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By email: [uchoi@ifrs.org](mailto:uchoi@ifrs.org)

Uni Choi  
IFRS Foundation  
Columbus Building  
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London  
E14 4HD  
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Dear Uni,

**IFRS Interpretations Committee Tentative Agenda Decision on Credit Enhancement**

Thank you for inviting our comments on the tentative agenda decision on Credit Enhancement. Our comments on the captioned topic are set out in the enclosed annex for your consideration.

Should you have any question, please contact our Manager Ms. Emily Ngan at 2526 6080 or our Officer Ms. Seiki Kwok at 2567 1363.

Yours sincerely,

Boey Wong  
Secretary

Enc.

c.c.: The Hong Kong Institute of Certified Public Accountants

*Chairman* Standard Chartered Bank (Hong Kong) Limited  
*Vice Chairman* Bank of China (Hong Kong) Limited  
The Hongkong and Shanghai Banking Corporation Limited  
*Secretary* Boey Wong

主席 渣打銀行（香港）有限公司  
副主席 中國銀行（香港）有限公司  
香港上海滙豐銀行有限公司  
秘書 黃凱儀

## HKAB’s Comments on Consultation on IFRS Interpretations Committee’s Tentative Agenda Decision on Credit Enhancement in the Measurement of Expected Credit Loss

Seq.	Relevant Extract	HKAB Comments
1.	<p><b><u>Appendix A – Defined Terms of IFRS 9</u></b></p> <p>“Credit loss” - The difference between all contractual cash flows that are due to an entity in accordance with the contract and all the cash flows that the entity expects to receive (ie all cash shortfalls), discounted at the original effective interest rate (or credit-adjusted effective interest rate for purchased or originated credit-impaired financial assets). An entity shall estimate cash flows by considering all contractual terms of the financial instrument (for example, prepayment, extension, call and similar options) through the expected life of that financial instrument. <b><u>The cash flows that are considered shall include cash flows from the sale of collateral held or other credit enhancements that are integral to the contractual terms.</u></b> There is a presumption that the expected life of a financial instrument can be estimated reliably. However, in those rare cases when it is not possible to reliably estimate the expected life of a financial instrument, the entity shall use the remaining contractual term of the financial instrument.</p> <p><b><u>IFRS 9 B5.5.55</u></b></p> <p><b><u>“For the purposes of measuring expected credit losses, the estimate of expected cash shortfalls shall reflect the cash flows expected from collateral and other credit enhancements that are part of the contractual terms and are not recognised separately by the entity.</u></b> The estimate of expected cash shortfalls on a collateralised financial instrument reflects the amount and timing of cash flows that are expected from foreclosure on the collateral less the costs of obtaining and selling the collateral, irrespective of whether foreclosure is probable (ie the estimate of expected cash flows considers the probability of a foreclosure and the</p>	<p>Regarding the treatment of credit enhancement on expected credit loss determination, we understand that:-</p> <ol style="list-style-type: none"> <li>1. In the definition of “credit loss” in Appendix A of IFRS 9, it states that “<i>the cash flows that are considered shall include cash flows from the sale of collateral held or other credit enhancements that are <b>integral to the contractual terms</b></i>”, whereas,</li> <li>2. The guidance in IFRS9 B5.5.55 refers that, for the purposes of measuring expected credit losses, the estimate of expected cash shortfalls shall reflect the cash flows expected from collateral and other credit enhancements that are:- <ol style="list-style-type: none"> <li>(i) <i>part of the contractual terms and</i></li> <li>(ii) <i>are not recognised separately by the entity.</i></li> </ol> </li> </ol> <p>Since the term “<i>integral to the contractual terms</i>” was not explicitly defined in IFRS 9, we would like to seek clarification from IASB whether the two characteristics of cash flows set out under IFRS9 B5.5.55 are regarded as the definition of cash flows “<i>integral to the contractual terms</i>” as stated in Appendix A – defined terms of IFRS 9.</p>

Seq.	Relevant Extract	HKAB Comments
	<p>cash flows that would result from it). Consequently, any cash flows that are expected from the realisation of the collateral beyond the contractual maturity of the contract should be included in this analysis. Any collateral obtained as a result of foreclosure is not recognised as an asset that is separate from the collateralised financial instrument unless it meets the relevant recognition criteria for an asset in this or other Standards.”</p>	