GROUP OF 100

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Mr H. Hoogervorst
Chairman
International Accounting Standards Board
30 Cannon Street
London EC 4M 6XH
UNITED KINGDOM

Dear Mr Hoogervorst

ED/2013/3 'Financial Instrument: Expected Credit Losses'

The Group of 100 (G100) is an organization of chief financial officers from Australia's largest business enterprises with the purpose of advancing Australia's financial competitiveness, supports the Board's efforts to resolve these issues. We are pleased to provide comments on this Exposure Draft.

Question 1

a. *Do you agree that an approach that recognises a loss allowance (or provision) at an amount equal to a portion of expected credit losses initially, and lifetime expected credit losses only after significant deterioration in credit quality, will reflect:*
   i. *the economic link between the pricing of financial instruments and the credit quality at initial recognition; and*
   ii. *the effects of changes in the credit quality subsequent to initial recognition?*

   If not, why not and how do you believe the proposed model should be revised?

   Recognising an amount for expected credit losses on initial recognition of a loan is inconsistent with the pricing of a security, in this case a loan, at market rates after allowing for the credit quality of the loan. Our understanding is that financial institutions already take account of expected credit losses when pricing a loan.

   Recognising a loss allowance at the inception of a loan on the basis proposed results in the early recognition of credit losses which does not reflect the underlying economics of loan transactions and has the potential for double counting of credit losses.

b. *Do you agree that recognising a loss allowance or provision from initial recognition at an amount equal to lifetime expected credit losses, discounted using the original effective interest rate, does not faithfully represent the underlying economics of financial instruments? If not, why not?*

We do not believe that lifetime expected credit losses should be recognised at initial recognition as this is likely to bring forward recognition of expected credit losses given that initial pricing of a loan would include expectations of credit losses.

Question 2

a. *Do you agree that recognising a loss allowance (or provision) at an amount equal to 12-month expected credit losses and at an amount equal to lifetime expected credit losses after significant deterioration in credit quality achieves an appropriate balance between the faithful representation of the underlying economics and the costs of implementation? If not, why not? What alternative would you prefer and why?*
The G100 believes that the proposed approach provides for a better process for the recognition of expected credit losses in a cost effective manner.

b. *Do you agree that the approach for accounting for expected credit losses proposed in this ED achieves a better balance between the faithful representation of the underlying economics and the cost of implementation than the approaches in the 2009 ED and the SD (without the foreseeable future floor)?*
We consider that the approach is pragmatic and is likely to achieve a better balance.

c. *Do you think that recognising a loss allowance at an amount equal to the lifetime expected credit losses from initial recognition, discounted using the original effective interest rate, achieves a better balance between the faithful representation of the underlying economics and the cost of implementation that this ED?*
The G100 does not believe that this approach reflects the underlying economics of the transaction.

Question 3

a. *Do you agree with the proposed scope of the ED? If not, why not?*
The G100 agrees with the proposed scope.

b. *Do you agree that, for financial assets that are mandatorily measured at FVOCI in accordance with the Classification and Measurement ED, the accounting for expected credit losses should be as proposed in this ED? Why or why not?*
The proposed treatment will result in outcomes that are inconsistent with fair value measurement, as for example, occurs where the recognition of a gain in OCI offsets the impairment loss recognised in the income statement at initial recognition.

Question 4

Is measuring the loss allowance (or a provision) at an amount equal to 12-month expected credit losses operational? If not, why not and how do you believe the portion recognised from initial recognition should be determined?

The G100 is concerned that determining a portion of the loss allowance equal to the 12-month expected credit losses will introduce complexity and lead to different approaches in practice.

We suggest that the approach should be modified to require recognition of the allowance for 12-months expected losses unless the entity can demonstrate that the proposed allowance is inappropriate, in which case it should determine the allowance on the basis of a shorter period.

Question 5

a. *Do you agree with the proposed requirement to recognise a loss allowance (or a provision) at an amount equal to lifetime expected credit losses on the basis of a significant increase in credit risk since initial recognition? If not, why not and what alternative would you prefer?*
b. *Do the proposals provide sufficient guidance on when to recognise lifetime expected credit losses? If not, what additional guidance would you suggest?*
c. *Do you agree that the assessment of when to recognise lifetime expected credit losses should consider only changes in the probability of a default occurring, rather than changes in expected credit losses (or credit loss given default (LGD)? If not, why not and what would you prefer?*
d. *Do you agree with the proposed operational simplifications, and do they contribute to an appropriate balance between faithful representation and the cost of implementation?*
e. *Do you agree with the proposal that the model shall allow the re-establishment of a loss allowance (or a provision) at an amount equal to 12-month expected credit losses if the criteria for the recognition of lifetime expected credit losses are no longer met? If not, why not and what would you prefer?*

The G100 supports the proposed approaches where:

- **credit quality assessment on a portfolio basis for financial assets with similar credit risk characteristics is permitted**
- **lifetime expected credit losses are recognised when the borrower's credit rating has suffered significant deterioration and reversed when credit rating (quality) improves.**

We are concerned that where approaches do not reflect credit management practice entities will incur additional costs to implement systems which, while enabling compliance with the requirements, do not provide information used by management or by the users of financial statements.

Question 6

a. *Do you agree that there are circumstances when interest revenue calculated on a net carrying amount (amortised cost) rather than on a gross carrying amount can provide more useful information? If not, why not, and what would you prefer?*
b. *Do you agree with the proposal to change how interest revenue is calculated for assets that have objective evidence of impairment subsequent to initial recognition? Why or why not? If not, for what population of assets should the interest revenue calculation change?*
c. *Do you agree with the proposal that the interest revenue approach shall be symmetrical (ie that the calculation can revert back to a calculation on the gross carrying amount)? Why or why not? If not, what approach would you prefer?*

The G100 believes that if there is objective evidence of impairment interest revenue in respect of the loan should not be recognised on a gross basis and that the interest revenue approach should be symmetrical to enhance comparability between entities for similar financial assets.

Question 7

a. *Do you agree with the proposed disclosure requirements? Why or why not? If not, what changes do you recommend and why?*
b. *Do you foresee any specific operational challenges when implementing the proposed disclosure requirements? If so, please explain.*
c. *What other disclosures do you believe would provide useful information (whether in addition to, or instead of, the proposed disclosures) and why?*

The G100 is concerned about the overall level and detail of disclosures in IFRSs and in respect of financial instruments in particular. We believe that before the proposed disclosures are mandated appropriate field work on their costs and benefits should be undertaken. Such field work should determine whether the proposed disclosures are consistent with credit management practices.

We note that cross-referencing other documents in the disclosures may not be permitted in some jurisdictions including Australia.

Question 8

Do you agree with the proposed treatment of financial assets on which contractual cash flows are modified, and do you believe that it provides useful information? If not, why not and what alternative would you prefer?

The G100 agrees with the proposed treatment in respect of credit impaired financial assets.

Question 9

a. *Do you agree with the proposals on the application of the general model to loan commitment and financial guarantee contracts? Why or why not? If not, what approach would you prefer?*
b. *Do you foresee any significant operational challenges that may arise from the proposal to present expected credit losses on financial guarantee contracts or loan commitments as a provision in the statement of financial position? If yes, please explain.*

The G100 agrees with the application of the general model but a concern about the proposals relating to loan commitments and financial guarantees is whether such provisions satisfy criteria for recognition in the statement of financial position.

Question 10

a. *Do you agree with the proposed simplified approach for trade receivables and lease receivables? Why or why not? If not, what changes do you recommend and why?*

b. *Do you agree with the proposed amendments to the measurement on initial recognition of trade receivables with no significant financing component? If not, why not and what would you propose instead?*

The G100 agrees that these proposals relating to trade and lease receivables are a pragmatic response to reducing the burden of implementation for non-financial institutions.

Question 11

Do you agree with the proposals for financial assets that are credit-impaired on initial recognition? Why or why not? If not, what approach would you prefer?

The G100 agrees with the proposals.

Question 12

a. *What lead time would you require to implement the proposed requirement? Please explain the assumptions that you have used in making this assessment. As a consequence, what do you believe is an appropriate mandatory effective date for IFRS 9? Please explain.*
b. *Do you agree with the proposed transition requirements? Why or why not? If not, what changes do you recommend and why?*
c. *Do you agree with the proposed relief from restating comparative information on transition? If not, why?*

As indicated in our previous submissions the G100 believes there should be a significant period between the issue of the standard and its operative date and suggest that it be at least 3 years. We also believe that it is preferable that all phases of IFRS 9 have the same operative date with early application permitted.

We agree with the proposed retrospective application and the proposed relief in respect of comparative information on transition.

Yours sincerely
Group of 100 Inc

Terry Bowen
President