Key Messages

- The EACB appreciates the IASB efforts to develop an expected credit loss approach in order to address the widely criticized shortcomings of the incurred loss model. Although the new model included in the ED does not perfectly reflect the economic link between the pricing and the initial credit quality by recognising a portion of the initial expected credit losses at initial recognition, the EACB thinks that at this stage it can be considered an adequate proxy.
- We warmly welcome the principle-based approach of the IASB's ED. From our point of view, principle based rules are vital in ensuring that banks' respective risk management practices can be implemented and are adequately reflected in credit loss provisions. In this respect, we would like to highlight that banks that do not apply the 'internal rating based' (IRB) approach according to Basel II and do not base their internal risk management processes on expected loss concepts should not be obliged to implement the respective regulatory processes and parameters solely in order to base the calculation of the 12-month expected loss upon them. The final standard should rather require the determination of the 12-month expected loss based upon the risk management processes in place. The wording of the exposure draft is in some parts misleading, especially regarding the utilization of the notion "probability of default (PD)". As mentioned above, the assessment of the credit quality in many banks is not based upon statistically determined PD's resulting from internal rating processes. The final standard should therefore allow for an assessment of the credit quality based upon the credit processes in place and not oblige those banks to implement highly complex statistical approaches which are not adequate for the respective business model.
- Bank risk management uses a wide range of indicators (not only PD) in order to highlight a significant deterioration. So, it is necessary that entities be allowed to use for accounting purposes all the instruments used to manage the risk of their financial assets;
- Regarding the operational simplifications provided:
    - -the "investment grade" notion should not be too rules-based;
    - -30-day rebuttable presumption might not be a clear indicator of a real deterioration in the credit quality of the loans;

Question 1

(a) Do you agree that an approach that recognises a loss allowance (or provision) at an amount equal to a portion of expected credit losses initially, and lifetime expected credit losses only after significant deterioration in credit quality, will reflect:

(i) the economic link between the pricing of financial instruments and the credit quality at initial recognition; and
(ii) the effects of changes in the credit quality subsequent to initial recognition?

If not, why not and how do you believe the proposed model should be revised?

Question 1(a)(i)

The EACB appreciates the IASB efforts to develop an expected credit loss approach in order to address the significant concerns widely raised by several interested parties on the IASB's original 2009 Exposure Draft (2009 ED) and 2011 Supplement Document (2011 SD). Although the new model included in the ED does not perfectly reflect the economic link between the pricing and the initial credit quality by recognising a portion of the initial expected credit losses at initial recognition, the EACB thinks that at this stage it can be considered a good compromise between implementation costs and the need to provide an earlier recognition of credit losses. However, while some EACB members welcome and support the IASB's proposal, other members have some concerns on it as explained better below (see answers to Questions 2, 4, and 5).

Question 1(a)(ii)

We support the proposed approach as long as it distinguishes between high-quality (performing) and low-quality (non-performing/impaired) financial assets, and thus provides useful information about the credit quality of an entity's financial assets, its credit risk management activities and the effect of those activities on the entity's financial statements). We agree that once a significant deterioration in credit quality has occurred an impairment allowance based on expected lifetime losses should be recognised.

Nevertheless, it seems fairly important that the interpretation of a "significant" deterioration in the credit quality is consistent with existing risk management practices and that all information used to manage the credit risk of the financial instrument (both of a quantitative and qualitative nature) will be taken into account for the assessment.

(b) Do you agree that recognising a loss allowance or provision from initial recognition at an amount equal to lifetime expected credit losses, discounted using the original

effective interest rate, does not faithfully represent the underlying economics of financial instruments? If not, why not?

We agree. As stated above an impairment approach should distinguish between performing and low-quality non-performing/impaired loans. This is also adequate with regard to the underlying economics of lending. This means that the level of the required loss allowances should be based on the degree of the credit quality. Such a differentiation would be consistent with banks' risk management practices. From an economic point of view, it seems not evident that loss allowances for potential losses over the entire lifetime have to be recognised already on day one of the loan accommodation of "healthy" loans (cf. FASB proposal). Moreover, we doubt that this would provide users of financial reporting data with adequate information on the financial position of the entity. Furthermore, (at least in the event of open portfolios) a general requirement for loss allowances for lifetime losses implies the creation of reserves of significant amount which, however, could never be used and thus have the character of a capital buffer. Hence, such aspects should rather be covered by the regulatory frameworks. They appear out of place in an accounting standard.

In addition to this, a unintended negative consequence could be that it could prevent financial institutions from financing real economy, notably SMEs, or retail customers with a higher risk profile and who have no access to financial markets.

It can also lead to favour short term loans, which can have bad consequences for the economy.

__Question 2__

(a) **Do you agree that recognising a loss allowance (or provision) at an amount equal to 12-month expected credit losses and at an amount equal to lifetime expected credit losses after significant deterioration in credit quality achieves an appropriate balance between the faithful representation of the underlying economics and the costs of implementation? If not, why not? What alternative would you prefer and why?**

The proposed credit deterioration approach essentially presents a balanced model for recognising a loss allowance. We welcome the proposed regime for low risk financial instruments.

However, (given the required follow-up and in view of the necessary data storage) the implementation of the relative approach incurs an enormous degree of complexity on the level of the individual loan. Hence, it is vital that the standard is principle-based and that presentations / examples which are inconsistent with that principle-based nature are deleted. We understand that the IASB does not seek to promulgate any requirements / interpretations concerning the point in time when a credit quality deterioration shall be deemed "significant". However, this seems inconsistent with the language under paragraph B15 which does precisely this. Paragraph B15 lists an example (involving various facts and figures) which gives rise to the impression that a "significant" deterioration of extremely high-quality credits will be triggered fairly quickly, notwithstanding the fact that these credits, on the whole, still possess a good rating (e.g. if there is a change in the PD from 0.4

% to 0.7 %, which – in terms of percentage figures - translates into a 75 % deterioration). Yet, on the other hand, loans of a lower quality will feature a "significant" deterioration only at a substantially later point in time. However, such an interpretation would lead to a situation where the majority of loans would migrate to stage 2 thus incurring recognition of lifetime losses in the absence of any economic justification for this. Hence, the consideration of qualitative criteria is of paramount importance during the assessment of the significance and this is already shown by this one example. We therefore suggest deleting the figure-based example provided under paragraph B15.

The IASB seeks to allow practical simplifications for low credit risk loans. We welcome this approach. Based on the foregoing it is our understanding that the presentations under section 6 of the ED mean that investment grade rated loans shall not see an automatic transfer to stage 2 if they shift into the non-investment grade range; instead, such transfer shall exclusively be predicated on a "significant deterioration".

In this context, we would like to add that for reasons of consistency, paragraph B20e should be amended as follows: *"an actual or expected* ***significant*** *internal credit rating downgrade…"* For the purposes of consistency, we also recommend revising the entire paragraph B20 in order to include the term "significant" wherever appropriate.

Furthermore, we would like to ask for a clarification regarding the "low credit risk criterion". Paragraph 6 of the ED states, that "as an exception" the requirements of paragraph 5 (recognition of lifetime-EL) are not met if "the credit risk on a financial instrument is low at the reporting date". This means that an assessment, whether the credit risk has increased significantly and therefore the criterion in paragraph 5 is fulfilled, has not to be executed for those instruments, which have an overall low credit risk. From our understanding, the term "investment grade" is only supposed to serve as an example to clarify, what is meant by "low credit risk". However, including a specific example in the main body of the standard is not in line with the principle-based approach of the IASB and may lead to misinterpretations. So that the example is not mistaken for a "bright line", we ask to delete it from the final standard. In our opinion, it is vital to keep the standard principle based and provide the opportunity to individually define the term "low credit risk" for any specific portfolio.
Regarding the 12-month expected loss it is as well of utmost importance that the requirements of the final standard are principle-based and realize the IASB's intention of implementing a management approach that relates the impairment model to existing risk management practices. Banks that do not apply the 'internal rating based' (IRB) approach according to Basel II and do not base their internal risk management processes on expected loss concepts should not be obliged to implement the respective regulatory processes and parameters solely in order to base the calculation of the 12-month expected loss upon them. The final standard should rather require the determination of the 12-month expected loss based upon the risk management processes in place. The wording of the exposure draft is in some parts misleading, especially regarding the utilization of the notion "probability of default (PD)". As mentioned above, the assessment of the credit quality in many banks is not based upon statistically determined PD's resulting from internal rating processes. The final standard should therefore allow for an assessment of the credit quality based upon the credit processes in place and not oblige those banks to implement highly complex statistical approaches which are not adequate for the respective business model.

(b) Do you agree that the approach for accounting for expected credit losses proposed in this Exposure Draft achieves a better balance between the faithful representation of the underlying economics and the cost of implementation than the approaches in the 2009 ED and the SD (without the foreseeable future floor)?

As the new model clearly distinguishes loans deteriorated from those that are not, and it does not prescribe a loan loss allowance based on the lifetime estimates at initial recognition of each instrument, we should see that model as an improvement on the previous approach.

(c) Do you think that recognising a loss allowance at an amount equal to the lifetime expected credit losses from initial recognition, discounted using the original effective interest rate, achieves a better balance between the faithful representation of the underlying economics and the cost of implementation than this Exposure Draft?

No, we do not take that position (see our response to question 1(b))

<u>Question 3</u>

(a) **Do you agree with the proposed scope of this Exposure Draft? If not, why not?**

We agree with the proposed scope of this Exposure Draft.

(b) **Do you agree that, for financial assets that are mandatorily measured at FVOCI in accordance with the Classification and Measurement ED, the accounting for expected credit losses should be as proposed in this Exposure Draft? Why or why not?**

We feel that it would be appropriate to apply a consistent impairment model for amortised cost and FVOCI assets.
We note that when the model is applied to the amortised cost category or the FV-OCI category there is a difference in the impact on equity while the same on profit or loss pattern (Example 10, IE63-IE67). When applied to the FV-OCI category, on initial recognition the model results in a debit in profit or loss that is offset by a credit in other comprehensive income.

<u>Question 4</u>

Is measuring the loss allowance (or a provision) at an amount equal to 12-month expected credit losses operational? If not, why not and how do you believe the portion recognised from initial recognition should be determined?

EACB believes that the proposed approach could use information and parameters from the internal credit risk assessment systems that banks have developed for regulatory purposes, notably those using an 'internal rating based' (IRB) approach under Basel II. Therefore, with regard to the 12-month expected loss we consider the proposal operational, due to the

synergies with the Basel II framework even if we expect that some adjustments to prudential input would be necessary. However, the corresponding adjustments (in terms of the downturn PD, TTC vs. PIT etc.) incur considerable costs and are linked to a high degree of uncertainty whenever they are based on forecasts. We recommend a solution where the identification of the 12-month EL in stage 1 is permitted to be conducted in line with the Basel requirements without the need for any additional adjustments for the banks using the IRB approach. The Basel requirements are taken into account for those banks' internal management. Hence, the aforementioned recommendation would be a more user friendly implementation. Such an approach would facilitate a timely implementation of stages 1 and 2 in line with IFRS9 impairment.

In this context we suggest deleting BC 193. After all, this paragraph implies that it will not be possible to use the Basel PDs due to the fact that the determination of PDs fails to consider current information. We do not think that this is true: The rating systems are calibrated on the basis of historic data. The individual rating, however, has to be based on current data or, moreover, on the borrowers' latest financial statements, thus seeking to provide an assessment of the PD that is as up-to-date as possible even when using the Basel ratings based approach. In this regard, we would like to point out that Annex VII Part 4 para. 18 of the Directive 2006/48/EC relating to the taking up and pursuit of the business of credit institutions (Banking Directive) clearly requests that the rating be based on "current information". If the rating is based on mathematical-statistical models, Annex VII Part 4 para. 30 of the Banking Directive sets out that the model result will still have to be complemented by means of individual assessments. Essentially, this also involves answering qualitative questions. Also overrides imply the use of current information. After all, this is the only way in which all relevant information will be adequately reflected in the rating grade. The rather formal rules on handling overrides are laid down in the provisions under Annex VII Part 4 para. 25 of the Banking Directive and under the 2006 CEBS guideline (point 460 - 461).

Nevertheless, we would like to highlight that banks that do not apply the 'internal rating based' (IRB) approach according to Basel II and do not base their internal risk management processes on expected loss concepts should not be obliged to implement the respective regulatory processes and parameters solely in order to base the calculation of the 12-month expected loss upon them. The final standard should rather require the determination of the 12-month expected loss based upon the risk management processes in place. The wording of the exposure draft is in some parts misleading, especially regarding the utilization of the notion "probability of default (PD)". As mentioned above, the assessment of the credit quality in many banks is not based upon statistically determined PD's resulting from internal rating processes. The final standard should therefore allow for an assessment of the credit quality based upon the credit processes in place and not oblige those banks to implement highly complex statistical approaches which are not adequate for the respective business model.

<u>**Question 5**</u>

(a) **Do you agree with the proposed requirement to recognise a loss allowance (or a provision) at an amount equal to lifetime expected credit losses on the basis of a significant increase in credit risk since initial recognition? If not, why not and what alternative would you prefer?**

With regards to the proposed requirement to recognise a loss allowance (or a provision) at an amount equal to lifetime expected credit losses on the basis of a significant increase in credit risk since initial recognition, the EACB members have divergent views on the IASB's proposals in the ED.

- Some EACB members agree with the IASB's proposals as they think it is the most appropriate solution at this stage. Recognising the Lifetime-EL only after a significant increase in the credit risk since initial recognition in their opinion most adequately depicts the economics of lending while the relative approach in assessing a significant increase complies with the principle based approach that allows for an appropriate illustration of any specific financial instrument.
- Other members however believe that the IASB "relative" approachadds operational complexity by requiring entities to track movements in an asset's credit quality relative to its initial credit standing, whereas it does not correspond to their credit risk management practices and could not be performed on an open portfolio basis; the latter members would suggest that the IASB finds a solution, which should be different, however, to the FASB model.

In addition, instead of an assessment on the basis of the lifetime PD, EACB recommends the assessment of a "significant" deterioration on the basis of the 12-month PD becoming a mandatory default method (unless there are any reasons to believe that this will lead to different results than the use of the lifetime PD). While in principle this is an option granted by the IASB (in exceptional cases), we fear that – whenever an institution uses the 12-month PD – it is under the obligation to prove beyond reasonable doubt that the results achieved will not be any different. Thus, while the IASB essentially grants derogations, such derogations do not ease the (operational) burden for entities. This is due to the fact that entities usually have to provide conclusive evidence for the potential immateriality (comparison lifetime PD versus 12-month PD) which is similarly requested by the auditors. A respective comparison of the lifetime PDs may theoretically be correct. However, due to e.g. the need for annual recalibrations (new PD assumptions, mere time elapsed) this still ties up an extreme amount of resources without yielding any benefit justifying these expenses. Operationally the use of lifetime PDs will require entities to retain large libraries of PD curves and lead to different trigger points for credit deterioration between loans, not just based on credit quality but maturity.

Furthermore, the use of the 12-month PD is compatible with the IASB's underlying rationale. The lifetime PD is comprised of three components: 12-month PD, migration matrixes and maturity effect. Under the provisions of paragraph B14, when assessing the change in the credit quality, the maturity effect will have to be eliminated by means of the PD, anyway. Assuming that the underlying migration matrixes are constant over time, the 12-month PD approach invariably leads to the same results as the lifetime PD. Consequently, the use of the 12-month should be allowed as long as there is no indication that there is a lack of consistency in the migration matrices or, moreover, as long as the change of the 12-month PD is consistent with the lifetime PD.

Based on the reasons highlighted above, paragraph B11 should be clarified as follows: „However an entity may use the 12-months probability of default occurring to determine

whether credit risk has increased significantly since initial recognition if there is no objective evidence that the outcome would differ."

(b) **Do the proposals provide sufficient guidance on when to recognise lifetime expected credit losses? If not, what additional guidance would you suggest?**

We prefer principle based rules and we are against any fixed threshold values or similar parameters. For this reason, the deterioration criteria, including the "low credit risk exception" should not be too rules-based. This is because the level above which a loan can be granted in one market for one entity is not necessarily the same for different entities in different markets, with a very limited possibility to have a common threshold valid for each market.

We also feel that there is no need for additional guidelines / examples etc. Thus the figures used as an example under paragraph B15 should be deleted.

Paragraph B20(e) might give rise to the conclusion that even the mere expectation that there will be an internal credit rating downgrade will warrant a mandatory transfer to bucket 2. In our view, such a transfer trigger would be premature. The language should therefore be amended to include a qualifier, e.g. "significant" (cf. also the other scenarios listed under paragraph B20).

(c) **Do you agree that the assessment of when to recognise lifetime expected credit losses should consider only changes in the probability of a default occurring, rather than changes in expected credit losses (or credit loss given default ('LGD'))? If not, why not and what would you prefer?**

We understand that risk management uses a wide range of indicators (not only PD) in order to highlight a significant deterioration. So, it is necessary that entities be allowed to use for accounting purposes all the instruments used to manage the risk of their financial assets.

Furthermore, there should be a further clarification to the effect that under certain conditions in which collateral values (e.g. LGDs or LTVs) have an impact on the probability of default these can similarly be considered during the assessment of a stage transfer. This would equally be in line with the assessment in risk management. Along with specific legal provisions in a number of jurisdictions, this particularly concerns business involving various non-recourse funding transactions and funding transactions through special purpose entities. Whilst paragraph 18 refers to the admissibility of loss rates which implicitly also include an LGD and paragraph B20(j) refers to collateral values, from our point of view this is not sufficient in order to achieve this objective; instead, a clarification should also be included under paragraph 8.

Finally, the bucket movement should not only be driven by PD deterioration alone, but also consider the probability of an increase in the expected credit losses (includiging LGD for example). This would be consistent with an expected credit loss model. A credit deterioration which is (more than) offset by e.g. additional collateral value should not lead to a movement from bucket 1 to 2 and hence cause higher loan provisioning. The

considerations regarding expected credit loss probabilities are more complex and go beyond PD movements. Therefore it should be optional to base the bucket movement on the broader concept of "expected credit losses" than on PD only.

Finally, there should be a clarification that – in exceptional cases - the significance of the credit quality change shall not have to be determined merely on the basis of the PD. In the absence of a rating (e.g. for trade receivables or separate trust asset exposures) the assessment should, for instance, also be allowed based on other criteria..

(d) Do you agree with the proposed operational simplifications, and do they contribute to an appropriate balance between faithful representation and the cost of implementation?

During the expected loss calculation, prepayments, call options and similar options shall be taken into account (Appendix A). We recommend granting banks the right to ignore options whenever the respective influence on the expected loss is insignificant. Partly, this would lead to a substantial reduction in the cost of implementation.

We endorse the simplification pursuant to which, in the event of a "low probability of default" it will be possible to waive the assessment of a significant deterioration of the credit quality and to keep the asset directly in stage 1.

We welcome the simplification concerning leasing exposures.

We believe that a 30-day rebuttable presumption might not be a clear indicator of a real deterioration in the credit quality of the loans. "Significant" deterioration is not the same for different markets/jurisdictions, and it is not evaluated in the same way by different risk management practices. For these reasons, this requirement should not necessarily reflect a significant increase in credit risk for all kind of loans. Moreover, we note the divergent approaches adopted by the IASB: in this case the IASB has decided to establish a quantitative threshold; vice versa, with regard to the "solely payment of principal and interest" (SPPI) test, it used a qualitative approach (i.e. the "more than insignificant" concept).
furthermore, especially, in the case of corporate activities the text could be understood as requiring entities to prove in every single case on which grounds they rebut this presumption, which would make the application of this presumption an extremely burdensome exercise.

(e) **Do you agree with the proposal that the model shall allow the re-establishment of a loss allowance (or a provision) at an amount equal to 12-month expected credit losses if the criteria for the recognition of lifetime expected credit losses are no longer met? If not, why not and what would you prefer?**

We agree with the proposal. In order to arrive at a true and fair view of credit quality trends, a switch back to stage 2 or 1 is indispensable.

Question 6

(a) **Do you agree that there are circumstances when interest revenue calculated on a net carrying amount (amortised cost) rather than on a gross carrying amount can provide more useful information? If not, why not and what would you prefer?**

We welcome the presentations in the ED to the effect that under IFRS 9 there shall not be any changes concerning the collection of interest revenue compared to IAS 39. However, in view of the fact that apparently this is still not sufficiently clear to parts of the community, we kindly invite the IASB to provide a corresponding clarification.

(b) **Do you agree with the proposal to change how interest revenue is calculated for assets that have objective evidence of impairment subsequent to initial recognition? Why or why not? If not, for what population of assets should the interest revenue calculation change?**

Cf. response to question 6a.

(c) **Do you agree with the proposal that the interest revenue approach shall be symmetrical (ie that the calculation can revert back to a calculation on the gross carrying amount)? Why or why not? If not, what approach would you prefer?**

Cf. response to question 6a.

Question 7

(a) Do you agree with the proposed disclosure requirements? Why or why not? If not, what changes do you recommend and why?

We would like to underline that under a principle-based standard it is important for users of financial reporting information that the disclosures provide them with appropriate information concerning the expected loss model and the respective, underlying parameters. The requested disclosures are very detailed as well as excessively elaborate. In order to avoid a potential information overload for users of financial statements, the requirements should be revisited and streamlined for the sake of transparency and the reduction of complexity.

We regret that the IASB has not analysed the redundancy of the disclosures asked in this ED with the requirements in IFRS 7.
We would also like to point out that it would be easier if all the disclosures relative to financial instruments are located in only one standard (i.e. IFRS 7 as it was the philosophy behind the development and publication of this standard).
Furthermore, whilst not limited to, this particularly applies to the reconciliation statement of the gross carrying amounts (paragraph 35, 36) which would require the integration of credit risk control data into financial accounting on the basis of individual business transactions. In order to create meaningful balancing entries which allow a further analysis, the transfer to a

different stage would have to trigger an account entry. Effects due to changes in the consolidation scope and due to currency conversions have to be treated separately. This would affect the entire portfolio of transactions belonging to the categories AC and FVOCI including portfolios featuring low PDs (stage 1). To date, loss allowances could be determined by means of a subledger accounting and could be booked in an aggregated form.

Furthermore, due to the fact that these issues would incur tremendous implementation cost (e.g. tracking past modifications, calculation of the re-default rate, disclosure of enforcement actions), we recommend a review of the disclosure requirements on direct write downs and modifications.

The implementation of additional disclosures that are requested (e.g. examples 12 and 13 (see pages 79 ff.), paragraphs 37, 38, 39, 40, 41, 44 and 45) is extremely complex and does not generate decision relevant information for readers for instance :

- Paragraph 38 a. requires to disclose gross carrying amount throughout their remaining life, for modified and written-off assets which is very laborious,
- Paragraph 39 requires the explanation of changes in estimates of expected credit losses and the causes of those changes which represents very extensive supplementary documentation and could be very voluminous and not easily readable as banks have numerous portfolios and different changes in credit losses may occur for different reasons,
- Thhe same also applies for paragraph 40 which requires explanation of changes in the quality of collateral as a result of deterioration. The value of collateral often fluctuates and such fluctuations may be in opposite sense depending on portfolios and types of collateral. It would imply to perform numerous calculations to quantify the effects of deterioration which, according to us, will not lead to give useful information. We believe recommendation n° 30 of the EDTF report should be followed *"Provide qualitative information on credit risk mitigation, including collateral held for all sources of credit risk and quantitative information where meaningful. Collateral disclosures should be sufficiently detailed to allow an assessment of the quality of collateral.",*
- Paragraph 41 requires positive or negative effects caused by a portfolio or a geographical area. Clarification should be added that this information should be provided only if useful and related to a particularly noticeable event,
- Paragraph 44 illustrated by the example IE73 is too prescriptive and not relevant for all types of loans, i.e. internal grade is not relevant for consumer loans or external grade is not relevant for corporate loans when loss allowances are based on internal grades. Only main relevant indicators effectively used by the entity for determining loss allowances should be disclosed..

We therefore recommend keeping the solution where there is a comparison between two assessments made on specific dates. This would also be in line with a principle based standard.

(b) Do you foresee any specific operational challenges when implementing the proposed disclosure requirements?If so, please explain.

We are concerned about the complexity inherent in the reconciliation of the gross carrying amounts requested under paragraph 35a. This is due to the fact that this requires the aggregation of data on existing holdings and of movements. Maintaining these data (e.g. gross exposures which have been transferred from stage 1 to stage 2 during the fiscal year and *vice versa)* requires a comprehensive database thus incurring considerable costs.

In our view, there is no adequate cost/benefit ratio concerning the information provided on write-offs. At present, entities already provide detailed recovery information. In this respect, the ED proposals require historical data as a precondition. Such data are either entirely absent or no longer available (for instance, due to the fact that a loan has already been written down thus meaning that the corresponding information will no longer be available in the system). Furthermore, the ED does not provide a concept clarification of the term "active enforcement".

In terms of the disclosures requested under example 12, we would like to point out that it is difficult to differentiate loans extended in previous years from new lendings. This is first and foremost owed to the fact that prolongations cannot be assigned to one of the two categories in an unambiguous manner.

A comprehensive implementation of the disclosure requirements by 2016 will be virtually impossible. It is obvious that there will be challenges or, moreover, high implementation costs. Whilst not limited to, this is particularly owed to the scope and the granularity of the information requested.

In order to avoid information overload for users of annual financial statements, for the sake of transparency and for the purposes of cutting complexity (cf. above), the requirements should rather be reduced.

Assessing the exposure draft in the context of the whole set of IFRS, there is no evidence of a desirable harmonization between the risk-related disclosure requirements regarding expected credit losses introduced in the exposure draft and the established requirements of IFRS 7. For instance, the relevant credit volume according to IFRS 7 can be measured in line with the internal risk controlling approaches. The exposure draft on the other hand refers to the gross carrying amount of the assets.
Furthermore, the direct link between internal ratings and the gross carrying amount is not supportable as it does not comply with the risk management practice in credit institutions. Risk management practices commonly use definitions of credit exposures that differ from the balance sheet approach. Therefore, an open approach to (risk) reporting is preferable and in line with the IASB's goal of connecting the accounting for expected credit losses to the internal risk management. This open approach should be principle based and provide a sufficient degree of flexibility in designing the disclosure in line with the actual internal risk management approaches.

Another critical issue regarding the disclosure requirements introduced in the exposure draft concerns the discrepancy between the proposed expected loss approach by the IASB and the impairment rules of the Basel Committee of Banking Supervision which currently form the basis of external risk reporting of many banks. At present, cross-references from the risk report according to Basel II to the risk reporting attached to the financial statements according to IFRS are being made by these banks. This proceeding is enabled by the management approach comprised in IFRS 7, i.e. the risk reporting may be based on the internally applied risk management processes ("through the eyes of management") which are generally based on regulatory requirements. As described in the answer to question 4, the wording of the exposure draft suggests that regulatory expected credit loss approaches (and especially parameters) do not entirely fulfill the requirements of an expected credit loss approach for accounting purposes for which reason adjustments have to be made. If the risk reporting for accounting purposes as a consequence diverges from the regulatory requirements, cross-referencing is no longer possible and therefore two different risk reports have to be prepared. The underlying intention of the currently conducted cross-referencing is to reduce the amount and complexity of disclosures as well as to reduce the need for reconciliations. Diverging reportings do not lead to any information gain for the users of financial statements and do not contribute to the decision usefulness of the information provided. We, therefore, claim to sustain the opportunity for cross-references from the risk report according to Basel II to the risk reporting attached to the financial statements according to IFRS.

In particular, the accounting perimeter for consolidation of big banks may from the regulatory perimeter. This is why it could be very hard to reconcile data from these two perimeters. In addition, to aforementioned reasons of consistency, the disclosure requirements regarding the expected credit loss model proposed in the exposure draft should be included in IFRS 7 which is supposed to comprise the disclosures regarding financial instruments. Thus, institutions who would like to reconcile accounting and regulatory perimeters should be able to do it in the management report.
Correspondingly, the final standard should provide an opportunity (but not a necessity) to give the required disclosures by cross-reference from the financial statements (or the risk report attached to them) to the regulatory risk reporting if the respective credit institution is subject to an effectual supervision. The designated opportunity for a cross-reference in paragraph 32 of the exposure draft is however not sufficient as it only relates to the communication medium and not to the provided information itself (as opposed to IFRS 7 which explicitly allows for the 'management approach').

Consequently, to be consistent, the disclosure requirements regarding the expected credit loss model proposed in the exposure draft should be included in IFRS 7 which is supposed to comprise the disclosures regarding financial instruments.

Question 8

Do you agree with the proposed treatment of financial assets on which contractual cash flows are modified, and do you believe that it provides useful information? If not, why not and what alternative would you prefer?

We do not agree with the proposed treatment of financial assets on which contractual cash flows are modified.

We should not assess the deterioration of modified credit-impaired loans credit risk by comparing credit risk at the reporting date and at initial recognition when the contractual terms of the contract are unmodified. The tracking of the original quality of the credit risk based on an individual assessment of loans would be too burdensome.

The treatment of modified financial assets should be limited to modifications of credit-impaired financial assets and should not be extended to modifications for commercial reasons.

In many business models, contractual changes are a standard practice. The requisite differentiation between credit quality driven changes and other contractual changes incurs considerable additional implementation costs.

Furthermore, from our point of view, problems result from the relationship to the definition of forbearance by the EBA which is unclear by now. In principle, we would welcome convergence between the definitions and disclosure obligations under accounting standards on the one hand and under supervisory rules on the other hand and we would also like to point out that the requirements proposed by the IASB are already sufficiently comprehensive.

During lending transactions, it is paramount for banks that they are capable of responding to the borrower's latest economical circumstances. The more stringent disclosure requirements as well as the resulting implementation costs would severely impair this very capacity to respond on the part of banks.

Question 9

(a) **Do you agree with the proposals on the application of the general model to loan commitment and financial guarantee contracts? Why or why not? If not, what approach would you prefer?**

Although this may incur costs for the technical implementation that are considerably higher, we agree with the proposal on the application of the "general model" to financial guarantees and loan commitments.

(b) **Do you foresee any significant operational challenges that may arise from the proposal to present expected credit losses on financial guarantee contracts or loan commitments as a provision in the statement of financial position? If yes, please explain.**

No, we do not foresee any such challenges. This is due to the fact that, already today, it is presented as a provision.

Question 10

(a) **Do you agree with the proposed simplified approach for trade receivables and lease receivables? Why or why not? If not, what changes do you recommend and why?**

In principle, we welcome the exemption rule. On the one hand, waiving the set up of 12-month EL in stage 1 translates into low costs for monitoring and assigning contracts / portfolios in stage 1 or, moreover, stage 2. However, in the decision on exercising the right to choose, the impact on the regulatory own funds shall and must be taken into account.

(b) **Do you agree with the proposed amendments to the measurement on initial recognition of trade receivables with no significant financing component? If not, why not and what would you propose instead?**

We agree (although this is of minor relevance).

Question 11

Do you agree with the proposals for financial assets that are credit-impaired on initial recognition? Why or why not? If not, what approach would you prefer?

We agree with the proposals in principle. However, in this context it is not sufficiently clear how loans should be treated which were initially classified in stage 3 after a modification (i.e. derecognition and recognition modified loan). Even if the assumption is that, following the modification, the loan can subsequently be serviced in a regular manner, banks' risk management policies and guidelines stipulate that a stage 3 classification (impaired) will be adequate at least for the first year. Provided there are no renewed payment difficulties etc., we hold the view that, also afterwards, it should be possible to transfer such loans again into stages 1 and 2 (the purpose of the modification being to avoid said payment difficulties in future). We would like to ask the IASB to provide a clarification in this respect.

Furthermore, we would like to draw attention to a potential problem in the context of phase 1 under IFRS 9. Pursuant to the rules on classification / measurement proposed by the IASB, financial instruments shall be recognised at fair value if the cash flows fail to pass the SPPI test (e.g. high leverage etc.). To us, it is not sufficiently clear whether this rule also covers (purchased) PCI assets, i.e. assets featuring a high discount. This is due to the fact that, at least in theory, it is possible to preserve the initial nominal value (100%) even if this cannot be taken for granted at the point in time where these assets are being purchased. Yet, such an approach – provided there is a rigorous interpretation of IFRS 9 phase 1 – would subsequently lead to a FV measurement of PCI assets. We feel that this is not sufficiently clear and invite the IASB to elaborate this further.

Question 12

(a) What lead time would you require to implement the proposed requirements?

At the present forecasts are extremely difficult due to the forthcoming complex implementation stage. We believe that the entities should have at least three years to implement IFRS 9 after the completion of all phases. Should the IASB insist on its disclosure requirements in their entirety, this time would even be longer.

For the leasing industry, it would be a good if the amended IAS 17 was implemented at an earlier date or at least at the same time as IFRS 9. Otherwise, there will be increased implementation costs. We would therefore like to advocate a synchronisation of the timetable for introducing IFRS 9 and the amended IAS 17.

(b) **Do you agree with the proposed transition requirements? Why or why not? If not, what changes do you recommend and why?**

Regarding transition requirements, the proposal must be considered in the light of some problems due to currently available information. In particular, an entity would be required to use the information about credit quality at inception. In order to guarantee a sufficient comparability to appreciate changes in credit quality, without excessive costs, it is necessary to propose some practical expedient (e.g., introducing a temporal backward limit to retrieve the original rating or the adoption of statistical/inferential approaches, at sub-portfolio level as well).
In the absence of any (initial) PD for a loan, we advocate e.g. for the possibility of assuming the first available and quality assured PD.

(c) **Do you agree with the proposed relief from restating comparative information on transition? If not, why?**

We agree.

Question 13

Do you agree with the IASB's assessment of the effects of the proposals? Why or why not?

As has been pointed out in paragraph BC166, the impact for the individual user depends on the nature and scope of the individual users' existing financial instrument holdings. We also expect an increase in loss allowances.
We appreciate the distinction between loans that have deteriorated significantly and those that have not. This model is an improvement on the previous approach and the main benefit compared to IAS 39 is an early recognition of credit losses.