

STAFF PAPER

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Introduction

1. In November 2012 the IASB tentatively decided to modify the criteria for the recognition of lifetime expected losses (the lifetime loss criteria) in the proposed impairment model. Because the transition requirements tentatively decided on during the July 2012 meeting include consideration of the lifetime loss criteria, the staff have updated these requirements accordingly to reflect the current decisions. This paper outlines the consequences of these changes and asks the IASB to confirm the proposed modification to align the transition requirements with the modified lifetime loss criteria.

Background

2. The IASB tentatively decided to clarify the lifetime loss criteria in November 2012. The previous criteria were that the probability of not collecting all contractual cash flows:
 - (a) has increased more than insignificantly since initial recognition (the deterioration criterion); and
 - (b) is at least reasonably possible (**the credit quality criterion**).

3. In November the IASB tentatively decided to simplify the lifetime loss criteria to contain only one criterion, namely that an entity should recognize lifetime losses if there has been a significant deterioration in credit quality (considering the term of the asset and the original credit quality).
4. In addition, the IASB tentatively decided to provide an exception to the assessment of the lifetime loss criterion for high quality assets by requiring the recognition of lifetime losses when assets deteriorate below “investment grade”.¹
5. The transition requirement tentatively decided on in July 2012, for if the transition provision of credit quality at initial recognition is not used, is that:
 - (a) if the credit quality at initial recognition is not used at the date of initial application, due to such information requiring undue cost or effort to obtain, the transition provisions should require these financial assets to be evaluated only based on **whether it is at least reasonably possible that the contractual cash flows will not be collected (i.e. on the basis of the credit quality criterion)**.

Proposed update to transition requirements

6. The transition requirement in paragraph 5(a) provides that entities who do not use the initial credit quality information for existing financial assets when applying the new impairment model should evaluate those assets using only the credit quality criterion.
7. As a consequence of the clarifications to the lifetime loss criteria in November 2012, the staff propose updating this transition requirement accordingly. The modification would ensure consistency with the modified lifetime loss criteria but does not fundamentally change the transition requirement.
8. To update the requirement for the change in the credit quality criterion, the staff recommend the following adjustment:

if the credit quality at initial recognition is not used at the date of initial application, the transition provisions should require these financial assets to be evaluated only on the basis ~~that the likelihood that contractual cash flows~~

¹ Any references to rating grades in this paper are for the purpose of facilitating discussion.

~~may not be collected is at least reasonably possible (i.e. on the basis of the credit quality criterion)~~ **of whether the credit quality is below “investment grade” at the date of initial application.**

Question for the IASB

Does the IASB agree with the staff recommendation to update the transition provision if credit quality at initial recognition is not used to reflect the change in the lifetime loss criteria as outlined above?

Appendix A: Tentative transition requirements

A1. The following are the transition requirements tentatively decided on by the IASB in the July 2012 meeting.

- (a) an entity should be required to use the credit quality at initial recognition for existing financial assets when initially applying the new impairment model, unless obtaining such credit quality information requires undue cost or effort.
- (b) if the credit quality at initial recognition is not used at the date of initial application, due to such information requiring undue cost or effort to obtain, the transition provisions should require these financial assets to be evaluated only based on whether it is at least reasonably possible that the contractual cash flows will not be collected (i.e. on the basis of the credit quality criterion).
- (c) the restatement of comparative periods should be permitted but not required if the information is available without the use of hindsight.
- (d) the disclosures in paragraph 28(f) of IAS 8 should not be required but should be permitted for prior periods if the information is available without the use of hindsight.
- (e) the disclosures in paragraph 28(f) of IAS 8 should be required for the current period.