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Sent to: *director@fasb.org*

EACB Comments on Supplement to IASB ED/2009/12 *Financial Instruments: Amortised Cost & Impairment*

1 April 2011

The European Association of Co-operative Banks (EACB) is the voice of Co-operative Banks in Europe. It represents, promotes and defends the common interests of its 28 members and co-operative banks in general. Co-operative banks form decentralised networks which are governed by banking as well as co-operative legislation. The co-operative banks business model is based on three pillars: democracy, transparency and proximity. Through those pillars co-operative banks act as the driving force of sustainable and responsible development by placing the individual at the heart of their activities and organization. In this respect they widely contribute to the national and European economic and social objectives laid down in the Lisbon Agenda. With 63.000 outlets and 4.200 banks, co-operative banks are widely represented throughout the enlarged European Union playing a major role in the financial and economic system. In other words, in Europe one out of two banks is a co-operative. Co-operative banks have a long tradition in serving 160 million customers, mainly consumers, retailers and SMEs. They have also developed a strong foothold in the corporate market providing services to large international groups. Quantitatively co-operative banks in Europe represent about 50 millions members, 750,000 employees with a total average market share of about 20%.

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EACB AISBL – Secretariat • Rue de l'Industrie 26-38 • B-1040 Brussels
Tel: (+32 2) 230 11 24 • Fax (+32 2) 230 06 49 • Enterprise 0896.081.149 • lobbying register 4172526951-19
www.eurocoopbanks.coop • e-mail : secretariat@eurocoopbanks.coop

Introduction

The members of the European Association of Cooperative Banks (EACB) are pleased to comment on the Supplement Document to the ED/2009/12 "Financial Instruments: Amortised Cost and Impairment" jointly published by the International Accounting Standards Board (IASB) and the Financial Accounting Standards Board (FASB) in January 2011.

Preliminary remarks on consultation process

EACB members strongly support the effort of the IASB and the FASB to achieve a single set of high-quality global accounting standards. In this respect, convergence of GAAP and IFRS on measuring and recording impairment is crucial. Common impairment standard will be of high quality only if the information provided is understandable and it is operational on all practical levels.

Since the impact of this standard on our members' financial statements will be significant, EACB appreciates that the Boards agreed to take more time to re-deliberate issuing a supplement to the ED.

However, while, we recognise the efforts made in consulting stakeholders, we strongly regret the **inadequate 60 days comment period time** for this consultation regarding the important and complex matter of impairment for banks.

In particular, EACB members would have to perform simulations on their loan portfolios to respond properly, in order to ensure that the proposal could be applied to all financial assets managed in open portfolios, in particular bond portfolios. Therefore, EACB members would appreciate that the Boards provide more time for constituents in the future.

We would like to take this opportunity to recall our plea to give greater consideration to the number of amendments that users and preparers of financial information can reasonably absorb within certain timeframes. Moreover, we believe that the Boards should foreseen sufficient resources to assess the impact of proposals.

It has to be underlined that **banks generally need more time to assess all the massive consequences of the application of the new**

IFRS 9 from a management perspective as well as regarding the internal processes, IT systems, personal training etc.

A simplified expected loss model for open portfolios

In our comment on the June 2010 IASB's ED *amortised cost and impairment*, EACB expressed its support to an expected loss model providing for the credit risk of financial assets at amortised cost but raised strong concerns regarding the overall complexity of the ED.

We therefore welcome the development of a more operational and simplified expected loss model for open portfolios. In particular, EACB members welcome the following improvements:

- the "**management approach**", which allows a better alignment of the internal credit risk management of the entity regarding the portfolio segmentation;
- The **differentiation between good book and bad book** that would allow our banks to be close to their risk management monitoring;
- The **recognition of expected loss (and changes in estimates) in profit or loss** on a time proportional basis over the life of the portfolio;
- The **decoupled approach** to recognize interest revenue separately from depreciation instead of an integrated EIR; and
- The **flexibility** regarding the use of a discount rate for the good book.

Further improvements needed

While, the proposed approach in the supplement seems to be generally suitable and equally addresses the November 2009 proposals without its operational drawbacks, it still has some important shortcomings.

Vague concepts that do not allow practical application

In particular, EACB members do not understand all of the aspects of the proposal. Moreover, we fear that the proposed approach could be applied in our members' organisations consistently. .

For instance, some major source of concerns, are the calculation of a floor for the good book allowance and the ability to reverse of the good book allowance during an economic downturn.

Floor & "Foreseeable" future.

First, EACB members do not understand the rationale sustaining the floor mechanism regarding the conceptual approach of the ED. According to the supplement proposal, the calculation of the floor, would require two calculations of impairment allowance, the time-proportional amount and the "floor amount", which our members find very complicated to implement.

Moreover, our members assess the concept of "foreseeable future" as described in the supplement to be wide and uncertain. Under the proposal, the definition of "the foreseeable future" for the calculation of the floor would be the key factor for the allowance measurement, especially if it is greater than 12 months as expected by the Board (§B16). Indeed, should the floor be reached at the end of each reporting period, which is very likely for short term loans (i.e. consumer loans), the time proportional method would become inadequate. Therefore, this concept of "foreseeable future" driving in most cases the allowance amount and undermining the time-proportional approach, would lead to generalize an approach, which EACB members do not support

Furthermore, under these circumstances, the model would incur a "day-one loss" model, which is not consistent with the recognition of loans at market rate in the financial statement of position, at their initial fair value. The floor, contrary to the time-proportional mechanism, appears to be a buffer with no connection with the recognition on a time basis (as revenue) of the risk premium included in the interest rate.

Reversal of books allowance

Secondly, according to the supplement document, it seems that the good book allowance would never be reversed during an economic downturn, for a stable good book. As described, allowance transfers between good book and bad book would be only based on the time proportional allowance, then a new estimate is calculated for the good book and additional allowance needed for the bad book is charged to the P&L account. Thus, the allocation mechanism would have a pro-cyclical effect.

Instead, EACB members consider that the bad book allowance is the appropriate floor for the whole impairment model. We think that the model proposed in the supplement document for open portfolios (without the floor) should be extended to closed portfolios because it would improve the representation of the economic effect of credit risk on financial assets measured at amortised cost (including loan commitment and financial guarantees accounted for under IAS 39).

However, we reiterate that the proposed approach is not appropriate for short term trade receivables for which an incurred loss approach under IAS 39 should be maintained

Disclosures

It is generally important that any method of determining expected losses has to be based on internal risk management practice.

However, we fear that the additional disclosures required by the proposal seem to be disproportionate. Moreover, we think that disclosures of the supplement should be e carried forward to the IFRS 7 Financial Instruments: *Disclosures.*

Transition period

The IASB originally proposed a transition period of three years from the current incurred loss impairment method to the expected loss model. In this respect, in our January 2011 comments on the IASB request for views on Effective Dates and Transition Methods, we reiterated that an earlier application of IFRS 9 in 2013 with comparative information for 2012 would not to be realizable from our perspective.

Since, we still strongly believe that the financial sector in Europe will need at least three years time for the implementation of IFRS 9, we would ask to postpone the effective date to 1 January 2015.

Moreover, our members advocate for applying a mechanism similar to the one applied for the transition to IAS 39 for first time adopters in 2005. The opening balance sheet should be restated with a reconciliation schedule between closing and opening balance sheets.

Furthermore, we would like to voice some of our members concerns located in those European countries, which, due to the economic crisis, are facing to some economic difficulties. They ask for bear in mind that increasing the amount of provisions for expected losses during a period of economic depression would represent a huge effort with an enormous impact in the accounts of the financial institutions in these countries, which cannot be compared with the immediate adoption of these measures by financial institutions from countries where the economy is already recovering and getting positive growth rates.

Please find below our detailed comment on the individual questions outlined in the supplement to the Exposure Draft below.

Contact:

Mr. Volker Heegemann, Head of Legal Department
(v.heegemann@eurocoopbanks.coop)

Ms. Johanna Cariou, Adviser, Accounting & Audit
(j.cariou@eurocoopbanks.coop)

EACB responses to the ED questionnaire

General

Question 1

Do you believe the approach for recognition of impairment described in this supplementary document deals with this weakness (ie delayed recognition of expected credit losses)? If not, how do you believe the proposed model should be revised and why?

EACB members think that the proposed approach in the supplement is generally suitable for recognizing losses earlier in time and thereby addressing in the same way as defined by the November 2009 proposals without its operational drawbacks, the weaknesses of the current incurred loss model.

In particular, the members of the EACB support the followings aspects:

- The better alignment with the internal credit risk management of the entity regarding the portfolio segmentation;
- The recognition of expected loss (and changes in estimates) in profit or loss on a time proportional basis over the life of the portfolio;
- The differentiation between good book and bad book;
- The decoupled approach to recognize interest revenue separately from depreciation instead of an integrated EIR ;
- The flexibility regarding the use of a discount rate for the good book;

However, as expressed under our general comments, EACB members have some severe concerns regarding the calculation of the floor on the good book (please as well our comments under question 9).

Scope- Open portfolios

Question 2

Is the impairment model proposed in the supplementary document at least as operational for closed portfolios and other instruments as it is for open portfolios? Why or why not?

Although the supplementary document seeks views on whether the proposed approach is suitable for open portfolios, the boards welcome any comments on its suitability for single assets and closed portfolios and also comments on how important it is to have a single impairment approach for all relevant financial assets.

The members of the EACB believe that the model proposed in the supplement is more operational for open portfolios than the original impairment model proposed in the ED/2009/12.

Moreover, as we support a consistent impairment model for all financial assets carried at amortised cost, we consider that a new approach for the impairment of financial assets should be applicable for both open and closed portfolios.

The expected cash flow approach as proposed in the ED/2009/12 has proved to be not operational for open portfolios, because the ongoing entry and outflow of assets does (other than in the case of a closed portfolio) not allow a comparison on a static basis. This weakness would be removed by the approach proposed in the supplement document. Therefore, EACB members consider that the supplement approach should be extend to closed portfolios as well.

In general we think that the scope exemption of short-term assets should be clarified to include also for example short-term credit card receivables, which are non-interest bearing.

EACB members consider that single assets within good book should not be excluded from the Expected Loss model. We think that flexibility should at least be maintained, to reflect the risk management policy if needed.

Differentiation of credit loss recognition

Question 3

Do you agree that for financial assets in the 'good book' it is appropriate to recognise the impairment allowance using the approach described above? Why, or why not?

Question 4

Would the proposed approach to determining the impairment allowance on a time-proportional basis be operational? Why, or why not?

Question 5

Would the proposed approach provide information that is useful for decision-making? If not, how would you modify the proposal?

The members of the EACB agree that the financial assets should be differentiated between the "good book" and "bad book" based on credit risk management criteria. In general, we consider the proposed approach is far more operational than the initial approach and we therefore welcome the IASB's decision to adopt a "decoupled" approach instead of an integrated EIR approach. In particular, we think that a time-proportionate recognition of expected losses is appropriate for financial assets in the good book.

EACB members support the efforts of the IASB to develop an operable and simplified model remaining compatible with the principles underlying an expected losses approach (i.e. to improve the representation of the economic effect of credit risk on revenues generated over the life of a financial asset measured at amortised cost). However, we would prefer IASB original time-proportional approach for the loss allowance for the "good book" without the foreseeable future floor.

In fact, our members strongly believe that the floor mechanism, leads to day-one loss recognition and is not consistent with the economics of loan origination mentioned above. We consider that the bad book mechanism is the appropriate floor to deal with the issue on portfolios with front-loaded loss emergence patterns, thus the floor mechanism is not necessary. Otherwise entities are required to carry out two expected loss calculations in order to determine the higher amount, which would create additional

operational burden and complexity without clear benefits. We also question the need of the floor for the "good book" because all expected losses for bad loans are recognised immediately. We recognise that creating loss estimates involve judgement but entity's own credit risk management criteria should be sufficient to ensure the adequacy of the allowance provision.

We agree that there should be an option to use either a straight-line approach (discounted or undiscounted) or an annuity approach for allocation of the expected losses. This would ease the operational application of the proposals. We agree that when the asset is transferred to the "bad book" the entire amount of the related expected loss should be recognised in proportion immediately. Moreover, we consider necessary to be able to use internal models of risk management when measuring expected losses; especially parameters of calculating expected losses under Basel II such as PD, LGD and EAD. Among other things, the challenge when implementing the new approach will be to adjust the Basel II approach, which is based on a one-year cycle, in order to consider the full life - time of the portfolio. Especially, in case historic data for the estimate of the probability of credit events are missing, new methods have to be developed, to enable computer systems to produce the information required.

Finally, EACB member consider that the proposed approach would provide useful information since it properly reflects the economics of credit activity. We regard information about determining the risk allowance as important, since risk allowance policy constitutes an essential element of financial management. The proposed approach through the time proportional mechanism (excepted the floor mechanism) will be able to reflect the inherent credit risk of debt instruments in a timely manner by reserving the risk premiums covering credit losses as they are earned (i.e. on an accrued basis). If loans are priced according to market conditions, the risk premiums included in the contractual interest rate is calibrated to cover future credit losses and there is no reason to recognise in net income a credit loss at inception as required by the floor mechanism. In addition, we consider that the principle underlying the differentiation between the good book and the bad book is also useful for decision-making

Question 6

Is the requirement to differentiate between the two groups (ie 'good book' and 'bad book') for the purpose of determining the impairment allowance clearly described? If not, how could it be described more clearly?

Question 7

Is the requirement to differentiate between the two groups (ie 'good book' and 'bad book') for the purpose of determining the impairment allowance operational and/or auditable? If not, how could it be made more operational and/or auditable?

Question 8

Do you agree with that proposed requirement to differentiate between the two groups (ie 'good book' and 'bad book') for the purpose of determining the impairment allowance? If not, what requirement would you propose and why?

EACB members believe that the entity's credit-risk management criteria are sufficient to differentiate between the assets from the "good book" and the "bad book". In addition, we note that the distinction between the "good book" and the "bad book" is clearly described in the supplement and generally consistent with our members' credit risk management.

We believe that the requirement to differentiate between the "good book" and "bad book" for determining the impairment allowance could be operational and auditable even though it involves judgement. We are also of the opinion that the differentiation is practicable, because it is based on entity-specific internal risk management practices.

Minimum impairment allowance amount

Question 9

The boards are seeking comment with respect to the minimum allowance amount (floor) that would be required under this model. Specifically, on the following issues:

a. Do you agree with the proposal to require a floor for the impairment allowance related to the 'good book'? Why or why not?

b. Alternatively, do you believe that an entity should be required to invoke a floor for the impairment allowance amount related to the 'good book' only in circumstances in which there is evidence of an early loss pattern?

c. If you agree with a proposed minimum allowance amount, do you further agree that it should be determined on the basis of losses expected to occur within the foreseeable future (and no less than twelve months)? Why or why not? If you disagree, how would you prefer the minimum allowance to be determined and why?

d. For the foreseeable future, would the period considered in developing the expected loss estimate change on the basis of changes in economic conditions?

e. Do you believe that the foreseeable future period (for purposes of a credit impairment model) is typically a period greater than twelve months? Why or why not? Please provide data to support your response, including details of particular portfolios for which you believe this will be the case.

f. If you agree that the foreseeable future is typically a period greater than twelve months, in order to facilitate comparability, do you believe that a 'ceiling' should be established for determining the amount of credit impairment to be recognised under the 'floor' requirement (for example, no more than three years after an entity's reporting date)? If so, please provide data and/or reasons to support your response.

a. As commented to question 3, our members disagree with the floor proposed for the impairment on the good book. We don't understand the rationale sustaining the floor mechanism regarding the conceptual approach of the ED. Recognising a credit loss at inception (a day one loss) is not consistent with the recognition of loans (at market rate) in the financial statement of position at their initial fair value. Furthermore, it requires in practice two calculations for the impairment allowance. Therefore, we consider that the bad book specific

impairment method would be the appropriate floor of the whole impairment model. There is no need for a second floor mechanism on the good book that in practice may undermine the time-proportional approach (see Q10).

b. As an alternative to the proposed floor, the 9b proposal could be further explored by the Board even though we consider that the good book/bad book concept will address circumstances in which there is evidence of an early loss pattern.

c. One more reason why we disagree with the proposed floor mechanism: we consider that the calculation of the floor is not accurate enough, since the concept of "foreseeable future" is unclear and the judgement involved reduces comparability.

d. The concept of a floor may also cause additional volatility, because the predictability of expected credit losses depends on estimates about market conditions. In fact, during the financial crisis entities experienced difficulties in making long-term projections due to increased uncertainty. Therefore, we believe that the period considered in developing the expected loss estimate should change on the basis of changes in economic conditions. And we consider that the good book/bad book concept would address such circumstances

e. We believe that foreseeable future for credit impairment purposes may vary between different portfolios.

f. We do not support establishment of the floor nor the ceiling due to increased complexity and additional expected loss calculations. In addition, we believe that this increases operational challenges and system requirements

Question 10

Do you believe that the floor will typically be equal to or higher than the amount calculated in accordance with paragraph 2.1(a)(i)? Please provide data and/or reasons to support your response, including details of particular portfolios for which you believe this will be the case.

First of all, we would like to stress that in order to answer this question exactly a typical test scenario would have to be calculated.

However, we would expect that an entity's credit-risk management systems would capture bad loans from the good book on a timely basis and transfer those loans from the good book to the bad book. Therefore, we would assume that it would be an exception, if the floor will be higher than the time-proportional amount. Moreover, since we consider that the time-proportional approach is more economical than the immediate recognition approach (through the floor mechanism), we are concerned that it may not be often applied in practice. The floor, as currently proposed, could lead to generalize an approach which is not appropriate (see also our answers to Q3 and Q9).

Thus, EACB members generally do not support an impairment model with a floor.

Flexibility related to using discounted amounts

Question 11

The boards are seeking comment with respect to the flexibility related to using discounted amounts. Specifically, on the following issues:

a. Do you agree with the flexibility permitted to use either a discounted or undiscounted estimate when applying the approach described in paragraph B8(a)? Why or why not?

b. Do you agree with permitting flexibility in the selection of a discount rate when using a discounted expected loss amount? Why or why not?

a. EACB members agree that the entities should be allowed to use either discounted or undiscounted amounts depending which one is operationally applicable.

b. We agree that flexibility regarding the use and the selection of a discount rate should be maintained.

Approaches developed by the IASB and FASB separately

Question 12

Would you prefer the IASB approach for open portfolios of financial assets measured at amortised cost to the common proposal in this document? Why or why not? If you would not prefer this specific IASB approach, do you prefer the general concept of the IASB approach (ie to recognise expected credit losses over the life of the assets)? Why or why not?

Since the members of the EACB do not approve the introduction of a floor (see our answer to question 9), we would prefer the original IASB approach for open portfolios. Moreover, we also welcome the introduction of a partial catch-up approach.

The original IASB approach recognises expected credit losses over the life of the assets based on the separate allocation of interest revenues and expected credit losses. In practice, it would solve the current timing mismatch between the recognition (as revenue) of the credit risk premium included in the interest charged to the borrower and the recognition of the related credit losses. This explains notably our disagreement on the minimum allowance amount (see Q9).

Question 13

Would you prefer the FASB approach for assets in the scope of this document to the common proposal in this document? Why or why not? If you would not prefer this specific FASB approach, do you prefer the general concept of this FASB approach (i.e. to recognise currently credit losses expected to occur in the foreseeable future at or after the first reporting date after initial recognition of the financial assets)? Why or why not?

EACB members generally consider that the FASB approach to recognise expected credit losses for the foreseeable future in the first reporting period, does not meet the economic conditions of credit transactions and the link between expected losses and the pricing of credit transactions. In particular, it is not clear how the concept of foreseeable future would be defined. E.g. it might depend on how reliable market conditions are estimated by an entity. In this respect we fear that a lack of comparability and a lot of volatility would follow.

Moreover, as explained in our answer to Q10, we expect that the floor mechanism would lead in many cases to apply only the FASB specific approach. The FASB approach would require recognizing losses in the first period of reporting which is inconsistent with the timing recognition of the credit risk premium as revenue. As mentioned in our answer on Q12, EACB members rather prefer the IASB specific approach, which is more economical (see Q12).

Therefore, EACB members do not support the FASB approach.

IASB only Appendix Z

Impairment of financial assets

Question 14Z

Do you agree that the determination of the effective interest rate should be separate from the consideration of expected losses, as opposed to the original IASB proposal, which incorporated expected credit losses in the calculation of the effective interest rate? Why or why not?

EACB members agree with the proposed expected cash flow model which is based on separate allocation (decoupling) of interest revenues allocated using EIR as currently defined in IAS 39 and expected credit losses as it is simplified and operationally more feasible. In fact, we consider separate calculation of both components as absolutely necessary, since a linkage between expected losses and effective interest rates could not be implemented because of the differing databases concerned. Therefore, decoupling, as proposed by the supplement document, constitutes a major simplification compared to the approach contained in the original exposure draft.

Scope – Loan commitments and financial guarantee contracts

Question 15Z

Should all loan commitments that are not accounted for at fair value through profit or loss (whether within the scope of IAS 39 and IFRS 9 or IAS 37) be subject to the impairment requirements proposed in the supplementary document? Why or why not?

Generally, for risk management purposes, EACB members all consider that the risk from loans should be managed on the same basis.

However, on this issue, EACB members have different views. Some members agree that, under the proposed approach, loans and loan commitments should have the same impairment treatment based on expected losses. Others think that it is appropriate to carry forward the existing rules.

Question 16Z

Would the proposed requirements be operational if applied to loan commitments and financial guarantee contracts? Why or why not?

EACB members agreed that for risk management purposes, the same impairment model should be applied for financial guarantees and for loans and loan commitments. However, EACB members have different views (see our response to question 15) whether it should be subject to the impairment requirements proposed in the supplementary document, or whether the rules under the current regime for financial guarantees should be carried forward to IFRS 9.

Presentation (paragraph Z5)

Question 17Z

Do you agree with the proposed presentation requirements? If not, what presentation would you prefer instead and why?

EACB members agree with the new presentation proposal that includes only two line items in the statement of comprehensive income i.e. gross interest revenue and impairment.

Disclosure (paragraphs Z6–Z15)

Question 18Z

(a) Do you agree with the proposed disclosure requirements? If not, which disclosure requirements do you disagree with and why?

(b) What other disclosures would you prefer (whether in addition to or instead of the proposed disclosures) for the proposed impairment model and why?

As long as the Basel Committee Approach towards impairment that banks must use for risk management purposes may be also used for reporting according to ED/2010/12, EACB members generally agree with the disclosure requirements except for the disclosures relating to the minimum allowance amount.

However, should the IASB impose a method to calculate expected losses, which differs materially from the Basel approach, EACB members would like to stress the following remarks:

i. General considerations when implementing a method to determine expected losses which differs from internal risk management practice

EACB members generally criticize a method of determining expected losses, which is not based on internal risk management practice. We think that such a method would cause quantitative disclosures to be not adequately in accordance with internal risk management practice.

The supplement would, required quantitative disclosures, which are based on the IASB's specific expected loss approach, (see Z7, Z8). However, there is a reference to the internal risk management approach. Paragraph Z6 provides an example of the formation of classes, which is in analogy to IFRS 7.6. Information, which would have to be provided in this case, would be only available to internal risk management. Therefore, this information could not be derived from the balance sheet directly.

Beyond that, Z14 and BZ20 require disclosures, which are based on regulatory information. The notions of "exposure at default" and "loss given default", which are relevant in that respect, are also available to internal risk management, but cannot be derived from the balance sheet as well.

Therefore, when implementing an approach that would be based on a model differing from internal risk management requirements, the aim of disclosing decision-useful information would not be met.

Moreover, quantitative information, which is produced for external accounting purposes only under the IASB's model, would be reported side-by-side with differing information based on internal risk management (see Z13 and Z15, BCZ100 and BCZ102).

Thus, EACB members fear that whether all information disclosed would be based on internal risk management only, disclosure would be misleading.

ii. Back testing

Z12 of the supplement requires disclosures about back testing of credit risk for loans, which are categorised as measured at cost. Since internal risk management does not divide the loan portfolio according to external accounting categories, information would have to be provided for external reporting purposes only. Thus, this information would not be useful for internal risk management purposes.

Moreover, this criticism is equally true for the required disclosure about credit risk stress testing (see ED/2009/12.20, B26 and BC60). In this respect, we would like to recall that the staff of the IASB recommended to not implementing such disclosures (see Staff Paper, Meeting 14.02.2011, paragraph 20).

Therefore, EACB members think that an equal treatment should be considered for Z 12 as well.

iii. Relation to IFRS 7

EACB members recommend to harmonize the disclosures of the supplement and IFRS 7 which correspond.

Moreover, we think that the following disclosures of the supplement, which go beyond or differ from those of IFRS 7 should be carried forward to IFRS 7:

- Credit risk Management (Z13 and Z15, BCZ100 and BCZ102; equals IFRS 7.33b-c,. IG15)
- Rating methods (Z15; equals IFRS 733, IG24-25)
- Structure of the credit portfolio (Z14; equals IFRS 7.36c and IFRS 7.37b)
- Risk allowance table (Z7; equals IFRS 7.16)

iv. Placement of Disclosures

EACB members would welcome the possibility, set out in Z17, to make the disclosures required outside the notes. This notably equals IFRS 7.B6 and

allows to collect risk management reporting in the management assessment.

Question 19Z

Do you agree with the proposal to transfer an amount of the related allowance reflecting the age of the financial asset when transferring financial assets between the two groups? Why or why not? If not, would you instead prefer to transfer all or none of the expected credit loss of the financial asset?

EACB members think that the rules concerning the transfer of financial assets between the good book and the bad book should be feasible. In case of loss event, when a loan must be transferred from the good book to the bad book, it should be possible to transfer the full allowance previously established for the portfolio. Incurred losses are the materialisation of expected losses, so expected loss allowances are built up to be used.

However, we think that there should be an option regarding the transfer of allowance. Since the expected loss method is based on a concept of portfolio loss mutualisation, it seems easier to have the option when an asset is transferred, to leave the allowance in the good book and recognize the entire loss in the bad book. This approach seems to be less burdensome according to some of our members accounting logic.