generating units & impairment of goodwill

Goodwill impairment



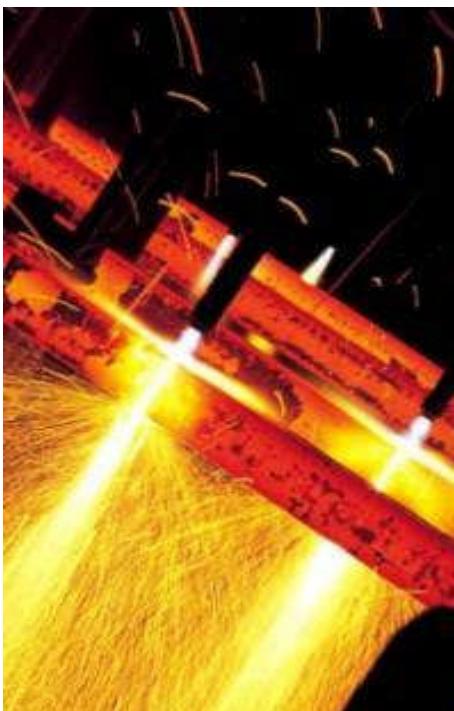
Measurement of goodwill



Value in Use

Value Concept

Value in use



“The present value of the future cash flows expected to be derived from the continuing use an asset or CGU and its disposal at the end of its economic useful lifetime.”

Key elements:

Internal value - company perspective

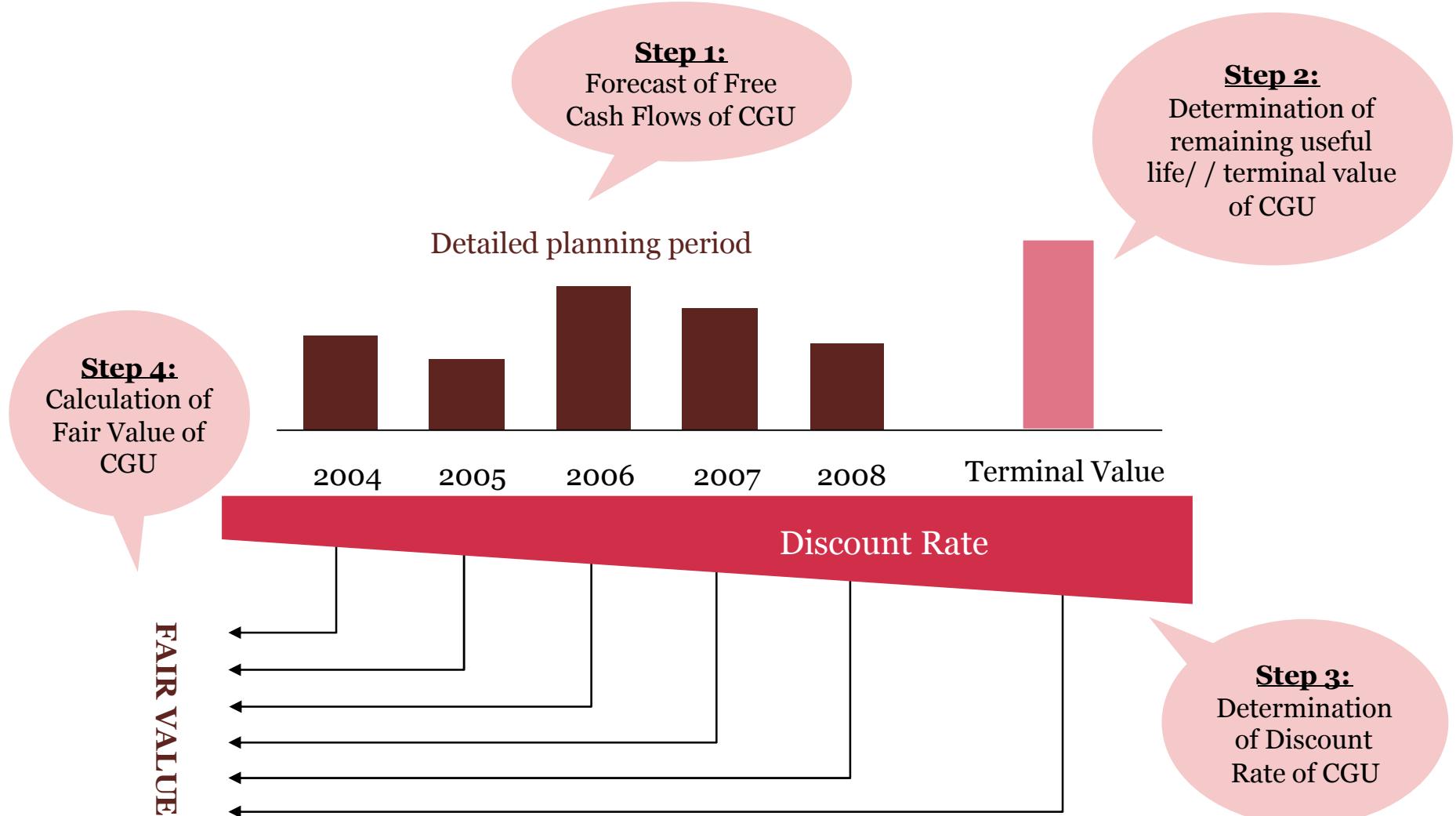
Company-related valuation parameters

Recognition of all synergies

Use pre-tax cash flows and discount rate

More detailed specifications in IAS 36

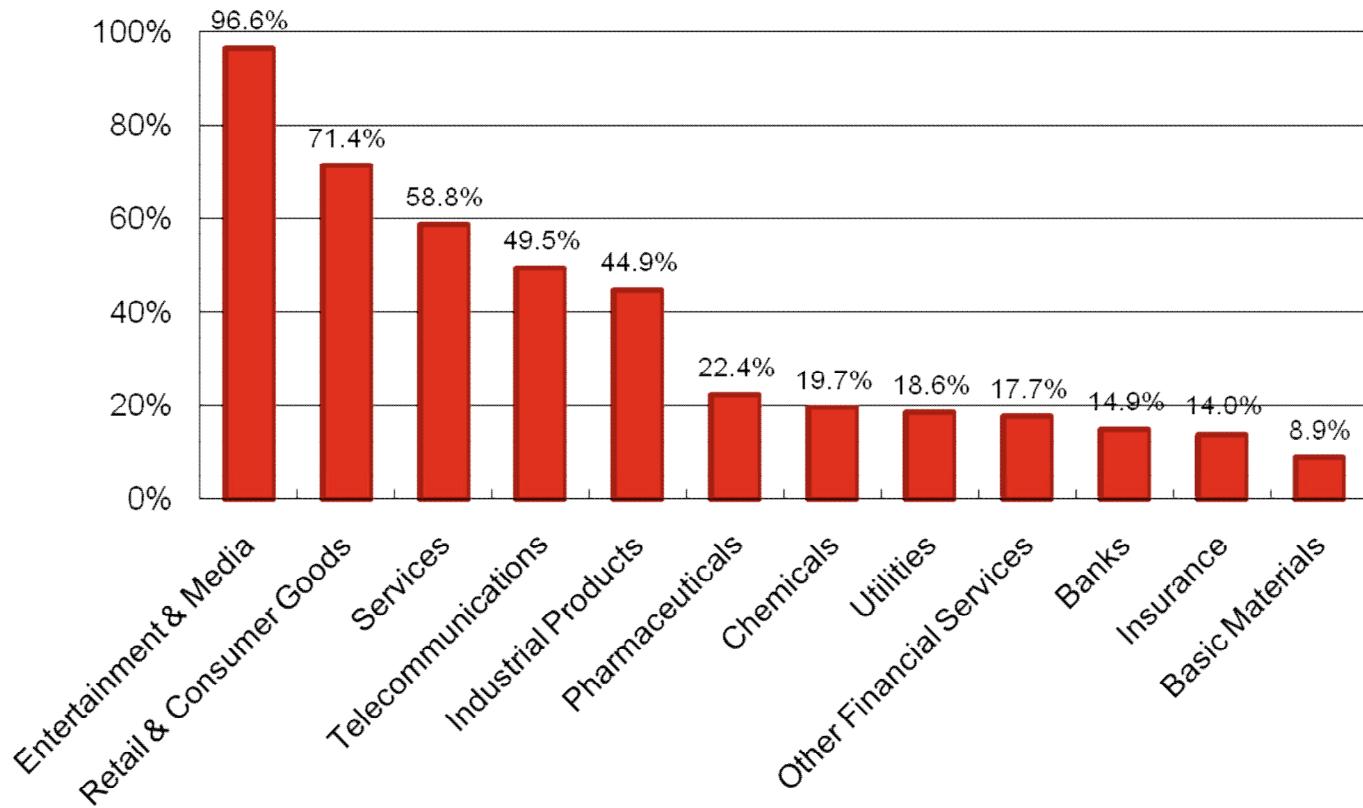
Value in Use of CGU Based on Income Approach



Common Errors Observed in Practice

- Underestimation on the complexity of standard requirements
- Lack of prior agreement between external auditor and management
- Lack of comprehensive knowledge of accounting standards
- Incomplete identification of assets
- Improper definition of CGU/RU
- Inclusion of synergies in financial projection
- Not enough analysis on comparables
- Incorrect cash flow calculation (e.g. double-counting)
- Discount rate used is not appropriate
- Incorrect calculation of carrying amount
- Other valuation errors

Average percentage of goodwill relative to total equity



Source: "Making acquisitions transparent" (Professors Glaum, Street, and Vogel, 2007)

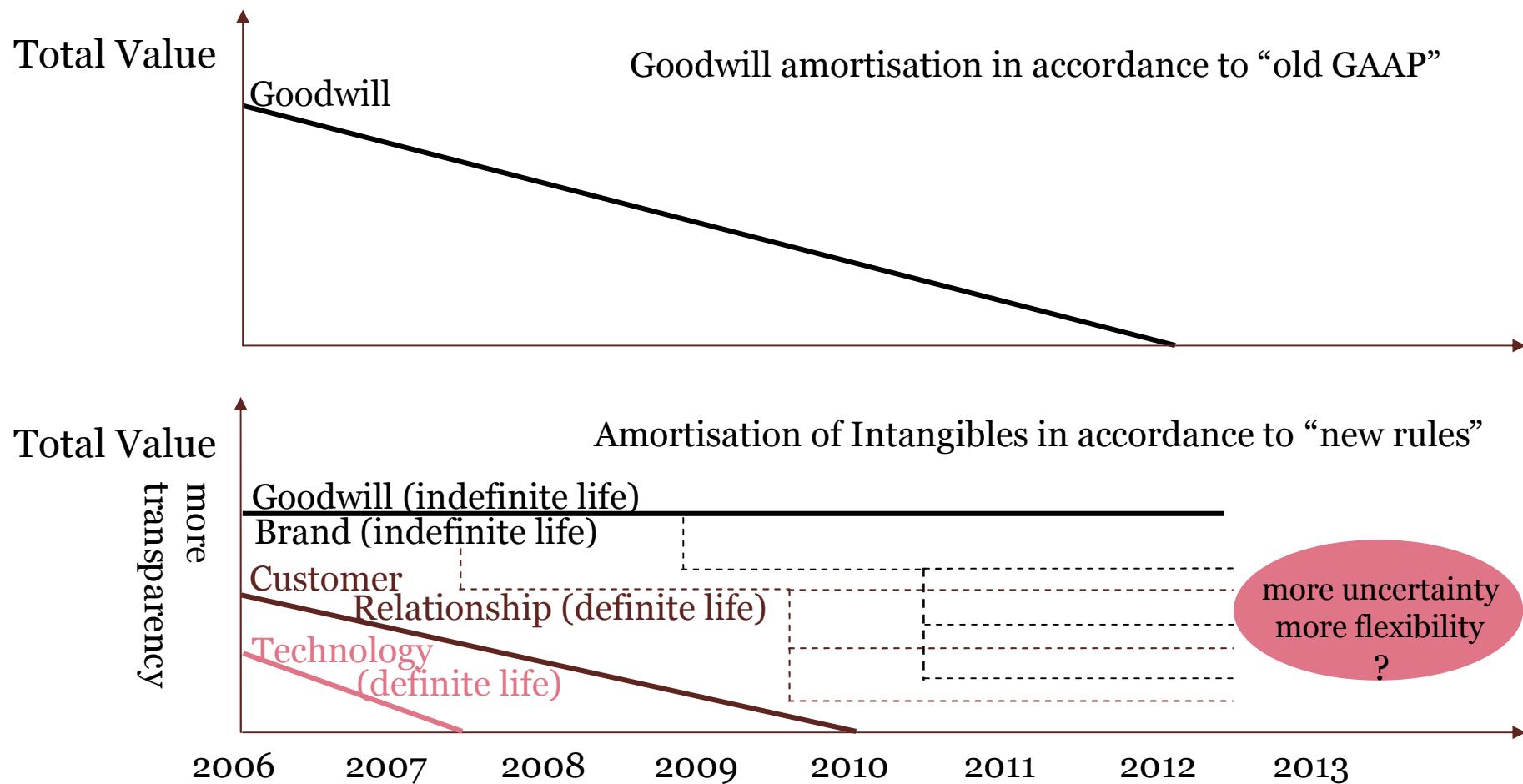
Capital Market Reaction on Goodwill Impairments



- Goodwill write-offs signal important changes in the company's future earnings potential
- Write-offs are difficult to assess due to their ambiguous nature
 - Impairments may represent **good news** when managers divest unprofitable operations to refocus on core competencies.
 - Impairments may represent **bad news** when reductions in asset values foreshadow even deeper troubles yet to come
- Immediate effect on announcement is typically negative with a drop of 3.0-3.5% of the company's stock price. Average impact within one-year after announcement is minus 11.0%

Source: Hirschey, M. und Richardson, V.J.: *Investor Underreaction to Goodwill Write-Offs*, in: *Financial Analyst Journal*, Nov./ Dec. 2003

Financial statements impact



How tax treats loss impairment on Goodwill?

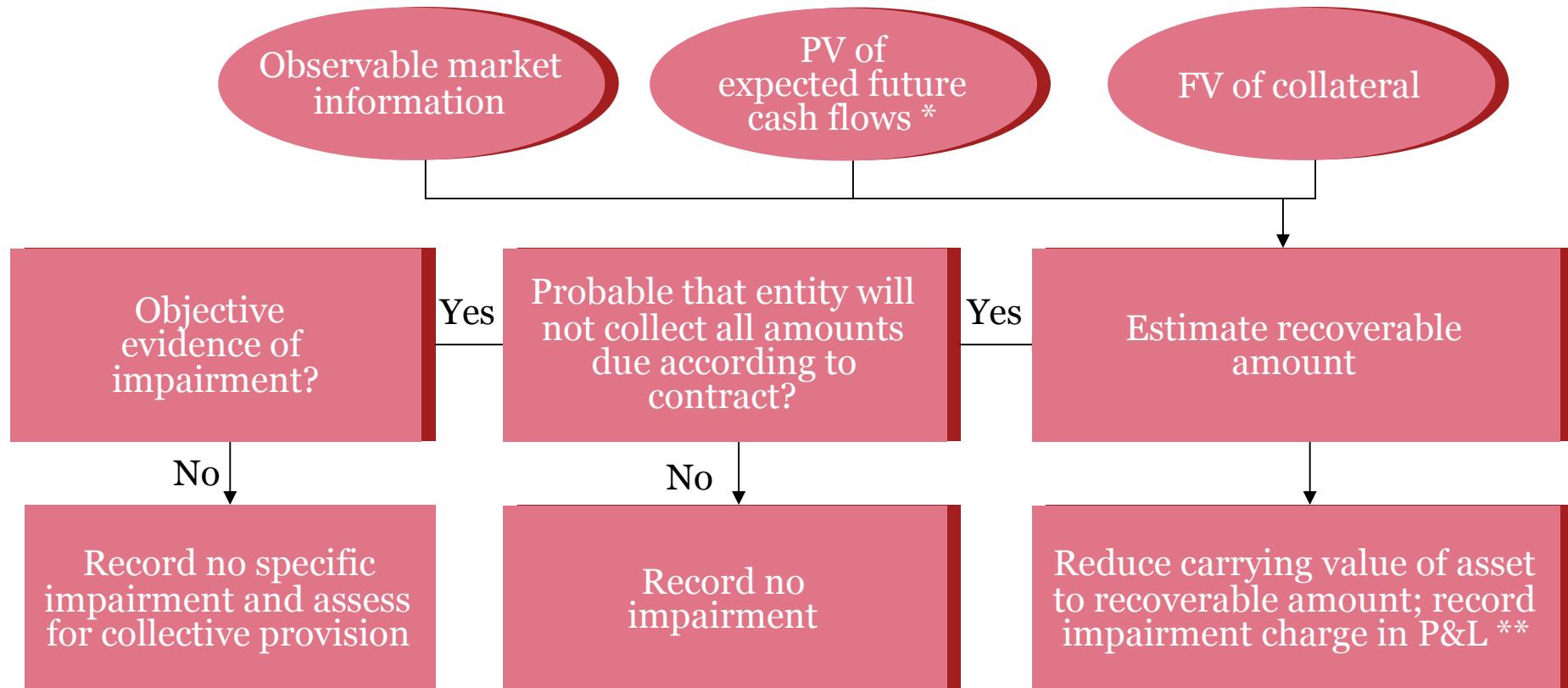
| Accounting | Goodwill | Tax |
|---|--------------------|---|
| Not amortised but subject to impairment | | Not subject to impairment but being amortised |
| Loss impairment | 1,000 4 years | Amortisation |
| (300) | Year 1 | (250) |
| (0) | Year 2 | (250) |
| (500) | Year 3 | (250) |
| (100) | Year 4 | (250) |
| <hr/> | | <hr/> |
| 100 | Goodwill in year 5 | 0 |

New *PSAKs*

- **PSAK 4R – Consolidated and Separate Financial Statements (IAS 27R)**
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Loan provisioning

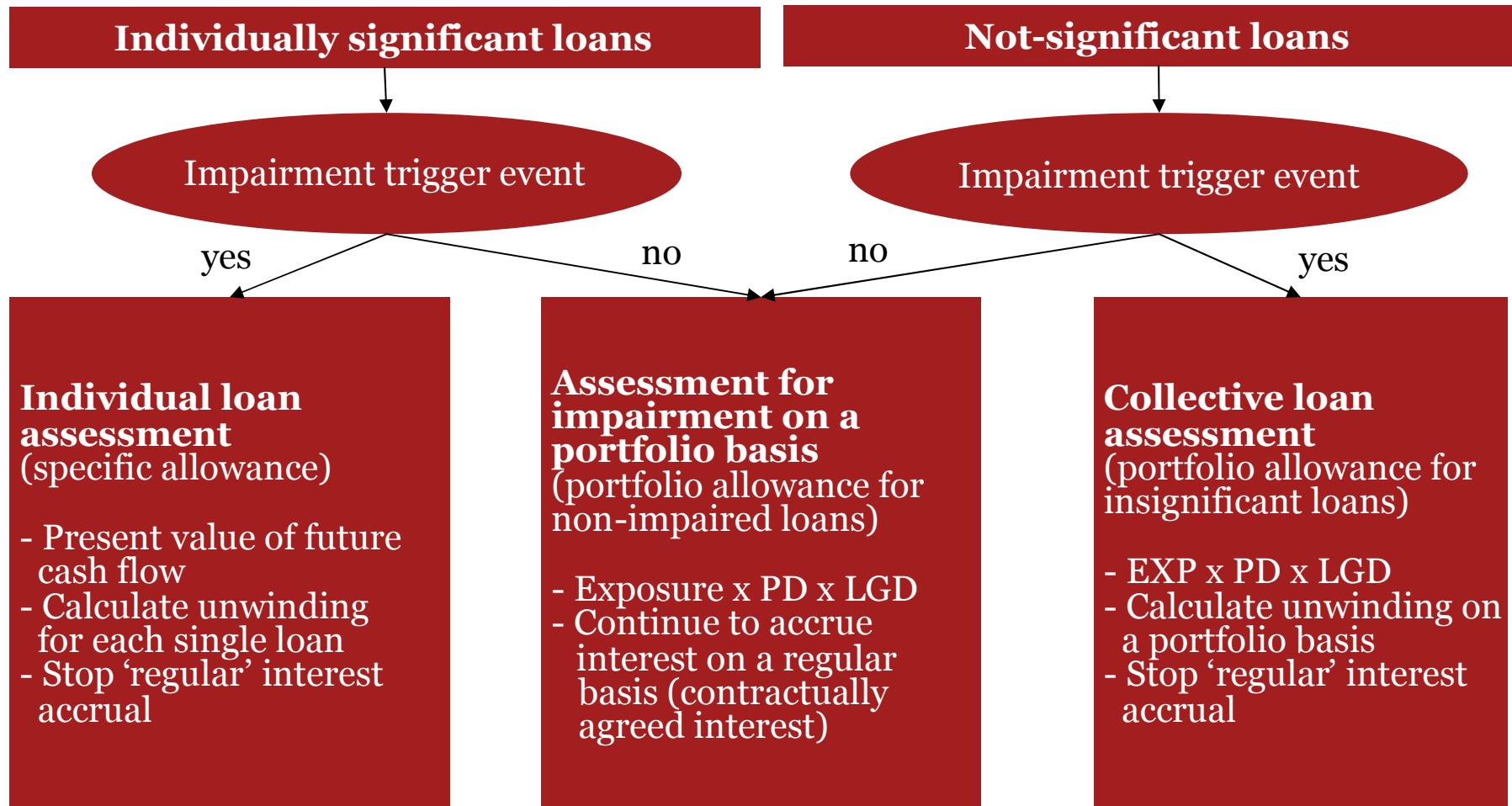
Decision Trees – Impairment Testing



(*) Use original effective interest rate or current effective interest rate, if variable
(**) can be subsequently reversed

Loan Impairment Methodologies

Different types of allowances



First time adoption of PSAK 55R – impairment (Technical bulletin No 4)

- Calculate impairment using the requirements under PSAK 55R on 1 January 2010
- The difference between new and previous amounts is recognised in the beginning retained earnings as of 1 January 2010

Statement of changes in equity

| | <u>Share capital</u> | <u>Additional paid-in capital</u> | <u>Retained earnings</u> |
|---|----------------------|-----------------------------------|--------------------------|
| Balance at 1 January 2010 | xxxxxx | xxxxxx | xxxxxx |
| Effect of adoption of PSAK 55R – impairment (note x) | _____ - | _____ - | <u>xxxxxx</u> |
| Restated balance at 1 January 2010 | xxxxxx | xxxxxx | xxxxxx |

Key take-aways

- Stay current on the future accounting standard changes
- Anticipate the potential impacts to business
- Increase internal accounting capabilities

Agenda

- Path to adoption of IFRS in Indonesia
- New PSAKs
- Tax Session
- Islamic Finance
- IT- How do you prepare for PSAK Implementation

Tax Session

Islamic Finance

*Accounting and Tax
Perspective*

Development in Islamic Finance

Shariah principle and implementation of SFAS 50/55 (Revised 2006)

- Effective interest rate
- Discounted cash flow method for calculation of impairment loss

Islamic Finance

Sharia Insurance

Accounting Standard for Sharia Insurance Transactions and its Implications

PSAK 108 “ Accounting for Sharia Insurance Transactions ” became effective on 1 Jan 2010

Key Differences

| Items | Before | After |
|-------|--------|-------|
|-------|--------|-------|

Accounting Standard for Sharia Insurance Transactions and its Implications

Key Differences

| Items | Before | After |
|-------|--------|-------|
|-------|--------|-------|

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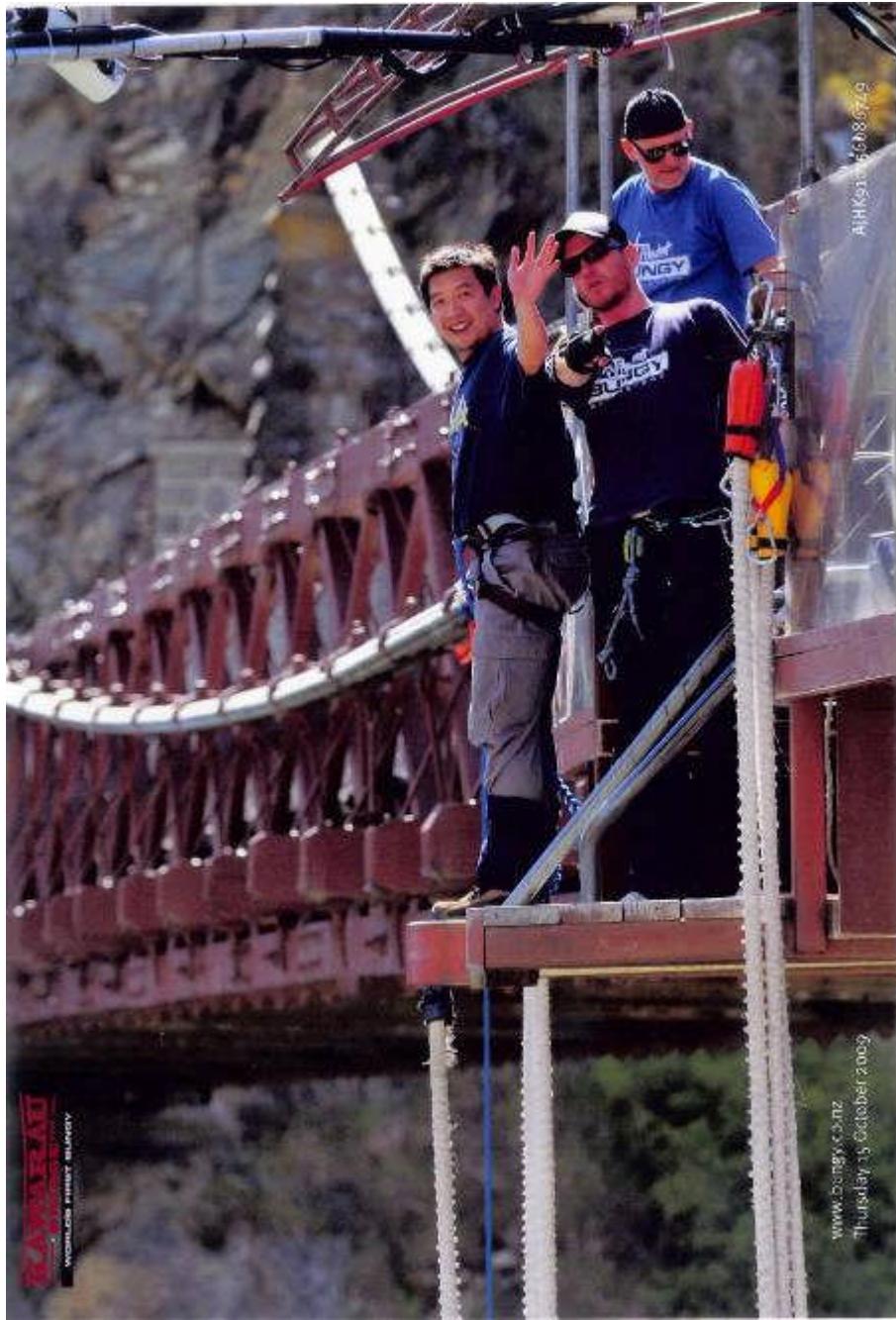
Accounting Standard for Sharia Insurance Transactions and its Implications

Tax implication

- Ujrah (fee) vs. investment management fee income – VAT and WHT issue
- Deductibility of reserve – Bapepam LK approval
- Tax on non-final investment income

PSAK 50 & 55

*IT Implementation – 1
Year After*



PwC





Move Forward – 1 year after

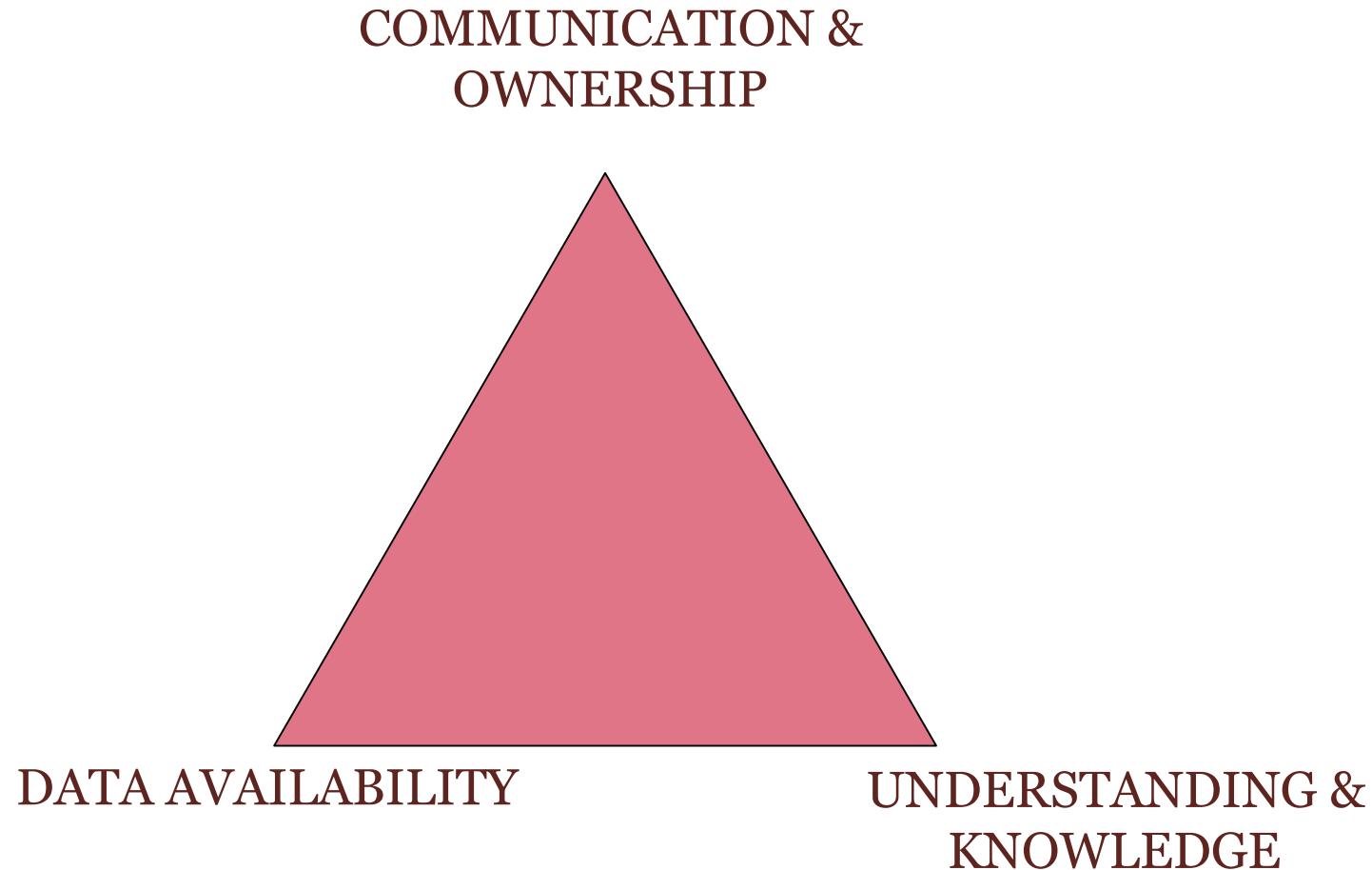
Assisted Various Clients

With Various

Scope, Size and Complexity

Share some stories to help you implement the new regulations/standards swiftly

3 Main Challenges



Challenge1 – Communication & Ownership

People / Departments

Ownership – Stakeholder, User and/or Other Parties

Challenge 2 – Understanding & Knowledge

Incl. How to

As-is Vs. Future

- Regulation
- Product
- System
- Strategy

Challenge 3 – Data Availability

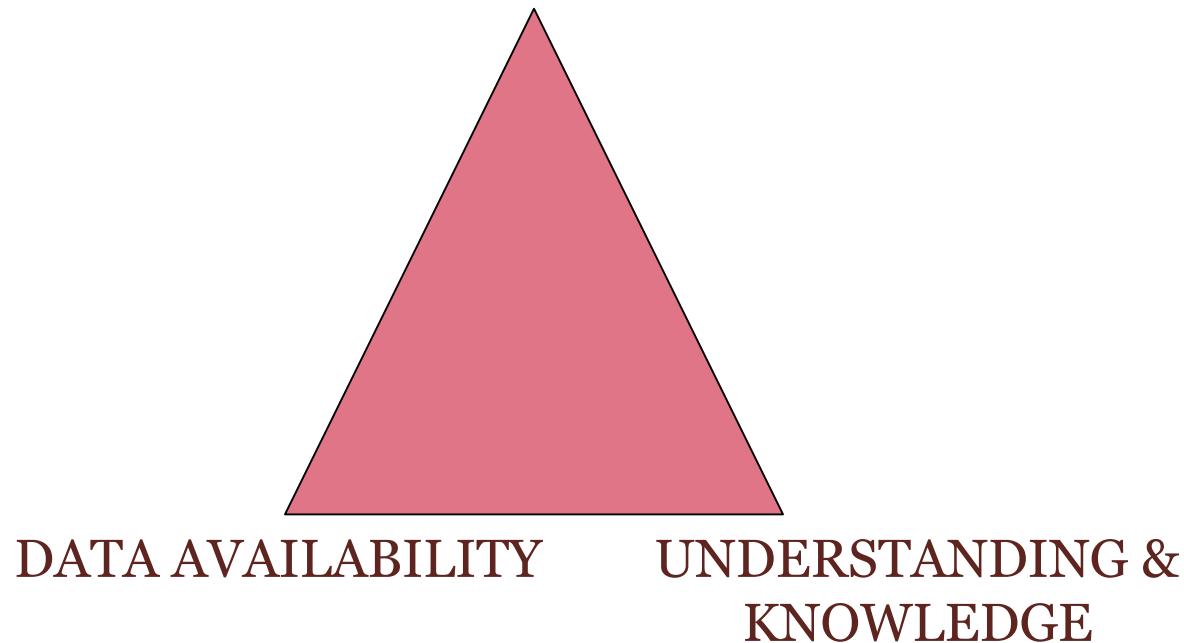
Existing data

Where does the data reside?

Obtaining the data

Conclude

COMMUNICATION & OWNERSHIP



If not sure— Quickly consult/ Escalate to higher MANAGEMENT for their APPROVAL

Our recent publications

US GAAP, IFRS and Indonesian GAAP
similarities and differences



2010 edition

PRICEWATERHOUSECOOPERS

PT INDONESIA Bank Tbk dan Anak Perusahaan
PT INDONESIA Bank Tbk and Subsidiary

Ilustrasi Laporan Keuangan Konsolidasian 2010
Illustrative Consolidated Financial Statements 2010



PRICEWATERHOUSECOOPERS



19 October 2010

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PT INDONESIA AND SUBSIDIARIES

Illustrative 2010 consolidated
financial statements



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