Review of accounting standards for Chilean Banks: last developments

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Conferencia Regional sobre Banca, Contabilidad Finanzas
CEMLA / Banco Central de Chile
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· Background
· Principal aspects of IFRS 9
· New version of the accounting standards for Chilean banks
· Challenges derived from the implementation
Background
Countries where the IFRS standards are required for use by all or most domestic publicly accountable entities, including listed companies and financial institutions.
The Superintendency of Banks and Financial Institutions (SBFI) decided to implement the IFRS standards in phases gradually:

**Phase 1 (2002):** Decision to adopt IFRS
- Internal Roadmap
- Classification of financial assets
- Hedge accounting
- Full adoption of financial reports (SFP and P&L)
- Adoption of IFRS
- Except carve-out by SBIF (provisions B1)
- Achieving comparability
- Work in progress
- Under public consultation period

**Phase 2 (2006):** Adoption of IAS39

**Phase 3 (2008):** New forms for the financial statements

**Phase 4 (2009):** First implementation of IFRS

**Phase 5 (2010):** Interim financial reporting under IFRS

**Phase 6 (2019):** Issue of reviewed/updated accounting standards manual

**SBIF Accounting Manual (IFRS) 2007**

**National Accounting Standards Board (IFRS) 2013**

**SBFI National background**
National background

- **Accounting Standards IFRS-based:** accounting manual for banks was first issued at the end of 2007

- **SBIF establishes IFRS exceptions:** SBIF decided on carve-outs due to exceptions and/or limitations to the IFRS standards

- **Permanent review of standards:** A periodic monitoring is being realized of the changes in the IFRS standards and the development of IASB’s work plan projects

- **Last development in Banks:** several new IFRS (9,15,16) have been issued lately together with changes in existing IFRS (7), many relevant to the banking sector
Principal aspects of IFRS 9
Principal aspects of IFRS 9

IFRS 9 (financial instruments) replaced IAS 39 and contains the following themes:

- Classification and measurement of financial asset
- Hedge accounting
- Impairment of financial assets
The classification of financial assets should be made on the basis of both:

a. **The entity’s business model** for managing the financial assets

b. **The contractual cash flow characteristics** of the financial assets
### Principal aspects of IFRS 9

**Importance of financial assets and liabilities**

<table>
<thead>
<tr>
<th>Measurement Basis</th>
<th>Accounting Concept</th>
<th>Relevance Total Assets (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Current Accounting Standards Manual for Banks</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Loans and receivables</strong></td>
<td>Loans and receivables, Commercial loans, Mortgage loans, Consumer loans, Loans to banks, Repurchase agreements</td>
<td>71,72</td>
</tr>
<tr>
<td><strong>Held to maturity</strong></td>
<td>Held to maturity, Non-Derivative Fin.Instr.</td>
<td>0,11</td>
</tr>
<tr>
<td><strong>Available for sale</strong></td>
<td>Available for sale, Non-Derivative Fin.Instr.</td>
<td>8,64</td>
</tr>
<tr>
<td><strong>Held for trading</strong></td>
<td>Held for trading, Derivative Fin.Instr., Non-Derivative Fin.Instr.</td>
<td>7,68</td>
</tr>
<tr>
<td><strong>“Other Financial assets”</strong></td>
<td>&quot;Other Financial assets&quot;, Cash on hand and on demand Derivatives for Hedging</td>
<td>6,87</td>
</tr>
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<td><strong>Other Non-Financial Assets</strong></td>
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<td>4,98</td>
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<td><strong>TOTAL ASSETS</strong></td>
<td></td>
<td>100</td>
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<tr>
<td><strong>New Accounting Standards Manual for Banks</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Amortized cost</strong></td>
<td>Amortized cost, Commercial loans, Mortgage loans, Consumer loans, Loans to banks, Repurchase agreements, Non-Derivative Fin.Instr.</td>
<td>71,83</td>
</tr>
<tr>
<td><strong>Fair Value Other Comprehensive Income (FVOCI)</strong></td>
<td>FVOCI, Non-Derivative Fin.Instr.</td>
<td>8,64</td>
</tr>
<tr>
<td><strong>Fair Value through Profit or Loss (FVTPL)</strong></td>
<td>FVTPL, Held for trading, Derivative Fin.Instr., Non-Derivative Fin.Instr., Mandatorily: Non-Derivative Fin.Instr.</td>
<td>7,68</td>
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Principal aspects of IFRS 9

Hedge accounting

In November 2013 were issued the new hedge accounting requirements within IFRS 9.

Those new requirements are better aligned with the entity’s risk management activities.

The qualifying criteria for hedge accounting and hedge effectiveness requirements are based more upon principles, thereby eliminating for example the quantitative range of 80%-125% for effectiveness in IAS 39.

In summary, more flexibility with a principles based approach, but balanced with more disclosures about risk management activities.
Principal aspects of IFRS 9

Impairment

IAS 39 → Incurred loss model based on objective evidence of impairment (SBIF carve-out)

IFRS 9 → Expected credit loss model (SBIF carve-out)

Except for loans
Principal aspects of IFRS 9

Impairment

1) Performing financial assets

2) Financial assets with significant increase in credit risk (under-performing)

3) Credit-impaired financial assets (non-performing loans)

For the first two phases interest is accrued on the gross carrying amount of the financial asset, meanwhile in phase 3 the interest is accrued on the amortized cost of the financial asset.

12-month expected credit losses

Lifetime expected credit losses
New version of the accounting standards for Chilean banks
Project for review and update of the accounting standards manual for banks

Information Requirements

· Change in the presentation forms established for the statement of financial position and statement of profit and loss

· New presentation forms established for:
  ~Statement of other comprehensive income.
  ~Statement of changes in equity

· Changes in monthly information requirements established in the accounting plan due to new forms of the different statements (coding and description of accounts)
Project for review and update of the accounting standards manual for banks

Information Requirements

- Modification of content required for certain notes to the financial statements due to IFRS 7

- Incorporation of new items in the accounting plan to disclose an opening of “other” items
Project for review and update of the accounting standards manual for banks

Exceptions

Limitations and/or exceptions to the IFRS contained in the accounting standards manual (special features of the Chilean model with carve-outs):

- Impairment of loans
- Criteria for stop accruing interest on impaired loans
- Criteria for writing-off loans based on number of days past due
- Write-off of assets received or adjudicated in lieu of payment of loans
- Measurement of tangible and intangible assets
Effects of the modifications

- New version of the accounting standards manual for banks with first application as from 1 January 2020 (proposal)

- Principal effects expected with regards to:
  - New classification of financial instruments to the measurement categories of IFRS 9 ➔ Marginal effects
  - Hedge accounting ➔ Marginal effects
  - Impairment ➔ Without effects to loans due to carve-out of this materia from IFRS 9
  - Change in criteria for accruing interest on impaired loans subject to group evaluation ➔ Initial application of change in criteria registered to equity
Effects of the modifications

· Other effects expected:
  ~ **Tecnological**: Changes needed to IT systems (in banks / SBFI / Central Bank of Chile)
  ~ **Cultural**: Changes in the financial and accounting language
  ~ **Change in the supervisory model of SBFI**: More detailed and explained information, improves the supervisory performance
  ~ **More and better public information available to stakeholders**: Improved decision making by depositors, investors and general public
Challenges derived from implementation
Some Challenges

- Finishing the consultation process and Issuing of the new version of the accounting standards manual for Banks
- Assessing the financial impacts in Banks derived from the implementation of the new version of the accounting standards manual
- Achieving a coherent model of provisioning and Basel III capital requirements
- Reviewing and updating the accounting standard manuals for the other credit industries

More and better information about risk management activities. Accounting information will create more value added to stakeholders.
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