# IFRS 7 Financial Instruments Disclosures

***Practical Workshop for NBU Staff and Bankers***


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# IFRS 7 Financial Instruments Disclosures

# Approach and introduction

- IFRS 7 requires clear and meaningful disclosures in specific areas.
- Users should be able to see the trail from notes to statement of financial position and vice-versa.
- Information should be sufficiently detailed ie too much aggregation not useful.
- Preparers should not confuse between classes and categories (4 in IAS 39).
- This session will focus mainly on credit risk disclosures.

# Credit Risk

- By class of financial instruments
  - The amount that best represent its maximum exposure to credit risk without taking into account collateral
  - Description of collateral held as security
  - Information about credit quality of financial assets that are neither past due nor impaired
  - For either past due or impaired financial assets:
  - An analysis of the age of financial assets that are past due as at the end of the reporting period but not impaired; and
  - An analysis of financial assets that are individually determined to be impaired as at the end of the reporting period , including the factors the entity considered in determining that they are impaired
  - If collateral meets the recognition criteria in other IFRSs, an entity shall disclose the nature and carrying amount of the assets

# IFRS 7 Disclosures: Credit Risk

- Credit risk:  the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation
- Past due: a financial asset is past due when a counterparty has failed to make a payment when contractually due

# IFRS 7 Disclosures: Credit Risk

- Disclosures required for credit risk (and also market and liquidity risk) should be given in the financial statements or incorporated by cross-reference from the financial statements to management commentary or risk report available to users of the financial statements
- Without the information incorporated by cross-reference, the financial statements are incomplete
- When management uses several methods to manage risks, the entity shall disclose information using the method or methods that provide the most relevant and reliable information

# ANZ annual report 2015 Excerpt, p. 66

**ii) Use of estimates and assumptions**

The preparation of these financial statements requires the use of management judgement, estimates and assumptions that affect reported amounts and the application of accounting policies. Discussion of the critical accounting treatments, which include complex or subjective decisions or assessments, are covered in note 2. Such estimates, judgements and assumptions are reviewed on an ongoing basis.

**iii) Basis of measurement**

The financial information has been prepared in accordance with the historical cost basis except that the following assets and liabilities are stated at their fair value:

- derivative financial instruments;
- available-for-sale financial assets;
- financial instruments held for trading; and
- assets and liabilities designated as fair value through profit or loss.

In accordance with AASB 1038 Life Insurance Contracts (‘AASB 1038’), life insurance liabilities are measured using the Margin on Services model.

In accordance with AASB 119 Employee Benefits (‘AASB 119’), defined benefit obligations are measured using the Projected Unit Credit Method.

# ANZ annual report 2015 Excerpt, p. 70

**iv) Net loans and advances**

Net loans and advances are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They arise when the Group provides money to a debtor with no intention of trading the loans and advances. Loans and advances are initially recognised at fair value plus transaction costs that are directly attributable to the issue of the loan or advance. They are subsequently measured at amortised cost using the effective interest rate method (refer note 1(B)(i)) unless specifically designated on initial recognition as fair value through profit or loss.

All loans are graded according to the level of credit risk.

Net loans and advances includes direct finance provided to customers such as bank overdrafts, credit cards, term loans, finance lease receivables and commercial bills.

**Impairment of loans and advances**

Loans and advances are reviewed at least at each reporting date for impairment. Credit impairment provisions are raised for exposures that are known to be impaired. Exposures are impaired and impairment losses are recorded if, and only if, there is objective evidence of impairment as a result of one or more loss events that occurred after the initial recognition of the loan and prior to the reporting date, and that loss event, or events, has had an impact on the estimated future cash flows of the individual loan or the collective portfolio of loans that can be reliably estimated.

Impairment is assessed for assets that are individually significant (or on a portfolio basis for small value assets) and then on a collective basis for those exposures not individually known to be impaired.

# ANZ annual report 2015 Excerpt, p. 70

Exposures that are assessed collectively are placed in pools of similar assets with similar risk characteristics. The required provision is estimated on the basis of historical loss experience for assets with credit risk characteristics similar to those in the collective pool.

The historical loss experience is adjusted based on current observable data such as changed economic conditions. The provision also takes account of the impact of inherent risk of large concentrated losses within the portfolio and an assessment of the economic cycle.

The estimated impairment losses are measured as the difference between the asset’s carrying amount and the estimated future cash flows discounted to their present value.

As the discount unwinds during the period between recognition of impairment and recovery of the cash flow, it is recognised in interest income.

Impairment of capitalised acquisition-related expenses is assessed through comparing the actual behaviour of the portfolio against initial expected life assumptions.

# ANZ annual report 2015 Excerpt, p. 70

The provision for impairment loss (individual and collective) is deducted from loans and advances in the balance sheet and the movement for the reporting period is reflected in the income statement.

When a loan is uncollectable, either partially or in full, it is written-off against the related provision for loan impairment. Unsecured facilities are normally written-off when they become 180 days past due or earlier in the event of the customer’s bankruptcy or similar legal release from the obligation. In the case of secured facilities, remaining balances are written-off after proceeds from the realisation of collateral have been received if there is a shortfall.

Impairment losses recognised in previous periods are reversed in the income statement if the estimate of the loss subsequently decreases.

A provision is also raised for off-balance sheet items such as loan commitments that are considered to be onerous.

# ANZ annual report 2015 Excerpt, p. 105

**Concentrations of credit risk**

Concentrations of credit risk arise when a number of customers are engaged in similar business activities or activities within the same geographic region, or when they have similar risk characteristics that would cause their ability to meet contractual obligations to be similarly affected by changes in economic or other conditions.

The Group monitors its portfolios, to identify and assess risk concentrations. The Group's strategy is to maintain well-diversified credit portfolios focused on achieving an acceptable risk-return balance. Credit risk portfolios are actively monitored and frequently reviewed to identify, assess and guard against unacceptable risk concentrations. Concentration analysis will typically include geography, industry, credit product and risk grade. The Group also applies single customer counterparty limits to protect against unacceptably large exposures to single name risk. These limits are established based on a combination of factors including the nature of counterparty, probability of default and collateral provided.

# ANZ annual report 2015 Excerpt, p. 105

## Concentrations of credit risk analysis

Composition of financial instruments that give rise to credit risk by industry:

| Consolidated | Cash, settlement balances owed to ANZ and collateral paid 2015 $m | Cash, settlement balances owed to ANZ and collateral paid 2014 $m | Trading securities and AFS[1] 2015 $m | Trading securities and AFS[1] 2014 $m | Derivatives 2015 $m | Derivatives 2014 $m | Loans and advances[2] 2015 $m | Loans and advances[2] 2014 $m | Other financial assets[3] 2015 $m | Other financial assets[3] 2014 $m | Credit related commitments[4] 2015 $m | Credit related commitments[4] 2014 $m | Total 2015 $m | Total 2014 $m |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Australia** | | | | | | | | | | | | | | |
| Agriculture, forestry, fishing and mining | – | 21 | 60 | 21 | 691 | 225 | 15,192 | 13,970 | 119 | 95 | 9,713 | 10,753 | 25,775 | 25,085 |
| Business services | 4 | 12 | – | 3 | 108 | 46 | 6,254 | 5,658 | 49 | 38 | 3,365 | 3,679 | 9,780 | 9,436 |
| Construction | – | – | 23 | 3 | 20 | 94 | 5,516 | 5,688 | 43 | 38 | 4,568 | 4,353 | 10,170 | 10,176 |
| Electricity, gas and water supply | – | – | 99 | 237 | 837 | 692 | 3,462 | 4,000 | 27 | 27 | 2,388 | 2,895 | 6,813 | 7,851 |
| Entertainment, leisure and tourism | – | – | 37 | 1 | 323 | 89 | 8,908 | 8,087 | 70 | 55 | 2,494 | 2,751 | 11,832 | 10,983 |
| Financial, investment and insurance | 21,885 | 18,927 | 18,722 | 19,115 | 49,733 | 38,387 | 22,061 | 14,351 | 174 | 98 | 6,757 | 7,521 | 119,332 | 98,399 |
| Government and official institutions | 130 | 135 | 32,305 | 25,595 | 685 | 241 | 707 | 541 | 6 | 4 | 2,081 | 298 | 35,914 | 26,814 |
| Manufacturing | 4 | 4 | 1,382 | 1,528 | 2,535 | 1,057 | 6,844 | 7,129 | 54 | 48 | 7,815 | 7,537 | 18,634 | 17,303 |
| Personal lending | – | – | – | – | – | – | 252,242 | 231,807 | 1,983 | 1,569 | 48,282 | 44,950 | 302,507 | 278,326 |
| Property services | – | – | 79 | 48 | 677 | 433 | 27,034 | 26,234 | 212 | 178 | 10,199 | 11,774 | 38,201 | 38,667 |
| Retail trade | 2 | 2 | 50 | 6 | 221 | 153 | 11,273 | 10,225 | 89 | 69 | 3,639 | 4,645 | 15,274 | 15,100 |
| Transport and storage | 2 | – | 181 | 70 | 951 | 368 | 7,052 | 7,386 | 55 | 50 | 4,145 | 3,943 | 12,386 | 11,817 |
| Wholesale trade | 354 | 183 | 12 | 7 | 1,520 | 702 | 6,287 | 6,320 | 49 | 42 | 8,212 | 4,867 | 16,434 | 12,121 |
| Other | 30 | 21 | 251 | 208 | 453 | 258 | 10,397 | 9,426 | 82 | 64 | 5,878 | 5,501 | 17,091 | 15,478 |
| | 22,411 | 19,305 | 53,201 | 46,842 | 58,754 | 42,745 | 383,229 | 350,822 | 3,012 | 2,375 | 119,536 | 115,467 | 640,143 | 577,556 |

**1** Available–for–sale assets.
**2** Excludes individual and collective provisions for credit impairment held in respect of credit related commitments, and includes Esanda dealer finance assets classified as held for sale.
**3** Mainly comprises regulatory deposits, investments backing policy liabilities and accrued interest.
**4** Credit related commitments comprise undrawn facilities and customer contingent liabilities.

# Conclusion

- Banks should pay particular attention to credit risk disclosures.
- It is important to provide meaningful information and not just data in tables.
- A clear information trail from notes to primary statements is crucial to help the reader of financial statements.