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Joint position paper on ED IFRS 9 Classification and Measurement

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Association of German Banks
Burgstraße 28
10178 Berlin | Germany
Telephone: +49 30 1663-0
Fax: +49 30 1663-1399
www.germanbanks.org
USt.-IdNr DE201591882

German Insurance Association
Wilhelmstraße 43/43 G
10117 Berlin | Germany
Telephone: +49 30 2020-5000
Fax: +49 30 2020-6000
www.gdv.de

The Association of German Banks[1] and the German Insurance Association[2] have discussed the ED IFRS 9 Classification and Measurement and agreed on the following common position. As a primary objective, banks and insurance companies as well as other industries should be able to reflect their business model under IFRS 9. Defining the measurement and presentation categories for debt assets based on business models in dependence of the frequency of sales as currently proposed in IFRS 9 might be a reasonable starting point, but would not reach this objective completely and might even create accounting mismatches in some cases.

Banks are generally able to reflect their business models for financial assets held to collect contractual cash flows measured at AC or for financial assets held for trading measured at FVPL. Insurance companies generally also hold assets to collect contractual cash flows, however might need to sell certain assets in order to match their long-term insurance liabilities. For the insurance industry a measurement of financial assets at FVOCI would permit to better align the measurement of financial assets with the measurement and presentation of insurance liabilities under IFRS 4. Also, other industries have raised concerns that the business model definitions in IFRS 9 are designed for financial institutions only, and do not meet their needs. All industries have in common that certain financial assets do not meet the cash flow characteristics (SPPI) test or that are held for trading which would be measured at FVPL.

In general, we believe, that the dividing line between AC measurement and FVOCI measurement in IFRS 9 is difficult to draw. In particular, there should be no arbitrary split between business models of entities in dependence of the frequency of sales of their financial assets as currently proposed in IFRS 9 between a business model "hold to collect cash flows" - with some sales possible and "hold and sell strategy" - with more frequent sales. This will potentially lead to major practical application problems for preparers, auditors and regulators.

We believe, that only the "trading" business model can be clearly defined in terms of a frequent selling strategy to be measured at FVPL.[3] The measurement and presentation categories AC and FVOCI should be compounded in a residual category in addition to the "trading" business model.

We propose that the residual category should be eligible for all financial assets that

- meet the cash flows characteristics test as "solely principal and interest" and
- are not held for trading or are not managed on a FVPL basis (FVO), as defined in IAS 39

We propose that for financial assets in the residual category an entity has an unconditional option to select at initial recognition the FVOCI category.

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[1] The Association of German Banks represents more than 210 private commercial banks and 11 member associations.

[2] The German Insurance Association represents the common view of 471 German insurers.

[3] This would include financial assets which are managed on a FVPL basis (FVO).

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We believe that this approach would have the following advantages:

1. It would permit to better reflect the business models of all industries and avoid accounting mismatches.
2. The complexity to define the arbitrary dividing line between the AC category and the FVOCI category would disappear.
3. The net income effect for both measurement categories would be the same.
4. The same impairment rules would apply for debt instruments measured at AC and those measured at FVOCI.
5. The cash flow characteristics test in addition to the definition of the trading business model would ensure that non-simple debt instruments and trading assets would be measured at FVPL.
6. There would be no "selling" constraints to irrevocably select AC or FVOCI at inception of a debt instrument in accordance with an entity's business model, whilst at the same time the information on an entity's performance in net income remain comparable.
7. Comparable and transparent information would be provided to users, because for financial assets measured at FVOCI fair value information would be provided in the balance sheet, whilst for financial assets measured at AC, an entity would have to provide fair value information in the notes. In the accounting policy statement an entity would have to clearly state why it selected AC or FVOCI at inception in accordance with its business model.

In addition, we propose to broaden the current restrictive cash flow characteristics test (SPPI test) in IFRS 9 for eligible debt instruments, as it would require a significant number of debt instruments to be measured at FVPL on a mandatory basis. This could lead to an accounting mismatch where corresponding liabilities are measured at either AC or FVOCI and thus would not reflect the economic substance of these investments under a business model which is not held for trading. In particular, we believe that debt assets which are only insignificantly different from simple debt instruments, i.e. financial assets which are priced similarly to simple debt instruments, should not be mandatorily classified as FVPL. For example, redemption rights which are contingent on future events other than credit deterioration should not trigger FVPL.

Association of German Banks	German Insurance Association
Dr. Michael Kemmer	Dr. Jörg Freiherr Frank von Fürstenwerth
General Manager	Chairman of the Executive Board
Member of the Board of Directors	