

# **CHANGES TO IAS 39 AND IFRS 7 IN RESPONSE TO THE CRISIS**

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# BASIC STANDARDS FOR THE FINANCIAL INSTRUMENTS

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- ✘ International Accounting Standards 32 (IAS 32) *Financial instruments: presentation*
- ✘ International Accounting Standards 39 (IAS 39) *Financial instruments: recognition and measurement*
- ✘ International Financial Reporting Standard 7 (IFRS 7) *Financial Instruments: Disclosures* effective

# **DEFINITIONS OF FINANCIAL INSTRUMENT IAS 32 AND IAS 39**

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**Financial instrument is any contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity.**

# FINANCIAL INSTRUMENTS ARE:

- × cash,
- × demand and time deposits,
- × commercial paper,
- × accounts, notes, and loans receivable and payable,
- × debt and equity securities.,
- × asset backed securities such as collateralised mortgage obligations, repurchase agreements, and securitised packages of receivables,
- × derivatives, including options, rights, warrants, futures contracts, forward contracts, and swaps.

# IAS 39 – VALUATION AT THE BEGGINING

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**Initially, financial assets and liabilities should be measured at fair value** (art. 43)

**Fair value** -the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction (similar to market value)

# IAS 39 VALUATION DURING THE YEAR

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For valuation of financial assets are divided into four groups

**1. Financial assets - held for trading**

(at fair value through profit or loss);

**2. Available-for-sale financial assets**

(at fair value through profit or loss);

**3. Loans and receivables**

(are valued at amortised cost);

**4. Held-to-maturity investment**

(are measured at amortised cost). (art.45)

# IAS 39 VALUATION DURING THE YEAR

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For valuation of financial liabilities are divided into :

1. Financial liabilities at fair value through profit or loss
2. Other financial liabilities measured at amortised cost using the effective interest method.

# BEFORE CRISIS

Changes in value of instruments held for trading

- cost or revenue changes financial result

Changes in value of financial assets for sale

- cost or revenue changes financial result

Changes in value loans and receivables

- amortised cost changes revaluation capital

Changes in value held-to-maturity investment

- amortised cost changes revaluation capital

Changes other financial liabilities

- amortised cost changes revaluation capital

changes in the income statement

Changes in statement of changes in equity



# AMORTIZED COST

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Amortized cost is calculated using the effective interest method.

The **effective interest rate** is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument to the net carrying amount of the financial asset or liability.

# IN 2005 INTRODUCED CERTAIN RESTRICTIONS ON THE USE OF OPTIONS

In June 2005 the IASB issued its amendment to IAS 39 to restrict the use of the option to designate any financial asset or any financial liability to be measured at fair value through profit and loss (the fair value option).

# IFRS 7 - 2005

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On 18 September 2005, the Board of ISA published **International Financial Reporting Standards 7 (IFRS) *Financial Instruments – revealing information.***

The aim of IFRS 7 is to impose responsibility on business entities to reveal information in financial reports which allows the users of these statements to evaluate how financial instruments owned by entities affect its financial situation and the results of activity

# IFRS 7-2005

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**Business entities are required to reveal the character and range of risk resulting from ownership of financial instruments, to which a business entity is exposed during the reporting period, as well as the risk management method used by a particular business entity.**

# CHANGES ON 2008

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On 15 October 2008, the European Commission passed changes to standards IAS 39 and IFRS 7.

The changes, in exceptional situations, enable reclassification of specific financial instruments from the category “held for trading” and “financial assets available for sale” to category “financial instruments preserved to due date” or “loans and receivables”.

# THE CRISIS CAUSED

Groups of instruments for sale and held for trading

reclassification and changes of valuation

Groups of instruments due date, held -to maturity or loans and receivables

The financial result is not charged changes, differences in valuation are transferred to revaluation capital

profit and loss statement does not include the dramatic depreciation of financial instruments

# CHANGES

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Established on 1 July 2008 the market value of the instrument has been recognized as a new amortized cost.

The market value after 1 July 2008 could not be regarded as fair value because it was undermining the credibility of the market price.

Companies do not have to show in its financial statements arising from fluctuations in the value of liquidity in certain markets, or even suspension of listing. Dramatic drop in value of investments was no longer in the reports for the third quarter of 2008.

# SUMMING UP, PUT TWO SAFETY CHANGES

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1. Effects of changes in the value financial instruments could be presented in capital (not financial result). Financial instruments could not be sold in a short period and has five instances an exceptional event (such as the financial crisis);
2. All information on the causes and direction of changes - reclassification must be disclosed in the supplementary data.
3. Companies could use to valuation price before crisis.



# IN POLAND

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**On 18 December 2008, the Minister of Finance issued a regulation amending the Regulation on detailed rules for the recognition, valuation, disclosure and presentation of financial instruments**

Accounting Act gives powers in this regard, the Minister of Finance.

# **IN POLAND** (DZ. U. Z 2003 R. )

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**Financial assets held for trading and for sale can be reclassified to categories loans and receivables and held-to-maturity investment.**

**All information related to the reclassification must be disclosed.**

# **IN POLAND (REGULATIONS)**

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**The company can valuated financial instruments according prices befor the crisis - from 1 July 2008.**

**The regulation applies to the first financial statements prepared for the fiscal year beginning in 2008**

# **SUMMARY**

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**The international and national regulations set out ways to reduce the impact of the crisis. The financial results do not fall dramatically, and the readability of the reports could be maintained.**

# PROJECT OF STANDARDS

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In 2009 the International Accounting Standards Board (*IASB*) published the project of standard “Financial instruments – Recognition and Measurement”.

The project is the Board’s response to the worldwide financial crisis and it is consistent with the recommendations of the G-20 Group.

# PROJECT OF STANDARDS

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The draft standard introduces two approaches to stop the recognition of financial assets:

1. a model based on the concept of control and preferred by the majority of the Council,
2. alternative view model, supported by the other five members.

# CURRENT MODEL IN IAS 39

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The current IAS 39 model is mainly based on the concept of risk and reward, but provides an additional test based on the control when the risks and benefits are neither substantially transmitted nor preserved.

# **NEW MODEL IN PROJECT**

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**The concept of control is central to the model proposed and the risks and benefits are considered as an alternative test of continuing involvement in transferred assets. This is of the hope of reducing one of the elements to the current model is so complicated.**



# **PROJECT OF STANDARDS**

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**The draft standard proposes a significant extension of the quantitative and qualitative information requirements.**

**The purpose of disclosure is to enable users of financial statements understand the sensitivity of the results and financial position of the financial assets owned.**

# IT SHOULD BE NOTED THAT:

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- ✘ IASB reacts very quickly to crises;
- ✘ The changes are protective for entities and users of the reports - who have invested capital in the specified company;
- ✘ Polish law – Accounting act respect International Accounting Standards and IFRS;
- ✘ Changes in Accounting Standards are considered very fast EU countries - the issue regulations FM

# IT SHOULD BE NOTED THAT:

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Accounting changes indicate a slow shift away from market model - where the valuation is based on market value or fair value, **to the present value model**, in which balance sheet items are valued at amortized cost using the effective interest rate (taking into future inflows and outflows related with balance position) Income model is not so much dependent on the market, financial market.