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Basel Committee on Banking Supervision
Bank for International Settlements
CH-4002 Basel
Switzerland
Submitted electronically through the BIS website (www.bis.org)

30 April 2015

Dear Basel Committee members,

Invitation to comment – Consultative Document: *Guidance on accounting for expected credit losses*

Ernst & Young Global Limited, the central coordinating entity of the global EY organisation, welcomes the opportunity to offer its views on the above Consultative Document.

We agree with the Committee that there needs to be a high quality implementation of the new expected credit loss (ECL) approach to measure the impairment of financial instruments. Its introduction will be a major challenge for the banks, auditors, users of the accounts and supervisors. The challenge for the banks for all ECL approaches includes sourcing historical loss data, making forecasts of future economic conditions and adjusting historical experience to reflect current products and economic circumstances and expectations. For those banks reporting under IFRS 9, there is the additional requirement to determine when there has been a significant increase in credit risk, which will be especially challenging when there is little forward-looking information available at the individual obligor level and this determination has to be made on a collective basis.

It is worth stressing that the US ECL model has not yet been finalised and there are a number of IFRS 9 interpretation and implementation issues that will need to be discussed at further meetings of the IASB's Impairment Transition Resource Group (ITG). Some of these discussions may lead to clarification of IFRS 9 by the IASB or the IFRS Interpretations Committee. Meanwhile, the Enhanced Disclosure Task Force will develop common ECL disclosure practices, while the International Auditing Standards Board is writing a standard on how to audit ECLs. We are pleased that the Basel Committee is involved in the ITG and, ideally, there should be no need for separate guidance on the ECL model to be provided by banking supervisors. However, if such guidance is to be issued, we strongly agree that any guidance should be issued by the Basel Committee, rather than by individual country supervisors. We agree with the Committee that implementation of the ECL model by internationally active banks should be as consistent as possible around the world and a single source of guidance will help promote this. We hope that supervisors will continue to work together to apply this guidance in a consistent manner. We are also pleased that the Committee has sought to provide the guidance quickly, given that it will have a major impact on the manner in which banks implement the new standard and major investment decisions need to be made in the next few months if a high quality implementation is to be achieved in the available time.

In this letter we have sought to provide constructive comments on the Consultative Document, based on our understanding of ECL accounting requirements and, particularly, IFRS 9 and the challenges that it will pose. This is set out under three headings:

1) Comments on the structure of the draft guidance

2) Whether the guidance can be read to conflict with the requirements of IFRS 9 *Financial Instruments*

3) Other comments on the content of the draft guidance

We also attach an appendix that sets out wording of the draft Guidance that is unclear, or could be improved, together with our suggested solutions.

1) Comments on the structure of the draft guidance

a) Scope of the document

The title of the document is "*Guidance on Accounting for Expected Credit Losses";* paragraph 1 limits the scope to include credit risk practices affecting the assessment and measurement of credit loss allowances. This is narrower than the scope of the 2006 guidance, as described in paragraph 2, that the new Guidance would replace. However, the document actually contains a mixture of guidance on the accounting for expected losses and, in addition, guidance on wider aspects of credit risk management; the title of the main section is "Credit practices that *interact* with expected credit loss measurement" (emphasis added).

Guidance that does not affect the assessment and measurement of credit loss allowances includes:

i) Paragraph 19 (a), which refers to compliance with applicable laws and regulations

ii) Paragraph 19 (b), which includes reflecting allowances appropriately in supervisory reports

iii) Paragraph 24 (n), which refers to policies and procedures on write offs and recoveries, more broadly than just the accounting for these events

iv) Paragraph 24 (j), which requires banks to have a realistic view' of their lending activities

v) Paragraph 31, which refers to sound underwriting practices, a topic that goes beyond the initial assessment of the probability of default and into the bank's tolerance of risk. Also, a subsequent reduction in risk tolerance does not mean that the risk of an exposure has significantly increased.

vi) Principle 7 and paragraphs 31 and 66, which refer to the pricing of credit risk and that it should reflect inherent risks. Pricing reflects many factors, such as required profit margins, costs of funding and capital, the value of ongoing banking relationships and competitive pressures and aspirations. It also depends on the level and quality of collateral, which is not necessarily related to the probability of default. This is a much wider subject than the measurement of ECLs.

vii) Much of the guidance in paragraph A8 on lending to high risk exposures is not aimed at the measurement of expected credit losses

We understand that supervisors are keen to emphasise the importance of embedding ECL accounting in credit risk management practices, and wish to use the introduction of IFRS 9 to upgrade credit risk management more broadly. However, the mixing of guidance on both the application of an ECL approach and more general credit risk management makes for a complex document, not least because the language that supervisors use to describe credit risk management differs from the language normally used by accountants and which appears in accounting standards such as IFRS 9. Meanwhile, the language introduced by the Committee includes a large number of superlatives (e.g., 'highest quality', 'best practices', 'full spectrum') to describe the Committee's *aspirations*, which do not sit comfortably alongside accounting standards. The guidance would certainly be clearer if it focused on ECL accounting and how it should build on and link to credit risk management practices. Much of the wider material could usefully be included by cross reference to existing guidance, since changes in the accounting model should not necessarily change the way that credit risk is managed.

A number of the issues we raise in this response arise because the present drafting mixes the two separate subjects of risk management and an ECL accounting model. If the Committee intends to continue with the inclusion of the wider credit risk guidance then there will need to be a number of adjustments to the text (not least to its title and the scope as described in paragraph 1) as we recommend in this letter and the appendix.

b) Banks in scope

We understand why the Committee has chosen to provide guidance to those banks that are internationally active or sophisticated in the business of lending and we agree that, as set out in Principle 1, the credit practices and internal controls to determine credit risk practices should be commensurate with the size, nature and complexity of lending exposures. However, as drafted, the guidance suggests that a 'high quality' implementation, without concern for cost or effort should be applied to all of the activities of internationally active banks. We believe that the application should be 'proportionate', to those activities, so that a less costly approach may be suitable for smaller portfolios for which the accounting benefit is small and where the effect is not material. As the guidance will be read by risk managers and others who may not be familiar with normal accounting concepts of materiality, it would be helpful to make it clear that implementation should not lose sight of materiality.

Further, the quality of information available to implement the ECL model will often vary by location within a bank, so that, in some countries, it may be necessary for the approach to be less sophisticated than in others. A more flexible, proportionate approach would be consistent with that used currently for supervisory purposes, as not all parts of a bank's business are regarded as suitable for A-IRB capital models. Any approach must be operationally robust, with regard to the local environment and data constraints.

It is also worth stressing that the determination of which banks are deemed to be internationally active banks and those banks more sophisticated in the business of lending will need to be made by banking supervisors. Also, to the extent that the supervisors adopt a proportionate approach for other, less complex banks, as mentioned in paragraph 12 of the draft Guidelines, the supervisors will need to set out their expectations of this 'proportionate approach'.

c) Individual versus portfolio assessment and measurement

The document would be clearer if it were organised so as to differentiate better the aspects relevant for situations where forward-looking information is available at the individual exposure level, and for those where it is not and so banks must 'overlay' obligor-specific information with a collective assessment or calculation.

- At one extreme, for larger or more specialised corporate exposures, any assessment of significant increase in credit risk or estimation of ECLs is likely to be bespoke for the customer. For such exposures, the requirements of paragraphs 29 (a) (requiring banks to demonstrate how ECL estimates will fluctuate with changes in forward looking assumptions), and (d) (on backtesting), will be less applicable. Also, while forward-looking information including macroeconomic forecasts will *inform* the risk assessment and estimation of ECLs, it will often not be possible to attribute the allowance to individual macroeconomic 'drivers' and, hence, it will not be possible to provide the information required by paragraphs 34, 76, 79, and A21.
- At the other extreme, for many retail exposures, significant use will need to be made of collective assessments and calculations, both where there is a significant increase in credit risk, and for measuring the ECLs. For this group, paragraphs such as parts of 27 (borrower assessment) and 37 and 40 (credit rating systems) cannot often be applied. Also, the procedures required by paragraph 27 may be carried out on initial assessment but will not all occur in subsequent periods, e.g., it would be rare that the bank will fully update its records of a mortgage customer's income and financial position. Subsequent assessment tends, instead, to be carried out at a portfolio level. Meanwhile, if a bank uses a credit rating system for retail customers, this will not usually make use of forward-looking information, but will be driven by delinquency, credit scores and other historical data, which is why some form of overlay will usually be needed to assess significant increases in credit risk and to measure ECLs.
- There will also be a third category of exposures that fall between the two extremes and for which some, or parts, of these paragraphs will be relevant but not others.

2) Whether the guidance can be read to conflict with the requirements of IFRS 9

While we understand that it was not the Committee's intention that the guidance should conflict with IFRS 9 and that representatives of the IASB have not identified any such conflicts, the wording, in places, is not very clear and can be read to conflict. The main instances include the following:

a) Paragraphs 24 (f) includes as a factor that might require a qualitative adjustment, credit concentrations. While we understand the importance of this topic for risk management and supervision and that it features in the way that loss allowances are required to be measured in the US, we do not understand how this would be relevant for application of the IFRS 9 ECL model or how, in practice, such an adjustment would be made.

b) Paragraph A5 states, on the subject of what is a 'default', "the list of elements provided in the Basel framework as indications of unlikeliness to pay should be supplemented with other factors ... either on an individual or collective basis and adjusted to incorporate current conditions and forward-looking information." This seems to combine 'default' with the assessment of significant increases in credit risk, and implies that banks should extend the notion of default in the 12-month ECL estimation to situations when an actual default will have not yet occurred. This would not comply with IFRS 9 and should be removed. Also, the list of indicators of unlikeliness to pay in the Basel framework includes making an 'account-specific provision'. Given that all exposures will have an account-specific provision under an ECL model (even if this is sometimes calculated collectively), this would logically mean that all exposures are in default from day one.

c) We do not understand why paragraph 24(f) says that a qualitative adjustment to the allowance may be required for a change in underwriting standards or lending policies – such changes do not necessarily affect the credit risk of existing financial assets. For instance, a change in underwriting standards or lending policies might reflect a change in risk tolerance or strategic direction. (Banks will have a different attitude to risk and its pricing if they are seeking to break into a market or to reduce their involvement, which would not necessarily affect the risks of existing exposures). Similarly, paragraphs 24(q) and 28(c) refer to 'changes in the bank's business model', even though such a change would not necessarily affect the credit risk of existing exposures. We agree that a change in collection methods may affect the level of expected losses, but this would be a much narrower type of change than those described in the draft Guidance.

d) Paragraph 47 states that when the credit risk increases on a group basis, the entire group should migrate to a higher credit risk rating. Combined with the assertions made in paragraph A27, this implies that the whole group should subsequently be measured on a lifetime ECL basis. This is supported by paragraph A35, which states "the Committee expects that, in instances where it is apparent that one or more exposures in a group have experienced a significant increase in credit risk, the relevant group or subgroup will transfer to LEL measurement of ECL". This would seem to conflict with IFRS 9, as illustrated by the top-down approach shown in Example 5 of the Implementation Guidance to IFRS 9, in which only 20% of floating rate loans are deemed to be measured on a lifetime ECL basis. We understand that this reading was not intended and we recommend the wording should be amended so as to make this clear.

e) In paragraph 63, the reference to ‘determine either a single amount ...’ can be read to conflict with the requirement in IFRS 9 B5.5.42 to reflect ‘at least two outcomes’.

f) Paragraph A7 states that “a bank must be able to demonstrate that these exposures have *not* experienced a significant increase in credit risk since initial recognition” (emphasis added). This can be read to imply that exposures should be recorded using lifetime ECLs by default unless the bank can justify using a 12 month basis. This would subtly amend the requirement of IFRS 9 paragraph 5.5.4 that a lifetime basis should be used where there is a significant increase in credit risk considering all reasonable and supportable information. (Moreover, in practice it is very difficult, if not impossible, to demonstrate a negative).

g) In paragraph 80, the statement that ‘recoveries of amounts previously written off’ should be an item in the allowance reconciliation is incorrect under IFRS. Under IFRS, a write-off is a derecognition event and the accounting for a subsequent recovery would not make use of an allowance account.

3) Other comments on the content of the draft guidance

While we list a number of concerns about the drafting of the document in the Appendices, the following are the most problematic, in addition to those already listed:

a) The document uses may terms that are different from those used in IFRS 9, are undefined and are often unclear. These include words such as ‘sound’, ‘robust’, ‘timely’, ‘notch’, ‘suitable’, and ‘appropriate’. The guidance would be more useful if the words of the IASB are used to the maximum extent feasible and that any new terminology introduced to help provide guidance is defined and used consistently so that the Committee’s meaning is clear without the need for further guidance.

b) There are several references to ‘forward-looking information *and* macroeconomic factors’, whereas macroeconomic factors are *an example* of forward looking information. Given the number of times that this phrase is used in the document, it would be useful to list examples of what is considered “forward-looking information” in more detail. For example, does it include borrower-generated financial forecasts, or industry published growth projections, or analyses of predicted technological change? These examples, while certainly forward-looking information, could potentially double-count macroeconomic factors like GDP growth, interest rate changes, or measures of inflation. The two items, forward-looking information and macroeconomic factors are not as separable as the document seems to suggest. Also, the provision of examples of what types of forward-looking information might be used to assess ECLs in an individual exposure or at portfolio level, and how to avoid double counting of their effect, would provide useful guidance to banks and help clarify supervisory expectations.

c) The Guidance is inconsistent in its emphasis on the level of judgement that will be required in applying an ECL model. For instance, paragraph 61, rightly, points out that it may not always be possible to demonstrate a strong link between the information available and the credit risk of some exposures or portfolios. Yet paragraph A29 states that ‘reliable’ calibration of the linkages between drivers and increase in credit risk will be ‘critical’. In practice, calibrations will always be estimates, hypotheses based on past experience and judgements about the future. And, as history rarely repeats itself, these estimates will often differ from how situations actually unfold. It is important that banks strive to find calibrations that are as reliable as is practically achievable, but to describe them as ‘reliable’ implies that the exercise is much simpler and more mechanical than it will actually be. There is a risk that the guidance in A29 could lead to solutions that are unduly complex, are too focused on past data and imply a spurious level of accuracy.

   The application of the ECL model will certainly require the application of experienced judgement, with the consequence that no two banks will come to the same assessment or measurement of two identical exposures. But the last line of paragraph 61 probably places too much emphasis on the use of judgement (since it implies that ‘experienced credit judgement’ can substitute for forward-looking information and is not necessarily ‘supportable’ evidence as required by the standard. It would be helpful to provide consistent guidance that seeks a middle way between the approaches described in paragraphs 61 and A29.

d) Paragraph 75 indicates that the Committee expects disclosure of the sensitivity of ECL estimates to change in assumptions. This goes beyond what is currently required by IFRS 7 or IFRS 9 and, without further guidance, could result in disclosures with limited comparability between entities. It would probably be better to remove disclosure as a topic from the Guidance, perhaps removing Principle 8, and to feed these concerns into the planned project of the Enhanced Disclosure Task Force to devise suitable disclosures for the ECL model.

Should you wish to discuss the contents of this letter with us, please contact Tony Clifford on +44 (0)207 951 2250.

Yours faithfully

Ernst & Young Global Limited

Appendix: Wording of the draft Guidelines that is unclear, or could be improved

Comment number	Paragraph reference in the draft		Suggested solution
1	Para 1	The paragraph states that “the scope of credit risk practices is limited to those practices affecting the assessment and measurement of allowances …” yet the title of the second section of the document refers to “practices that interact with expected credit loss measurement” and contains guidance that does not relate to assessment and measurement of allowances.	We recommend that the scope of the document is reassessed. If the objective is confirmed to be consistent with paragraph 1, then certain material should be deleted, as set out in our cover letter. If the Committee decides to keep the wider scope, the title of the Guidance and paragraph 1 should be amended.
2	Para 7	In this paragraph the term ‘robust’ is used for the first of many times. We understand that the word is already used in regulatory guidance, but what is it supposed to mean in the context of assessing and measuring expected credit losses? It would seem that its meaning is intended to be broader than its common usage as ‘resilient’.	We recommend that the Committee does not introduce new terminology over and above that already contained in the standard or, where to do so would help provide useful guidance, to provide a set of definitions. ‘Robust’ should ideally be replaced with a word that describes more precisely what the Committee means in each context.
3	Para 11	While we agree that internationally active banks and those banks which are more sophisticated in the business of lending should implement an ECL model well, most will have smaller operations for which the amount of investment and complexity of approach should be commensurate with their scale and risks, as required by	We recommend adding “commensurate with the size, nature and complexity of their lending exposures” to the end of the paragraph.

		Principle 1.	
4	Para 13	The scope of the paper is unclear as to which activities of banks are covered by the Guidance and which are not. For instance, are deposits with other banks and central banks deemed to be ‘lending exposures’ and when would reverse repos or leasing activity fall within the scope of the Guidance? The reference to ‘debt securities’ (paragraph 13) does not work well for a document with international relevance. Neither IAS 39 nor IFRS 9 differentiates between loans and securities and some items held by banks that arise from lending activities may be securities in legal form.	It would be helpful to clarify what is meant by ‘lending exposures’, possibly by adding to the list of what it is not deemed to cover, such as (potentially) deposits, reverse repos and finance leases, all of which are (normally) in the scope of the IFRS 9 ECL model. While we support the idea that the low risk simplification should be available for exposures that do not arise from lending arrangements, we suggest amending the text to ‘such as debt securities and other financial assets traded in active markets’.
5	Para 21	In the third sentence, the reference to ‘updated each reporting period’ is not consistent with the many references in the document such as ‘regular’ and ‘timely’ but with little guidance on what they might mean. For instance, when paragraph 84(a) uses the word ‘timely’ does this mean banks must continuously assess all collateral? Paragraph 42 requires credit ratings to be reviewed whenever new information is received, yet a formal review need only be annual, while paragraph 49 uses “as early as possible” and paragraph 55 refers to periodically “consistent with the bank’s financial and regulatory	It would be helpful if the guidance were clearer on this issue.

		reporting requirements". At the 22 April ITG meeting, the IASB members appeared to confirm that IFRS 9 only requires impairment allowances to be assessed and measured a the period end, except when assets are derecognised.	
6	Para 21 (second sentence)	The reference to 'interpretation' is erroneous in this context, since interpretation of the accounting framework is not related to the use of information and assumptions across the bank.	Remove the reference to 'interpretation'.
7	Para 24(a)	A method cannot include a process that 'equips'. A method can only be designed to achieve an outcome and cannot, on its own, guarantee that outcome, as that will be dependent on execution.	The wording should perhaps refer to a 'process *designed to* equip'.
8	Para 24(b)	The statement that macroeconomic factors 'may be at the local level' is a contradiction and even the reference to 'regional' is questionable, given that 'macroeconomic' is normally defined as relating to a national economy.	Replace 'macroeconomic' with 'economic'.
9	Para 24(f)	This sub-paragraph indicates that a qualitative adjustment might be necessary for "changes in expectations of macroeconomic trends and conditions". Also, it is unclear how risk concentrations would affect	Wouldn't any adjustment have to be quantitative, even if arrived at using judgement rather than an algorithm? Delete the reference to 'credit concentrations', or

		expected loss allowances under IFRS 9.	else explain how they might affect an IFRS ECL application.
10	Para 24(h)	Any approach that describes the situations in which methods, inputs or assumptions would need to change would be uninformative, since it would merely be when they are no longer appropriate.	More helpful might be to refer to the triggers that might prompt a reassessment of the methods, inputs or assumptions.
11	Para 24(q) and 80	Paragraph 24 (q) refers to ‘collective allowances’, while paragraph 80 states that the Committee expects the reconciliation of the allowance account to be provided separately for ’collective and individual allowances’, implying those that are *measured* collectively or individually. However, the example given in paragraph IG 20B of the Implementation Guidance of IFRS 9 refers to lifetime losses that are *assessed* collectively and individually, implying those that are determined to require lifetime ECLs on a collective or individual basis. Did the Committee intend to add a new requirement? Note, also, that if a measurement overlay is used to include forward-looking information, then the allowance for an individual asset would be measured partly individually and partly collectively. Splitting out these two components would not seem to be very informative. The concept of a ‘collective allowance’ makes more sense in	In paragraph 80, replace ‘that this will be provided separately for collective and individual allowances’ with ‘that lifetime loss allowances will be provided separately for those exposures assessed individually and collectively’. The term ‘collective allowances’ should be avoided.

		the context of IAS 39 than IFRS 9.	
12	Para 28(e)	Under IFRS, 'charge-off' is a mere accounting concept, reflecting the timing of when a loan and any associated allowance are removed from the financial statements. Consequently, it is not a factor that would affect the bank's ability to recover amounts due.	Remove the reference to 'charge-off', or else make it clear how the term might be relevant for credit risk assessment
13	Para 29(b)	This paragraph talks about documenting the process for determining the time horizon, including 'how ECL is estimated in the period following that which is reasonably estimable' and then in a footnote, indicates that the term 'reasonably estimable' is not included in IFRS 9. The Committee should consider removing this reference to 'reasonably estimable' as it implies that anything beyond that horizon must not be reasonably estimable, and will encourage entities not to try to develop better methods and systems and collect better data sets to forecast losses for longer periods. While we understand the Committee's aim in this paragraph, the wording may be misleading without the context that has been explored in the US discussions, including how projections should revert to historical experience.	Consider removing the reference to 'reasonably estimable', or else expand the discussion to provide some useful guidance on this topic for IFRS-reporting banks.
14	Para 29(d)	The reference to backtesting could be inferred to include backtesting the macroeconomic	We recommend that this wording is amended to avoid

		assumptions themselves, which would not be a valuable exercise.	this risk.
15	Para 30	The term ‘full spectrum of information that is relevant’ implies that the bank should have access to and use all information that might ideally exist, whether or not it actually exists and whether or not it is accessible for the bank. This makes the requirement unachievable or unclear. Further, it is unclear whether any assessment of future macroeconomic conditions should be probability weighted, such that the uncertain outcome of a high impact future event (e.g., an independence referendum) should be brought into the ECL calculation based on the relative probabilities of the possible outcomes. The problem with such an approach, particularly if the same assumptions are required to be used to underpin budgets, strategic and capital plans, is that a probability-weighted forecast of the future is one that will certainly never occur. Also, the quantitative results of such high magnitude events will often be impossible to model with any confidence. It makes more sense to use something like a consensus view when it comes to macroeconomic assumptions, which will be informed by an understanding of future possibilities. The potential effect of such uncertainties would more usefully be qualitatively	The term should be replaced with something that is clearer and more achievable. The words in paragraph A6, ‘all reasonably available information’ are probably closer to what the Committee intends. It is possible that discussion on this subject may occur at future ITG meetings. If not, then it would be useful for the Committee to make its expectations clear. In any event, the wording about using the ‘full spectrum’ is unhelpful.

		disclosed for financial reporting and quantitatively captured only through stress testing for prudential purposes.	
16	Principle 4	Principle 4 is strangely worded. How could ECLs calculated under IFRS 9 and US GAAP *both* be said to be 'consistent' with what the Basel Core Principles describe as 'adequate'? We note that the Basel Core Principles refer to "If […] provisions are deemed to be inadequate for prudential purposes (e.g. if […] the provisions do not fully reflect losses expected to be incurred), the supervisor has the power to require the bank to adjust its classifications of individual assets, increase its levels of provisioning, reserves or capital". The 'losses expected to be incurred' originally envisaged by the Core Principles were presumably regulatory 12-month ECLs, and the text was drafted to reflect an incurred loss accounting model. If, alternatively, these expected losses are taken to refer to lifetime ECLs, then the wording would seem incompatible with the phased recognition model in IFRS 9 that starts with 12-month ECLs and also conflicts with the IFRS 9 accounting for purchased or originated credit-impaired financial assets. Instead, this sounds more like the FASB lifetime ECL model.	We suggest that references to the Basel Core Principles are deleted, unless the Principles are to be amended.
17	Para 33	It would be helpful to explain what is meant by 'components of	Clarify what is meant by 'components of credit risk'.

		credit risk'.	
18	Paras 33 to 42	Paragraphs 33 to 42 (relating to credit assessment and credit rating systems) do not relate to Principle 3, which is about 'appropriate grouping' of lending exposures on the basis of shared credit risk characteristics under an ECL accounting approach.	There seems to be a principle missing, to which these paragraphs would better relate, or else the principle should be reworded to delete this guidance and, instead, just explain how rating systems should be used or adjusted for ECL accounting purposes.
19	Para 36	While significant increases in credit risk may be assessed on a portfolio basis, it would be unusual to assess credit ratings on a portfolio basis unless the change in conditions affects the whole portfolio. For instance, when a top down approach is used to assess deterioration, as set out in IE 39 of the Implementation Guidance to the standard, it would be unlikely that all floating rate borrowers or an arbitrary 20% of such borrowers would be downgraded.	Amend the wording to make it clear that the use of 'portfolio' in this context is closer to the 'bottom up' assessment in IE 38.
20	Para 41	What is meant by 'the full range of credit risk'? Does this refer to all sources of risk or all possible outcomes?	Clarify what is meant by 'full range of credit risk'.
21	Para 42, 48 and A18	Para 42: indicates that 'credit risk ratings assigned should receive a periodic formal review (e.g. at least annually or more frequently if required in a jurisdiction) to reasonably ensure that those ratings are accurate and up to date.' Does the wording "if required in	If the Committee meant that the bank should carry out a formal review as often as it reports to shareholders, paragraph 42 could be revised to: 'e.g. at least annually or more frequently if the bank issues interim financial statements'. In practice, it may be possible to

		a jurisdiction' refer to where the entity reports to shareholders more often than once a year? If so, in practice, entities may have some discretion as to the frequency with which they prepare interim financial statements, so 'if required' is not quite right. Or does the Committee expect a formal review once a year unless banking regulatory requirements would require a formal review more often? Similarly, paragraph 48 indicates that 'the group of exposures assigned should receive a periodic formal review (e.g. at least annually or more frequently if required in a jurisdiction) to reasonably ensure that those groupings are accurate and up to date'. Paragraph A18 discusses the need for timely transfer to LEL as soon as credit risk has increased significantly. How is this consistent with paragraph 42 and 48 that seem to indicate an annual review might be sufficient?	comply with the standard without a full formal risk review every quarter. Meanwhile, paragraph 48 could be perhaps reworded to say the groupings should be reviewed when significant circumstances change. It would be helpful if these expectations were harmonised using consistent language.
22	Para 45	Paragraph 45 in unclear. Presumably it means that the groups should be sufficiently granular that increases in credit risk in some sections of the group should not be obscured, but that point is already made in the next paragraph.	Clarify or possibly delete paragraph 45.

23	Para 46	The second sentence should refer to 'information obtained that would indicate' changes in credit risk after initial recognition (see paragraph 48) and logically would follow that paragraph.	Amend accordingly.
24	Para 47 and A 33	Paragraph 47 states that when the credit risk increases on a group basis, the entire group should migrate to a higher credit risk rating. Combined with the assertions made in paragraph A27, this implies that the whole group should subsequently be measured on a lifetime ECL basis. This is supported by paragraph A35, which states 'the Committee expects that, in instances where it is apparent that one or more exposures in a group have experienced a significant increase in credit risk, the relevant group or subgroup will transfer to LEL measurement of ECL'. "This would seem to conflict with IFRS 9, as illustrated by the top-down approach shown in Example 5 of the Implementation Guidance to IFRS 9, in which only 20% of floating rate loans are deemed to be measured on a lifetime ECL basis. This paragraph says that, 'in instances where it is apparent that one or more exposures in a group have experienced a significant increase in credit risk, the relevant group or subgroup will transfer to LEL measurement of ECL even	Presumably these paragraphs should say that 'a portion of the group or a sub-group should migrate or will transfer...'

		though it is not possible to identify this on an individual exposure basis'. As worded, this means that it only takes one exposure within a group to show evidence of a significant increase in risk for the allowance for the entire group to be required to be measured on a lifetime ECL basis. This would clearly be wrong and would conflict with the standard. We understand that this reading was not intended.	
25	Para 52	The reference to 'simple averages' is hard to understand. We would expect that any average would at least be weighted by the size of the loans or defaults.	Was this intended to read, instead, 'simple techniques such as averages ...'?
26	Para 58(c)(ii)	Why is there reference to 'plausible stresses'? Does this just mean that the model can *accommodate* relatively stressed assumptions, or is there a suggestion that stressed assumptions form part of the calculation of ECLs (which would conflict with the standard)?	Explain what is meant by 'plausible stresses' or else delete the reference.
27	Principle 6 and para A49	Principle 6 refers to 'reasonably available' information. This is in tension with the statement in paragraph A49, that banks 'should develop systems and processes to use *all* reasonable and supportable information' (emphasis added). To use *all* the information would be unduly expensive, operationally complex and, correspondingly, less robust. There will always be	If the Committee had not intended for banks to look for 'all reasonable information', but rather to ensure a 'robust' implementation of the standard, then the wording of paragraph A49 should be amended accordingly.

		the need to apply judgement in deciding what information to use, to ensure that process is manageable. Also, as with all accounting estimates, there is a trade-off between reliability of evidence on the one hand and relevance on the other. Some information will be more reliable than others and some will be more relevant.	
28	Para 63	This says that 'in estimating ECL, banks may determine either a single amount or a range of possible amounts' This can be read to conflict with the requirement of paragraph B5.5.42 of IFRS 9, which requires a probability-weighted calculation that reflects at least two possible outcomes.	It is suggested that this wording is deleted or else conformed to the wording in the standard.
29	Para 75	The bank's basis for grouping lending exposures into portfolios with similar credit characteristics is not a 'policy' or 'definition' – it is a judgement made in making an estimate. It is also unclear what is meant by 'management and users have different objectives'.	We suggest the wording be amended to 'to highlight policies, definitions *and judgements made* that are integral to the estimation ...' We suggest deleting these words.
30	Para 77	Paragraph 77 includes documentation of process and duplicates (or perhaps belongs under) principle 3.	We recommend that process documentation is deal with under Principle 3.
31	Para 79	In paragraph 79, does the Committee require quantitative disclosure? If so, it would be helpful to make this clear.	Clarify whether quantitative disclosures are required. As we write in our cover letter, we recommend that the guidance should not

			address disclosures, since this will duplicate the EDTF initiative.
32	Para 80	The statement that ’recoveries of amounts previously written off’ should be an item in the allowance reconciliation is incorrect under IFRS. A write-off is a derecognition event and the accounting for a recovery will not involve the allowance account.	Remove the reference to ‘recoveries of amounts previously written off’ and make this a separate disclosure recommendation. However, as we write in our cover letter, we recommend that the guidance should not address disclosures, since this will duplicate the EDTF initiative.
33	Para 81	Should product concentrations, etc., have been referred to before paragraph 81 in principle 8? It seems odd to ask for items to be regularly reviewed without asking them to be disclosed in the first place. Also, product concentrations seem to be a separate issue from ECLs.	We suggest that the reference to ‘product concentrations’ is deleted or amended accordingly.
34	Para 82(c)	It is unclear why the timely identification of changes in credit risk is emphasised for ’riskier exposures’ when it is already required by the draft Guidance for all exposures (see paragraphs 42, 48 and 87).	Clarify the emphasis for ’riskier exposures’.
35	Para 84(c)	The reference to the allowance being appropriate in accordance with the relevant accounting requirements *and* in relation to the total credit risk in the bank’s portfolio, implies that the allowances could be appropriate in accordance with relevant accounting requirements and yet not be appropriate in relation to the total credit risk	The meaning of this is unclear and it should be deleted or reworded.

		exposure. This cannot be right.	
36	Para A1	IFRS 9 is not ‘the impairment standard’. Also, contrary to what is written in A1, nil allowances will not be rare where the exposures are adequately collateralised, such as for much mortgage lending. This should be addressed in the main text, rather than explained in the footnote, for two reasons: a) As many exposures will be fully collateralised, a nil allowance will be common. b) The message in the second half of the footnote: ’as valuation of collateral may change over the life of the loan’ seems too important to be relegated to a footnote.	Delete the word ‘impairment’ in the first line. In line 5, we recommend revision to ‘exposures, and that (unless the exposure is fully secured by collateral) a nil allowance will be rare’ and that footnote 26 is deleted. The warning in footnote 26 that valuation of collateral may change over the life of the loan, would warrant an entire paragraph in the main text, that an ECL model requires continued monitoring of collateral values.
37	Para A7	The last sentence places a burden on banks to demonstrate that there has been no significant increase in credit risk since initial recognition. In practice, it is very difficult, if not impossible, to demonstrate a negative and banks can only work with the evidence they have. It can also be read to conflict with the requirement as set out in IFRS 9.	We suggest deleting the sentence.
38	Para A8	While high-risk exposures are likely to more rapidly decline in credit quality because of greater volatility, the IFRS 9 ECL model	Clarify that lifetime ECL allowances are only required when there has been a significant increase in credit

		only requires allowances to be measured on a lifetime ECL basis if there has been a significant increase in credit risk since initial recognition. It is clear in the standard that, if the exposure is initially high risk, then a significant deterioration would involve a greater increase in the absolute PD than if the exposure was initially lower risk. In addition, there is guidance in this paragraph that goes beyond the scope of the appendix, including the requirement to document the rationale for high-risk lending along with the governance processes, and to have sound commensurate underwriting practices.	risk and realign the wording in the paragraph with IFRS 9. We suggest that the Committee should delete the wording in this paragraph that does not relate to the assessment and measurement of expected credit losses under IFRS 9.
39	Para A9	The wording ‘taking account of the migration of credit risk’ is confusing since it implies that the 12-month ECL requirement should anticipate ‘migrations’ to a lifetime ECL measure, which would not be consistent with the standard. Further, only exposures can ‘migrate’, credit risk cannot.	Presumably what this paragraph is trying to say is that if the credit risk is considered to have increased, then this should be reflected in the 12-month ECL measurement before the increase is sufficiently significant that the allowance is measured on a lifetime basis. This could be achieved by deleting ‘taking into account the migration of credit risk’.
40	Para A15	The rationale cited as a ‘belief’ of the Committee is a fact, even if, in practice, pricing will take into account other factors as well. In particular, there may be a significant increase in the probability of default on a fully secured loan with no effect on	We suggest deletion of ‘The Committee believes that …’.

		pricing, or a change in pricing due to competitive pressures without any significant change in credit risk. Also, because loan pricing takes account of many factors other than credit risk, it is likely that there may be reasonably wide bands of credit risk that would be priced similarly. Hence, it is probably not true that '*any* post-origination increase in credit risk is unlikely to be fully compensated by the interest rate charged' (emphasis added). This is an important point since the notion of 'significant increase' in the standard does not imply *any* increase, and this issue is reflected in a number of paragraphs in the appendix.	Possible wording might be to turn this around, to say, 'If the post-origination credit risk has increased to such an extent that it is unlikely that it is compensated by the interest rate charged, it is likely that there has been a significant increase in credit risk'. We also recommend deleting the footnote reference to the Snapshot, first, because it is not needed and second, because this document has no authoritative status.
41	Para A17	This paragraph states that 'Ensuring that the approach is consistent across entities within a group is important'. Yet, the complexity of lending activity and the range of reasonable and supportable information that is available may differ from one entity to another, so that there may well need to be differences in approach. Similarly, the economic assumptions should be appropriate to the different jurisdictions in which a bank operates.	We believe that the intention here is that there needs to be consistent interpretation of the requirements of the standard, a consistent overall methodology, consistent approaches to forecasting economic conditions and consistent governance processes.
42	Para A22	It is not true that 'delinquency data [is] seldom appropriate in the implementation of an ECL approach by banks'. It is just that, at least for the more sophisticated lenders, it will only	We recommend that this sentence is amended to add 'on their own' between 'seldom' and 'be appropriate'.

		ever form part of the information that is used and would be inappropriate on its own.	
43	Para A23	The word ‘objective’ in ‘objective level of credit risk’ is not correct– it is the nature of credit risk that it is never objective.	It is not clear what the use of this word is supposed to mean in his context. Could ‘objective’ be deleted?
44	Para A27	This paragraph is unclear. Why has the Committee decided to require that ‘particular attention’ be paid to only a few of the indicators set out in paragraph B5.5.17 of the standard? Is it the Committee’s intent that these should be given higher priority than the ‘may be relevant’ wording used in the standard? In which case, is *any* downgrade considered to be a significant increase in credit risk? And does ‘deterioration of relevant factors’ in subparagraph e) effectively mean ‘anything else’, in which case, the words ‘particular attention’ have no practical meaning? Also, footnote 33 does not recognise that elements of loan pricing include profit margin, risk appetite and strategy. For instance, a bank may price a particular type of loan more highly not because the risk has increased, but because the bank is no longer seeking to expand its business in that direction. To make it a rebuttable presumption that any increase in spread is due to an increase in credit risk would appear unduly	We would recommend deleting this paragraph, or else amending it so as to make the Committee’s intentions clear. We recommend that the footnote is deleted.

		conservative. The presumption would also be difficult to rebut. Further, the rebuttable presumption refers to 'any increase in credit spread', which would be impossible to apply if the bank cannot distinguish increases in credit spread from changes in gross margin due to other factors. Hence, as worded, the test is unworkable.	
45	Para A29	The statement that 'small changes in credit quality can be associated with a large increase in the probability of default' is contradictory – we question how credit quality would be defined if this statement were true. The wording later in the paragraph that 'it is necessary to look beyond how many "notches" a rating downgrade entails because the change in PD for a one notch-movement is not linear'... reads oddly, since (as already stated in this paragraph) the IFRS 9 ECL model is based on relative rather than absolute increases in credit risk, and so a non-liner gradation system would seem to provide what is needed. There would only be a problem if a one notch movement was based on a linear and absolute change in PD. Also in paragraph A29, a 'notch' can be read to refer to the smallest gradation used by the credit rating agencies, in which case it is unclear what would be	What is possibly intended here is that some grades or rating categories can span a large range of PDs so that there can be a large increase in PD within a single grade. Possible wording might be, 'a small change in the grading can be associated with a large increase in the probability of default.' If this was the Committee's intended meaning, we recommend that the second half of the paragraph starting with 'It is also necessary' is replaced by 'Depending on how finely graded is a bank's exposure grading system, it is possible that a significant increase in credit risk might occur before an exposure is downgraded.' Alternatively, if the Committee was concerned that loan gradings may not reflect all the information required to make an individual assessment, the wording would have to be completely different. As we have already noted in the

		meant by, 'it is possible that a significant increase in credit risk could occur before lending exposures experience even a one-notch downgrade'. In what circumstances would a decline smaller than one notch be significant? Or is the Committee trying to make the point that a loan grading system may not provide all the information necessary to assess whether there has been a significant increase in credit risk, i.e., where this will need to be assessed on a top down portfolio basis?	cover letter, the guidance would be much clearer if those sections appropriate to loans assessed individually were separated from those that relate to a collective assessment. In any event, the term 'a notch' should be avoided, or else defined.
46	Para A33	Wouldn't the 'differences in the seniority of individual exposures' be relevant for the loss given default rather than for the probability of default? In general, an obligor is likely to default on all of its obligations at the same time, particularly given the way that default events are often defined.	We suggest deletion of 'in the seniority of individual exposures'
47	Para 44 and A34	Generally, the word 'homogenous' is too strong when considering exposures managed on a portfolio basis. The best that can probably be achieved is that a portfolio will be 'reasonably homogenous'.	Shouldn't the wording just refer to 'shared risk characteristics' as used in the standard? Hence, remain homogenous' in paragraph A 34 would be written as 'continue to share risk characteristics'?
48	Para A35	See item 23 concerning paragraph 47.	
49	Para A36	Strictly, IE39 should not be described as a paragraph of IFRS 9 – the IEs are not part of	We suggest this is rewritten as 'Consistent with paragraph IE 39 of the Implementation

		the standard and, thus, do not have the same authoritative status.	Guidance to IFRS 9'.
50	Paras A 31 and A37	The wording of paragraph A37 can be improved. It is obvious that the 'significant' notion in IFRS 9 has nothing to do with the notion of significance in statistics. But the next clause, 'meaning that the assessment should not be based solely on quantitative analysis' is a non-sequitur. The point is not about qualitative versus quantitative analysis, but that 'significant' has nothing to do with statistical significance. Also paragraph A31 again seems to mix statistical significance and the IFRS 9 significant increase criterion, and the point it makes would be clearer without this potential source of confusion.	We recommend that paragraph A37 is simplified to say, 'Significant' should not be equated with statistical significance'. Meanwhile, in paragraph A31 we suggest the deletion of 'the deterioration in a particular factor is statistically very small (judged in relation to past data on it), or'
51	Para A49	The final sentence states that 'This will potentially require costly upfront investments in new systems and processes but the Committee considers that the long-term benefit of a high-quality implementation far outweighs the associated costs, which should therefore not be considered undue.'	The Committee might consider amending the final sentence to 'This will potentially require costly upfront investments in new systems and processes *and acquisition or calculation of historical loss information,* but the Committee ....'
52	Para A57	Paragraphs A53 to A58 seem unnecessary if the target banks are not expected to use the low risk simplification. Presumably this guidance is not intended to be applied to securities, as they are outside the scope of this	Consider removing paragraphs A53 to A58.

		Guidance.	