INSTITUTE OF INTERNATIONAL FINANCE

International Banking Federation

September 18, 2015

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Re: IIF-IBFed Comments on EDTF draft report – Impact of ECL approaches on bank risk disclosures

Dear Messrs.,

The Associations (the Institute of International Finance (IIF) and the International Banking Federation (IBFed)) and their member institutions very much welcome the opportunity to comment on the EDTF draft report, "Impact of ECL approaches on bank risk disclosures."

In the context of the new and forthcoming Expected Credit Loss (ECL) impairment standards of the IASB and the US FASB, in order to achieve greater consistency and comparability of disclosure across internationally active banks, the Associations welcome the fact that the EDTF has been mandated to establish recommendations on public disclosures relevant to the standards. The Associations understand the EDTF's commitment to users' needs and interests, and to avoiding information overload or unduly voluminous disclosures that users might ultimately ignore as not being decision-useful information.

The Associations appreciate the quality of the work done by the EDTF and are in agreement that high quality disclosure when introducing ECL-based provisioning will be particularly important as the accounting will include a greater degree of management judgement; model based provisioning is

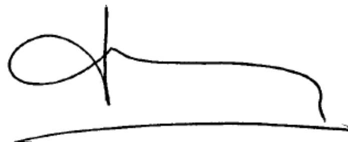
inherently complex; and the requirements for the calculation of accounting ECL will differ from those for regulatory Expected Loss (EL) for capital purposes.

The Associations support the EDTF document in that it provides new guidance on (a) the applicability of its existing fundamental EDTF risk disclosure principles; (b) the application of the existing 32 recommendations; (c) where necessary, additional considerations to apply the recommendations in the context of an ECL framework, including both temporary considerations which will cease to apply following the transition to the ECL framework, and permanent considerations; and (d) further guidance on application of these additional considerations specifically to IFRS 9. Nonetheless, some specific comments and suggestions have been marked directly into the proposed draft for your consideration. Those areas include suggested wording to:

- enhance users' awareness on the degree of change implied by the new accounting standards within each banking organization;
- clarify the EDTF proposal on the use of sensitivity analysis;
- clarify the definition of adjustments as part of the collective assessment of ECL; and
- strike the right balance between the information need and the way to present it to ensure that enough flexibility is left for preparers faithfully to depict each bank's individual business model in accordance with accounting standards.

Finally, the Associations understand that the EDTF has committed to sharpening up the distinction between temporary and permanent recommendations and commentary, which is also a critical issue for members.

Very truly yours,



David Schraa
Regulatory Counsel
IIF

Hedwige Nuyens
Managing Director
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Consolidated comments

9/18/15

IMPACT OF ECL APPROACHES ON BANK RISK DISCLOSURES

Report of the
Enhanced Disclosure Task Force

[X October 2015]

ENHANCED DISCLOSURE TASK FORCE

X October 2015

Mr. Mark Carney, Chairman
Financial Stability Board
Bank for International Settlements
Centralbahnplatz 2
CH-4002 Basel
Switzerland

Dear Mr. Carney,

On behalf of the Enhanced Disclosure Task Force (EDTF), we are pleased to present you with our report, [*Title as Front Cover]*.

- .....
- ......

Sincerely,

Ralf Leiber Russell Picot Christian Stracke

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1. Introduction

The EDTF and its role in enhancing disclosures

The Enhanced Disclosure Task Force (EDTF) was established by the Financial Stability Board (FSB) in May 2012. The EDTF aims to improve the quality, comparability and transparency of risk disclosures by uniquely bringing together a broad spectrum of private sector participants including banks, investors, analysts and auditors.

Over the last few years, accounting standard setters have been developing standards that will require banks to adopt new approaches for measuring and accounting for credit losses. In part, these changes respond to requests by the FSB and the G20 during the financial crisis, consistent with a widely shared view that the impairment methodologies should incorporate a broader range of credit information.

The International Accounting Standards Board (IASB) introduced a new credit-impairment approach in International Financial Reporting Standard 9 *Financial Instruments* (IFRS 9) issued in 2014 to replace International Accounting Standard 39 *Financial Instruments: Recognition and Measurement*. The US Financial Accounting Standards Board (FASB) has substantially completed re-deliberations on its credit impairment standard with issuance of a revised standard expected later in 2015. Although the new impairment approaches are expected to differ in some details, both are based on the concept of measurement of expected credit losses (ECL).

To promote high quality implementation of these new accounting standards, the Basel Committee on Banking Supervision (BCBS) is finalising guidance on accounting for expected credit losses.

Given the importance of these changes to banks, the FSB requested the EDTF to consider disclosures that may be useful to help the market understand the upcoming change in provisioning based on ECLs (whether under US Generally Accepted Accounting Principles (US GAAP) or International Financial Reporting Standards (IFRS)) and to promote consistency and comparability.[1]

The EDTF is not a standard setter nor does it seek to provide accounting or disclosure requirements. Instead, it aims to help the users of financial statements better understand the risks taken by banks, through supporting banks in ensuring such risks are properly reflected in their financial statement and risk disclosures. The EDTF also aims to achieve greater consistency and comparability of disclosures across internationally-active banks. High quality disclosure when introducing ECL based provisioning will be particularly important as the accounting will include a greater degree of management judgement, model based provisioning is inherently complex and the requirements for the calculation of accounting ECL will differ from those pertaining to regulatory Expected Loss (EL) for capital purposes.

IFRS 9 requires an entity to base the measurement of its credit impairment allowance on ECL using a three-stage impairment approach. This applies to debt instruments measured at amortised cost as well as at Fair Value Through Other Comprehensive Income, although for Fair Value Through Other Comprehensive Income only the impairment charge is recognised in profit or loss since fair value is recognised on balance sheet. The amount of ECLs recognised depends on the extent of credit deterioration since initial recognition as follows[2]: a) "12-month ECLs" (Stage 1), which applies to all items (from initial recognition) as long as there is no significant increase in credit risk; and (b) "Lifetime ECLs"

[1] This discussion applies only to banks subject to ECL requirements under IFRS or US GAAP (or other equivalent standards). Banks not subject to ECL requirements need not take this ECL-specific discussion into account but should continue to consider the original EDTF principles and recommendations in preparing their risk disclosures.

[2] Excluding purchased or originated credit impaired financial assets and financial assets to which the simplified approach (IFRS9 5.5.15) is applied (e.g. trade receivables, lease receivables).

(Stages 2 and 3[3]), which applies when a significant increase in credit risk has occurred, whether assessed on an individual or collective basis. The assessment of a significant increase in credit risk and the measurement of ECL must be based on "reasonable and supportable information that is available without undue cost or effort," and must reflect historical, current and forward-looking" information. IFRS 9 is effective for annual periods beginning on or after 1 January 2018,[4] with early application permitted.

The FASB is expected to replace its existing incurred loss approach with a current expected credit loss (CECL) one which requires entities to measure credit impairment allowances based on lifetime ECLs for all loans and other debt instruments measured at amortised cost. The FASB has not yet determined an effective date, but it expects to issue a final standard during the second half of 2015. While the FASB's decisions on impairment may differ from the IASB's, both are expected to use ECL concepts.

Building on existing EDTF principles and recommendations

In the context of the new and forthcoming impairment approaches, the EDTF seeks to provide guidance on (a) the applicability of its existing fundamental principles; (b) the application of its existing recommendations; (c) where necessary, additional considerations to apply the recommendations in the context of an ECL framework including both temporary considerations which will cease to apply following the transition to an ECL framework and permanent considerations which will continue to apply following ECL framework adoption; and (d) further application of these additional considerations specifically to IFRS 9.

The guidance is framed in terms of the existing EDTF principles and recommendations in the 2012 report.[5] The new accounting requirements should result in banks reconsidering their implementation of the 2012 report in light of key matters of interest to users resulting from ECL accounting.

Scope of recommendations and disclosure frequency and location

The scope of the recommendations and the recommended frequency and location of disclosures are consistent with the EDTF's 2012 report as summarised below.

The fundamental principles are applicable to all banks. The EDTF has developed the recommendations and associated considerations with large international banks in mind, although they should be equally applicable to banks that actively access the major public equity or debt markets. Some of the recommendations, therefore, are likely to be less applicable to smaller banks and certain subsidiaries of listed banks and the EDTF would expect such entities to adopt only those aspects of the recommendations that are relevant to them. This report was not specifically developed for other types of financial services organisations, such as insurance companies, though the fundamental principles and recommendations contained herein may provide some appropriate guidance.

This report has been produced in the context of the existing legal and regulatory requirements for banks' public reporting. The EDTF believes that certain risk disclosures in relation to ECL accounting approaches should be made more frequently than in annual reports and therefore could be included within interim reports. Specific recommendations have been made in relation to timing of transition disclosures following the initial adoption of the relevant accounting standard.

In making its recommendations, the EDTF generally does not specify where any new disclosure should be made, nor does it suggest that banks change the current location of their reported information when adopting the enhancements. Banks should retain appropriate flexibility in ~~what~~where they choose to disclose information in their annual reports and other filings, such as their Pillar 3 reports, within regulatory requirements.

[3] Stages 2 and 3 represent items that are not credit impaired and are credit impaired respectively
[4] Subject to endorsement by the European Union for banks within this jurisdiction
[5] A copy of the 2012 EDTF report is available at: http://www.financialstabilityboard.org/source/edtf/

Areas of focus in light of expected loss provisioning

Credit provisioning is a key aspect of a bank's performance and the related disclosures are important to users. The expected loss approach is expected to increase the credit loss allowances on transition compared to the existing approach for many banks, and users will want to understand the specific reasons for changes in provisions. Key areas of focus include:

- Concepts, interpretations and policies developed to implement the new ECL approaches, including the significant credit deterioration assessment required by IFRS 9;
- The specific methodologies and estimation techniques developed;
- The impact of moving from an incurred to an expected credit loss approach;
- Understanding the dynamics of changes in impairment allowances and their sensitivity to significant assumptions;
- Any changes made to the governance, processes and controls over financial reporting, and how they link with existing governance, processes and controls over other areas including credit risk management and regulatory reporting; and
- Understanding the differences between the accounting ECLs and regulatory capital EL.[6].

Since the areas of focus are broad and impairment allowances are a key component of a bank's performance and financial position, it will be important that the disclosure is appropriately targeted at material aspects, particularly the more significant portfolios and those factors and risks that create variability in their expected credit loss measurements.

Extent of required internal changes

Users should be aware that the ECL approach requires substantial internal changes within banks, including extensive data, systems, and procedural changes. These changes require substantial resource investments, and require integration of additional skill sets and new procedures to inform the increased use of judgement and forward-looking information that is required. Banks will need to go through a disciplined process of adjustment, data improvement, and development before the implementation of full ECL provisioning. The challenges are substantial for all banks, but smaller and emerging-market banks may have special challenges given constrained resources.

Once ECL requirements are fully in force, the use of forward-looking information (including macroeconomic factors), modelling and judgement that ECL requires will continue to inform the process and will result in somewhat different applications and outlooks by banks. Each bank's provisioning will therefore reflect such specific internal processes.

During transition and on an on-going basis, achieving comparability in ECL disclosures among different banks will be a particular challenge given the level of judgment involved in estimating provisions under the new standards, the differences between IFRS 9 and CECL, and differing business models, risk approaches and appetites between banks. By providing clear and sufficiently granular explanations about the concepts and estimation techniques used, banks can improve comparability. Users, however, will need to understand and adapt to the inherent limitations on comparability of forward-looking provisioning standards.

Gradual and phased approach and the aim to enhance comparability

The EDTF has extensively discussed the timing of providing disclosures in the transition period. Given the changes ~~introduced by the ECL approach, which require extensive data, systems and procedural~~

[6] BCBS is currently reviewing the interaction of ECL accounting with the current Basel Accord. The results of this review and related proposals, if any, are not expected to be published until mid-2016.

~~changes within banks~~within banks necessitated by the switch to ECL accounting, a gradual and phased approach during the transition period (which is expected to be generally consistent for IFRS 9 and CECL) would be most useful to users, to give them clearer insights into the likely impacts of the new standards as they develop and to allow increasing comparisons between banks. The initial focus should be on qualitative disclosures. Quantitative disclosures should be added as soon as practicable and reliable[7] impacts can be determined and, at the latest, in 2017 annual reports. A gradual and phased approach means that: (a) the initial timing of information being provided, whether qualitative or quantitative, should be weighed against reliability; and (b) the nature and extent of disclosures will expand over time.

The timing of providing disclosures to reflect the EDTF recommendations in their external reporting is likely to vary between banks due to differences in their individual timetables for developing and implementing ECL provisioning.

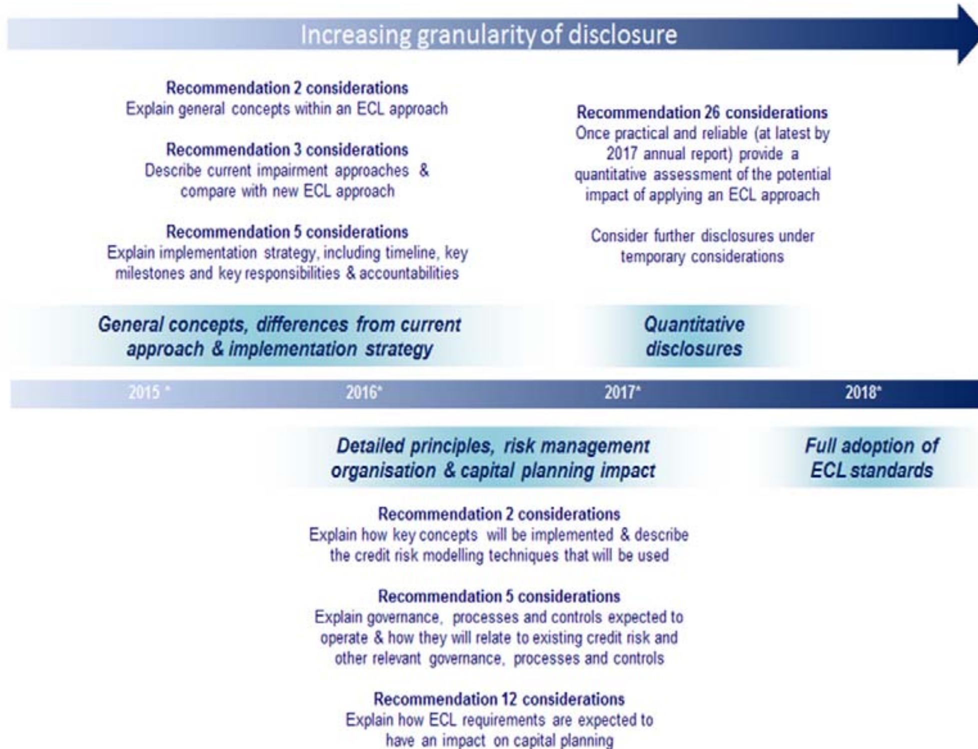
The information provided during the transition phase should be reliable and as comparable as possible.

~~During transition and on an ongoing basis, achieving comparability in ECL disclosures among the different banks will be a particular challenge given the extensive judgment involved in estimating provisions under the new standards, the differences between IFRS 9 and CECL, and differing business models, risk approaches and appetites between banks. By providing clear and sufficiently granular explanations about the concepts and estimation techniques used, banks can improve comparability. Users, however, will need to understand and adapt to the inherent limitations on comparability of forward-looking provisioning standards.~~

The discussion about timing has been framed in terms of banks with December year ends that are required to apply the new accounting standards from 1 January 2018. Banks with other year ends and implementation dates are expected to adapt the indicative timeline as necessary for their circumstances.

[7] The use of the term "reliable" in this Report is meant to be consistent with the term "reasonably estimable" as envisaged by IFRS and other securities regulators.

The following figure provides an indicative timeline that banks should consider for implementing the existing EDTF recommendations in light of ECL approaches.



2. Applicability of existing EDTF fundamental principles

The volume and complexity of banks' reporting has continued to increase in recent years, which has proved challenging for users seeking to understand the most significant items reported. The EDTF believes that increased volume of disclosure at the expense of clarity is unlikely to be helpful. Indeed, an emphasis on clarity of disclosure was captured in Principle 1 within the EDTF's existing seven fundamental principles for risk disclosures from their 2012 report which are as follows:

1. Disclosures should be clear, balanced and understandable.
2. Disclosures should be comprehensive and include all of the bank's key activities and risks.
3. Disclosures should present relevant information.
4. Disclosures should reflect how the bank manages its risks.
5. Disclosures should be consistent over time.
6. Disclosures should be comparable among banks.
7. Disclosures should be provided on a timely basis

After consideration of all existing principles the EDTF concluded that the introduction of ECL based provisioning would not create the need for any additional principles. However existing principles should be carefully considered by preparers of financial statements as discussed below.

Application to an ECL methodology

The EDTF reviewed the applicability of the existing principles against the new and forthcoming ECL requirements and it was emphasised that it will be more challenging for users to understand ECL measurement compared to existing incurred loss measurement. The reasons for this include:

- All lending will have an allowance, not just impaired loans.
- There will be increased judgement involved in determining forward looking economic and credit assumptions over the life of a loan, and how those assumptions are incorporated into the measurement of expected credit losses.
- The method used to calculate expected credit losses is likely to be more complex, with a number of banks expecting to use models that are comparable to those used for their IRB advanced approaches for capital purposes.
- There will be more factors that create variability in expected credit losses. For example, ~~all~~where PD-based methodologies are adopted, movements in PDs ~~will~~may lead to ~~changes in~~higher volatility of the quantum of impairment recorded under an ECL approach which was not necessarily the case under an incurred loss model.

This reconfirmed to the EDTF the importance of all of the existing principles, in particular Principle 1 that disclosures should be clear, balanced and understandable. There should be 'an appropriate balance between qualitative and quantitative disclosures' and they 'should provide straightforward explanations of more complex issues'.

The importance of Principle 3, that disclosures present relevant information, was also emphasised. Banks needs to 'provide disclosures only if they are material and reflect their activities and risks. Banks should assess which factors and risks create variability in their expected credit loss measurements. Banks need to explain why those variables are the most significant and provide associated quantitative and qualitative disclosures for only those factors and risks. Disclosures should be eliminated if they are immaterial or redundant.

Lastly Principle 6 was considered of particular importance because (i) banks will ground their ECL provisions in methods and techniques tailored to their respective business models and needs and (ii) different IFRS and US GAAP accounting requirements will hinder full comparability. In both cases, high quality disclosure can help users better understand and assess those differences.

3. Application of existing EDTF recommendations in light of expected credit loss accounting approaches

The EDTF reviewed the applicability of the existing thirty-two recommendations for enhancing the banks' risk disclosures from the 2012 report against the new ECL requirements. The review concluded that recommendations made in the following areas were relevant for ECL approaches:

- general recommendations;
- risk governance and risk management / business model recommendation;
- capital adequacy and risk weighted asset recommendations; and
- credit risk recommendations.

The review found that additional considerations could be developed for these recommendations to support disclosures which will incorporate the new ECL requirements.

The EDTF confirmed that other aspects of the 2012 report remain applicable to other risk disclosures as appropriate.

Additional considerations to existing recommendations in the context of new accounting ECL approaches

Additional considerations which are likely to be relevant to all ECL approaches are provided under the EDTF recommendation to which it relates; additional considerations which are IFRS 9 specific are provided in a separate box. The recommendations in the 2012 report remain unchanged, and this report should be read in conjunction with it.

Some additional considerations are temporary, relating to the period before and upon transition to the ECL approach. The remaining considerations are expected to be permanent for continuous consideration in the context of ECL approaches.

In the pre-transition period, banks should ~~identify forward-looking statements incorporated in disclosures.~~make clear that disclosures anticipating the effects of ECL before ECL requirements come fully into effect reflect best-effort indications of what the results would be at the time made. These should be accompanied with meaningful cautionary statements identifying important factors that could cause actual results ~~on~~after transition to differ materially from those in the ~~forward-looking statements~~transitional disclosures.

A. General recommendations

EDTF Recommendation 2:

Define the bank's risk terminology and risk measures and present key parameter values used.

ECL approaches aim to measure losses that are likely to occur in the future based on expectations at the balance sheet date. The concept of expected credit losses already exists in regulatory frameworks, in pricing and underwriting processes and is now imminent in both US and International accounting standards, but as the objectives of these frameworks vary, so too does the manner in which the ECL is calculated.

Regulatory capital requirements (and the associated EL calculations) are designed to ensure that banking organisations maintain more than sufficient capital resources to cover both expected and unexpected credit losses. As a result, regulatory capital EL (under Advanced and Foundation Internal Ratings Based methods) includes prudential floors, deliberate conservatism and downturn estimates.

An approach taken by many banks when measuring the quantum of expected losses is broadly a combination of four principal factors:

- A probability of default (PD) – an expression of how likely a default event is to happen.
- A loss given default (LGD) – an expression of how much loss may result on default.
- An exposure at default (EAD) – a measure of the outstanding balance when default occurs
- Discounting – a measure of the time value of money

Although both regulatory and accounting frameworks are likely to use calculations with *similar* concepts, their explicit objectives mean that the definitions of these and other terms will ~~be different.~~differ in several areas. These differences may be subtle but can have a significant impact on the quantum of ECLs and consequently on a user's understanding of the financial statements. In order to properly inform users when interpreting figures in expected loss calculations, it is vital that such terms are defined when they are used by individual banks.

Banks should make clear disclosures defining all significant terms used in the calculations of ECL, with a focus on making clear the difference between definitions as applied in determination of ELs within the regulatory capital framework (for example as used in Pillar III disclosures) and those used in determining ECLs for accounting purposes.

Banks also use terms that do not actually have a formal definition in official texts, such as "through the cycle", "point in time" and "behavioural life" when referring to risk parameters. Equally, banks may use similar terms in internal risk management processes. Banks should define such terms in a manner that helps users understand and interpret each bank's quantitative disclosures and associated commentaries on movements and balances.

Where other methodologies are adopted, such as loss rates, these could also be explained.

Permanent considerations to apply this recommendation in an accounting ECL framework include:

- **Describe how the bank interprets and applies the key concepts within an expected credit loss approach.**

  It would be helpful to provide users with a description of the key concepts relating to the application of an ECL approach and how the bank interprets and applies these concepts. Material assumptions or estimates under each concept could be highlighted, particularly when there is a considerable level of uncertainty or subjectivity. The EDTF anticipates that the granularity and specificity to a bank of the explanations provided will increase as the date of adoption of an ECL approach gets nearer.

An example of a key concept is the definition of default, where banks could consider describing how default is defined for use within an ECL model, including clarifying whether the accounting definition of default is consistent with the definition used for internal credit risk management purposes and how that compares to the regulatory definition of default. A further example is the time horizon over which ECL should be measured for types of contract where a specific interpretation is required, such as for current account or revolving facilities.

IFRS 9 specific considerations

Key concepts within the expected loss approach such as how a 'significant increase in credit risk' is determined are critical to a user's understanding of IFRS 9. When similar concepts exist in IAS 39, it would be helpful to explain if and how they differ from IFRS 9 and the impact of these differences, as relevant. Specific concepts that banks should consider include:

Default: In addition to the considerations on the definition of default set out above, banks could consider describing whether the 90 day rebuttable presumption[8] is intended to be used and in what circumstances.

Credit impaired Banks could consider explaining how the concept of "credit impaired exposures"[9] relates to the definition of default used for IFRS 9 purposes, as this is used in calibrating probability of default.

Significant increase in credit risk The concept of "significant increase in credit risk" in IFRS 9 will drive the timing of recognising lifetime ECL (i.e. those exposures assigned to Stage 2) as opposed to 12 month expected credit losses (i.e. Stage 1) in the measurement of the impairment allowance.[10] Users are very interested in the policies and approaches banks apply in determining a significant increase in credit risk that will ~~trigger~~be the basis for a transfer to Stage 2. Banks should consider:

(a) Describing how the significant increase in credit risk is determined and implemented, distinguishing between individual assessments, portfolio assessments, and the application of any ~~overlays.~~temporary collective adjustments (as discussed below). This involves defining the concept clearly ~~for~~in a way that would cover its application to each significant portfolio or product type.[11] This description should address:

- Risk indicators such as the use of credit risk ratings, past due status, probability of default, watch lists or other indicators used in the bank's risk management
- Interpretation of "significant" credit deterioration at an appropriate level of segmentation and granularity (e.g., depending on the portfolio and the initial credit quality, the magnitude of a change in rating or PD or the criteria for being on a watch list, or other criteria derived from the bank's risk management practices or a combination of factors)
- The bank's policies and procedures for incorporating forward-looking information and the types of information used.

(b) When a portfolio assessment is applied to identify a significant increase in credit risk, banks could consider explaining how they will identify the exposures to be moved to Stage 2. This may include, for example, the identification of specific exposures or specific sub-portfolios affected by a deterioration in macroeconomic conditions ('bottom-up approach'), or the application of a percentage to the entire portfolio ('top-down approach').

Initial Recognition For exposures where it may be difficult to determine credit risk at initial recognition (such as current accounts, revolving facilities and renewable exposures), banks could consider describing their approach to determining significant deterioration.

Modifications Banks should consider setting out:

Their policies as to what circumstances should lead to de-recognition of loans as a result of modification of contractual terms and the recognition of new loans;

- How forbearance situations are treated under IFRS 9 including where such exposures are transferred to stage 2, their procedures for transfer of exposures back to Stage 1 where the borrower's condition has recovered or problems with the exposure have been cured. This should include any specific criteria defined to determine when to transfer forborne exposures back to stage

[8] IFRS 9.B5.5.37
[9] IFRS 9 Appendix A Defined terms.
[10] The size of lifetime ECL may not materially differ from 12 month ECL. This may be the case, for instance, where lifetime of a credit exposure is less than 12 months, or if the credit exposure, is highly collateralised as part of its contractual terms.
[11] For the avoidance of doubt, note that it is not necessary to discuss application of the concept to each portfolio or product type separately, except insofar as there are material differences from the bank's general practice. This point does not imply increase in the granularity of disclosure over wheat is required in paragraph 6 of IFRS 7.

1.

- An explanation of the circumstances in which forborne exposures are considered credit-impaired and the criteria used to assess whether they are no longer credit-impaired.

When specific regulatory rules exist around modifications (for example BCBS or European Banking Authority guidance), the bank could explain how these rules are reflected in its IFRS 9 approach.

As with other risk disclosures, disclosures should consider the most significant concepts and issues with respect to material items, at a level of aggregation and using language that will make the information useful to users generally; cf. Principle 3.

- **Disclose the credit loss modelling techniques developed to implement the expected credit loss approach.**

Banks should consider describing the techniques used for the measurement of allowances under the new impairment approach. In particular, where relevant, banks could describe how credit risk measures such as the probability of default (PD), loss given default (LGD), exposure at default (EAD) and credit conversion factors (CCF) are derived and adapted to meet the needs of ECL accounting. The information provided should include the types of inputs used, the most relevant assumptions and judgments made, and the uncertainty involved.

The EDTF anticipates that the granularity and specificity of the explanations provided will increase as the date of adoption of an ECL approach gets nearer. Disclosures could be made in the following areas:

Forward-looking information

Banks ~~c~~should consider describing the types of forward-looking information (including macro-economic factors) that are used to meet ECL requirements and how the impact of this information on ECL is determined. The information provided should include both discussion of the judgment required ~~for determining the relevant forward-looking information~~ and how it is applied in determining the allowance.

Leveraging existing sources

For portfolios where advanced Basel models are used as the starting point, banks could consider explaining the extent to which they rely on these models and how they adapt the methodology to comply with the requirements of the new accounting standards. In particular, users have indicated it is very important to them for IFRS 9 preparers to explain how they move from 12 month ~~PD to stage 2.~~ECL to lifetime ECL, in order to understand both the decision-making process and the sizing of any resulting changes.

Other differences in methodology that are likely to be relevant include:

- Floors
- Downturn adjustments
- PD substitutions and / or
- Joint obligor and guarantor default modelling
- Time horizons
- Discount factors used

For portfolios where the parameters for accounting purposes are not based on Basel model parameters, banks ~~c~~should consider describing the techniques developed to arrive at the ECL for accounting purposes.

Data limitations

A description of data limitations or simplifying assumptions (such as proxies) applied in modelling the ECL risk, including how such limitations and assumptions are addressed on transition.

Temporary Collective ~~overlays~~adjustments

Explanation of the intended use and nature of temporary collective ~~overlays,~~adjustments on allowances to capture factors not specifically embedded in the model. While many adjustments are part of the normal modelling process (e.g. to adjust PDs as defined for capital purposes to accounting requirements or to incorporate forward-looking information), temporary collective adjustments may be taken when needed in the firm's judgement, to reflect macro-economic or other forward-looking or global information, on top of the basic calculation.

Information

Banks could disclose a description of how they obtain information in order to calculate ECL risk measures (for example, whether this is leveraging Basel or other regulatory approaches, using a model developed specifically for IFRS 9, or reliance on expert judgment, which may be especially relevant for low-default or low-volume portfolios).

EDTF Recommendation 3:

Describe and discuss top and emerging risks, incorporating relevant information in the bank's external reports on a timely basis. This should include quantitative disclosures, if possible, and a discussion of any changes in those risk exposures during the reporting period.

Investors and regulators have indicated that they want clear information as to the key drivers of change to bank's most significant credit risks and the impact of those changes on impairment allowances. In this context, sensitivity disclosures have been a topic of much discussion since the financial crisis.

The EDTF considered different types of sensitivities that could be disclosed by banks, including individual parameter sensitivities and alternative economic scenarios. In these discussions the EDTF highlighted that there are certain limitations, as well as benefits, to different types of sensitivity disclosures. Banks need to carefully assess the relevance of sensitivities before including them in their disclosures.

Additional permanent considerations to apply this recommendation include:

- **Consideration should be given to disclosing individual parameter sensitivities, but only where they are meaningful and relevant to understanding how the impairment allowance ~~can~~might be materially changed by variations in such factors.**

The complexity of expected credit loss provisioning means that changes in any individual risk factor or parameter would be likely to be associated with correlated changes in others. Disclosures of the mechanical changes in model outputs when some individual parameters are varied, particularly models with multiple inputs, are unlikely to be useful to users.

However, there will be some portfolios where an individual risk parameter does have a significant impact on the overall credit risk of the portfolio. Sensitivities to these risk parameters could provide useful disclosure. Where these sensitivities to individual risk parameters are included in information that is used for internal decision making and risk management purposes by key management, the board and the board's risk committee, disclosure of these sensitivities should be considered where they are material.

Examples of sensitivities that might usefully be disclosed include:

- Variables that cause an impact to a loan portfolio on an ongoing basis. For example, the sensitivity to house price indices for a residential mortgage book.
- Changes that emerge at a point in time for specific lending portfolios. For example, this could be where there has been an economic shock to either a specific country or industry.

~~For other risks, sensitivities may be a less appropriate~~The EDTF considered as an alternative to individual parameter sensitivities modelling an alternative economic scenario, which would include changes in multiple underlying parameters. The conclusion was that modelling of an alternative economic scenario would imply a much broader and more complex analysis of interrelated factors and that users are likely to be more interested in understanding the hypothetical expected impact of the alternative scenario on the business as a whole, rather than on the impairment allowance in isolation. Related considerations in relation to stress testing disclosures under an ECL approach are set out under EDTF recommendation 8.

For many risks, individual sensitivities or more complex scenario analysis may be less appropriate as means of disclosure, notwithstanding that those risks are relevant and should be considered. Sensitivities may be less ~~appropriate~~relevant for such risks ~~due to the subjectivity in estimating their impact, or~~ because they relate to a potential risk that is not yet appropriate to be captured in the measurement of provisions. Such risks could include potential economic or political developments, particularly where the impact on credit risk is uncertain. For these risks, it may be more appropriate to provide qualitative disclosures of the risks and how they have affected (or not) provisioning.

Regardless of whether sensitivities are provided or not, it is important that all top and emerging risks are discussed and their impact (or not) on ECL provisioning is covered in disclosures, either quantitatively or qualitatively as appropriate.

~~An alternative to individual parameter sensitivities would be to model an alternative economic scenario, which would include changes in multiple underlying parameters. The modelling of an alternative economic scenario would be more akin to a stress test. In this case, users are likely to be more interested in understanding the hypothetical expected impact of the alternative scenario on the business as a whole rather than the impairment allowance in isolation. Further considerations in relation to stress testing disclosures under an ECL approach are set out under EDTF recommendation 8.~~

Additional temporary considerations to apply this recommendation in the context of upcoming accounting ECL framework include:

- **Provide disclosures describing how the concepts applied and modelling techniques under the current impairment approaches compare with the new ECL approach**

In particular, the differences between collective assessment under existing standards (IAS 39/ Financial Accounting Standard 5 (FAS 5)) and an ECL approach should be discussed.

Disclosures under this recommendation would include changes in the scope of impaired assets; changes in the timing of recognition of losses; and the impact of forward-looking information, including any anticipated increase in volatility in provisions and therefore earnings as compared to the incurred loss approach.

Consistent with EDTF recommendation 2, banks could describe the techniques which will be used for the measurement of allowances under the new impairment approach. It is expected that the disclosures would become more detailed over time.

A significant number of large internationally active banks use aspects of EL based measures to comply with IAS 39 and FAS 5. They should disclose how these operate and what changes they intend to make to comply with ECL requirements.

Banks should consider supplementing their existing disclosures that describe their provisioning policies and modelling approaches under existing incurred loss models (i.e. the starting point for transition to ECL) to allow users to better understand how they compare to ECL concepts. For example, how incurred but not reported approaches (IBNR) will compare to ECL requirements~~ (including for IFRS preparers how IBNR compares to the 12 m EL).~~.

Banks should consider disclosing in a qualitative discussion the anticipated effects of an ECL approach on the quantum of provisions as compared to provisions determined under incurred loss standards. The quantitative effects should be disclosed in the 2017 annual report at latest as set out under recommendation 26.

IFRS 9 specific considerations

Banks could also consider explaining how individual triggers and measurement under IAS 39 compares with the treatment of 'credit impaired exposures' under IFRS 9.

Users would like to understand which portfolios will be significantly affected by the transition to IFRS 9 and would welcome disclosure on:

(a) The key characteristics that will affect ECL impairment, for example the behavioural life and amortisation profile of loans~~ (this is intended to allow~~, allowing users to have a sense of the impact that lifetime ECL may have for Stage 2 exposures~~)~~.

(b) The absolute level of credit risk of portfolios

(c) How ~~any development~~broad developments expected in the bank's strategy or portfolio composition might affect the expected impact from IFRS 9.

Users should understand that, in considering these recommendations, banks will have due regard to the commercial or competitive sensitivity of the information discussed, in accordance with Principle 4.

EDTF Recommendation 4:

Once the applicable rules are finalised, outline plans to meet each new key regulatory ratio, e.g. the net stable funding ratio, liquidity coverage ratio and leverage ratio and, once the applicable rules are in force, provide such key ratios.

Under the current regulatory framework (Basel II and III as implemented in most major jurisdictions), where the stock of provisions determined for accounting purposes is less than the one-year regulatory expected loss amount (EL), the difference is taken as a deduction from capital (Core Tier 1). However where the stock of accounting provisions is greater than the EL, the surplus over the EL is allowable to count towards capital resources (Tier 2 capital), subject to a ceiling.

In the absence of any amendments to regulatory rules, the new ECL approach may affect the quantum of regulatory capital resources and hence regulatory capital ratios. Banks should consider disclosing the impact that the revised accounting allowance for credit losses may have on regulatory capital (under current regulatory rules).

It is possible that existing regulatory capital requirements will be revised by the Basel Committee in due course as a result of the new ECL methodology. An assessment of the potential, combined impact of any such changes should be provided when they become known with sufficient reliability.

B. Risk governance and risk management strategies/business model recommendations:

EDTF Recommendation 5:

Summarise prominently the bank's risk management organisation, processes and key functions.

The adoption of an ECL framework requires banks to carefully consider their implementation strategies. This may include changes to the bank's risk management organisation, processes and key functions both in the transition period for the purpose of the implementation plan and after the transition date when the ECL methodology becomes the mandatory impairment approach.

Additional temporary considerations to apply this recommendation in the pre-transition period include:

- **Banks should consider describing the intended implementation strategy including the responsibilities and accountabilities of the different functions involved in implementation and the current timeline for the implementation.**

Banks could consider describing the ~~project~~ governance ~~structure,~~of the transition process, the general types of resources engaged in the implementation ~~project~~of the ECL approach, and the level of interaction amongst the bank's various business units. Disclosures could include the following factors:

- A description of the key milestones, such as the methodologies to be determined and the models to be built and tested;
- How the bank has ensured that the appropriate corporate governance structures have been implemented across the related systems and processes;
- The business units responsible for the oversight of the implementation project;
- The allocation of responsibilities across business units and level of interaction between business units and risk management.

It may also be useful to ~~discuss~~describe the anticipated management structures and control of ECL processes after full implementation.

Additional permanent considerations to apply this recommendation would include:

- **Disclose how the risk management organisation, processes and key functions have been organised to run the ECL impairment methodology.**

Banks could consider highlighting how credit practices and policies form the basis for the implementation of the expected credit loss requirements. Furthermore, banks could describe the impact of the new methodology on existing processes and the changes required to controls, governance practices and operational processes.

EDTF Recommendation 7:

Describe the key risks that arise from the bank's business models and activities, the bank's risk appetite in the context of its business models and how the bank manages such risks. This is to enable users to understand how business activities are reflected in the bank's risk measures and how those risk measures relate to line items in the balance sheet and income statement.

Disclosure of a bank's business models ~~are~~is intended to provide users with a description of how it creates, delivers, and captures value. In order to enable users to understand how risk measures relate to line items in the balance sheet and income statement, banks may have to adapt their descriptions to reflect any changes resulting from the revisions to impairment accounting.

EDTF Recommendation 8:

Describe the use of stress testing within the bank's risk governance and capital frameworks. Stress testing disclosures should provide a narrative overview of the bank's internal stress testing process and governance.

Additional permanent considerations to apply this recommendation to the new ECL framework include:

- **Describe how the new credit loss methodology will be or is reflected in internal stress testing**
- **~~Disclose~~Describe the relationship between the stress testing programs and the implementation of ECL accounting requirements.**

Given the significant developments in stress testing in certain territories over the last few years, banks should re-evaluate the disclosures incorporated in their annual reports and consider how they could be linked to other disclosures made around credit risk and regulatory capital requirements to help users understand the risk factors the business is exposed to. Any links between stress testing methodology, assumptions and processes and the implementation of an ECL methodology should be explained.

C. Capital adequacy and risk-weighted asset recommendations:

EDTF Recommendation 12:

Qualitatively and quantitatively discuss capital planning within a more general discussion of management's strategic planning, including a description of management's view of the required or targeted level of capital and how this will be established.

The introduction of the new accounting standard will potentially affect capital measures as discussed above.

Additional temporary considerations to apply this recommendation in the pre-transition period to the new ECL framework would include:

- **Banks should consider explaining how ECL requirements are anticipated to have an impact on capital planning, particularly meeting capital adequacy requirements, including any strategic changes expected by management, to the extent the impact is material. To the extent regulatory requirements are unclear or not yet fully determined, the effects of such uncertainty should be discussed. As discussed in the introduction to this Report, banks' understanding of these issues will develop and change over the implementation period of ECL requirements, in response to developing regulatory and accounting guidance and their own analysis of the implications of the new ECL standard.**

EDTF Recommendation 15:

Tabulate credit risk in the banking book showing average probability of default (PD) and loss given default (LGD) as well as exposure at default (EAD), total RWAs and RWA density for Basel asset classes and major portfolios within the Basel asset classes at a suitable level of granularity based on internal ratings grades. For non-retail banking book credit portfolios, internal ratings grades and PD bands should be mapped against external credit ratings and the number of PD bands presented should match the number of notch-specific ratings used by credit rating agencies.

Additional permanent considerations to apply this recommendation in the new ECL framework would include:

- **Banks should consider whether credit quality disclosures can be made that are similar to those used for regulatory capital purposes.**

Banks could provide credit quality disclosures for accounting purposes on a similar basis to those in recommendation 15 and the illustrative capital disclosures in Figure 3 (as presented in the EDTF 2012 report). Using the same number of PD bandings as in the bank's implementation of Figure 3 would allow:

- Comparisons between an individual bank's PD, LGD and EAD measures for accounting and regulatory capital purposes. In providing these disclosures, it will be critical that banks clearly explain the measures used for accounting, the differences between PDs, LGDs and EADs for accounting and regulatory capital purposes and the consequential impact on the quantum of those measures, as noted in Recommendation 2.
- Comparisons between banks of PDs, LGDs and EADs for their lending portfolios. ~~The bandings in Figure 3 should be taken as a minimum.~~ Banks should assess ~~whether further~~appropriate bandings ~~are necessary~~ in order to convey the differences in credit quality across their lending portfolios at a reporting date.

As indicated, the above measures will differ between accounting and regulatory capital purposes for several reasons, including conceptual and standard differences, but also differences in model versions because of required conservatism (which does not correspond to the objectivity required for accounting) or other requirements arising from regulatory approvals. Banks could consider how best to meet the recommendation to provide explanations of differences in an understandable matter, without the use of overly technical language. Banks should also consider the appropriate level of disaggregation by asset class and the appropriate level of granularity of data of the type shown on an indicative basis in Table 3. As is always the case with EDTF-recommended disclosures, it is up to each bank to determination the most appropriate format and location of such disclosures. As indicated in the introduction to this Report, users should be aware of the systems and other developmental requirements which may mean that such disclosures are only achievable post-implementation.

- **Use of other approaches to measuring ECL**

PDs, LGDs and EADs may not be used by banks for measuring expected credit losses for all their portfolios. Disclosures consistent with Figure 3 are only relevant for balances that use PDs, LGDs and EADs to calculate expected credit losses. If other approaches to measuring ECL are used, it would be helpful to analyse the balance sheet total between the different approaches used. Consideration could be given to breaking down the calculation and disclosing material components of such approaches separately.

Figure 3. Illustrative Example of advanced IRB credit exposures by internal PD grade (reproduced from EDTF 2012 report)

Internal ratings grade (or band of grades)	PD range	Exposure at default	Average PD	Average LGD	RWAs	Average risk weighting	External rating equivalent
	0.000%	US$m	%	%	US$m	%	
1	0.000 to 0.010	500	0.010	21	25	5	AAA
2	0.011 to 0.020	1,000	0.018	22	90	9	AA+
3	0.021 to 0.030	500	0.029	21	55	11	AA
4	0.031 to 0.040	2,000	0.035	26	300	15	AA
5	0.041 to 0.050	100	0.047	28	18	18	A+
6	0.051 to 0.070	500	0.061	33	100	24	A
7	0.071 to 0.110	800	0.078	41	200	25	A–
8	0.111 to 0.180	750	0.122	38	210	28	BBB+

9	0.181 to 0.300	1,000	0.292	45	310	31	BBB
10	0.301 to 0.500	1,250	0.400	48	475	38	BBB–
11	0.501 to 0.830	1,500	0.650	47	780	52	BB–
12	0.831 to 1.370	1,750	1.112	46	1,033	59	BB
13	1.371 to 2.270	500	2.001	51	370	74	BB–
14	2.271 to 3.750	100	2.500	57	94	94	B+
15	3.751 to 6.190	250	4.011	42	280	112	B
16	6.191 to 10.220	150	7.020	47	204	136	B–
17	10.221 to 16.870	750	12.999	55	1,312	175	CCC+
18	16.871 to 27.840	500	20.020	49	1,560	312	CCC
19	27.841 to 99.999	200	75.020	75	1,282	641	CCC–
20	100.000	200	100.000	75	100	50	Default
Total		14,300			8,798		

Note:

The above Figure is for illustrative purposes only, as the number of internal rating grades, the PD range for each grade and the respective external rating equivalent will differ for each institution.

D. Credit Risk recommendations:

EDTF Recommendation 26:

Provide information that facilitates' users understanding of the bank's credit risk profile, including any significant risk concentrations. This should include a quantitative summary of aggregate credit risk exposures that reconciles to the balance sheet, including detailed tables for both retail and corporate portfolios that segments them by relevant factors. The disclosure should also incorporate credit risk likely to arise from off-balance sheet commitments by type.

Additional temporary considerations to apply this recommendation in the context of upcoming accounting ECL framework include:

- **Banks should consider whether existing segmentation for disclosure purposes is sufficiently granular to appropriately understand credit risk under an ECL approach**

The EDTF's discussions on ~~expected credit losses~~ECL reaffirmed the need for quality quantitative disclosures in respect of a bank's credit risk exposures at a reporting date. The impact on the financial statements should be described with sufficient granularity to allow users to understand how the adoption of the ECL approach contributes to a change in the allowance balance compared to the previous incurred loss approach and how the impact varies across the bank's portfolios. Banks could revisit their existing disclosure segmentation to consider whether it continues to be appropriate.[12] When determining the appropriate level of disclosure segmentation, banks should give consideration to whether their internal reporting has become more granular in response to moving to an ECL approach.

As discussed with respect to Recommendation 26 in the original EDTF Report, disclosures could break down portfolios by geography, line of business, product, credit quality and vintage.

[12] For the avoidance of doubt, it should be understood that there is no presumption that segmentation for either measurement or disclosure purposes would necessarily change for any bank.

As specific risks emerge, banks should ~~ensure that they~~ consider providing separate disclosures segmented for the affected lending. Such emerging risks could relate to a specific territory, industry or type of lending. Any disclosure provided should be designed to highlight the relevant risks. Banks should ensure that such disclosures are removed as the identified risks diminish.

The consideration is also relevant for banks' transitional disclosures.

- **Once practical and when disclosures would be reliable,[13] ~~,~~ provide users with a quantitative assessment of the potential impact of applying an expected credit loss approach.**

The quantitative assessment of the potential impact can only be based on current portfolios and information. Businesses, portfolios and economic conditions will continue to evolve but such changes cannot be anticipated prior to transition. It should therefore be made clear that any quantitative assessment disclosed ahead of transition is not an estimate of the future transition impact but rather an indicative application of the new methodology to current portfolios based on current circumstances and available forecasts as at a particular date. ~~The reliability of~~ The information should therefore be assessed by users on th~~is~~at basis.

~~In the early phase of the implementation projects, it would be helpful for banks to indicate when they expect to be able to provide initial impact assessments based on current portfolios.~~

IFRS 9 specific considerations

The EDTF expects quantitative disclosures to be made in the 2017 annual report at the latest. The extent and nature of quantitative disclosures provided will be dependent upon progress and milestones reached in the bank's implementation project and therefore should be consistent with the timetable and milestones described under recommendation 5.

- **Provide the transition disclosures required by the new accounting standards in the first interim financial statements following the initial application of the standard.**

The transition impact is likely to be reflected in the first interim report following the date of initial application. Although not necessarily required by the standards, the transition disclosures should therefore be provided in the first interim report or earlier to help users understand the bank's analysis of the anticipated transition impact, within the limitations noted above.

The type of disclosures provided ahead of the transition date and on the date of initial application should be consistent. That is, the disclosures provided in the first interim report following the date of initial application should enable users to understand how the changes in methodology described during the pre-transition period have been translated into the financial statements.

IFRS 9 specific considerations

The transition disclosures required by IFRS 9 include reconciling the ending allowance in accordance with IAS 39 and IAS 37 to the opening IFRS 9 allowance. This disclosure is required by IFRS to be provided for each measurement category in accordance with IAS 39 and IFRS 9 and to show separately the effect of the changes in the measurement category on the loss allowance at that date.

In addition, banks could consider describing:

- How exposures are spread across stages at the date of initial application and how this allocation

[13] As elsewhere in this Report, the use of the term ~~'~~"reliable~~'~~" in the context of this consideration is meant to be consistent with the term ~~'~~"reasonably estimable~~'~~" as envisaged by IFRS and other securities regulators.

compares with the scope of impaired exposures under IAS39, both individually and collectively

- The changes in allowance balance introduced by the new standards for particular product or business portfolios
- Any simplified approach applied on transition that would not be applicable permanently (for instance the transitional provisions under IFRS 9, if lifetime ECL has been applied to all financial instruments unless they were low credit risk).

Comment [TT1]: Note for EDTF: It is not totally clear what banks should do here: Compare the allocation of Stages 1-3 (including non-impaired loans) with impaired loans of IAS 39? Would it be sufficient to compare them with stages 2/3? What do you mean with "... compares with the scope"?

- **When restated comparatives are prepared, clarify the basis upon which they were prepared and the limitations of their information content.**

Disclosures on the basis of measurement underlying the comparative figures are necessary to avoid potential confusion on the part of users of financial statements, as the application of the transition provisions may require the information for comparative periods to be prepared on a mixed basis.

Banks which provide restated comparative figures outside the financial statements that do not fully comply with the transition requirements of accounting standards could consider disclosing that fact and explaining how the underlying assumptions used for these non-GAAP restated comparatives compare with what the transition requirements would require.

IFRS 9 specific considerations

When a bank provides accounting comparatives that are compliant with the transition provisions of IFRS 9, it needs to clarify the basis of measurement as the application of the transition provisions of IFRS 9 would require the information for comparative periods to be prepared on a mixed basis, partially under IFRS 9 and partially under IAS 39. This is because IFRS 9 requires the "business model assessment" to be performed at the date of initial application and applied retrospectively and prohibits retrospective application for assets de-recognised before the date of initial application.

- **Provide disclosure of vintage, but only where it aids understanding of credit risk exposures**

One permanent consideration within this recommendation concerns vintage analysis. As noted in the 2012 report vintage analysis can be useful in understanding credit risk exposures, particularly when there is a lending portfolio with heightened credit risk, and the period in which it was originated has a bearing on the extent of that credit risk and the resulting ECL.

EDTF Recommendation 27:

Describe the policies for identifying impaired or non-performing loans, including how the bank defines impaired or non-performing, restructured and returned-to-performing (cured) loans as well as explanations of loan forbearance policies.

EDTF recommendation 27 specified that a bank should define what it considers to be an impaired or non-performing loan. The use of an expected credit loss framework means that all financial assets will have a loss allowance of some kind. Therefore under an ECL approach, this recommendation should be interpreted as defining non-performing and credit-impaired loans. Overall risk terminology is considered under recommendation 2.

EDTF Recommendation 28:

Provide a reconciliation of opening to closing balances of non-performing or impaired loans in the period, and the allowance for loan losses. Disclosure should include an explanation of the effects of loan acquisitions on ratio trends and qualitative and quantitative information about restructured loans.

Additional permanent considerations to apply this recommendation in the new ECL framework would include:

- **A reconciliation of the opening to closing allowance for loan losses (which is required under IFRS 9) should separately disclose:**
  - **Transfer to lifetime ECL[14]~~[14]~~;**
  - **Transfer to credit-impaired financial assets[14]~~[14]~~;**
  - **Transfer to 12-month ECL[14]~~[14]~~;**
  - **Financial assets that have been derecognised during the period (including write-off);**
  - **New financial assets originated or purchased;**
  - **Changes to models used for ECL calculation;**
  - **Changes in credit risk parameters (model inputs)**
  - **Changes due to modification that did not result in derecognition; and**
  - **Others**

An indicative example of a possible reconciliation of ~~both~~ gross carrying amounts and allowance for loan losses is set out below in figure A. [14] This would be one means of disclosing key drivers for changes in the gross carrying amount to the extent that it contributes to changes in loss allowance during the period.

Where models are used for determining expected credit losses, there may be a lack of clarity between model changes and changes to credit risk parameters. Users have indicated they would like to see more information from banks about the quantitative impact that changes to models and risk parameters have on their reported numbers.

A risk parameter is an input to a credit risk model. Examples include macro-economic conditions such as interest rates, the arrears status of a loan or overdraft usage. These characteristics will change from period to period, and will result in changes in modelled expected credit losses. In contrast model changes are expected to be less frequent.

Banks should clearly define their risk parameters and models as part of their overall explanation of their expected credit loss methodology as set out in recommendation 2.

Given the nature of the process by which banks make model changes, it might not always be feasible to ~~clearly~~provide a precise split between the impact of model changes ~~from~~and the impact of credit or economic risk parameter changes. If banks are able to distinguish this split, then changes in risk parameters and models should be separately disclosed in the allowance reconciliation. Where banks are unable to do this, separate disclosures on the impact of material model changes should be provided. The disclosures around any material model changes should explain the nature of the change and why management chose to make the change.

The sequencing of movements is important when preparing an allowance reconciliation. Changes in the sequencing can affect the quantification of each movement. For example, if transfers between stages are considered to take place at the start of the period, the amount transferred could be based on the closing balance from the previous period, which would not include any difference in measurement as a result of the change in stage or as a result of any change in assumptions. Alternatively, if transfers between stages are considered to take place at the end of the period, the amount transferred could be

[14] Transfers to lifetime ECL, credit-impaired financial assets and transfer to 12 month ECL are only relevant for IFRS 9 preparers.

based on the period end balance which may or may not include any difference in measurement as a result of the change in stage but could include the effect of changes in assumptions. Similarly, if changes in measurement due to movements in risk parameters is the first in the sequence, this will give a different amount for the transfer as a result of change in stage than if the change in stage is first in the sequence.

Banks should consider outlining the basis of preparation of their allowance reconciliation, including the order in which movements have been calculated, as well as any other key assumptions made in preparing the disclosure.

- **Disclosure should be provided to explain significant movements in gross balances that contribute to changes in the allowance measured using expected credit losses.**

  Users find understanding significant changes in gross balances (for example new lending, write-offs, etc.) important when assessing the allowances against those balances.

IFRS 9 specific considerations

It will be important to explain ~~the significant~~material flows of balances between 12 month EL, stage 2 and credit impaired, as well as the required disclosures around allowance movements.

In determining the disclosures made, consideration should be given to the flows experienced both ways, particularly from 12 month EL to LEL and from LEL to 12 month EL. If these gross flows are ~~significant~~material, disclosures should be made to explain them (even if the net flow between 12 month EL and LELs is relatively stable).

Comment [DS2]: EDTF to consider whether anything needs to be said about Stage 3.

Figure A – *Example reconciliation of gross carrying amounts and allowances*

Movement table

Financial assets at amortised cost

	Subject to 12-month ECL		Subject to lifetime ECL		Excluding purchase/ originated credit-impaired		Purchase/ originated credit-impaired		Total	
	Gross carrying amount	Allowance for ECL	Gross carrying amount	Allowance for ECL	Gross carrying amount	Allowance for ECL	Gross carrying amount	Allowance for ECL	Gross carrying amount	Allowance for ECL
	US$m	US$m	US$m	US$m	US$m	US$m	US$m	US$m	US$m	US$m
As at 1 January	X	X	X	X	X	X	X	X	X	X
Amount charged to profit or loss		X		X		X		X		X
Transfer to lifetime ECL		(X)		X		X	-	-	-	-
Transfer to credit-impaired financial assets		(X)		(X)		X	-	-	-	-
Transfer to 12-month ECL		X		(X)		(X)	-	-	-	-
Financial assets that have been derecognised during the period (including write-off)		(X)		(X)		(X)		(X)	(X)	(X)
New financial assets originated or purchased		X	-	-	-	-		X	X	X
Changes to model used for ECL calculation	-	X	-	X	-	X	-	X	-	X
Changes to risk parameters (model inputs)	-	X	-	X	-	X	-	X	-	X
Changes due to modification that did not result in derecognition		-		-		-		-	X	X
Others	X	X	X	X	X	X	X	X	X	X
Foreign exchange		X		X		X		X		X
As at 31 December	X	X	X	X	X	X	X	X	X	X
Carrying amount as at 31 December		X		X		X		X		X
Total amount of undiscounted ECL for financial assets initial recognised during the year								X		
Contractual amount outstanding written off that are still subject to enforcement activities	X		X		X		X		X	

Appendix A: Members of the Enhanced Disclosure Taskforce

Appendix B: Glossary