Comment Letters
IASB
30 Cannon Street
London EC4M 6XH
United Kingdom

Paris, 5 July 2013

RE: Exposure Draft Financial Instruments: Expected Credit Losses

Dear Sir / Madam,

We are pleased to comment on the Exposure Draft Financial Instruments: Expected Credit Losses, published by the IASB in March 2013.

General comments

We recognise the IASB’s determination and time spent in developing a new impairment model which would take into account expected credit losses and would therefore ensure an earlier and timelier recognition of credit losses. We also acknowledge that this is a complex, sensitive and crucial issue (especially for financial institutions) on which consensus is hard to establish.

We consider the general direction taken by the IASB is a right step forward. In particular we believe that it addresses the weaknesses of the current impairment model under IAS 39 that was severely criticized during the recent financial crisis such as the ‘too late and too abrupt’ phenomenon. We acknowledge as well the IASB’s efforts in trying to achieve an operationally feasible model, by means of introducing simplified models and other simplifications/exceptions when compared to the previous proposals.

We support the Board’s decision to maintain a dual measurement approach. We also agree with the proposal that entire expected lifetime losses shall be recognised for assets classified in the higher risk category, but not for all instruments. In this respect, we thus strongly disagree with the FASB proposal since recognising full EL from the outset would generate potentially significant ‘Day One’ losses which in our opinion would not faithfully reflect the underlying economic reality of the instruments impaired.
We also welcome the proposal to align the impairment approaches for on-balance sheet debt instruments (including loans and bonds in the FV-OCI category) and also financial guarantees and loan commitments, since all these instruments undergo similar credit risk management processes.

Nevertheless, we consider that the proposed model should be further developed in order to address the remaining difficulties, in particular when it comes to the criteria for transfer between stage 1 (12-month expected losses measurement objective) and stage 2 (lifetime expected losses measurement objective). We are concerned that the tracking of credit risk over time will not be simple on the operational side, and that some entities may decide to interpret the proposed transfer criterion in a more restrictive manner than that currently intended by the IASB. In particular, preparers may be tempted to circumvent the tracking constraint by automatically transferring into Stage 2 any instrument that is ‘below investment grade’ as of reporting date. In this regards, it is crucial that the Board clarifies the reference to the “investment grade” as being an internal threshold which may be different from one business line to another.

Furthermore, we do not agree with recognising ‘Day One’ losses that would result from applying the 12-month expected losses measurement objective for instruments in stage–1 upon their initial recognition. Indeed, such accounting impacts would have no conceptual foundation as they are disconnected from the economic performance of financial instruments. Nevertheless, we understand that the Board is proposing such impairment measurement principle for stage-1 instruments as a practical expedient for the operational merits of such an approach. We encourage the IASB to carry out further outreach to provide more arguments on whether alternative measurement objectives for stage-1 instruments without Day One losses – such as time-proportional approach as proposed in the Supplementary Document (“SD”) of 2011 (but without the foreseeable future floor) – are or are not acceptable from an operational point of view.

We also have concerns about the complexity that the proposed model (and especially the requirement to calculate lifetime expected losses) would introduce for trade receivables and recommend that these assets continue to be impaired according to the existing incurred loss model of IAS 39.

Our detailed answers to the questions raised in the Exposure Draft and some additional comments are provided in the appendices attached to this letter. Please note that we have slightly changed the order of the first two 2 questions so as to permit the grouping of questions by subject (general approach proposed in the 2013 exposure draft, comparison with the proposed FASB model etc.).

Please do not hesitate to contact us should you wish to discuss any aspect of our comment letter.

Yours sincerely,

Michel Barbet-Massin

Head of Financial Reporting Technical Support
Appendix: Detailed answers to questions raised in the Exposure Draft
Financial Instruments: Expected Credit Losses

The main provisions of the general impairment model based on two distinct measurement objectives proposed by the IASB in the Exposure Draft of 2013 (2013 ED)

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?
...

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?
...

We agree that the new model on impairment should be based on expected credit losses and that it should have two distinct impairment measurement patterns as we are convinced that this approach is consistent with the way most entities manage their credit risk exposure. We also agree with the approach proposed for the second and third stages where the entire lifetime expected losses would be provisioned. These underlying principles, which are complemented with operational simplifications, should assure that the new approach to impairment is viable and sustainable.

However, we are of the opinion that the proposed approach will not reflect the economic link between the pricing of financial instruments and its credit quality at initial recognition. We consider that the recognition of Day One losses for stage-1 instruments has no conceptual basis and misrepresents the economic reality of the transactions. It seems to us that the time-proportional approach for recognising credit losses on good book assets (without the foreseeable future floor) in the 2011 SD provided a better representation of the financial performance of the entity (please refer to our comment letter to the SD for further details).

However, we agree that the proposed approach for stage-1 instruments is simple and helps to address the criticisms regarding delayed recognition of credit losses under IAS 39.

Therefore, in our opinion, this 2013 proposal could be an acceptable compromise if the Board is convinced that it is in practice operationally simpler to implement than the SD approach.

Regarding the proposed Transfer criteria, please refer to our answer to question 5.
Comparison with an alternative model (as currently proposed by the FASB) with impairment amount based on Lifetime expected losses at all times

**Question 1**

... (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?

**Question 2**

... (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?

We strongly disagree with a model where the impairment amount is based on lifetime expected losses starting from initial recognition. Such a model does not provide for any symmetry between the recognition of credit losses and credit risk related revenue. Besides, it is likely to have perverse effects on the economy in discouraging the lending activity of banks (especially to counterparties that have lower risk ratings) due to potentially significant ‘Day One’ losses that each new loan would generate.
Comparison with the previous draft proposals on impairment

Question 2

... (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)?

We consider that the impairment and revenue recognition model proposed by the IASB in the exposure draft of 2009 was by far the most ‘pure’ approach from the conceptual point of view, allowing for a real symmetry between the pattern of recognition of credit losses and credit risk related revenue. However, we understand the concerns that it would have been extremely complex to implement in practice. Given that there are several operational simplifications in the approach proposed in the 2013 ED (and in particular, decoupling between credit loss and interest revenue recognition), we consider that it strikes a better balance between the faithful representation of the underlying economics and the cost of implementation than the 2011 ED.

When it comes to comparing the 2013 ED with the approach proposed in the Supplementary Document (“SD”) published in 2011 (but without the foreseeable future floor), the conceptual and operational advantages of the new proposal over the 2011 SD are in our opinion less obvious. For instance, the 2011 SD approach already proposed to separate (‘decouple’) revenue and loss recognition on financial assets, and it was also based on two distinct impairment measurement objectives. The 2011 SD does not require the tracking of credit risk deterioration since initial recognition, but requires a transfer into the bad book following a change in the entity’s credit risk management objectives. We therefore consider that it is simpler to implement and would result in quite similar outcomes (i.e. timing of transfer) as those we expect under the 2013 ED since many entities change their risk management objectives as credit risk of assets deteriorates significantly.

Besides, assuming the foreseeable future floor is removed, the 2011 approach would also solve the ‘Day One’ loss issue as credit losses for stage 1 assets would be calculated using the Time Proportional Approach (TPA). We are conscious however that TPA calculation can be complex to implement.

For all these reasons we consider that additional outreach is necessary in order to get feedback on the real operational benefit of this ED over the 2011 SD.
Scope

Question 3
(a) Do you agree with the proposed scope of this Exposure Draft? If not, why not?

(b) Do you agree that, for financial assets that are mandatorily measured at FV-OCI 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 agree with including in the scope of this project both instruments that are already on the balance sheet (such as drawn-down loans, bonds etc.) and irrevocable loans commitments and financial guarantees in the scope of IFRS 9.

As explained in our comment letter on the Exposure Draft Classification and Measurement: Limited Amendments to IFRS 9 dated 5 April 2013, we are also in favour of aligning the impairment rules of debt instruments classified in the FV-OCI category with those applicable to assets in the Amortised Cost category. This will help ensure that the credit risk on identical assets is reflected in profit or loss identically, whatever the measurement basis applied to these assets (i.e. FV-OCI or amortised cost).

Stage 1 measurement objective under the general model (12-month expected losses)

Question 4
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?

We consider that preparers of financial statements are better placed than us to answer this question, but we have nevertheless carried some outreach whose findings are presented below.

Our understanding is that, although the prudential definition of 12-month Probability of Default is not currently perfectly aligned with the one which would be applied in accounting in application of the 2013 ED, there should be no major operational challenges for banks. However, measuring this 12-month expected loss will be more challenging for corporate entities (please refer to our answer to question 10).
Assessing when an entity shall recognize lifetime expected credit losses under the general model

Question 5

(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?

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

(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?

(d) Do you agree with the proposed operational simplifications [30 days past due, low credit risk], and do they contribute to an appropriate balance between faithful representation and the cost of implementation?

(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?

a) We support the Board’s proposal to recognise the full lifetime expected credit loss for any instrument classified in stage 2.

We also agree that the use of significant credit deterioration as a transfer criterion and the distinction between assets that have deteriorated in credit quality from those that have not would provide relevant information to the users of financial statements. Moreover, this ensures that no originated loans whatever their initial credit quality, would be impaired up to their full lifetime EL upon initial recognition.

b) We believe that the proposed guidance needs to be improved and clarified in order to prevent some unintended consequences.

For instance, the reference to an internal rating equivalent to the external rating of ‘investment grade’ in paragraph 6 should be clarified. We consider that this threshold should be based on internal credit risk management objectives only and may be different from one business line to another. For example, lending to SMEs is generally riskier (in terms of probability of default “PD”) than lending to large corporates. This difference in PD is often addressed by a reduction of the Loss Given Default (LGD) thanks to additional collateral requirements. Were a single absolute PD-based ‘investment grade’ threshold be maintained in the final text, most retail loans would probably automatically appear in stage 2 on the first reporting date following their origination.
Furthermore, we consider that the articulation between the main principle of "credit deterioration" and the proposed "low credit risk" simplification should be better explained to clarify whether the approach remains fully relative (as suggested in paragraph 5 of the exposure draft) or if an absolute approach could be an acceptable approximation / shortcut. Our understanding is that this shortcut is currently envisaged by many entities given the complexity of implementing the tracking of credit risk, in particular for open portfolios.

If the Board were to consider an alternative approach for the transfer criteria, we would recommend reverting back to the 2011 SD proposal in this regards as:
- it relies more on the actual risk management of the entity; and
- it seems consistent with the objective of tracking credit deterioration as most entities change their risk management objectives as the credit risk quality of the asset deteriorates.

Moreover, we have concerns regarding the tracking of credit deterioration at an open portfolio level. The exposure draft (§ B13-14, BfC§72) states that the remaining maturity has to be taken into account when comparing the probabilities of default at two different dates for the same instruments, since for example a PD to maturity which is constant over time would seem to indicate that the credit quality of the instrument has deteriorated since initial recognition. We have difficulties in visualizing how such monitoring may be carried-out at an open portfolio level, since this would virtually require the tracking of credit risk on an instrument-by-instrument basis. Moreover, the procedure of identifying individually deteriorated assets within a portfolio and the consequences from removing them from the portfolio should be clarified.

c) When it comes to the transfer from stage 1 to stage 2, we agree with the proposal that this assessment should be based on changes in the PD (probability of default) parameter rather than on changes in the amount of expected losses.

d) We find the operational simplifications proposed pragmatic and we consider that they will greatly diminish the cost of implementing the proposed model.

Nevertheless, we are afraid that the 30 days past due period might be deemed too short in some jurisdictions (in which late payment is a habitual and accepted practice), thus making it necessary to explain why the presumption does not apply for most instruments. It is therefore critical that this presumption be rebuttable based on the usual practice in the economic environment of the transactions.

Please also see our comments on the 'low credit risk’ simplification in section b) above.

e) We agree with the proposal that the general model should be symmetrical (permitting a 12-month expected-loss allowance to be re-established in case of improvement in credit quality) as this helps better reflect the evolution of exposure to credit risk over time.
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?

(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?

(c) Do you agree with the proposal that the interest revenue approach shall be symmetrical (i.e., 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?

We agree that, from a conceptual point of view, where the credit risk of an asset has deteriorated to such an extent that losses are being incurred, the recognition of interest revenue on the ‘gross’ basis is no longer appropriate as this would not reflect faithfully the economic performance of the asset.

We therefore welcome the introduction of two financial asset categories for interest revenue calculation purposes, and agree that a transfer from the interest revenue recognition on a ‘gross’ basis to the interest revenue recognition on a ‘net’ basis (after deducting the impairment allowance) should generally occur at a later date than the date of transfer from stage 1 to stage 2 for impairment allowance measurement purposes.

Given that information on the objective evidence of impairment (the occurrence of which would trigger the accounting for interest revenue on net basis) is already collected in existing accounting systems, we consider that the cost of implementing this approach should not outweigh the above-mentioned presentation benefit.

Furthermore, we agree that the model for recognising interest revenue should be symmetrical, i.e., that assets whose credit quality has first deteriorated and then improved to an extent where the recognition of contractual return is justified should be allowed to have the interest revenue recognised on a gross basis.

For more comments on revenue recognition aspects regarding financial guarantees, please refer to our specific answer to question 9.
Disclosures

**Question 7**
(a) Do you agree with the proposed disclosure requirements? Why or why not? If not, what changes do you recommend and why?

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

(c) What other disclosures do you believe would provide useful information (whether in addition to, or instead of, the proposed disclosures) and why?

In our opinion, the proposed impairment model will leave more room for judgement and subjectivity than the existing incurred loss model under IAS 39. This is related to the fact that determining of the measurement objective and of the expected credit loss amounts will inevitably require the use of judgement. As a result, thorough and focused disclosures will be necessary to ensure at least some comparability across entities. Nevertheless, in our view clarity, relevance and quality should be given priority over quantity when it comes to disclosures.

Some quantitative information requirements seem quite ‘heavy’ from an operational perspective, with potentially not so much value added in terms of usefulness of such information. This is for instance the case for the reconciliation from the opening balance to the closing balance required by paragraph 35 both for gross carrying amounts and for impairment allowances, which would imply distinguishing between the assets that were acquired or sold during the reporting period. In our opinion, a simpler reconciliation of solely the impairment allowance amounts would be sufficient.

Another example is that of discount rates (expressed in percentage) as proposed in § 39d ii: in our opinion, information on discount rates used should be principles-based, with entities providing a range of main discount rates used rather than a complete list of discount rates. Furthermore, the illustrative example provided in § 1E73 seems to suggest that the requirement in paragraph 44 to disclose the allowance amounts by credit rating refers to external credit rating of each counterparty whenever such ratings are available. We recommend the Board to clarify the content of information required by § 44.

We provide below some additional disclosures that we believe the Board should consider:

- preparers could provide information on the differences between the losses expected by the entity on the date of the transfer to Stage 2 (requiring the provisioning of lifetime expected losses) and the actual final realised losses. This information would help the users of financial statement assess the quality of the entity’s loss expectations.

- we wonder why no information is required on assets for which interest revenue is calculated on a net basis, following an incurred loss event. Such information would act as a “bridge” between the expected loss and incurred loss dimensions.
The Board could also consider the possibility of providing two sets of disclosure requirements, with a less extensive list of disclosures applying to entities which are not exposed to significant credit risk. This could be achieved, for example, by establishing a list of minimum information requirements for all entities, and adding a list of supplementary information that has to be provided by entities with significant credit risk exposures. We note that the Board already proposes some disclosure exemptions for some trade and lease receivables in § 33, but in our opinion similar simplifications should be allowed for entities for which credit risk is not a material issue, whatever the type of instruments held by such entities.

Furthermore, it is also important to make sure that there is no overlap between the current disclosure requirements in IFRS 7 and the newly proposed disclosures on impairment methods and impaired assets under the 2013 ED.
Application of the model to assets that have been modified but not derecognized

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 agree with the approach proposed for modified assets.

However, we are concerned that, given the lack of guidance in IAS 39 and IFRS 9 on how the derecognition analysis should be performed for modified assets, the application of the proposed approach might lead to some unintended consequences.

To illustrate the potential consequences of non-aligned derecognition rules for modified assets we have set out the following example. Assuming an identical renegotiation of two similar loans originated by two banks to the same debtor takes place, the accounting consequences of this renegotiation might be quite different depending on the derecognition policy of each entity:

- Bank A, having a low threshold for what it considers as a ‘substantial change in contractual terms’, might conclude that a derecognition event has taken place. On the next reporting date, this entity will probably be able to classify the ‘newly recognised’ asset as a stage-1 asset (supposing no significant deterioration in credit risk takes place between the date of modification and the reporting date), and therefore impair it on the basis of 12-month expected losses.

- On the other hand, Bank B which has a higher threshold for derecognition might conclude that a derecognition event has not occurred and therefore maintain the ‘old’ asset on its balance sheet. Furthermore, if a significant deterioration in credit quality has taken place since the initial recognition of the asset, this bank will be obliged to classify this asset into stage 2 of the general impairment model (which requires the provisioning of the entire lifetime expected losses) and therefore it will probably record higher impairment losses than Bank A described above (even through the economic substance of the modification is strictly identical).

In our comment letter dated 10 July 2012 in response to the tentative decision of IFRS IC regarding the issue ‘Accounting for different aspects of restructuring Greek Government Bonds’, we agreed with the view of the IFRS IC that there were several approaches to analysing restructuring of assets and we urged the IFRS IC and the IASB to consider clarifying the accounting treatment of financial assets’ modifications/ restructurings either through a limited amendment to IAS 39 or as part of the finalisation of IFRS 9 Financial instruments. In relation to the new proposals on the impairment of modified assets, we therefore reiterate this demand, in order to tackle with modified assets in a more comprehensive manner and to prevent unintended consequences.
Application of the model to loan commitments and financial guarantee contracts

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?

(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.

We agree that financial guarantees and loan commitments in the scope of IFRS 9 which are not fair valued through P&L should follow the same impairment rules as on-balance sheet loans and debt securities which are exposed to credit risk, since banks use similar credit risk management processes for all these instruments.

Nevertheless, for loan commitments, we are concerned that it might be quite complex to assess the draw-down scenarios (credit conversion factor) within 12 months of the reporting date or during the entire remaining life to maturity (depending on the measurement objective applicable) on an instrument-by-instrument basis. Additional guidance on this issue (clarifying, for instance, whether draw-down estimates should or could be based on past experience and statistical data) would be helpful.

Finally, we wonder whether this was the Board’s intention not to deal with the revenue recognition aspects regarding financial guarantees. Were the Board to maintain the proposal on accounting for financial assets interest revenue (i.e. slowing down of revenue recognition as soon as the instrument is impaired as defined in IAS 39), it would seem to us that a similar principle should apply as well on the financial guarantee side because fees received on such instruments are 100% related to the cost of taking credit risk.
Exceptions to the general model

Question 10
Simplified approach for trade receivables and lease receivables

(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?
(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 appreciate and welcome the Board’s efforts in solving some of the practical implementation issues that will be faced (mostly) by corporates by introducing the simplified approach for trade receivables. However, we deem that even this approach will be overly complex for entities which do not manage their risk exposure resulting from trade receivables by using lifetime EL estimates. We would like to suggest excluding trade receivables from the proposed general model and retaining current IAS 39 principles, based on incurred loss calculations using statistical data (incurred but not reported losses (“IBNR”)) exclusively for the impairment of trade receivables in the finalised IFRS 9 standard.

However, if the IASB nevertheless maintains the proposed approach in the final text, we believe it should be more clearly stated whether the use of a provision matrix is permitted solely under the simplified approach or also for ‘long-term’ trade receivables to which the entity applies the general impairment model.

- Paragraph B35 of the ED seems to indicate that the IASB’s intention was to permit this practical expedient for both approaches,

- But we are confused by paragraph § 44 (which makes reference to § 12 which defines the simplified approach) which permits disclosures on credit risk based on provision matrices only for assets impaired under the simplified approach.

We agree with the proposal that trade receivables that do not have a significant financing component should be measured at their transaction price upon their initial recognition.

However, when it comes to lease receivables, we are of the opinion that more time should be given for preparers in order to clearly identify and understand the interactions between this ED and the proposals of the exposure draft on Lease contracts published in May 2013. As such the Board should consider re-exposing this limited issue at a later date.
Question 11
Financial assets that are credit-impaired on initial recognition
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?

Yes, we agree with this approach as it avoids the recognition of ‘Day One’ losses on such assets and thus the accounting more faithfully represents the fact that initial credit loss expectations have been incorporated in the acquisition price of the asset.

Effective date and transition

Question 12
(a) What lead time would you require to implement the proposed requirements? Please explain the assumptions that you have used in making this assessment. As a consequence, what do you believe is an appropriate mandatory effective date for IFRS 9? Please explain.

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

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

Given the significant system changes that the proposed impairment model would seemingly require, we recommend a lead time of a minimum of 3 years after the entire IFRS 9 standard has been finalised by the IASB. Supposing IFRS 9 is finalised by the end of 2013, the mandatory application date of IFRS 9 should in our opinion be postponed to 1st January 2017 or a later date.

We agree with the proposed relief from restating comparative information on transition.

Nonetheless, we would like to draw the Board’s attention to the consequences that the proposed transition requirements and in particular the proposed exception to the retrospective application of the transfer criterion described in paragraph C2a of the exposure-draft might entail. Indeed, the use of term ‘investment grade’ throughout the 2013 ED when referring to assets of ‘low credit risk’ might imply that, for instance, many loan portfolios of retail banks for which information on the initial credit quality is not available upon transition will potentially have to appear in Stage 2 until the derecognition of such instruments because of the higher inherent risk in retail business. Retail banks would therefore be unduly penalised as lifetime losses would probably be recognised for such loans. We therefore encourage the Board, as already explained in our answer to Question 5, to add an explicit statement in the final text that there is no single definition of ‘low credit risk’ and that the rating level for distinguishing between ‘low’ and ‘high’ credit risk instruments may differ from one business line to another.
Effects analysis

Question 13
Do you agree with the IASB’s assessment of the effects of the proposals? Why or why not?

We agree with the IASB’s analysis that the implementation of the proposed approach is likely to result in an increase in the loss allowance balance and also in a timelier recognition of credit losses, although the cost and effort involved in implementing and operating the model should not be underestimated.