Forward-looking financial reporting

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Personal comments
Introduction

• I agree with Mary Barth that the question is not whether, but how financial reporting should reflect estimates of the future

• I see defining the how is the challenge
  ➢ Uncertainty
  ➢ Time horizon
How should financial reporting reflect uncertainty?

• Reflect past risk experience which can be projected into the future, adjusted for revised expectations
  ➢ Expected losses: statistics
  ➢ Behaviour across market cycle: experience
• Uncertainty is not an absolute concept; there is room for learning from lessons from the past
• Forward-looking estimates, based on economic substance, facilitate economic decision-making
How far into the future should financial reporting reach?

- Economic decision-making takes places within a continuum. Financial reporting should allow an assessment of an entity’s performance over time by considering both short-term and long(er)-term inputs into the estimation process
  - Short-term, micro inputs, i.e. information arising from quarterly, (semi-)annual reporting cycle, adjusted for expectations at reporting date
  - Long(er)-term, macro inputs, i.e. information arising from business cycle and economic cycle, adjusted for expectations at reporting date
In summary: projecting information from multiple-period inputs

<table>
<thead>
<tr>
<th>Risk measurement</th>
<th>Short-term, micro inputs(^1)</th>
<th>Long(er)-term, macro inputs(^2)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Risk measurement error</td>
<td>Unexpected loss</td>
<td>Unexpected loss</td>
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</table>

1 For instance, counterparty information gathered in current and past reporting cycles, projected into the next reporting cycle
2 For instance, business sector information gathered in current and past business cycles, projected into the next reporting cycle
Is there a tension with the IFRS Framework?

- **Past transaction or event**
  - Statistics and experience relate to the past, not to the future; but can be projected into the future
  - Risk measurement models are becoming increasingly sophisticated, backed by multiple-period statistics, recognised in IAS 39

- **Control**
  - Considering realistic expectations is part and parcel of management decision-making, management operates in the context of those expectations
  - For instance, goodwill management and measurement, explicitly recognised in IFRS framework
Conclusion

• Expected losses and market cycle behaviour are concepts which are not necessarily in contradiction with the IFRS framework concepts of past transaction or event, coupled with control.

• Rather, it is a question of interpretation of those concepts.

• In this context, reliability criteria need to be considered.

• Disclosure of the related risk management framework is the accompanying ingredient.
Next steps

• Explore further the synergies between the asset/liability framework and future risks and the estimation of those risks

• The objective is to permit financial statement users to obtain a deeper understanding of the entity’s expectations of the future and to relate the entity’s estimates to other available benchmarks