The comments of regulatory treatment of accounting provisions under the Basel III capital framework

Basel Committee:

In response to regulatory treatment of accounting provisions made by Basel committee, ICBC researched the proposal with the current regulatory treatment of provisions thoroughly. ICBC supports the use of ECL approaches to achieve earlier recognition of credit losses than with current incurred loss models and proposes five comments on the consultative document and discussion paper about regulatory treatment of accounting provisions. The detail comments are demonstrated as the following:

The comments of transitional arrangements proposed on the consultative document

1. Considering that IFRS9 has not implemented, and the magnitude of the impact of the application of ECL accounting on aggregate capital requirements or capital requirements for individual banks is uncertain, in order to avoid a “capital shock”, ICBC suggests the period allowed for transition could be five years or even longer.

2. Basel committee suggests that transitional arrangement should applied only to any portion of a bank’s decrease in CET1 capital that is greater than a “modest” amount. Because the magnitude of the possible increase in accounting provisions arising from the adjusting of ECL accounting frameworks is not yet known, and the circumstances across countries and

banks is different, ICBC advises to take off the restriction of setting a "modest" amount as a materiality threshold.

The comments of the long-term regulatory treatment adjustment of provisions presented on discussion paper

1. Basel Committee proposed the treatment of excess provisions under Standardised Approach would be tentatively the same as the current IRB approaches (ie inclusion in Tier 2 capital up to 0.6% of credit RWAs). Considering that the impact of new ECL model on provisioning would be notably differently from that of incurred loss model, ICBC recommends to adjust or delete the bottom line set at 0.6% RWA for excess provisioning add-backs to Tier 2 capital based on the quantitative impact study (QIS) conducted by Basel Committee.

2. Basel committee introduced regulatory EL under SA and treated all accounting provisions in the same ways, aligning with the IRB approach. The Basel LGD and EAD estimates are based on loss severity experienced during economic downturn conditions, while accounting LGD and EAD models represent a neutral estimate based on expected economic conditions. As a consequence, the regulatory provision could be higher than the accounting provision in up-cycle periods, as an additional regulatory capital burden to banks by the inconsistency in the treatments of accounting provision and regulatory capital. ICBC advices to enhance consistency between accounting provision and regulatory capital in methodology.

Industrial and Commercial Bank of China

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