Project: **Financial Instruments – Recognition and Measurement**

Topic: **Impairment: Cover paper**

Background

Objective of the Board

1. The objective of the Board is to issue an exposure draft with proposals on the impairment methodology to be used for financial assets measured at amortised cost in October 2009.

2. The staff will be asking the Board to take some decisions at this meeting to allow drafting of the exposure draft (ED).

Previous deliberations

3. The Board had the following previous discussions related to the impairment of financial assets measured at amortised cost:

   (a) At the March 2009 joint board meeting the boards discussed possible approaches to impairment including an expected loss model. At that meeting the boards decided that impairment should be a separate work stream within the financial instruments project.

   (b) At the April 2009 meeting the IASB discussed the amortised cost measurement method[1], including possible impairment approaches for financial assets, one of which was an expected loss method. At that

[1] Agenda paper 14 of the April 2009 IASB meeting.

meeting the Board asked the staff to provide more information about the impairment approaches.

(c) At the May 2009 meeting the IASB discussed an expected cash flow (ECF) approach for financial assets measured at amortised cost.[2] That approach includes credit losses on an expected rather than an incurred basis. At that meeting the Board decided to ask for views on the operationality of the ECF approach by way of a website posting.

Request for information

4. In June 2009 a request for information (RFI) on the feasibility of the ECF approach was posted to the IASB website with responses requested by 1 September 2009. The RFI solicited feedback on the following aspects:

    (a) whether the approach is defined clearly;

    (b) whether the approach is operational;

    (c) switchover issues (costs of implementing the approach, ongoing costs thereafter, required lead-time);

    (d) how to apply the approach to variable rate instruments;

    (e) implications for the interplay between application on a portfolio and an individual instrument level; and

    (f) possible simplifications to the approach.

5. The staff has also conducted extensive outreach activities accompanying the RFI in order to get detailed interactive feedback on the feasibility of the ECF approach. These outreach activities covered different geographical areas, including emerging economies, and are still ongoing. The feedback from these outreach activities is consistent with the feedback included in the formal responses summarised below but allowed the staff to go into even more detail.

---

[2] Agenda paper 5A of the May 2009 IASB meeting.

Papers for this meeting

6. The papers for this meeting are as follows:

   (a) Paper 12A provides a summary analysis of the responses to the RFI.

   (b) Paper 12B sets out alternatives for how to proceed on an exposure draft, the related staff recommendations and questions to the Board.

Actions the Board should consider taking alongside issuance of an exposure draft.

7. The responses to the RFI highlight the significant operational challenges, and costs, of implementing an ECF impairment approach. Some of those challenges and costs may be reduced by the approach the Board takes in its proposals. The options to the Board in that respect are set out in paper 12B.

8. Some respondents to the RFI applauded the outreach efforts of the staff and Board, including the issuance of the RFI.

9. The staff strongly recommends that the Board consider, alongside issuance of an ED, the formation of an Expert Advisory Group. The objective of such a group would be to address further how some of the operational challenges of an ECF approach might be resolved, and hence the group should primarily be composed of credit risk professionals from preparers, auditors, regulators and others.

10. The staff also believes that some field testing of any proposals made by the Board is necessary before any proposals are finalised. The Expert Advisory Group could also be charged with that task.

11. The staff also notes that formation of such a group would be in line with recommendations made to the Board by some prudential regulators and others.

12. Separate from such an initiative, the staff would conduct extensive outreach to investors to obtain further information about the usefulness of the accounting information that would be produced as a result of any proposals made by the Board.