STAFF PAPER

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REG IASB Meeting

Project	**Financial Instruments: Impairment**		
Paper topic	IASB only disclosures		
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This paper has been prepared by the staff of the IFRS Foundation for discussion at a public meeting of the IASB and does not represent the views of the IASB or any individual member of the IASB. Comments on the application of IFRSs do not purport to set out acceptable or unacceptable application of IFRSs. Technical decisions are made in public and reported in IASB *Update*.

Purpose of paper

1. The purpose of this paper is to present IASB-only recommended disclosures for the impairment phase of the project to replace the accounting for financial instruments.

2. IASB Agenda Paper 5A/FASB Memorandum 166 is a joint paper being discussed at the joint portion of the July 2012 meeting which presents joint recommended disclosures related to this project[1].

3. Appendix A shows a comprehensive list of proposed disclosures (joint and IASB-only) and how they compare to IFRS 7. The Appendix states whether the proposed disclosure is specific to the proposed impairment model or whether the proposed disclosure would be appropriate in conjunction with any impairment model (including the incurred loss model of today). Also, the Appendix lists disclosures in IFRS 7 related to amortised cost and impairment and how they are affected by the proposals.

4. Disclosures related to impairment of financial assets measured at fair value through other comprehensive income are addressed in Agenda Paper 6D.

[1] IASB Agenda Paper 5A/FASB Memorandum 166 should be read in conjunction with this paper. Some terminology in first described in the joint paper, helping to fully understand the disclosures within this IASB-only paper.

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Proposed disclosures

Write-offs

5. The three disclosure requirements included in the Appendix related to write-offs were tentatively agreed upon by the IASB at the February 2011 meeting. The staff has not found any reason to readdress these disclosure requirements. Accordingly, the tentatively agreed upon disclosures included in Appendix A are part of the comprehensive recommended disclosure package.

Discount Rate

6. At the May 2012 meeting[2], the IASB tentatively decided to confirm the proposal included in the joint supplementary document (the SD)[3] to permit an entity to use a current discount rate between, and including, the risk-free rate and the IAS 39 effective interest rate (EIR) when discounting expected losses (including those for lease receivables). This selection of rates was proposed in order to provide operational relief to entities.

7. During the May 2012 meeting, the IASB considered the feedback received on the SD related to the choice of discount rate. One of the concerns was that comparability would be diminished if entities were permitted to select an appropriate discount rate. Other respondents believed comparability could be achieved by including disclosure of the discount rate used and any significant assumptions made.

8. The staff believes that when a model permits entities to make a choice, users would benefit from knowing what choice was made. Also, staff have received feedback from users that disclosing the rate would only be useful if quantitative information was included, in addition to the qualitative information. As a result, the staff recommend the following disclosures:

    (a) *The discount rate an entity has elected to use (ie risk-free rate, EIR, or something in between) and the reasons for that election.*

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[2] See Agenda Paper 5A from the May 2012 IASB-only meeting.

[3] Published in January 2011, *Financial Instruments: Impairment*.

(b) *The discount rate (percentage) used.*

(c) *Any significant assumptions used to determine the rate. For example, if the entity elected to use the risk-free rate plus a spread, the amount of the spread and why that spread is used.*

Modifications

9. In May 2012, the IASB discussed the application of the impairment model to financial assets at amortised cost that are renegotiated or otherwise modified, but that do not result in a derecognition of the financial asset.

10. Modifications for the purpose of that discussion were not limited to circumstances in which the lender, for economic or legal reasons, grants a concession to the borrower because of financial difficulties of the borrower) that the lender would not otherwise consider. This is because it is often difficult to assess the reason for modifications as noted in the Basis for Conclusions to the Amendments to IFRS 7 *Financial Instruments: Disclosures* issued in May 2010:

    > [T]he [IASB] was informed that commercial terms of loans are often renegotiated regularly for reasons that are not related to impairment. In practice it is difficult, especially for a large portfolio of loans, to ascertain which loans were renegotiated to avoid becoming past due or impaired.

11. At the May 2012 meeting, the IASB tentatively decided that modified assets would be treated consistently with the general impairment model. That is, modified assets should be categorised in either a 12 month or lifetime expected credit loss category depending on whether they meet the transfer criteria. The IASB also tentatively decided that the gain or loss upon modification should be recognised against the gross carrying amount of the financial asset.

12. Users have requested that entities disclose the gross carrying amount of assets that have been modified and subsequently improved in credit quality. In addition, the SD proposed disclosure of the nominal amount of financial assets for which the impairment allowance was no longer determined with a lifetime loss, but had moved back to the less than lifetime category as a result of a modification of contractual term(s). No significant issues were raised regarding operationality of

this disclosure proposal, because modified assets are typically monitored more closely than unmodified assets.

13. Users have also requested that the re-default rate on modified financial assets be disclosed. In other words, they would like to know if modified financial assets typically perform, or if they result in a default anyway. It is the staff's understanding that re-default rates are known by entities.

14. The staff notes that the profit or loss impact upon modification would result from both crystallised amounts (those that are a direct result of the modification resulting in an adjustment to the gross carrying amount) as well as the change in the lifetime or 12 month expected loss allowance recognised upon modification. Therefore, the staff believes that users would benefit from knowing the portion of the profit or loss impact related to crystallised amounts versus expected loss amounts on the modified asset.

15. As a result of the above, the staff recommends the following be disclosed:

    (a) The gross carrying amount of assets that have been modified.

    (b) The gross carrying amount of assets that have been modified for which the impairment allowance measurement has changed from a lifetime expected credit loss to a 12 months' expected credit loss.

    (c) The gain or loss resulting from the modification showing separately the adjustment to the gross carrying amount and the change in the impairment allowance.

    (d) The re-default rate on modified financial assets (ie the nominal amount of assets that defaults after a modification).

Financial Assets with a 100 Per cent Likelihood of a Loss

16. The transfer criteria[4] are based on the likelihood that some or all of the contractual cash flows may not be collected, excluding the effect of the severity of the loss. As a financial asset's likelihood of a loss approaches 100 per cent, there is an increased likelihood that the asset may be completely written off. However,

[4] An asset moves out of Bucket 1 when: (a) there has been a more than an insignificant deterioration in credit quality since initial recognition; and (b) it is at least reasonably possible that some or all of the contractual cash flows may not be collected.

the staff understands that some financial assets with a high likelihood of a loss may have very little, if any, lifetime expected losses (e.g., because the severity of the loss may be mitigated by collateral) or may not be written off (because the legal environment in some jurisdictions requires an entity to exhaust all legal avenues before being able to write off assets even if they are fully impaired).

17. The staff think that disclosures on this topic will be necessary for users to understand why financial assets with a likelihood of loss of 100 per cent have no, or little, related impairment allowance or have not been completely written off.

18. The staff understands that in some jurisdictions, most preparers do not measure impairment using the probability of loss as an explicit input. The staff believes that for these preparers, this disclosure would appear when default has already occurred. Therefore, the staff is recommending the following disclosures:

    (a) Gross carrying amount and related allowance, if any, of financial assets measured under the impairment model with a likelihood of default of 100 per cent or if a default has occurred.

    (b) Reasons why these financial assets have not yet been fully impaired or written off (eg assets are fully collateralised).

Financial Assets 90 Days Past Due

19. Under the tentative impairment model, entities will evaluate the notion of transfer differently depending on when they believe a more than insignificant deterioration in credit quality has occurred since initial recognition and the likelihood that all or some contractual cash flows may not be collected is at least reasonably possible. As discussed above, entities may use different credit quality indicators to determine when transfer is appropriate. That results in reduced comparability between entities. Through the disclosures proposed related to credit quality indicators and the transfer criteria, the staff would like to improve a user's ability to compare between entities.

20. The staff notes that there is already a requirement under US GAAP in paragraph 310-10-50-7 to disclose the recorded investment in loans and trade receivables 90 days past due or more and still accruing interest. Also, IFRS 7.37(a) requires an ageing analysis of past due assets which are not yet impaired. The staff believes

that this disclosure could be modified to provide increased comparability. Requiring entities to disclose the amounts of financial assets within the scope of the impairment model that are 90 days past due but continue to be measured with a 12 months' credit loss objective will enable users to understand how entities evaluate financial assets for transfer and at what stage they transfer financial assets to a lifetime credit loss objective. Although the staff believes that assets that are 90 days past due will likely satisfy the transfer criteria and have been moved out of Bucket 1, a high balance of 90 days past due financial assets with a 12 months' credit loss objective may indicate that an entity transfers financial assets at a relatively late stage. Such a disclosure would be similar to that tentatively agreed upon by the IASB in the February 2011 meeting and as discussed in paragraph A13(c) of Appendix A in IASB Agenda Paper 5A/FASB Memorandum 166[5]. Therefore, the staff is proposing the following disclosure:

(a) The balance of financial assets 90 days past due that are measured with a 12 months' expected credit loss measurement objective.

Interest revenue

21. Currently, the IASB's tentative decision related to interest revenue is that it should be calculated on the gross carrying amount of the asset (which does not include a deduction for the impairment allowance). As discussed in Agenda Paper 5C, this could cause interest income to be overstated after an impairment loss is recognised. Agenda Paper 5D recommends that an entity should be required to present interest revenue calculated on the net amortised cost (including the deduction for the impairment allowance) for a subset of financial assets[6]. To enhance the comparability of interest revenue, the staff proposes the following disclosure:

(a) The amounts of interest revenue:

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[5] For ease of reference, the paragraph from that appendix is reproduced herein: For financial assets measured at amortised cost the IASB tentatively decided to require a reconciliation of changes in non-performing financial assets during the period for assets that are 90 days past due, but not included in the 'bad book'.

[6] Agenda Paper 5D also explores '90 days past due' as one of the alternative criteria for triggering the switch to net interest revenue presentation, but does not recommend that alternative.

(i) *calculated on the basis of the gross carrying amount;*

(ii) *calculated on the basis of the net carrying amount; and*

(iii) *calculated on the basis of an effective interest rate adjusted for expected credit losses.*

Question
Does the IASB agree with the staff recommendations for the disclosures related to the IASB-only decisions? If not, what disclosures would the IASB prefer and why?

Appendix

A1. The following table shows the comprehensive IASB disclosure package, as well as disclosures currently in IFRS 7 *Financial Instruments: Disclosures* and how they are affected by the recommendations. The key to phrases used in the 'Affect' column is:

(a) **New due to model:** Disclosure in addition to that currently required by IFRS 7 and specific to the tentative impairment model.

(b) **New regardless of model:** Disclosure in addition to that currently required by IFRS 7, but could be applicable under any impairment model.

(c) **Amended …:** Disclosure is currently required by IFRS 7, but has been updated to reflect the tentative impairment model.

JOINT Proposed disclosures

	Topic	Proposed disclosure	Requirements in IFRS 7	Affect
1	Expected loss calculations	*A discussion of the inputs and specific assumptions the entity factors into its expected loss calculations. Such discussion would include the basis of inputs (eg internal historical information or rating reports).*	Expected loss information not required	New due to model
2	Expected loss calculations	*How the information above is developed and utilised in measuring expected losses. For example, the estimation techniques used.*	Expected loss information not required. However, paragraph B7 states that when an entity uses several methods to manage a risk exposure, the entity shall disclose information using the method or methods that provide the most relevant and reliable information (as described in IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*).	New due to model

JOINT Proposed disclosures

	Topic	Proposed disclosure	Requirements in IFRS 7	Affect
3	Transfer criteria	*A qualitative analysis that describes the indicators and information used to determine whether the transfer criteria has been satisfied.*	Paragraph B5(f) requires the disclosure of the criteria the entity uses to determine that there is objective evidence that an impairment loss has occurred.	Amend current requirements to reflect new model
4	Collateral disclosures	*A description of collateral held as security and other credit enhancements and, by measurement objective (ie 12 months' or lifetime expected credit losses), their financial effect (eg quantification of the extent to which collateral and other credit enhancements mitigate credit risk) in respect of the amount that best represents the maximum exposure to credit risk.*	Similar to paragraph 36(b).	New to require by measurement objective
5	Collateral disclosures	*Balances of fully collateralised financial assets.*	Not required	New regardless of model
6	Collateral disclosures	*A discussion of the quality of collateral securing an entity's financial assets.*	Paragraph 36(b) requires disclosure of a description of collateral held as security and other credit enhancements.	new to explicitly require discussion of quality of collateral
7	Collateral disclosures	*An explanation of any changes in quality of collateral, whether because of a general deterioration, a change in appraisal policies by the reporting entity, or some other reason*	Not required	New regardless of model

JOINT Proposed disclosures

	Topic	Proposed disclosure	Requirements in IFRS 7	Affect
8	Allowance rollforward narrative disclosures	*A discussion of the changes in credit loss expectations and the reasons for those changes (eg loss severity, change in portfolio composition, change in volume of assets whether purchased or originated, significant event or conditions that are affecting the calculation of the allowance that were not expected when originally calculated).*	Not required	New due to model
9	Allowance rollforward narrative disclosures	*A discussion of the changes in estimation techniques used and the reasons for the change.*	Paragraph 33(c) requires disclosure of any change in an entity's objectives, policies and processes for managing the risk and the methods used to measure the risk [this is required for each type of risk].	Adding explicit disclosure related to change in estimates of expected credit losses.
10	Allowance rollforward narrative disclosures	*Reasons for a significant amount of write-offs.*	Not required	New regardless of model
11	Allowance rollforward narrative disclosures	*How assets are grouped for disclosure purposes, if necessary, including specific information on what credit characteristics are considered similar to enable grouping.*	Not required (although paragraph 34 (c) requires an entity to disclose, for each type of risk, concentrations of risk if not apparent from summary quantitative data about its exposure to that risk at the end of the reporting period or the other credit risk disclosures).	New regardless of model

JOINT Proposed disclosures

	Topic	Proposed disclosure	Requirements in IFRS 7	Affect
12	Risk disaggregation	*A disaggregation of an entity's financial assets measured under the impairment model into lower, moderate, and higher risk categories, for each measurement objective.*	Paragraph 34(a) requires for each type of risk arising from financial instruments, an entity shall disclose summary quantitative data about its exposure to that risk at the end of the reporting period based on the information provided internally to key management personnel of the entity.	New due to model
13	Risk disaggregation	*A description of how the entity determines which financial assets fall into the lower, moderate, and higher risk categories.*	Not required	New due to model
14	Purchased credit-impaired assets (PCI)	*A comparison of purchased-credit impaired to other financial assets subject to impairment accounting. The gross carrying amount, impairment allowance, contractually required amounts expected to be collected, and contractually required amounts not expected to be collected for purchased-credit impaired financial assets must be displayed, along with the carrying amount and allowance for purchased and originated non-credit impaired assets.*	Not required	New regardless of model
15	PCI	*For purchased-credit impaired financial assets, the amount recognised due to the effect of favourable changes in the lifetime expectations of cash flows not expected to be collected (ie the non-accretable difference).*	Not required	New due to model

JOINT Proposed disclosures

	Topic	Proposed disclosure	Requirements in IFRS 7	Affect
16	PCI	*How the favourable change has affected net income.*	Not required	New due to model
17	PCI	*To which accounts the favourable changes have been reclassified.*	Not required	New due to model
18	Financial asset ending balances	*The balance of financial assets disaggregated by measurement objective and the allowance related to these financial assets.*	Paragraph 37(b) requires an analysis of financial assets that are individually determined to be impaired as at the end of the reporting period, including the factors the entity considered in determining that they are impaired.	Amended due to new model
19	Financial asset ending balances	*The balance of financial assets evaluated on an individual basis and for which impairment is measured with a measurement objective of lifetime expected credit losses and the allowance related to these financial assets.*	Paragraph 37(b) requires an analysis of financial assets that are individually determined to be impaired as at the end of the reporting period, including the factors the entity considered in determining that they are impaired.	Amended due to new model

IASB Only proposed disclosures

	Topic	Proposed disclosure	IFRS 7	Affect
20	Write-offs	*Entity's write-off policy should include discussion related to whether assets written off are still subject to enforcement activity.*	Not required	New due to model
21	Write-offs	*The balance of assets written off, but for which the entity is still pursuing collection.*	Not required	New due to model
22	Write-offs	*Recoveries of previously written-off assets*	Paragraph 16 requires a reconciliation of changes	Amended

IASB Only proposed disclosures

	Topic	Proposed disclosure	IFRS 7	Affect
		should be included as a separate line item in the reconciliation of changes in the allowance account.	in the allowance account (if used), but does not require specific line items (eg recoveries).	regardless of model.
23	Discount rate	*The discount rate an entity has elected to use (ie risk-free rate, EIR, or something in between) and the reasons for that election.*	Not required	New due to model
24	Discount rate	*The discount rate (percentage) used.*	Not required	New due to model
25	Discount rate	*Any significant assumptions used to determine the rate. For example, if the entity elected to use the risk-free rate plus a spread, the amount of the spread and why that spread is used.*	Not required	New due to model
26	Modifications	*The gross carrying amount of assets that have been modified.*	Not required	New regardless of model
27	Modifications	*The gross carrying amount of assets that have been modified for which the impairment allowance measurement has changed from a lifetime expected credit loss to a 12 months' expected credit loss.*	Paragraph B5(g) requires disclosures when the terms of financial assets that would otherwise be past due or impaired have been renegotiated, the accounting policy for financial assets that are the subject of renegotiated terms.	New due to model
28	Modifications	*The gain or loss resulting from the modification showing separately the adjustment to the gross carrying amount and the change in the impairment allowance.*	Not required	New regardless of model
29	Modifications	*The re-default rate on modified financial assets (ie the nominal amount of assets that*	Not required	New regardless of

IASB Only proposed disclosures

	Topic	Proposed disclosure	IFRS 7	Affect
		defaults after a modification).		model
30	Financial assets with 100 per cent probability of default (PD)	*Gross carrying amount and related allowance, if any, of financial assets measured under the impairment model with a likelihood of default of 100 per cent or if a default has occurred.*	Not required	New regardless of model
31	Financial assets with 100 per cent PD	*Reasons why these financial assets have not yet been fully impaired or written off (eg assets are fully collateralised).*	Not required	New due to model
32	90 days past due	*The balance of financial assets 90 days past due that are measured with a 12 months' expected credit loss measurement objective.*	Paragraph 37(a) requires an analysis of the age of financial assets that are past due as at the end of the reporting period but not impaired.	Amended due to new model
33	Interest revenue	*The amounts of interest revenue:* *(i) Calculated on the basis of the gross carrying amount;* *(ii) calculated on the basis of the net carrying amount; and* *(iii) calculated on the basis of an effective interest rate adjusted for expected credit losses.*	Interest income on impaired financial assets accrued in accordance with paragraph AG93 of IAS 39 (paragraph that discusses interest income after impairment recognition)	Amended due to new model

IFRS 7 disclosures not affected by proposals

Para Ref	Summary of requirement	Affect
20(a)	Net gains or net losses on: (v) financial liabilities measured at amortised cost (vi) financial assets measured at amortised cost (vii) financial assets measured at fair value through other comprehensive income	Remain
20(b)	Total interest income and total interest expense (calculated using the effective interest method) for financial assets that are measured at amortised cost or financial liabilities not at fair value through profit or loss.	Remain
20(c)	Fee income and expense (other than amounts included in determining the effective interest rate) arising from: (i) financial assets measured at amortised cost or financial liabilities that are not at fair value through profit or loss; and (ii) trust and other fiduciary activities that result in the holding or investing of assets on behalf of individuals, trusts, retirement benefit plans, and other institutions.	Remain
20A	An entity shall disclose an analysis of the gain or loss recognised in the statement of comprehensive income arising from the derecognition of financial assets measured at amortised cost, showing separately gains and losses arising from derecognition of those financial assets. This disclosure shall include the reasons for derecognising those financial assets.	Remain
33	For each type of risk arising from financial instruments, an entity shall disclose: (a) The exposures to risk and how they arise; (b) Its objectives, policies and processes for managing the risk and the methods used to measure the risk; and (c) Any changes in (a) or (b) from the previous period.	Remain
B8	For concentration risk disclosures include: (a) A description of how management determines concentrations (b) Description of the shared characteristic that identifies each concentration (eg counterparty, geographical area, currency or market); and (c) The amount of the risk exposure associated with all financial instruments sharing that characteristic.	Remain

IFRS 7 disclosures not affected by proposals

Para Ref	Summary of requirement	Affect
36(a)	Maximum exposure to credit risk at the end of the reporting period without taking account of any collateral held or other credit enhancements (eg netting agreements that do not qualify for offset); but not required if carrying amount best represents the maximum exposure to credit risk	Deleted as no longer applicable with expected loss model and recommended collateral disclosures.
B9	Maximum exposure to credit risk is typically the gross carrying amount, net of: (a) Any amounts offset in accordance with IAS 32; and (b) Any impairment losses recognised in accordance with IAS 39	Remain
B5(d)	When using an allowance: (i) The criteria for determining when the carrying amount of impaired FA is reduced/increased through allowance account use; (ii) The criteria for writing off amounts charged to the allowance account against the carrying amount of impaired financial assets	Deleted as no longer applicable under the model.