From 2018, the new financial instruments standard, IFRS 9, will apply for all companies, not just financial institutions.

The new standard brings major changes to how you classify financial assets and record impairment. It also brings a new hedge accounting model that is aligned with risk management and extensive new disclosures.

**IFRS 9 will affect…**

**Investments**
- Classification and measurement may change due to new criteria that require an assessment of the contractual cash flows and how the investment is managed.
- The new impairment model, which is based on expected credit losses and forward-looking information, will increase provisions and may require new processes and controls.

**Trade and lease receivables and contract assets**
- Bad debt provisions are likely to increase and become more volatile.

**Hedge accounting**
- Hedge accounting is potentially available for a broader range of hedging strategies.
- Switching to the new hedging model will require more judgement and revised processes and controls.

**Disclosures**
- Extensive new disclosures are required.
- System and controls changes may be necessary to capture the required data.

**The challenges of IFRS 9 reach beyond accounting and may require changes to systems and processes.**
## Determining the impact

### Investments

**Potential impact**
- The classification of financial assets as measured at amortised cost, fair value through profit or loss (FVTPL) or fair value through other comprehensive income (FVOCI) will depend on each investment’s contractual cash flows and how the entity manages groups of investments.
- All investments in equity instruments – including unquoted shares – will be classified as FVTPL subject to an option to present at FVOCI if the investment is not held for trading.
- Impairment losses must be recognised for all investments in debt securities not classified as FVTPL. These reflect probability-weighted estimates of expected credit losses (ECLs) based on historical experience and forward-looking information: 12-month ECLs for assets that have not suffered a significant increase in credit risk; lifetime ECLs for those that have.

**Actions to consider**
- Review the contractual terms of investments.
- Analyse and document the business models for managing investments.
- Review credit risk management processes and data availability.
- Design and test new impairment methodologies.

### Trade and lease receivables and contract assets

**Potential impact**
- The new classification model must be applied to all receivables. Trade receivables will generally meet the criteria to be held at amortised cost, but watch out for the impact of securitisation or factoring arrangements and more complex contractual terms.
- Bad debt provisions are likely to be larger and more volatile. Impairment of trade receivables and contract assets without a significant financing component will be based on lifetime ECLs.
- For trade receivables or contract assets with a significant financing component, and lease receivables, an entity may choose to either apply the general approach or recognise lifetime ECLs at all times.

**Actions to consider**
- Review contract terms, and securitisation and factoring arrangements.
- Redesign impairment methodology to comply with new standard.
- Evaluate impacts of different accounting policy choices.
- Review management information under the current requirements and assess how it could be aligned with the new classification and measurement, and impairment requirements.

### Hedge accounting

**Potential impact**
- IFRS 9 allows an entity to switch to a new hedge accounting model that is aligned more closely with risk management. Under the new model, more risk management strategies (e.g. related to commodity price risks) are likely to qualify for hedge accounting.
- The new model is more principles-based: the bright-line effectiveness test under IAS 39 falls away and a more judgemental approach is required in the assessment of qualifying, rebalancing and discontinuing hedge accounting.

**Actions to consider**
- Assess whether to adopt the new IFRS 9 hedging model or remain with IAS 39 hedge accounting.
- Assess and quantify the impact of applying the IFRS 9 hedging model to existing and new hedging relationships to determine the effort and changes required to implement.

### Disclosures

**Potential impact**
- Extensive new disclosures are required to explain how judgement is exercised as well as quantitative disclosures about financial assets.
- Extensive new disclosures are also required for those risk exposures to which an entity applies hedge accounting.

**Actions to consider**
- Assess current systems to identify data gaps that need to be filled to meet the new disclosure requirements.
A robust assessment phase is critical to laying the framework for a successful project, and it is important to start the assessment early to provide flexibility during the implementation phase.

<table>
<thead>
<tr>
<th>Activities</th>
<th>Actions</th>
<th>Deliverables</th>
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<tbody>
<tr>
<td>Accounting diagnostic</td>
<td>– Identify possible modifications to current impairment methodology and processes</td>
<td>– Gap matrix, heat map and contract review summaries</td>
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<td></td>
<td>– Identify new key controls or reconciliations to be performed</td>
<td>– Calculation of ECLs using KPMG’s Global Credit Loss Accounting Solution (gCLAS)</td>
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<tr>
<td>Process and information gap analysis</td>
<td>– Identify possible changes to hedging policies relevant for your organisation</td>
<td>– Business requirements document, process and information gap analysis report</td>
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<td>– Identify additional data requirements to meet new disclosure requirements</td>
<td>– Hedge documentation and effectiveness tests</td>
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<td>– Review internal management information arising from existing requirements and assess how these could be aligned with the new classification and measurement categories and ECL model</td>
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<tr>
<td>Broader impact evaluation</td>
<td>– Analyze future volatility</td>
<td>– Final gap matrix and heat map, implementation roadmap</td>
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<td>– Provide insight into emerging industry/peer practice issues</td>
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We have helped a number of clients to understand the impact of the new standard and how to implement the necessary changes. These projects have given us a detailed understanding of how companies will be affected and the steps that they can take now to help ease transition to IFRS 9. The following are just a few examples of how our cross-functional teams of experts have helped clients with the accounting and the operational challenges.

<table>
<thead>
<tr>
<th>Client</th>
<th>How we helped</th>
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<tr>
<td>A German automotive business</td>
<td>We helped our client with a detailed quantitative analysis of impairment models and assisted with the selection of an appropriate treasury management system.</td>
</tr>
<tr>
<td>A global shipping organization</td>
<td>We assessed the client’s treasury management systems and accounting and IT environment to identify any potential IFRS 9 implementation issues.</td>
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If you have any concerns about the impact of IFRS 9, or any other accounting issues, please speak to your usual KPMG contact or any of the following.

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