IFRS for Banks in Canada

January 10, 2011

ASSOCIATION DES BANQUIERS CANADIENS
CANADIAN BANKERS ASSOCIATION

A Note about Forward-Looking Statements

The following presentation discusses accounting changes that are expected to be significant to a majority of the Banks in Canada upon adoption of International Financial Reporting Standards (IFRS). The presentation contains a number of forward-looking statements discussing the adoption of IFRS by the Banks in Canada including statements relating to IFRS implementation dates, the financial reporting impacts of the adoption of IFRS, accounting changes on transition from Canadian generally accepted accounting principles (GAAP) to IFRS and accounting changes that may impact banks following the initial 2012 transition from Canadian GAAP to IFRS. The forward-looking information contained in this presentation is presented for the purpose of educating analysts and investors about the potential accounting and financial reporting impacts of the adoption of IFRS on the Canadian banking industry generally and may not be appropriate for other purposes. In particular, the presentation does not include a discussion of every accounting change that may impact Banks in Canada on or following the transition from Canadian GAAP to IFRS.

In addition, the presentation contains a number of historical and hypothetical examples relating to the impact of the adoption of IFRS. These examples are provided for illustrative purposes only and are not indicative of the expected impact of the adoption of IFRS on any specific Canadian bank.

Our expectations regarding the key impacts of our transition to IFRS are based on IFRS as issued by the International Accounting Standards Board (IASB) that are in effect as of this date. Should IFRS change prior to our transition to IFRS, our expectations of the key impacts of transition could change.

We caution readers not to place undue reliance on these forward-looking statements or illustrative examples as a number of factors could cause the impact of the adoption of IFRS to differ materially from bank to bank. Please refer to the caution regarding forward-looking statements provided by each of the banks during Q4/10 reporting for more detailed information.

We do not undertake to update any forward-looking statement that is contained in this presentation or in other communications except as required by law.

For further information relating to the impact of the adoption of IFRS on an individual bank, please consult that bank's public filings on SEDAR at www.sedar.com.

IFRS in Canada: An Overview

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Why IFRS?

- What’s in it for Canada?

The short answer

- Financial reporting is intended to serve the needs of the capital markets.
- The capital markets are global and investors are international. They want a common language.
- Canada’s capital market is too small to expect investors to learn special Canadian accounting rules to understand Canadian financial statements.
- Only two possible alternatives – US GAAP or IFRS.

We chose IFRS because…

- Similar philosophy of serving investor needs.
- Similar style and level of detail as Canadian standards.
- Experience in harmonizing with US GAAP.
- Developments after TFOSS report:
  - IASB up and running
  - European adoption
  - Norwalk agreement

How does our transition compare?

- Our consultation began 2004. Plan finalized 2006 with transition slated for 1/1/2011. Date confirmed February 2008.
- In Europe, IAS Regulation passed mid-2002 without widespread debate. Implementation 1/1/05.
- Similar timeline in Australia.
- Major standards to be applied for European transition not complete until March/June 2004.
- Many countries were applying standards on financial instruments, pensions, foreign currency translation, income taxes for the first time.

Result?

- Adoption went remarkably smoothly considering short timeframes and potential for confusion:
  - Many studies have shown no significant effect on overall capital markets
  - Share price effects generally company-specific as a result of enhanced disclosure.
- Took a couple of years to bed down. Improvements in comparability tended to be driven by market pressures.
- National flavours to IFRS:
  - People chose national GAAP where possible to minimize change
- Environmental differences:
  - They had more time to report (6 month interims)
  - Securities regulators without much enforcement power
  - No certification

The future

- Convergence with US GAAP:
  - US adoption not key to Board decision
  - Removal of SEC reconciliation requirement for Foreign Private Issuers following IFRS key step
  - All major projects are joint but getting Boards to agree sometimes a challenge
  - SEC reviewing the role of IFRS in the US, decision expected by the end of 2011
- We have adopted IFRS:
  - Board will not ‘adapt’, carve out or interpret
  - Actively participate in IASB process and facilitate communication with Canadian constituents

IFRS for banks in Canada

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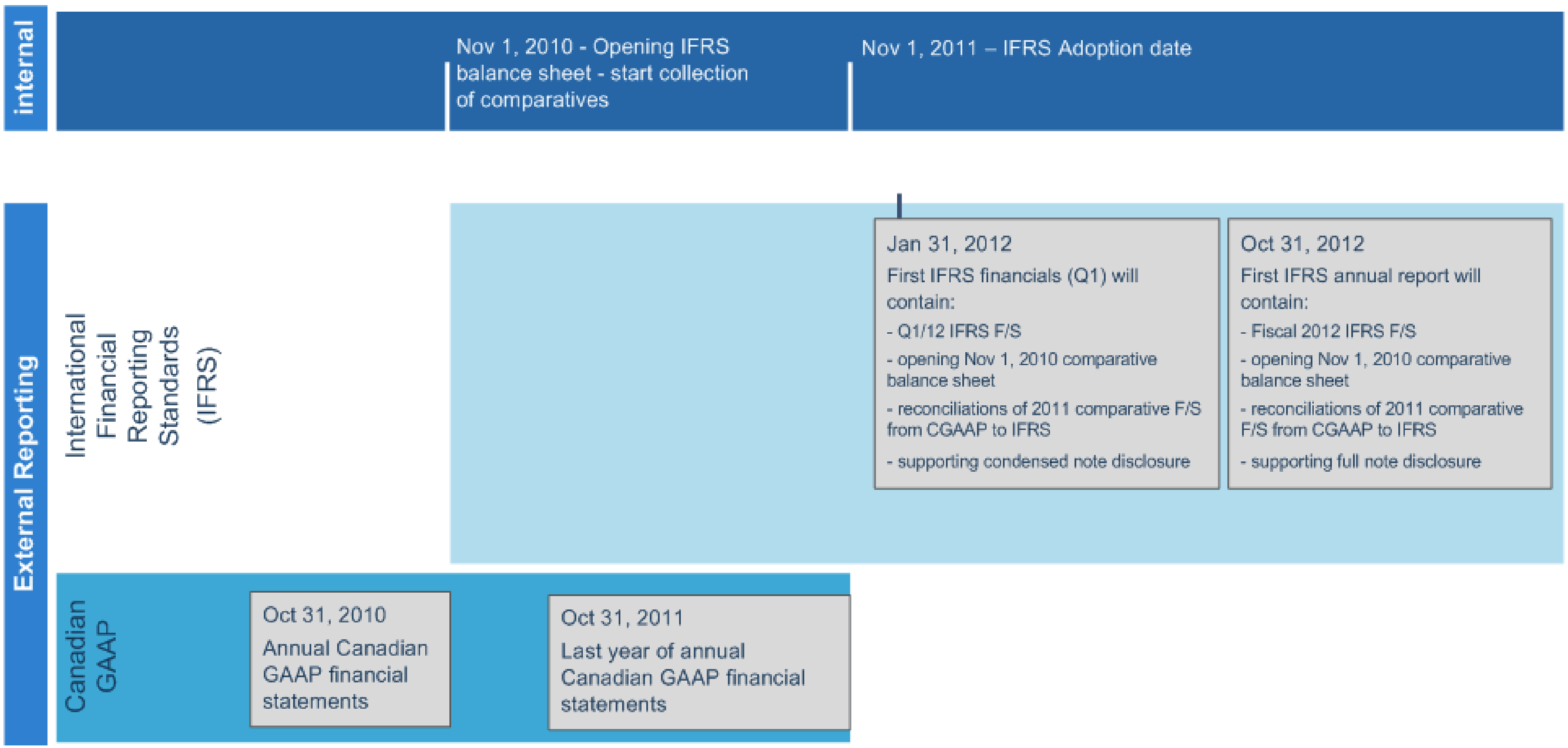
Discussion topics

- Key Dates and Milestones
- Financial Reporting Impacts
- OSFI Transitional Relief
- Future Changes to IFRS
- Key Takeaways

Key Dates and Milestones

When will we see the impacts of IFRS

- Based on October 31 year end



European bank illustrative example – reconciliation of profit

- Excerpt from HSBC Holdings plc Annual Report and Accounts 2005

Reconciliation or previously reported profit attributable to shareholders under UK GAAP to profit attributable to shareholders under IFRS for the year ended 31 December 2004.

	Year ended 31 December 2004 US$m
Profit before tax under UK GAAP	17,608
Goodwill amortisation	1,818
	19,426
Other goodwill adjustments	(102)
Retirement benefits	(170)
Leases	(90)
Share-based payments	(152)
Software capitalisation	25
Property	106
Tax on associates	(48)
Other	(52)
Profit before tax under IFRSs	18,943
Tax – UK GAAP	(4,507)
Tax – IFRSs adjustments	(178)
Minority interests – UK GAAP	(1,261)
Minority interests – IFRSs adjustments	(79)
Profit attributable to shareholders under IFRSs	12,918

Note: All items may not necessarily impact banks in Canada.

Financial Reporting Impacts

Accounting areas expected to be impacted most by the transition to IFRS

- Major accounting changes:
  - Securitization
  - Consolidation of off-balance sheet vehicles
  - Pension accounting
  - Acquisition accounting (including goodwill)
  - Transition and opening balance sheet

- Other areas of interest:
  - Other financial instrument topics

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Each accounting area may have a one-time transition and/or an ongoing impact

- Each topic will be assessed using the following criteria:

	Accounting Option	Balance sheet impact	Income statement impact		Tier 1	Asset-to-Capital Multiple (ACM)
		Book value per share	Earnings	Efficiency ratio		
One-time transition impact						
Ongoing impact						

X not applicable or no impact

✔ may impact (up or down)

- Book value per share = (total shareholder equity - preferred equity) / # of shares
- Earnings = pre-tax income
- Efficiency ratio = non-interest expenses / revenue (incl net and non interest income)

Accounting areas may impact balance sheet line items in varying degrees & magnitude

	Securitizations	Consolidation	Pensions	Acquisition accounting
Assets				
Cash				
Investments	✔	✔		
Loans	✔	✔		
Employee related assets			✔	
Derivatives				
Property, plant and equipment				
Goodwill				✔
Liabilities and equity				
Deposits				
Funding	✔			
Derivatives				
Employee related liabilities			✔	
Non-controlling interests		✔		✔
Share capital				

- Transitioning to IFRS may result in impacts of varying degree and magnitude to various line items on the financial statements
- Retained earnings will be impacted by transition adjustments

Securitizations - balance sheet leverage may increase

- Impacts
  - Certain securitized assets are expected to no longer receive off balance sheet treatment, examples include Canada Mortgage and Housing Corporation (CMHC) mortgage programs
  - Increase to assets and liabilities
  - Corresponding impact on Asset-to-Capital Multiple (ACM)
  - Previously recognized gains reversed through equity on transition including mark-to-market on seller's swap
  - Net interest and fees on securitized loans would then be recognized over the remaining term of the underlying loans

Securitizations may have both one-time transition and ongoing impacts

- Impacts – cont'd

	Accounting Option	Balance sheet impact	Income statement impact		Tier 1	Asset-to-Capital Multiple (ACM)
		Book value per share	Earnings	Efficiency ratio		
One-time transition impact	✔	✔	✔	✔	✔	✔
Ongoing impact	X	✔	✔	✔		

X not applicable or no impact

✔ may impact (up or down)

- Transitional relief provided by OSFI – Mortgages sold through CMHC Programs prior to March 31, 2010 are excluded from the calculation of the ACM
- Tier 1 impact for CMHC Programs can be phased-in over five quarters

Illustrative example - securitization

	Canadian GAAP	IFRS
Assets - Cash - Mortgage - Retained interest	 $102 - $3	 $102 $100 -
Liabilities	-	$102
Equity – one time	-	$(5)
Income Statement - one time - ongoing	 $5 -	 - $1

- Bank ABC securitizes $100 of 5 year mortgages
- Under Canadian GAAP, a gain of $2 is recognized on the sale and Bank ABC retains a $3 interest
- The Bank earns $1 per year of net interest margin
- Interests payments received are recognized over the life of the mortgage

Expected change to IFRS may provide some relief

- Ongoing Differences
  - Focuses on the substance of the transfer of risks and rewards to remove assets from the balance sheet, rather than the legal form as under Canadian GAAP

- Transition
  - Banks with October year ends will have a choice to apply IFRS securitization rules only from November 1, 2010 or from an earlier date
  - Choosing a date prior to transition would require securitization gains realized prior to transition to be reversed out of retained earnings increasing net interest margin under IFRS over the remaining term of securitized mortgages

Consolidation of previous off-balance sheet vehicles have one-time and ongoing impacts

- Impacts
  - More entities may be consolidated due to the different assessment of current off-balance sheet vehicles, thereby increasing assets and liabilities

	Accounting Option	Balance sheet impact	Income statement impact		Tier 1	Asset-to-Capital Multiple (ACM)
		Book value per share	Earnings	Efficiency ratio		
One-time transition impact	X	✔	✔	✔	✔	✔
Ongoing impact	X	✔	✔	✔		

X not applicable or no impact

✔ may impact (up or down)

- Ongoing Differences
  - Some entities that are off-balance sheet under Canadian GAAP may be consolidated under IFRS, although the inverse is also possible
  - The impact will vary depending on the type of entity that is consolidated

Illustrative example – consolidation of off-balance sheet vehicles

	Canadian GAAP	IFRS
Assets	$100	$1,000
Liabilities	-	$900
Equity - Non-controlling interest* - Retained earnings	 - -	 $60 $40
Income Statement	$4	$10

- Bank ABC has a $100 investment in an off balance sheet vehicle earning $4
- The vehicle has assets of $1,000, liabilities of $900 and earns $10
- Under IFRS, this vehicle is consolidated
- The impact will vary depending on the type of entity that is consolidated
- Under IFRS, the income statement includes 100% of the profit of the vehicle and disclosure is included below total profit on the income statement for profit attributable to the owners of the parent and to non-controlling interest

* Non-controlling interest is the equity in the vehicle not attributable, directly or indirectly, to the bank.

IFRS provides an opportunity to “start fresh” with pension accounting

- Impacts
  - Unrecognized market-related and other actuarial amounts may be recorded directly as a reduction in retained earnings at transition, depending on the choice made by the bank
  - If this choice is made, post-transition pension expense will be lower due to the reduced amortization of losses going forward as the losses would have been charged to retained earnings at transition
  - Ongoing impacts also dependent on policy option chosen to account for market-related and other actuarial amounts that arise post-transition

Pension accounting choices are available which may have impacts at transition and ongoing

- Impacts – cont'd
  - Assumption is that the transition choice is taken:

	Accounting Option	Balance sheet impact	Income statement impact		Tier 1	Asset-to-Capital Multiple (ACM)
		Book value per share	Earnings	Efficiency ratio		
One-time transition impact	✔	✔	✔	✔	✔	✔
Ongoing impact	✔	*	*	*		

X not applicable or no impact

✔ may impact (up or down)

* Policy choice on whether market-related and other actuarial movements that arise after November 1, 2010 may be:

- deferred and amortized to pension expense (current practice);
- recorded directly in equity; or
- recorded directly to the P&L.

Illustrative example – pension accounting

	Canadian GAAP	IFRS
Assets	$9,900	-
Liabilities	-	$100
Equity – at transition	-	$(10,000)
Income Statement – ongoing expense*	$400	-

- Bank ABC has a defined benefit plan with a plan deficit of $100 (plan obligations exceed plan assets by $100) and cumulative unrecognized losses of $10,000
- The average remaining working lives of the plan members is 10 years
- Under Canadian GAAP, the bank recognizes the amount outside the defined range ($6,000) over the average remaining working lives (i.e.$10,000-$6,000)/10 years =$400) to pension expense
- Under IFRS, Bank ABC makes the accounting policy choice to recognize at the date of transition the net market-related losses and any other actuarial movements in equity (fresh start)

*reduction in pension expense under IFRS equal to the amortization of unrecognized losses

Pension plans will have options that may change the accounting under IFRS

- Ongoing Changes
  - Banks in Canada commonly amortize movements outside the defined range into pension expense
  - Under Canadian GAAP, the equity approach is not permitted
  - There may be differences in the measurement basis between Canadian GAAP and IFRS (e.g. the way you measure the assets will be different)
  - The pension plan measurement date must coincide with year end (i.e. October 31st) under IFRS
- Transition
  - Option to recognize cumulative unrecognized losses as a reduction in retained earnings or elect to restate as if always following IFRS
  - Option provides fresh start on impact of pensions on income statement and equity
  - Accounting is operationally onerous, if restatement is chosen

Purchase prices are computed differently under IFRS

- Impacts
  - Purchase price is computed differently, for example, in cases where part of the purchase price is dependent on future outcomes (inclusion of contingent consideration) or where there is a share offer (acquisition vs announcement date)
  - Goodwill may have more frequent impairments depending on whether an entity concludes that it must test for impairment at a lower level
  - The below assessment assumes an election is taken to not restate acquisitions prior to transition and no acquisitions have been made in the comparative year

	Accounting Option	Balance sheet impact	Income statement impact		Tier 1	Asset-to-Capital Multiple (ACM)
		Book value per share	Earnings	Efficiency ratio		
One-time transition impact	✔	✔	X	X	X	X
Ongoing impact	✔	✔	✔	✔		

X not applicable or no impact

✔ may impact (up or down)

Contingent consideration and deal costs are accounted for differently

- Ongoing differences
  - Deal costs are expensed under IFRS
  - The part of the purchase price that is dependent on future outcomes must be recorded at acquisition date fair value with subsequent changes in fair value recorded in the income statement
  - In a share offer (under IFRS) the share price at the date of acquisition is used to value the share, while under Canadian GAAP the share price at date of announcement is used
  - Goodwill testing under IFRS can be assessed at a more granular level (i.e. groups of cash generating units versus reporting units) although in some cases the two will be the same
  - In a step acquisition when an entity gains control, under IFRS, the entity fair values the previous interest and recognizes a gain/loss in the income statement

Acquisition accounting can be onerous if applied retrospectively under IFRS

- Transition
  - Banks can choose to account for business combinations on an IFRS basis from November 1, 2010 onwards or elect a date prior to that and restate business combinations prospectively from that date
  - IFRS goodwill impairment testing will be performed at November 1, 2010, any impairment will be recorded in retained earnings

IFRS provides relief from retrospectively applying each standard

- IFRS 1 – First-time Adoption of IFRS
  - Overarching principle is that IFRS should be applied as if it had always been in effect (“retrospectively”) resulting in catch up adjustments in retained earnings
  - Due to the difficulties in applying IFRS retrospectively in certain cases, the IASB provides some exceptions to this general rule
  - First IFRS financial statements will contain the following:
    - Opening balance sheet;
    - Current and comparative periods under IFRS;
    - Reconciliation of total comprehensive income and shareholders’ equity under Canadian GAAP to IFRS; and
    - Financial statement footnotes disclosing the accounting policies under IFRS.

Cumulative foreign exchange difference may "start fresh" at transition

- IFRS transition exemptions impacting opening retained earnings (November 1, 2010) include:
  - Foreign Exchange
    - Banks can choose to transfer the cumulative foreign exchange differences on foreign operations (including hedging impacts) from other comprehensive income to retained earnings on November 1, 2010
    - This is a reclassification of shareholders' equity and therefore would not impact tier one capital
    - Future disposition of foreign operations would exclude the cumulative amount reclassified to retained earnings

European illustrative example – opening IFRS balance sheet

- Excerpt from 2005 Royal Bank of Scotland Annual Report and Accounts

Analysis of IFRS adjustments, excluding IAS 32, IAS 39 and IFRS 4.

	UK GAAP £m	Dividends £m	Income Tax £m	Leases £m	Consolidation £m	Software Development £m	Investment Property £m	Share Based Payment £m	Employee Benefits £m	Insurance £m	Total Adjustments £m	IFRS £m
Assets												
Cash and balances at central banks	3,822	-	-	-	-	-	-	-	-	-	-	3,822
Treasury bills and other eligible bills	4,846	-	-	-	-	-	-	-	-	-	-	4,846
Loans and advances to banks	54,392	-	-	-	(2)	-	-	-	-	1,013	1,011	55,403
Loans and advances to customers	252,531	-	-	(147)	1,798	-	(448)	-	-	(541)	662	253,193
Debt securities	79,949	-	-	-	123	-	-	-	-	1,076	1,199	81,148
Equity shares	2,300	-	-	-	-	-	-	-	-	1,745	1,745	4,045
Intangible assets	13,131	-	-	-	-	896	-	-	-	-	896	14,027
Property, plant and equipment	13,927	-	-	(127)	76	(78)	448	-	-	1	320	14,247
Settlement balances	2,857	-	-	-	-	-	-	-	-	-	-	2,857
Derivatives at fair value	14,087	-	-	-	-	-	-	-	-	(40)	(40)	14,047
Prepayments, accrued income and other assets	9,029	-	-	-	72	1	-	-	(10)	256	319	9,348
Long-term assurance assets	3,557	-	-	-	-	-	-	-	-	(3,557)	(3,557)	-
Total assets	**454,428**	**-**	**-**	**(274)**	**2,067**	**819**	**-**	**-**	**(10)**	**(47)**	**2,555**	**456,983**

Note: All items may not necessarily impact banks in Canada.

European illustrative example – opening IFRS balance sheet – cont'd

- Excerpt from 2005 Royal Bank of Scotland Annual Report and Accounts

Analysis of IFRS adjustments, excluding IAS 32, IAS 39 and IFRS 4 (Cont'd).

	UK GAAP £m	Dividends £m	Income Tax £m	Leases £m	Consolidation £m	Software Development £m	Investment Property £m	Share Based Payment £m	Employee Benefits £m	Insurance £m	Total Adjustments £m	IFRS £m
Liabilities												
Deposits by banks	68,281	-	-	-	-	-	-	-	-	-	-	68,281
Customer accounts	236,963	-	-	-	(1,002)	-	-	-	-	(495)	(1,497)	235,466
Debt securities in issue	41,016	-	-	-	3,129	-	-	-	-	-	3,129	44,145
Settlement balances and short positions	21,369	-	-	-	-	-	-	-	-	-	-	21,369
Derivatives at fair value	15,173	-	-	-	-	-	-	-	-	(105)	(105)	15,068
Accruals, deferred income and other liabilities	18,779	(1,059)	-	2	238	-	-	6	-	(3,596)	(4,409)	14,370
Retirement benefit liabilities	1,445	-	-	-	-	-	-	-	591	-	591	2,036
Deferred taxation liabilities	2,036	-	109	(75)	13	243	-	(2)	(584)	(4)	(300)	1,736
Insurance liabilities	-	-	-	-	-	-	-	-	-	7,781	7,781	7,781
Subordinated liabilities	16,998	-	-	-	-	-	-	-	-	-	-	16,998
Minority interests	2,713	-	-	-	(313)	5	-	-	-	(13)	(321)	2,392
Shareholders' equity	26,098	1,059	(109)	(201)	2	571	-	(4)	(17)	(58)	1,243	27,341
Long-term assurance liabilities	3,357	-	-	-	-	-	-	-	-	(3,557)	(3,557)	-
Total liabilities and equity	**454,428**	**-**	**-**	**(274)**	**2,067**	**819**	**-**	**-**	**(10)**	**(47)**	**2,555**	**456,983**

Note: All items may not necessarily impact banks in Canada.

Canadian GAAP and IFRS have mostly converged in some areas

- These items have a greater alignment with current Canadian GAAP reporting:
  - Financial instruments classification and measurement
    - Classifications consistent with Canadian GAAP (held to maturity, loans and receivables, available-for-sale, held for trading and fair value option)
    - Entities have the ability to change classification of financial instruments, in certain circumstances at transition
  - Loan loss provisioning
    - Change in nomenclature from specific to individual, general to collective
    - Potential ongoing change in the mix of individual versus collective provisions
  - Fair value measurement
    - No change in fair value measurement guidance
  - Hedge accounting
    - Canadian GAAP hedge accounting is similar to current IFRS
    - New hedges applied to assets and liabilities coming on balance sheet

OSFI Transitional Relief

OSFI has provided some transition relief to capital requirements

- Mortgages sold through the CMHC Programs prior to March 31, 2010 plus subsequent top-ups are excluded from the calculation of the asset to capital multiple
- Five quarter phase-in of IFRS transition impacts on capital
  - Irrevocable election at time of conversion (November 1, 2011)
  - Exclude reversal of gains or losses on sale related to securitizations other than CMHC Programs from phase-in
  - Additional disclosure
- The March 2010 OSFI advisory can be found on the OSFI website at:
  - http://www.osfi-bsif.gc.ca/app/DocRepository/1/eng/guidelines/capital/advisories/IFRS_e.pdf

Future changes to IFRS

A number of significant IFRS projects are underway and will impact post-transition

- A number of significant accounting standards are changing and could impact banks in Canada with October 31st year-ends as early as Q1, 2014 (this timing is under discussion):

- Financial instruments
  - Classification of financial assets
    - In general, a move to amortized cost or fair value through profit and loss
    - Removes the available-for-sale category except for equities in certain circumstances
    - Framework based on business model and nature of the instrument
    - Expectation is most loans will remain at amortized cost
    - Trading activities will be at fair value while, available-for-sale securities will be split between amortized cost or fair value through profit and loss

Some proposals are expected to simplify and others will be more complex

- Financial instruments – cont'd:
  - Hedging
    - Simplifying hedge accounting criteria, however, income statement will still reflect ineffectiveness
  - Impairment and loan loss provisioning
    - The IASB and FASB are working on an amended standard for loan loss provisioning
    - The objective of the project is the earlier recognition of loan losses

Some fundamental changes to accounting are in progress

- Pension accounting
  - The option to amortize market-related gains/losses and other actuarial amounts through pension expense may be removed
  - The impact of the proposed change is that the gains and losses would be recognized in equity
- Insurance accounting
  - More income statement volatility because different discount rates may be applied to assets and liabilities
- Leases
  - All leases may be recorded on the balance sheet resulting in balance sheet gross-ups and differences in the timing of recognition in earnings

Key Takeaways

Key Takeaways

- The transition to IFRS is complex
- Transition elections and accounting policy decisions to be made by individual banks
- Impacts will differ from bank to bank
- Reconciliations and disclosure to be provided to bridge between CGAAP and IFRS
- Uncertainty around future changes to key accounting standards

Panel Discussion

- Jean Dagenais
  Senior VP - Finance, Tax & IR,
  National Bank
- John Ferren
  VP Investor Relations, CIBC
- Cally Hunt
  Senior VP & Chief Accountant, BMO
- Linda Mezon
  Chief Accountant,
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- Manjit Singh
  Senior VP,
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- Maria Theofilaktidis
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