



IAS – Latest Developments

London, 15 April 2003

- **Improvements Project**
- **Roundtables**
- **Convergence Project**
- **UK developments**
- **Next steps**



Improvements Project

- Where are the ED's now?
- Where are they likely to get to?
- And what about FRED?



Roundtables

- Week commencing 10 March, London and Brussels
- 108 participants/observers from 170 comment letter submissions
- IASB Board met 19/20 March; next meeting 24-25 April
- Increased focus on European Banking Federation and EU processes
- Wait and see on revisions and re-exposure
- Are we nearly there yet?

De-recognition

- Limited support for continuing involvement model
- Participants preferred mixed model approach
- Existing rules likely to be tidied up
- IAS 27/SIC 12 to be reviewed
- Watch this space – but significant issues with SPVs still likely

Derivatives and hedging

- Mixed views on use of fair values for all derivatives
- IASB is firm on fair values and effective testing
- Preference for principles-based approach
- IASB to focus on simplification/modification of existing rules
 - Short-cut method unlikely to be adopted
 - Partial term hedging

Macro hedging and internal derivatives

- Strong support for economics of business to allow macro-hedging
- Working group to develop solution
- Need to build in effectiveness testing
- Internal derivatives
 - No revisions envisaged
 - Need clarification regarding requirements on external risk layoff

Impairment

- Focus on incurred loss model rather than expected loss
- Preference for IASB to keep requirements on detailed impairment methodology as principles-based rather than too much detail
- Participants concerned about availability of reliable historical data for models
- Explore more closely the link with Basel

Debt vs Equity

- Generally supportive of proposed changes
- Greater clarity in guidance would be welcomed
- Economic compulsion option to be explored further

Fair values

- Support for option of measuring all assets and liabilities at fair value and consequent impact on hedge accounting
- Preference for choice of allocation to trading category continuously
- IASB to explore option of cherry-picking on first-time adoption
- Day 1 profit recognition



Insurance

- Phase I
- Phase II
- Definitions?
- Next steps



IASB/FASB Convergence Project Norwalk Agreement

- Presentation of Financial Statements
- Accounting policies, estimates and errors
- Inventories (construction contracts)
- Property, plant and equipment
- Foreign currency translation (hyperinflation)
- Accounting for associates
- Governments grants
- Discontinuing operations
- Interim financial reporting
- Income taxes
- Provisions
- Post employment benefits (pensions)

Financial instruments

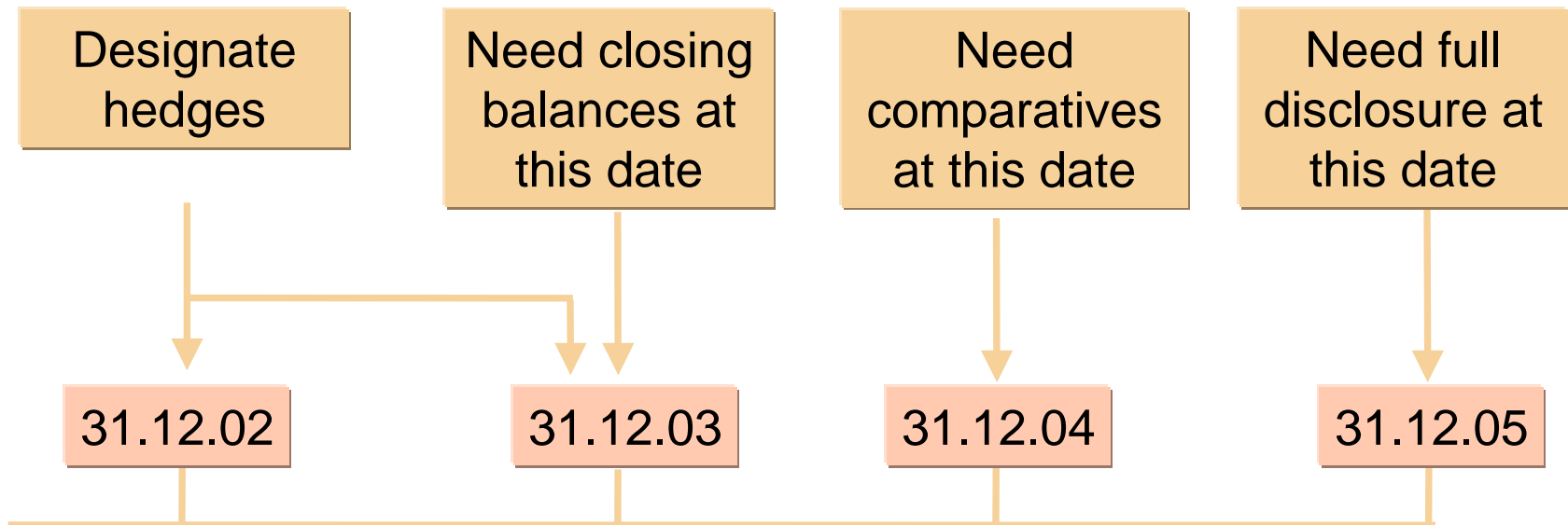
IAS 32 and IAS 39

**Business combinations, including
intangibles and impairment**

- **DTI – possible voluntary adoption for unlisted entities**
- **Inland Revenue**
- **FSA**

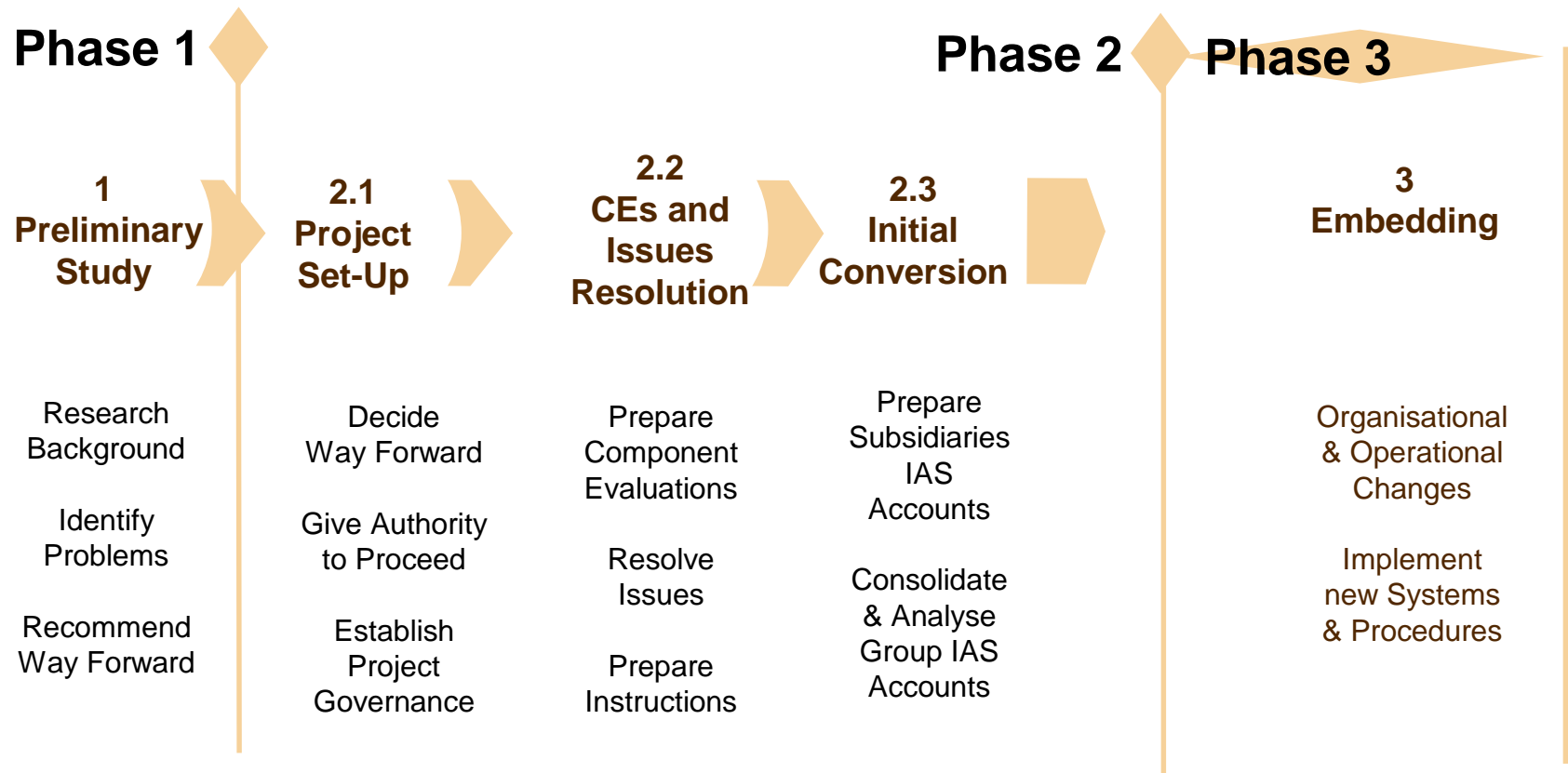
EU Adopted IAS Timeline

Companies will need to start preparing now



“Only applies to the consolidated accounts of listed companies”

Route Map : IAS Conversion and Embedding



Core components



Effective yield

Fair value
derivatives

Loan loss –
historical data

Embedded
derivatives

?

Off-balance sheet
structures

Hedge
documentation

Effectiveness
measurement

Netting



Practical conversion experience

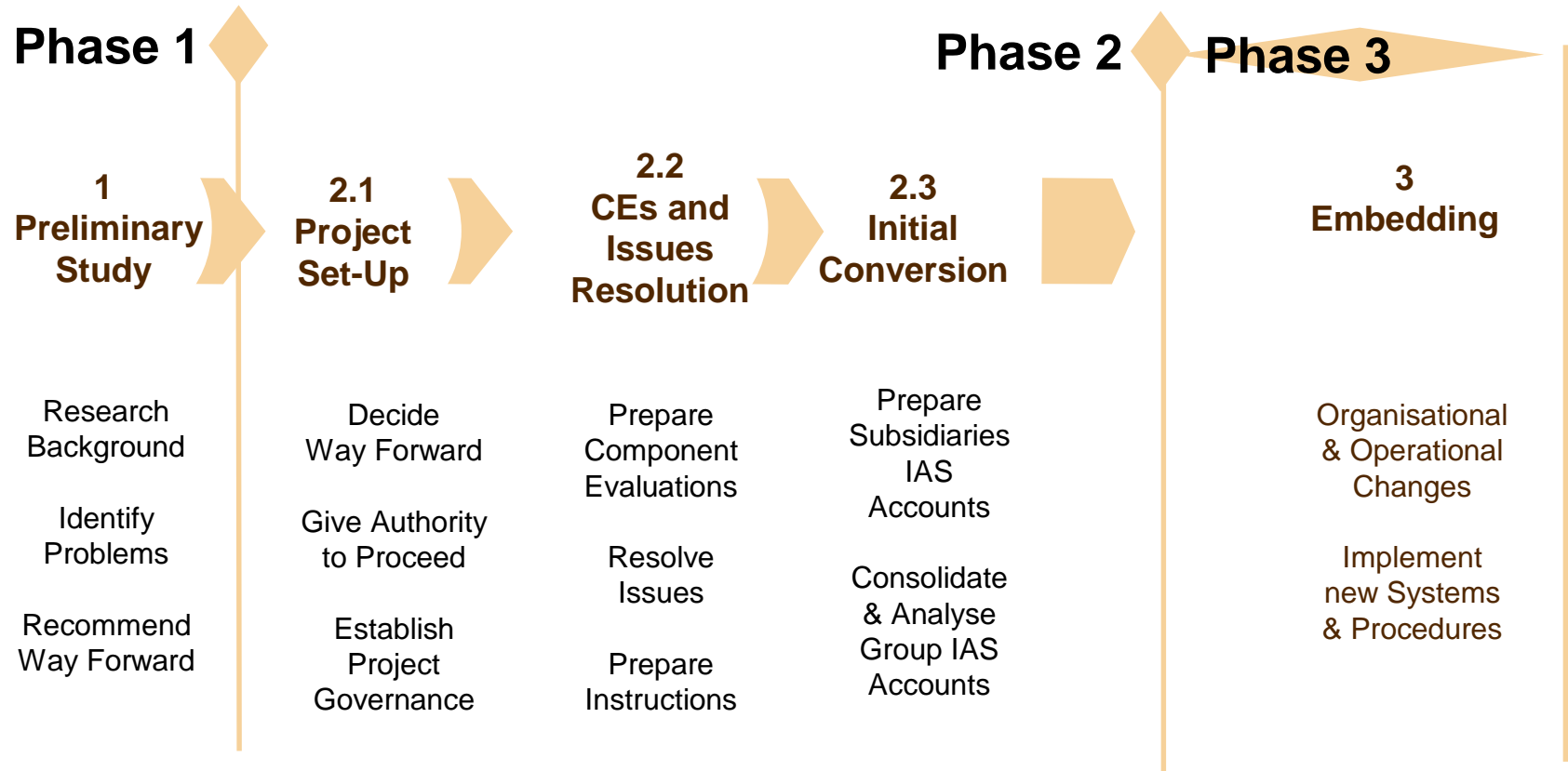
Mark Hannam, Partner



Agenda

- Conversion or embedding?
- IAS - It's still a moving target
- Some practical issues
- Where are entities now?

Route Map : IAS Conversion and Embedding





Conversion The concept

- Typical of a US GAAP reconciliation and reporting and often a compliance exercise
- Performed by consolidation team
- An identifiable exercise at each reporting date
- IAS is just another accounting framework along with UK GAAP, MIS, tax and regulatory

BUT,

Is this a viable solution if the underlying UK GAAP is also migrating to IAS?



Embedding The concept

- IAS becomes the reporting language of the organisation, including the basis for overall business performance measurement, KPIs, decision-making and product development
- The accounting and measurement is performed at the business unit level
- IAS-related data is captured at a transactional level
- Significant systems and process change may be necessary depending on complexity of operations and treasury activities



When is embedding complete?

- When the organisation at all levels uses, acts upon and thinks in terms of IAS
- External, MIS and budgetary reporting are systematically performed in IAS
- Automated processing
- Executive management can explain the numbers

The effort and resources necessary to achieve this should not be under estimated – the main lesson is “start early”



IAS – It's still a moving target

Maybe in places, however:

- The core building blocks for financial instruments require extensive data gathering, technical decisions or systems development:
 - Measurement and components of amortised cost/effective yields
 - Fair value accounting in banking book
 - Decisions on valuation engines and systems hierarchy
 - Embedded derivatives
- Non-financial instruments
- Group financial reporting and development of Chart of Accounts
- Group-wide awareness and strategy to implementation



Some practical issues Securities

- Categorisation eg HtM and transfers
- Measurement and identification of impairment
- Segregation of FX component for AFS debt securities
- Embedded derivatives
- Treatment of own issues and extinguishment of liabilities



Some practical issues

Loans

- Originated or purchased?
- Determination of amortised cost and components thereof
- Impairment
 - Definition and procedures for identification
 - Discounted cashflow techniques
 - Data warehouses
 - Segmentation of portfolios by risk characteristics
 - Historical loss experience
 - Data clean-up eg collateral databases
- Open: approach to portfolio measurement



Some practical issues Derivatives

- The devil does live in the detail
- Hedge accounting is time critical – there is no retrospective accounting
- Hedge accounting
 - Involve product accountants at all stages
 - Model hedge strategies
 - Model effectiveness testing methodologies
 - Internal deals and ALM strategies remain a significant problem
- Open: macro hedging techniques?



Where are entities now?

- PwC/EIU survey, “Illuminating value: the business impact of IFRS” indicated over half had not yet commenced implementation
- Observe significant embedding projects for 2005/07 entrants in Germany, however the practice across Europe appears variable
- Integrated software solutions e.g. SAP still in development
- Concern over hedge accounting and impairment with regards to timetable
- Embedded solutions from 1 January 2004 appear increasingly optimistic