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HKICPA issues HKFRS 9 (2014) Financial Instruments

12 September 2014

As you may already be aware, in July 2014 the IASB finalised their project on financial instruments by issuing IFRS 9 *Financial Instruments*.

On 5 September, in accordance with the HKICPA's full convergence policy, the HKICPA adopted IFRS 9 by issuing HKFRS 9, with the same effective date and transitional provisions.

HKFRS 9 will replace HKAS 39 *Financial Instruments: Recognition and Measurement* and provide new guidance for accounting for financial instruments in three broad areas.

a) **Classification and measurement of financial assets and financial liabilities.** Under HKFRS 9, financial assets are classified on the basis of the business model within which they are held and their contractual cash flow characteristics. Embedded derivatives are no longer separated from financial asset hosts, instead, the entire hybrid instrument is assessed for classification and measurement. For the classification and measurement of financial liabilities, HKFRS 9 retains almost all of the existing requirements from HKAS 39. However, the gain or loss on a financial liability designated at fair value through profit or loss (FVTPL) that is attributable to changes in its credit risk is usually presented in other comprehensive income (OCI); the remaining amount of change in fair value is presented in profit or loss.

b) **Impairment methodology.** HKFRS 9 replaces the 'incurred loss' model in HKAS 39 with an 'expected credit loss' model, which means that a loss event will no longer need to occur before an impairment allowance is recognised. In fact, all assets within the scope of the impairment model will have at least 12 months expected loss provision. The standard aims to address concerns about 'too little, too late' provisioning for loan losses, and will accelerate recognition of losses.

c) **Hedge accounting.** HKFRS 9 aims to align hedge accounting with risk management activities, establish a more principal-based approach to hedge accounting, and address inconsistencies and weaknesses in the previous model.

In the Headlines 14-13 (English / Chinese)

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HKFRS9 standards

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Which entities will be most affected by HKFRS 9?

HKFRS 9 applies to all entities, however, we expect that financial institutions and other entities with large portfolios of financial instruments which are currently carried at amortised cost will be most affected.

When will HKFRS 9 be effective?

HKFRS 9 is effective for annual periods beginning on or after 1 January 2018. Earlier application is permitted.

If an entity applies HKFRS 9 (2014) early, it is required to apply all the requirements of the standard at the same time. There are three exceptions to this principle:

- Until the mandatory effective date of 1 January 2018, an entity is allowed to early adopt the own credit requirement introduced by HKFRS 9 (2010) in isolation, without applying the other requirements of HKFRS 9. If an entity chooses this option, then it discloses this fact and provides on an ongoing basis the disclosures for financial liabilities that are designated as measured at FVTPL.

- When an entity first applies the standard, it may choose to continue to apply the hedge accounting requirements of HKAS 39 rather than those of HKFRS 9.

- There are special requirements for sequential adoption from previous versions of HKFRS 9.

2018 may seem like a long way off, but this extended transition period has been granted for a reason: it allows time for an entity both to assess the potential impact of HKFRS 9 on their business and to implement any systems changes necessary to enable the entity to collect the necessary data.

We therefore advise entities to start assessing the potential impact of HKFRS 9 on their accounting policies and business practices sooner rather than later, so that the remaining time can be focused on addressing any problem areas or opportunities which emerge.

More information

More information on IFRS 9 can be found by following the links in the right hand bar to a range of publications issued by KPMG. These introduce the requirements of the standard and also focus on the transition options and implications that we believe entities need to start thinking about sooner rather than later. Copies of these publications can also be obtained from your usual KPMG contact.