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27 September 2023

Dear Board members

Invitation to comment – Request for Information Post-implementation Review IFRS 9 Financial Instruments-Impairment

Ernst & Young Global Limited, the central coordinating entity of the global EY organisation, welcomes the opportunity to offer its views on the International Accounting Standards Board's (IASB or the Board) Request for Information, Post-implementation Review, IFRS 9 Financial Instruments (IFRS 9), Impairment (May 2023).

We support the Board's efforts to formally obtain information from stakeholders as part of the post implementation review of IFRS 9.

We would like to highlight the following high priority observations for the Board to consider:

- We acknowledge that the Expected Credit Loss (ECL) model in IFRS 9 is inherently judgemental. Consequently, there are potential limitations in meeting the disclosure objectives of IFRS 7 *Financial Instrument Disclosures* (IFRS 7). Acknowledging this need for judgment, we recommend that the appropriate response is not to move from a principle-based model to one that has uniform requirements for all entities. Rather, it is our proposal to enhance the disclosure requirements using illustrative examples and providing additional application guidance. If these disclosures are determined to be material to an entity, then their inclusion in the financial statements will facilitate the meeting of the disclosure objectives in IFRS 7, and enhance the comparability of the financial statements, thereby providing useful information to users.

- We detail in the response our concerns regarding the reference to 'all cash shortfalls' in the definition of credit risk in Appendix A of IFRS 9. This matter was highlighted as a result of the IFRS Interpretations Committee's agenda decision (AD) on the topic of lessor forgiveness of lease payments. This concept is fundamental to the application of the ECL model so it is critical that the matter be clarified.

- We also note, as a high priority, the application of the impairment requirements in IFRS 9 with other requirements, in particular, the interaction between the modification, impairment and derecognition requirements.

Our responses to the specific questions in the ED are provided in the Appendix.

Should you wish to discuss the contents of this letter with us, please contact Michiel van der Lof at

the above address or on +31 88 407 1030

Yours faithfully

Ernst & Young Global Limited

General comments

The table below outlines our rankings in terms of the prevalence and priority attached to the items discussed in this response.

An item was ranked as a low priority if:
- It relates to a presentation issue only;
- The measurement outcome may be similar between various interpretations; or
- Interpretation issues or gaps in the requirements exist, but a workable solution has been found, and consistently applied, in practice.

An item has been ranked as a high priority if:
- It is seen as a matter that gives rise to fundamental questions and elevated application challenges in practice, with extensive diversity in interpretation and application; or
- It is seen as a manner of addressing diversity in practice, or allowing enhanced comparability, and so is critical to ensuring more useful information is provided to users.

If a matter is determined to be neither a low or a high, priority, then it is deemed to be a medium priority.

Matter noted	**Response reference**	**Prevalence**	**Priority**
All cash shortfalls	#4-16	High	High
Intercompany loans	#17-22	High	Medium
Forward looking scenarios - Climate risk	#33	High	High
Post model adjustments	#34-37	High	Medium
Loan commitments - Measurement exemption	#38-46	High	Medium
Financial guarantee contracts issued	#47-51	Medium	Medium
Below market loan commitments	#52-54	Low	Medium
Impact of collateral	#55-57	Medium	Low
Financial Guarantees held	#58-66	High	Low

Matter noted	Response reference	Prevalence	Priority
Purchased or originated credit-impaired financial assets	#71-75	Medium	Medium
Application of the impairment requirements in IFRS 9 with other requirements			
- Interaction between modification, impairment and derecognition requirements	#78-82	High	High
- Presentation of modification gains and losses vs impairment	#83-85	High	High
- Write-offs	#86-99	High	High
Credit risk disclosures	#102-114	High	High

Question 1—Impairment

Do the impairment requirements in IFRS 9 result in:

(a) more timely recognition of credit losses compared to IAS 39 and address the complexity caused by having multiple impairment models for financial instruments? Why or why not?

(b) an entity providing useful information to users of financial statements about the effect of credit risk on the amount, timing and uncertainty of future cash flows? Why or why not?

EY's response

1. (a) In general, the IFRS 9 expected credit loss (ECL) model works well. Although the requirements are complex, and we are yet to see the effect of a full credit cycle, it is seen to be an improvement on the incurred loss model that it replaced. This is because the ECL model is more responsive to changes in credit risk and economic conditions and the multiple forward-looking information and scenarios are better able to capture uncertainty and possible losses.

2. 1(b) As the IFRS 9 ECL model is forward looking in nature, this model, together with the disclosures required in IFRS 7, provides users with information about the uncertainty of future cash flows that is more useful than information purely determined on an historic basis. However, as noted in the remainder of this response, there are certain limitations of IFRS 9 and IFRS 7 that impact the usefulness of the information provided to users. These limitations are outlined in the remainder of this letter, including issues relating to interpretation and disclosure comparability.

Question 2—The general approach to recognising expected credit losses

(a) Are there fundamental questions (fatal flaws) about the general approach?

If yes, what are those fundamental questions?

(b) Are the costs of applying the general approach and auditing and enforcing its application significantly greater than expected? Are the benefits to users significantly lower than expected?

EY's response

3. As noted in this response, while there are no fatal flaws, there are certain limitations to the general approach, which have been outlined in the remainder of this letter.

   All cash shortfalls

4. We note a concern that has arisen following the IFRS Interpretations Committee's AD on the topic of lessor forgiveness of lease payments, which relates to the requirement to consider all cash shortfalls in the determination of ECLs. As the issue relates to the definition of credit risk as described in IFRS 9 Appendix A, we consider it to be an issue that is fundamental to the application of the ECL requirements. For this reason, we include our discussion of the topic in this section of the letter. We note it as an issue with high prevalence and high priority.

5. Prior to the AD it was widely understood that credit loss related only to credit risk and application practice was consistent. The AD has introduced ambiguity in how the definition of credit risk is understood, as it could be read to imply that the definition of credit loss requires ECL to reflect estimated changes to the cash flows due to any potential future shortfall.

6. We discuss two broad scenarios which illustrate how and where this issue could arise and the complexities that result, as follows:
   - An expected future concession resulting in a change to the contractual cash flows anticipated by the lender for which discussions with the borrower have not yet commenced but where the borrower would be generally expected to agree to the change as it would reduce the contractual cash flows
   - A possible future change to the legal environment that has the potential to affect the contractual cash flows

   The two scenarios are not intended to be exhaustive.

7. The first illustrative scenario could arise, for example, if and when benchmark interest rates are expected to start to fall, such that lenders anticipate needing to reduce their contractual rates for commercial reasons. They may assess across their portfolio that some reductions will be necessary even though they do not yet know exactly which loans will be affected.

8. Since this type of possibility is not anticipated in the lending contract, the change in expectation is not captured as part of the EIR, which reflects changes to cash flows arising from the existing contractual terms of the loan.

9. A lender might assess the effect of a potential future contractual change that would reduce the cash flows due. The change is anticipated by the lender in advance of the borrower requesting a change. Since the expected future change will reduce the contractual cash flows, the borrower would be expected to agree to the change.

10. This scenario may be common especially when such assessment is made by a lender across a large portfolio of loans.

11. The AD results in significant uncertainty about whether an ECL is needed where a lender anticipates granting a concession to borrowers for reasons unrelated to credit risk and therefore it is important that the IASB clarify the requirements.

12. During the covid-19 pandemic, lenders were encouraged in various jurisdictions to grant payment holidays to borrowers, often with interest accruing but in some cases without. We note that the IASB in its public letter, dated 27 March 2020, *IFRS 9 and covid-19—Accounting for expected credit losses*[1], recommended that entities follow the guidance provided by prudential and securities regulators[2], which directed banks not to reflect in ECL, in circumstances where a concession measure is offered to all borrowers irrespective of their credit risk. The IASB indicated in the letter that it had worked with the regulators that had issued such guidance. We recommend that similar considerations and principles as expressed in the letter are included in IFRS 9 to indicate when expected changes to contractual cash flows should not form part of credit risk.

13. The second illustrative scenario is where there is a challenge to the legal enforceability of the cash flows, which creates the possibility that the contractual cash flows may no longer be fully recoverable. An example of this could be if the future outcome of a court case could affect the legality of the contractual cash flows, where the court case is unrelated to credit risk.

14. This type of possible change has the potential to affect a large number of borrowers in a market, often occurring on a country-wide basis as a result of a potential government or court decision that has not yet occurred. The uncertainty arises because if and when the contractual change is confirmed, it would retroactively affect the legality of cash flows due, where the change is outside the control of the borrower or the lender.

15. Whilst the possibility of reflecting this type of change as subject to ECL is not a direct result of the AD, it could be one of the broader consequences of credit loss reflecting all changes to contractual cash flows. Such changes to contractual cash flows may also be subject to provisioning under IAS 37, which would be recognised separately from the loan asset. Whether such a situation falls under IAS 37 or IFRS 9 can be complex to determine and could lead to significant diversity in practice.

16. We recognise that it would be challenging to distinguish between the different fact patterns presented in the scenarios above. For example, for scenario 1, determining whether a lender's concession is anticipated would be difficult to identify and track across a large portfolios of loans and for different entities to follow a consistent approach. For scenario 2, for potential future changes to a lender's legal ability to collect contractual cash flows, determining when the uncertainty commences could be very difficult, for example when the topic is subject to political

[1] 27 March 2020 IFRS 9 and covid-19 Accounting for expected credit losses applying IFRS 9 Financial Instruments in the light of current uncertainty resulting from the covid-19 pandemic.
[2] For example, 26 March 2020, Covid-19: IFRS 9, capital requirements and loan covenants, Bank of England, Prudential Regulation Authority

and legal processes. We consider that it would be very time consuming and complex for the IASB to develop amendments to IFRS 9 to clarify how to treat non-credit risk related changes to contractual cash flows. In light of this, we recommend that the IASB amends the definition of credit loss in Appendix A to clarify that the calculation of ECL is relevant only for changes to contractual cash flows that relate to credit risk and not to other changes to contractual cash flows.

Intercompany loans

17. In terms of assessing the cost against the benefits of the general model, there are ongoing challenges with intercompany loans, particularly for companies without sophisticated modelling capability (i.e., outside financial institutions). This includes, for example, determining and accounting for ECLs on intercompany loans that are not payable on demand, especially where there is no experience of losses, or no expectation of losses in the future. Another challenge is where intercompany financial guarantees are issued, either over intercompany loans or external debt.

18. Intercompany loans that are documented as on demand, but in substance provide long-term finance, can also be problematic when it comes to determining the appropriate ECL. In particular, if the borrower would be unable to repay the loan if it were called at short notice, because it does not currently have access to the means to repay it or to other sources of financing.

19. It may also be that, due to the nature of the intercompany relationship, the lender may look to the manner of recovery of the amount due when calculating the ECL. This may mean that it would allow the group company a number of years to accumulate the funds to repay the loan, or as a group would look to secure alternative funding if repayment was demanded.

20. It is noted that in the situations above, where an entity has a dual role of lender and stakeholder, this gives rise to complexities in the calculation of ECL. It is, therefore, suggested that, in these situations, guidance is added to IFRS 9 outlining the specific judgements that may be needed when assessing the SICR and measurement of ECLs, for example, as an extension to the guidance in IFRS 9.B5.5.17(l). In addition, overarching guidance for intercompany loans (for example loans given between subsidiaries) should be added highlighting the judgements made when performing the cost-benefit analysis in B5.5.49. For example, if the reporting entity is a bank, or the borrower has going concern questions, there would presumably be a higher hurdle to determine what credit risk information would require undue cost or effort than if the reporting entity did not have fiduciary responsibilities, there were no going concern questions in relation to the borrower, and the information in the financial statements would not be used by external parties.

21. It is noted that this matter only arises in jurisdictions where stand-alone company accounts are required to be presented. In those jurisdictions, the challenges associated with calculating ECL for intercompany loans are noted as highly prevalent. This has been determined as a medium priority on the basis that it does give rise to fundamental interpretation questions, and is it only a presentation issue.

22. It has been determined as a medium priority on the basis that it is not deemed to give rise to elevated application challenges in practice, but a workable solution has not been found that is consistently applied in practice.)

23. In terms of the costs of auditing the general approach, particularly for financial institutions, the need for specialists is noted due to the complexity and forward looking nature of the calculations. With regard to the intercompany exposures outlined above, for less sophisticated entities there may be exposure to credit risk on their assets, but those entities may find it challenging to make the materiality judgements needed in this regard, which may result on a high burden on the auditors.

Question 3—Determining significant increases in credit risk

(a) Are there fundamental questions (fatal flaws) about the assessment of significant increases in credit risk? If yes, what are those fundamental questions?

(b) Can the assessment of significant increases in credit risk be applied consistently? Why or why not?

EY's response

24. (a) We acknowledge, that IFRS 9 uses a principle-based approach for assessing significant increases in credit risk (SICR), instead of a prescriptive rules-based approach. Whilst we are not aware of any fatal flaws in this approach, it does inherently result in entity specific judgements, which may consequently result in different outcomes between entities when determining SICR.

25. (b) EY's benchmarking exercises show this diversity in the judgements of the SICR triggers amongst retail and wholesale portfolios and amongst various financial institutions. We also note differences in the choice and range of secondary indicators – 30 days past due, watchlist and forbearance are common triggers for most banks, but the other triggers vary.

26. As a result of these inherent differences it may be prohibitively difficult for users to understand the nature and extent of the risks arising from the financial instruments, thereby limiting the fulfilment of the disclosure objectives in IFRS 7. Therefore, while we do not disagree with a principles-based approach, we do support having disclosures that will better allow users to understand the nature and extent of the risks. Please see the response to Question 9 (point #111).

27. With regard to Spotlight 3 and in line with the points outlined above, we are supportive of the principle-based approach to determining SICR, and acknowledge that consequently, in most cases significant judgement will be needed to apply the SICR requirements, with resulting disclosure and comparability challenges. Therefore, we are of the view that while entities may be able to apply the requirements consistently (and may be encouraged to do so by financial regulators in some jurisdictions), differences in entities' credit risk management practices mean that it may not be possible for users to always fully understand the consequential results of these judgments, or the impacts they have on different entities. Acknowledging the need for judgments, it is proposed that the counter to this is not necessarily to change the underlying requirements, but rather to enhance the disclosures, as outlined in the response to Question 9.

Question 4—Measuring expected credit losses
(a) Are there fundamental questions (fatal flaws) about requirements for measuring expected credit losses? If yes, what are those fundamental questions?
(b) Can the measurement requirements be applied consistently? Why or why not?

EY's response

28. (a) We acknowledge, that IFRS 9 uses a principle-based approach to measure ECLs, allowing an entity to determine the most appropriate techniques to satisfy those principles, and that IFRS 9 does not prescribe particular techniques. As noted in this response, while there aren't fatal flaws, there are however limitations in the application of the measurement requirements and these have been outlined in the remainder of the letter.

29. As a result of the inherent differences that arise between entities when applying a principle-based approach, it can be difficult for users to compare different entities, thus diminishing the usefulness of the information provided to users. Therefore, whilst we do not disagree with a principle-based approach, we do support having disclosures that will better allow users to understand the outcomes amongst different entities. These disclosure suggestions have been noted below in each of the subsections, and in response to Question 9.

30. (b) We have noted diversity in the application of the IFRS 9 requirements. These application issues are outlined below.

Forward-looking scenarios

31. EY's benchmarking exercises show that diversity in practice is prevalent with regards to the number, profile (severity or optimism) and weightings of scenarios. For example, some entities use and disclose 3 scenarios (base, positive, negative), while other entities disclose more economic scenarios.

32. This diversity is inherently driven by the principle-based nature of the requirements, of which we are supportive, as this allows for a single impairment model to be implemented across a wide range of entities. However, it can be difficult for users to compare different entities, thus diminishing the usefulness of the information. Therefore, whilst we do not disagree with a principle-based approach, we do support having disclosures that will better allow users to understand the outcomes amongst different entities. Please see the response to Question 9, point #112. In addition, we do think that it would be useful for the IASB to provide application guidance or examples about how particular risks should be reflected in the forward looking information and scenarios when measuring expected credit losses.

33. Stakeholders and regulators are increasingly looking to financial statements for disclosures of the impact of climate risk on the reporting entity, and consequently climate risk is becoming a high focus area for preparers. Accordingly, it is important for example to be added to IFRS 9 illustrating how the impact of climate risk is incorporated in the forward-looking information. These suggested examples should illustrate how both physical and transition risk should be incorporated in the ECL estimate and in the disclosures. This matter is seen as a prevalent consideration for entities and a high priority, as without clear guidance on this there will be increased disclosure diversity between entities.

Post-model adjustments or management overlays (PMA[3]s)

34. ECLs have seen a large increase in the incorporation of PMAs in recent reporting cycles. This is largely as a result of increased economic uncertainty in recent years, particularly with regards to economic conditions for which historical information is not necessarily representative of the future economic outlook. Furthermore, as PMAs can be seen as a means of incorporating future looking information into the ECL calculation (IFRS 9.5.5.17, B5.5.52), and are not in contravention of any specific IFRS 9 requirements, it is likely that the use of PMAs will continue .

35. However, due to the increased use of PMAs, and the growing impact that they have on the determination of ECLs, as IFRS 7 does not contain explicit requirements relating to PMAs, in many cases this has resulted in the reduction of the usefulness of information provided to users. It could be argued that the need to disclose PMA information is encompassed in the IFRS 7 principles to disclose at the appropriate level risk, management practices, information and reasons to evaluate ECLs, inputs, assumptions and techniques used, and how forward-looking information has been incorporated (IFRS 7.35). However, these over-arching requirements have not necessarily driven useful disclosures of PMAs that allow users to compare similar entities, or within a specific entity to understand:
    i. The nature and amount of the PMAs, how they were determined, and the circumstances driving their existence
    ii. The extent to which PMAs have been incorporated into the ECL recognised
    iii. How the PMAs interact with other credit risk disclosures (e.g., where ECL is disaggregated per segment, stage or class of asset, how has the overlay been treated for those purposes?)

36. Therefore, we suggest that application guidance or illustrative examples be added demonstrating how the IFRS 7 principles would result in useful information relating to PMAs. For example, guidance illustrating:

    i. Disclosure of the impact of PMAs compared to the modelled outcomes, including the underlying reasons for the PMA's
    ii. Disclosure of information about how the PMAs unwind
    iii. Disclosures relating to PMAs which mirror the disclosures of the modelled outcomes e.g. with a breakdown per risk ratings, sectors, staging etc

    These disclosures should be provided with sufficient granularity to allow users to understand the impact of the PMAs and compare entities with similar issues.

    See Question 9, point #113, for more details on suggested disclosures in relation to PMAs, in particular Appendix A (II) & (III) for examples on the disclosure relating to i) above.

37. We consider this a topic with high prevalence and high priority.

[3] The abbreviation PMA is used here to incorporate post-model adjustments and management overlays, and is seen as distinct from in-model adjustments, which are out of the scope of this discussion.

Off-balance-sheet exposures

Loan commitments

Measurement exemption

38. IFRS 9.5.5.20 requires the issuer of a facility that contains both a drawn and an undrawn commitment to calculate ECLs based on the period over which they expect to be exposed to credit risk. In practice, this exception is commonly applied to revolving credit facilities (RCF). In May 2017, the IASB issued a webcast on this topic entitled "IFRS 9 Impairment: The expected life of revolving facilities".

39. This matter is considered to have a high prevalence and medium priority. It has been determined as a medium priority on the basis that it is not deemed to give rise to elevated application challenges in practice, but a workable solution has not been found that is consistently applied in practice.)

Scope of the exemption

40. The words of the exemption have not been consistently interpreted in practice. The exemption in IFRS 9.5.5.20 relates to financial instruments that 'include both a loan and an undrawn commitment component and for which the entity's contractual ability to demand repayment and cancel the commitment does not limit the entity's exposure to credit losses to the contractual notice period'. Despite the use of the word 'both', this guidance is deemed to apply even if the facility has yet to be drawn down. It also applies if the facility has been completely drawn down, as it is the nature of revolving facilities that the drawn down component is periodically paid off before further amounts will be drawn down again in future.
41. The treatment of corporate overdrafts and similar facilities is also not clear as the IFRS Transition Resource Group for Impairment of Financial Instruments (ITG) and IASB discussions referred to credit cards and retail customers and not corporate exposures.
42. In addition, IFRS 9.B5.5.39(c) indicates that instruments in the scope of the exemption are generally 'managed on a collective basis'. However, it is unclear exactly what is meant by 'managed on a collective basis', and diversity has arisen as to whether facilities that are managed on an individual basis are outside the scope, for example corporate facilities that are managed on an individual basis but with various levels of frequency and information available to update the assessment.

Other matters relating to the exemption

IFRS 9.5.5.20 and B5.5.40 outline the period over which to measure ECLs, however there have been challenges in the consistent application of the requirements. In practice, some entities have also used the guidance on this from ITG discussions, and the IASB webcast on the matter

43. Finally, it is unclear the extent to which the period over which to measure ECLs is restricted by the normal derecognition principles of IFRS 9 and what could constitute a derecognition of the facility. In particular, it is unclear whether the existence of a contractual life and/or the lender's ability to revise the terms and conditions of the facility based on periodic credit reviews would be regarded as triggers for derecognition, and so would also limit the life for ECL measurement.

Suggestions relating to the exemption

44. It is therefore suggested that the IASB clarify the scope of the exemption, in particular with regards to the uncertainties as noted above. Furthermore, the key requirements of the ITG and IASB webcast on this matter should be embedded into IFRS 9. The interaction between the exception, and other elements of IFRS 9 (such as derecognition), should also be made clear.

45. It could be argued that IFRS 7.B8C should be read to require information about the estimated maximum period considered when determining estimated credit losses in respect of revolving credit facilities. This was confirmed by ITG discussions in December 2015. However, it is suggested that this should be clarified and made more explicit that disclosure is required of the life of the RCF over which the entity is exposed to credit risk and ECL has been calculated.

Financial guarantee contracts issued

46. IFRS 9 requires financial guarantees and off-market loan commitments to be measured at the 'higher-of' the amount initially recognised less cumulative amortisation, and the ECL. Issued financial guarantee contracts could require the holder to pay premiums after initial recognition. Consequently, as a result of the 'higher of' test, and the reference to the amount initially recognised, the timing of the receipt of premiums may have an effect on the measurement of the guarantee. This is because if the premiums are receivable after initial recognition, they will not be considered in the 'higher of' test with regards to amounts initially recognised. This is in contrast to when the premium is received in full upfront, and therefore it will be taken into account in the 'higher of' test at initial recognition.

47. Accordingly, the timing of the receipt of the premiums results in a different outcome between two otherwise similar guarantees.

48. We have not noted diversity in the application of the requirement because in most cases premiums are paid over time and ECL is therefore provided for in a similar manner as loans (where future premiums are not deducted from ECL). Consequently, we regard this item as having a medium prevalence, and a medium priority.

49. We have also noted that there are application challenges where multiple entities jointly and severally guarantee another entity. In practice it can be challenging for each guarantor to calculate the ECL needed to be recognised in their separate financial statements. When doing so, they will need to consider the likelihood and quantum should they be called upon. We suggest that it would be useful to have additional guidance on how to measure obligations under these guarantee arrangements and the resulting ECL, both for initial and subsequent measurement.

50. We note this issue as medium prevalence, and medium priority.

Below market loan commitments

51. Another issue that arises as a consequence of the 'higher of' test outlined above relates to below market loan commitments. This issue may arise more commonly in business combinations where loan commitments are acquired where there may have been an increase in interest rates or credit

risk since origination of the loan commitment. As below market rate loan commitments tend not to be common outside of this context, we believe these matters have a low prevalence. Since this issue gives rise to application challenges in practice, but without extensive diversity noted in application, we believe this to be a medium priority.

52. It is also not clear how the measurement rules for an undrawn loan commitment interact with the initial recognition of the loan once drawn. For example, as illustrated below, it is not clear whether the entire 'higher-of' amount needs to be recorded as a reduction of the carrying amount of the drawn loan at initial recognition, with a separate charge to profit or loss to recognise the ECL allowance (option 2). This gross treatment would be consistent with the accounting for at market loan commitments for which an upfront fee is received. An alternative argument is that the portion of the 'higher-of' related to ECL already represents an ECL allowance, and therefore, this portion would be reclassified as part of the ECL allowance on drawdown of the loan rather than being factored into the initial fair value of the loan. This net approach is less intuitive in instances where the 'higher-of' amount is not based on the ECL but is more intuitive when 'higher-of' is based on the ECL (option 1). There is no guidance in the standard to define which approach should be applied, whether a policy choice is available, or whether different approaches are possible depending on what the 'higher-of' is based on at the draw down date.

Simple example to illustrate

- A below market loan commitment (LC) is issued and has a fair value of CU 10 at initial recognition. This fair value correlates to the fee of CU10 that was received for issuing the LC.
- On the next day, the ECL on the LC is CU12, and the loan of CU100 is drawn down. Taking into account the credit risk, the fair value of the loan at draw down is CU88.

Journal entries before draw down:

Dr Bank 10

Cr LC liability 10

Dr ECL charge 2

Cr LC liability 2

Which of the following journals would be acceptable on draw down of the loan:

Option 1

Dr Receivable 90

Dr ECL charge 10

Cr Cash 100

Dr LC liability 12

CR ECL allowance 12

This option results in the cumulative ECL charge being CU12, which is reflective of the credit risk. However, the downside of this approach is that the receivable is not initially recognised at fair value.

Option 2

Dr Receivable 88

Cr Cash 100

Dr LC liability 12

Dr ECL charge 12

Cr ECL allowance 12

This option results in the receivable being recognised at initially at fair value. However, the downside of this approach is that the cumulative ECL charge is CU14, which is in excess of the credit risk.

53. We suggest that additional guidance be added to IFRS 9 to clarify these points. Alternatively, a gross model similar to the accounting for at market loan commitments for which upfront fees are received (with the initial fee deferred as a liability and amortised to revenue in terms of IFRS 15; and a separate ECL allowance being recognised) may serve as a more straightforward model to apply.

Other matters noted when measuring expected credit losses

Impact of collateral

54. Where assets are highly or fully collateralised, but are in default (e.g., because payments are more than 90 days past due), it is not clear if the assets would qualify as credit-impaired, and therefore have to be transferred to Stage 3. This is because there is tension between the definition of credit-impaired in Appendix A of IFRS 9 which refers to 'a detrimental impact on the estimated future cash flows' (and it is not clear whether this should be read to include any recoveries from the realisation of collateral), and IE 22 which states that the assessment of SICR is irrespective of the value of collateral it holds. This has led to divergence in practice relating to the treatment of highly collateralised assets in default.

55. Consequently, we would suggest aligning the definition of credit-impaired, with those for assessing whether it is in default, even if the asset is fully collateralised i.e. linking significant increase in credit risk, to the risk of a default occurring. Otherwise the outcome would seem inconsistent (and potentially confusing for users) if the value of collateral is considered for Stage 3 allocation, especially if the collateral value were to influence the Stage 3 allocation, resulting in instability between Stage 2 and 3 if exposures would potentially go back and forth depending on the collateral value.

56. We note this a medium prevalence and a low priority as it has generally been accepted in practice that that collateral does not impact staging (but only the measurement) and this approach appears to be consistently applied.

Financial guarantees held

57. The issues outlined below with regards to financial guarantees are noted as a high prevalence, and low priority. The prevalence is noted as high on the basis that the use of credit enhancements and financial guarantee contracts is widespread. As in many cases the net position in the SOFP and SOCI is largely the same whether or not the contract is determined to be integral, and due to the fact that accepted practice has emerged limiting the diversity in practice, it is noted as a low priority (there may also be an impact on coverage ratios if there is an impact on ECL).

58. There are application issues noted in practice with regard to guarantees held, in particular relating to the interpretation of when a financial guarantee is 'integral to the contractual terms' when it is not mentioned in the contractual terms of the loan (IFRS 9.B5.5.55).

59. The issue was addressed by the ITG (meeting 11 December 2015 – Agenda paper no. 5), specifically whether the credit enhancement must be an explicit term of the

related asset's contract for it to be considered in the measurement of ECL, or whether other credit enhancements that are not recognised separately can also be taken into account. However, the ITG discussion did not answer the question of how to interpret when a financial guarantee is "integral to the contractual terms" when it is not mentioned in the contractual terms of the loan.

60. Consequently, it is noted that there is diversity in practice with regards to how these requirements are applied in practice.

61. To the extent that the guarantee is considered integral to the loan, it would be consistent with this notion to treat the cost of the guarantee as a transaction cost of making the loan. This means that the lender would add this cost to the initial carrying amount of the loan and so reduce the future EIR. It does not make a difference to the accounting for the loan whether the guarantee premium is paid upfront or in instalments over the life of the loan. If the premium is payable in instalments, it follows (at least, in theory, although the effect is unlikely to be material) that the full cost of the guarantee needs to be included in setting the loan's EIR. However, it would be useful if the IASB confirms this approach.

62. If the credit enhancement is required to be recognised separately by IFRS Standards, an entity cannot include the cash flows expected from it in the measurement of ECL. With regard to the treatment of the guarantee held, there are a number of approaches adopted in practice, for example making an analogy to a reimbursement right under IAS 37, or an indemnification asset under IFRS 3. Except for the possible treatment of the guarantor's credit risk, using either of these approaches the overall effect on profit or loss for the lender may be often the same as if the guarantee was included in the measurement of the ECL of the guaranteed asset. The right would, however, be presented as an asset rather than as a reduction of the impairment allowance [IFRS 9.B5.5.55, IAS 37.53, IFRS 3.57].

63. It is also not clear from IFRS 9 how to account for premiums paid for guarantees when the guarantee is not considered integral. If the entity that makes a loan, and at the same time pays for a guarantee, records both the unamortised cost of the guarantee, plus also a reimbursement or indemnification asset equivalent to the 12-month ECLs, the total amount at which the guarantee is initially recorded in the financial statements will likely exceed its fair value. This is because the cost of the guarantee will already include the guarantor's expectations of future losses.

64. One view is to consider this to be 'double counting' and so, to restrict the reimbursement/indemnification right to the excess (if any) of the ECL over the cost of the guarantee that is already reflected in the balance sheet. There is another view that recognising both the unamortised cost of the guarantee and a reimbursement right/indemnification asset equal to the ECL is necessary to be consistent with the accounting for the loan.

65. A possible solution for defining whether or not a guarantee is integral, would be to reflect the impact of guarantees held in the ECL calculation if the contracts meets the definition of financial guarantee contracts (as defined in Appendix A of IFRS 9). This should also in effect reduce the complications arising from guarantees that are not integral, as the instances when guarantees would then be outside the scope of the ECL calculation would likely decrease.

Question 5—Simplified approach for trade receivables, contract assets and lease receivables

(a) Are there fundamental questions (fatal flaws) about the simplified approach? If yes, what are those fundamental questions?

(b) Are the costs of applying the simplified approach and auditing and enforcing its application significantly greater than expected? Are the benefits to users significantly lower than expected?

EY's response

66. (a) We are of the view that the simplified approach achieves the IASB's objective of reducing the costs and complexities of applying IFRS 9 impairment requirements to trade receivables, contract assets and lease receivables. As such, we have not noted fundamental questions (fatal flaws) relating to the simplified approach.

67. In general, the costs of applying the simplified approach are not significantly greater, and the benefits are not lower, than expected. However, in this regard please note the points below with respect to non-financial institutions.

68. We have noted concerns that non-financial institutions struggle to implement the requirements of IFRS 9 impairment and the related disclosures in IFRS 7. Smaller and non-banking entities often don't have the systems or data available at a sufficiently granular enough level to make the required disclosures. See point #103-104 below where this is discussed in more detail.

69. With regards to the application of the simplified approach, despite the wording in IFRS 9.5.5.15, in practice we have observed that some entities mistakenly view the simplified approach as only reflecting historical loss patterns, without taking into account forward looking information. It would therefore be useful if an example could be added to IFRS 9 illustrating the application of the simplified approach, and, in particular, the incorporation of forward-looking information into the ECL calculation. This could possibly take the form of an example whereby historical information is used as a starting point, and a scaler impact is added to this to incorporate the effect of forward-looking information.

Question 6—Purchased or originated credit-impaired financial assets

Can the requirements in IFRS 9 for purchased or originated credit-impaired financial assets be applied consistently? Why or why not?

EY's response

70. We are broadly comfortable with the IFRS 9 requirements to account for POCI financial assets and consider that they provide a suitable solution for the majority of instances where they are applied. However, some challenges can arise which we outline below along with a discussion of potential improvements that could be made.
71. A particular issue is with respect to POCI financial assets that experience an improvement in credit quality to the extent that the assessment of lifetime ECL decreases below the estimate at initial

recognition. The effect of the change is to increase the carrying value of the asset and to recognise an impairment gain, applying the guidance in IFRS 9.5.5.14.

72. IFRS 9 does not provide any guidance on where in the statement of financial position (SOFP) the debit entry that results should be recognised. Some entities recognise the debit entry as a reduction to the ECL allowance, and others by increasing the value of the gross asset. The net effect on the SOFP is the same under either approach but the effect on the coverage ratios is different. This diversity in practice makes comparison between entities more difficult.

73. One approach is to allow an accounting policy choice between the two alternatives. This is how some entities address the issue currently. However, we consider that this is not an area of IFRS 9 where an accounting policy choice is helpful. It would be more useful to have consistency in this area to aid comparability between entities. We suggest that the IASB provides further guidance in IFRS 9.5.5.14 to state which approach should be applied. Our recommendation is for the debit entry to be recognised on the balance sheet as an adjustment to the gross carrying value rather than ECL. This is preferable to an approach that results in the cumulative ECL being negative for loans with lifetime ECL that is lower than at initial recognition with the original estimate of lifetime ECL continuing to reverse through the credit adjusted EIR.

74. This issue has not been observed to be particularly widespread in practice, although the ECL of some POCI assets improves after acquisition. However, it must also be acknowledged that the ECL of many POCI assets does not improve, and if this is the case the issue does not arise. It would be a comparatively straightforward point for the IASB to address. We therefore rate this issue as of medium prevalence with a medium priority.

Question 7– Application of the impairment requirements in IFRS 9 with other requirements

Is it clear how to apply the impairment requirements in IFRS 9 with other requirements in IFRS 9 or with the requirements in other IFRS Accounting Standards? If not, why not?

EY's response

75. The interaction of the ECL requirements and the other requirements of IFRS 9 frequently give rise to complex questions of interpretation, which result in different treatments and inconsistent application. It is an area with a high prevalence of issues occurring and we, therefore, consider it to be a high priority to be addressed as part of the PIR.

76. We note in the conclusion of the PIR of the IFRS 9 Classification and Measurement requirements, the IASB decided to add a project to its research pipeline to consider modifications under IFRS 9 and application of the effective interest rate. These are high priority areas that interact with the ECL requirements, which we consider are a high priority for the IASB to tackle. We encourage the IASB to identify potential solutions as part of the ECL PIR where possible, as this will provide clarity sooner than if the issues are addressed only after the ECL PIR is complete. We discuss the issues in further detail and suggest some potential solutions below.

Interaction between modification, impairment, and derecognition requirements

77. We consider that the interaction between the ECL requirements and those in IFRS 9 for modification and derecognition would benefit from clarification. We regularly see challenges arising in these areas and consider that there would be significant benefit in terms of improving consistency and comparability if the IASB could provide further guidance.

78. A particular challenge arises in the case of a modification that takes place in the context of a loan restructuring. It is not clear, when applying IFRS 9, how to determine whether a modification is significant such that derecognition is required. We see different approaches applied in practice. The outcome is important since for a distressed loan that is modified such that the derecognition requirements are met, a gain or loss is recognised on disposal and, assuming the restructure results in the credit quality of the loan improving, the new loan will be classified as Stage 1, measured at fair value at initial recognition with a new EIR. The ECL movement tables will show a Stage 3 loan having been derecognised and a new Stage 1 loan entered into. Alternatively, if the modification does not result in derecognition the loan will transition back to Stage 1 of Stage 2 with no gain or loss on derecognition and the original EIR retained. This will show in the ECL movement tables as a movement from Stage 3 to Stage 1 or Stage 2. Whether the modification results in derecognition therefore significantly affects the accounting and related disclosure.

79. We observe that financial regulators in some locations appear to have a preference for entities not to derecognise a loan subject to restructuring but for it to be treated as modified. In such cases, regulators consider that reclassification of the loan to Stage 1 or Stage 2 provides greater transparency than if the loan were derecognised, which includes showing the evolution of loans subject to forbearance.

80. As a result of this type of intervention, banks may develop policies to align with certain regulators' expectations and this may give rise to diversity in practice, as expectations may differ between regulators and as unregulated entities may come to a different conclusion.

81. In light of this, tackling the areas of IFRS 9 that have been the focus of regulatory intervention, such as accounting for loan restructuring, we consider as a high priority.

Presentation of modification gains and losses versus impairment

82. When a modification arising from a loan restructuring does not result in derecognition, we observe different practices for how the modification gain or loss is presented. One approach is to present the gain or loss within impairment in the profit and loss, as it is considered to have arisen as a result of a credit deterioration. Another approach is to present it separately from ECL as a modification gain or loss, as it is considered to have arisen separately from the process by which ECL is calculated. It would be helpful if clarification were provided on the required treatment to improve consistency and comparability.

83. We suggest that it should be clarified that when a modification which is directly credit related arises, such as when a restructuring takes place, any gain or loss should be recognised as ECL. When a modification takes place which is not credit related e.g., it is due to normal commercial negotiations, the gain or loss should be accounted for in line with the requirements of IFRS

9.5.4.3 when the contractual cash flows are changed, or as part of the effective interest rate [IFRS 9 B5.4.5 and B5.4.6] when the estimated contractual cash flows change.

84. It should be reasonably straightforward to identify whether a modification is credit related as the lender will have recorded the credit status of the borrower for the purpose of its internal reporting and risk management. We propose that where the restructuring is to any extent credit related, the whole of the gain or loss should be recognised as ECL, i.e., we do not advocate trying to split the gain or loss between a portion that is credit related and a portion that is not. Only where there is evidence that the restructuring is not credit related to any extent, would the gain or loss be recognised as non-ECL.

Write-offs

85. There are various challenges associated with recognising write-offs, which we describe below.

Timing of write-off recognition

86. IFRS 9 provides guidance on when the ECL allowance is used, i.e., when it is applied against the gross carrying amount of a financial asset. This occurs when there is a write-off of a financial asset, which happens when the entity has no reasonable expectations of recovering the contractual cash flows on a financial asset in its entirety or a portion thereof. At the point of write-off, the entity has no reasonable expectation of obtaining further economic benefits. When this is the case, write-off occurs and is considered a derecognition event. [IFRS 9.5.4.4, IFRS 9.B3.2.16(r)].

87. Because IFRS 9 requires a loan to be written off in part when it is no longer expected that a portion of the amount due will be collected, the loan may be written off in partial amounts as Stage 3 progresses. This means that there may be no single 'write-off point'.

88. Practice varies in terms of the timing of the write-off and is sometimes dependent on the influence of prudential regulators. Write-off requirements in IFRS 9 are considered at each reporting date and are not delayed until some arbitrary past due date has been reached. On the other hand, if collection efforts continue and have some possibility of success, total write-off would also seem to be inappropriate.

If loss on write-off is greater than accumulated ECL

89. If the amount of loss on write-off is greater than the accumulated loss allowance, EY's view is that the difference will be an additional impairment loss. However, IFRS 9 is not clear on how this amount should be presented and there are different views, resulting in diversity in practice.

90. In situations where a further impairment loss occurs, the question has arisen as to how it is presented: simply as a loss in profit or loss arising on derecognition with a credit directly to the gross carrying amount; or first, as an addition to the ECL allowance that is then applied against the gross carrying amount. The difference between those alternatives is whether the additional impairment loss flows through the ECL allowance, showing up in a reconciliation of the allowance as an addition and a use (i.e., a write-off), or whether such additional impairment bypasses the allowance and is reflected in the income statement as a gain or loss on derecognition. The IASB's original 2009 ED (see section 1.1 above) explicitly mandated that all

write-offs could only be debited against the allowance, meaning that any direct write-offs against profit or loss without flowing through the allowance were prohibited. IFRS 9 does not presently include any similar explicit guidance on this issue. We suggest that it would be beneficial to include guidance consistent with that in the 2009 ED.

Subsequent recoveries and re-recognition

91. The standard does not provide guidance on accounting for subsequent recoveries of a financial asset. Arguably, there could be a higher threshold when recognising an asset that has been previously written-off and this is likely to be when cash is received rather than when the criteria for write-off are no longer met. It might also be argued that such recoveries are often not significant, as a write-off only occurs when there is no reasonable expectation of recovering the contractual cash flows. The occurrence of large recoveries subsequent to the recognition of total write-offs might suggest entities should reconsider their approach to future write-offs.

92. As the nature of such recoveries is similar to reversals of impairment, our view is that it makes sense to present such recoveries in the impairment line in profit or loss as it would provide useful and relevant information to the users of the financial statements [IAS 1.82(ba)]. This could be helpfully clarified as part of the PIR.

IFRS 7 disclosure of write-off versus enforcement activity

93. IFRS 7 requires an entity to disclose its policies in relation to write-offs and also, the amounts written off during the period that are still subject to enforcement activity. It is noted that there is a tension between this requirement and the criteria in IFRS 9 for write-offs, since it may be difficult to argue that there is no reasonable expectation of recovering the contractual cash flows if the loan is still subject to enforcement activity [IFRS 7.35F(e), IFRS 7.35L].

94. We note that this disclosure is intended to provide narrative information about the policy for balances that have previously been written-off so there is no reasonable expectation of recovery, but there is still a small chance that there will be a recovery, albeit the likelihood is extremely low [IFRS 7.BC 48J]. Any post-write-off recoveries arising from this outcome would correspond to the description in the paragraph above. It would be helpful if the IASB's intention for this disclosure were clarified in the body of the standard rather than in the BC.

Definition of 'no reasonable expectation of recovering'

95. It is noted that the requirement that the entity "has no reasonable expectations of recovering" in paragraph 5.4.4 of IFRS 9 is considered to be unclear with the result that there are different possible interpretations of when this condition is met.

96. We suggest that the judgments entities should make in relation to determining when write-off occurs, should include the interaction with the requirements for modification and forbearance. We expect that a write-off would not occur whilst discussions between the lender and the borrower are ongoing with respect to forbearance or potential modifications. Only when these have concluded and the lender expects to receive no further benefit, would a write-off occur.

Distinguishing between the effects of modification and write-off

97. If an entity has no reasonable expectation of recovering a portion of the financial asset, which is subsequently forgiven, then this amount is arguably written off, as a partial derecognition. The gross carrying amount would be reduced directly before a modification gain or loss is calculated. This would mean that the loss will be recorded as an impairment loss, rather than as a loss on modification, and presented differently in the profit or loss account.

98. In practice, it is often difficult to disentangle the effects of modification and write-off, as some forgone cash flows may be compensated for by a higher interest rate applied to the remaining contractual amounts due. It would be helpful if the IASB were to provide further application guidance in this area, to encourage consistency and comparability.

Question 8—Transition

Were the costs of applying the transition requirements and auditing and enforcing their application significantly greater than expected? Were the benefits to users significantly lower than expected?

EY's response

99. We consider that the transition requirements upon initial adoption of the ECL requirements work well and allow a reasonably smooth adoption. We support the general approach of IFRS 9 which does not require a restatement of comparative periods but an adjustment to opening retained earnings. This helped to reduce the challenge of what was anyway a complex implementation exercise.

100. Whilst this approach resulted in a lack of comparative information upon initial adoption, we are not convinced that the comparative information could have been accurately produced without undue cost and effort if had it been required. This is because entities would not have had sufficient data to retrospectively recreate the results for a comparative period. Alternatively, the date of mandatory application could have been delayed, allowing a comparative period to be produced more easily, but this has two notable disadvantages;

i) The reporting benefits to users of entities applying IFRS 9 would have been deferred; and
ii) Preparers would have had the increased cost and complexity of running two credit loss impairment models in parallel, in full.

We therefore support the transition approach required for ECL.

Question 9—Credit risk disclosures

(a) Are there fundamental questions (fatal flaws) about the disclosure requirements in IFRS 7 for credit risk? If yes, what are those fundamental questions?

(b) Are the costs of applying these disclosure requirements and auditing and enforcing their application significantly greater than expected? Are the benefits to users significantly lower than expected?

EY's response

101. (a) We acknowledge that the Expected Credit Loss (ECL) model in IFRS 9 is inherently judgemental. Consequently, there are potential limitations in meeting the disclosure objectives of IFRS 7 Financial Instrument Disclosures (IFRS 7). Acknowledging this need for judgment, we recommend that the appropriate response is not to move from a principle-based model to one that has uniform requirements for all entities. Rather, it is our proposal to enhance the disclosure requirements using illustrative examples and application guidance. If these disclosures are determined to be material to an entity, then their inclusion in the financial statements will facilitate the meeting of the disclosure objectives in IFRS 7, and enhance the comparability of the financial statements, thereby providing useful information to users.

102. It is also acknowledged that IFRS 7 is a general purpose (and not an industry specific) standard, and, therefore there needs to be a balance between the disclosures relevant for larger financial service entities, and those relevant to other entities. If there are illustrative examples or application guidance embedded in IFRS 7, then an entity would need to assess if the disclosure is relevant, or material, to their users. It may be helpful to acknowledge this in the application guidance.

103. IFRS 7 provides objective-based disclosure requirements for credit risk. However, we are of the view that for ECL disclosures, in order to aid comparability, a preferred approach would be to add minimum mandatory disclosures, specify the format of some disclosures or add particular illustrative examples in IFRS 7.

104. In line with the points above, the direction taken by the Taskforce on Disclosures about Expected Credit Losses (DECL) in the UK is useful to consider. In 2017 key stakeholders jointly came to the conclusion that, to help encourage high-quality ECL-related disclosure "something more was needed" than the requirements of IFRS 7 (and IFRS 9) alone. The objective of the report is "to promote high-quality disclosures about ECL and, over time, to take steps to encourage greater consistency between and comparability of those disclosures, whilst recognising the need for the disclosures to reflect each reporting entity's facts and circumstances." It is clear from the direction taken involving a number of key stakeholders across the industry, that more guidance and standardisation of disclosures is needed in order to improve quality and drive consistency. It is proposed that many of the disclosure recommendations from the third DECL report[4] would be a good starting point for improving disclosures and comparability.

105. (b) With regards to the question on whether the IASB should add specific disclosure requirements for credit risk, we recommend that the IASB should add minimum mandatory disclosures, specify the format of some disclosures or add particular illustrative examples. This will add more useful information for users by consistently outlining the nature and extent of the risks arising from the financial instruments. As requested, we have described those requirements in Appendix A and explained how they will provide useful information to users of financial statements.

[4] A third report prepared by The Taskforce on Disclosures about Expected Credit Losses

106. ECL disclosures can also be particularly difficult to compare between entities due to the lack of standardised levels of granularity and disaggregation. This is also as a result of the requirement that certain disclosures required by IFRS 7 should be provided by class of financial instrument. In determining these classes, financial instruments in the same class should reflect shared economic characteristics with respect to credit risk [IFRS 7.IG21]. It is clear from this requirement that the classes used are not necessarily the same for each disclosure provided, e.g., one set of classes may be used to present information about credit risk and another for information about day 1 profits. In particular, classes should be determined by the entity and are, thus, distinct from the categories of financial instruments specified in IFRS 9, and will largely differ from entity to entity.

107. Therefore, we consider it critical to clarify what constitutes a 'class' of financial instrument, which should be linked to how an entity manages risk. Therefore, in addition to clarifying what constitutes a class, the requirements could also be illustrated by means of an example. For instance, it could be demonstrated that if retail loans are modelled and managed differently to credit card loans, then these would constitute different classes. Importantly, the example should also illustrate disclosure of how these classes were defined, and any judgements related thereto. As 'class' is the cornerstone for the IFRS 7 disclosures, this would help improve comparability between entities.

108. With regards to the question on whether entities' credit risk disclosures are compatible with digital reporting, and specifically whether users of financial statements can effectively extract, compare and analyse credit risk information digitally, we note that this is essentially linked to the point above relating to consistent application of what constitutes a class. That is consistent application of 'class' will more effectively allow users to extract, compare and analyse credit risk information digitally.

109. IFRS 7 does not always require the gross carrying amount and ECL to be disclosed at the same time for the same disclosure, which hinders the granularity of the disclosures, and decreases the usefulness of that disclosure. For example, the maximum exposure to credit risk, and concentration of credit risk disclosures are often provided on a net basis (after ECL) or on a gross basis without disclosing what the related ECL is. It would be more useful if both the gross carrying amount and the related ECL were disclosed at the same time so that users could understand both the risk exposure and how it has been provided for. For example, it would be useful if the information required in IFRS 7.35M of credit risk exposure by credit risk rating grades were required for both the gross carrying amounts, and the associated ECLs. This would allow calculation of coverage ratios. See Appendix A (VII).

110. With regards to Question 3, when it comes to staging, it is unclear how the SICR triggers work in practice when different entities are compared. It is suggested that it would be useful for entities to disclose the reliance on the '30 days past due' trigger when it comes to the SICR assessment, as this is a commonly used trigger that users understand. Similar to the DECL III guidance in F5 (see Appendix A (IV) and (V)), it would be useful if entities disclosed how much of the movement into Stage 2 was due to reliance on the 30 days assessment; and how much of the total stage balance relates to 30 days past due accounts. Furthermore, it would be useful to understand the credit quality at origination of the asset. As SICR is based on a relative increase in credit risk, it is important to understand the starting point for such relative analysis.

111. Related to Question 4 on forward looking scenarios, to increase users' understanding of the judgements being applied, and to increase the consistency and comparability of disclosures, key recommended disclosures for users would be:

i. Qualitative and quantitative information on the weighting of the multiple economic scenarios). See Appendix A (IX).

ii. Inputs and assumptions used in the ECL calculation, including the actual and forecasted inputs. See Appendix A (VIII).

(Note, See Appendix A (X) where the 2 points above are disclosed together i.e. disclosure of scenario weightings, together with current and forecasted inputs and assumptions)

iii. Related sensitivity disclosures. It would be useful if these disclosures were defined in order to standardise the sensitivity disclosures. For example, this could be similar to the disclosures required by IFRS 13.93(h). An option could also be to disclosure the effect on ECL resulting from applying a 100% weighting to selected scenarios. See Appendix A (VI). It may also be useful to provide a graph for a selected macroeconomic assumption, such as GDP to illustrate the overall shape of the scenarios. To the extent that other macroeconomic assumptions are expected to behave differently and not follow the overall shape, it may be appropriate to provide additional graphs. See Appendix A (XI).

112. In line with the concerns noted in Question 4 relating to PMAs, if PMAs are a significant or material judgement for the entity, then disclosures of these adjustments should be made. Useful recommendations would be to:

- Disclose the impact of PMAs vs modelled outcomes, including the underlying reasons for the PMA's. For examples on this see Appendix A (II) & (III).
- To provide information about how the PMAs unwind. For example, this could be linked to the reason for the PMA i.e. if a PMA was created relating to Covid, then disclosure would include management's expectations with regards to when or how this PMA would unwind.
- For the disclosures relating to PMAs to mirror the disclosures of the modelled outcomes e.g. to break down per risk ratings, sectors, staging etc.

113. More detailed disclosure of an entity's write-off policy will also aid transparency, complimented by quantitative disclosures or illustrative examples (it is acknowledged that there are requirements in IFRS 7.35F (e) relating to write-off disclosures, and as such, this may benefit from illustrative examples). See example in Appendix A (I).

Question 10—Other matters

(a) Are there any further matters that you think the IASB should examine as part of the post-implementation review of the impairment requirements in IFRS 9? If yes, what are those matters and why should they be examined?

(b) Do you have any feedback on the understandability and accessibility of the impairment requirements in IFRS 9 that the IASB could consider in developing its future IFRS Accounting Standards?

EY's response

114. (a) and (b) EY has no further views on these matters and has addressed any additional matters while answering the previous questions.

Appendix A

It is our proposal to enhance the disclosure requirements through illustrative examples and application guidance to clearly facilitate the meeting of the disclosure objectives in IFRS 7. We have included below suggestions of useful disclosures noted in practice.

I. Write off disclosures

Example of write-off disclosures
Changes in impaired financial assets written-off from the balance sheet

	2022	2021
Balance at the beginning		
Increase		
Decrease:		
Re-financing or restructuring		
Cash recovery		
Foreclosed assets		
Sales		
Debt forgiveness		
Time-barred debt and other causes		
Exchange differences		
Balance at the end		

II. Impact of PMAs vs modelled outcomes - example as per the DECL report

B.8 Example 1 – Quantitative disclosure (includes a split by DECL Groupings)

The disclosure below provides an illustrative example of a quantitative disclosure of judgemental adjustments made in accordance with this recommendation. The disclosure does not include a description of all the judgements required to estimate ECLs.

	31 December 20XX		
	Retail - mortgages**	**Corporate loans****	**Total**
	£m	£m	£m
ECL before judgemental adjustments (A)	**x**	**x**	**x**
Judgemental adjustments			
*Impact of government support measures**	*x*	*x*	*x*
*Adjustment for vulnerable sectors**	*x*	*x*	*x*
*Adjustment to modelled forecast parameters**	*x*	*x*	*x*
Other judgemental adjustments	*x*	*x*	*x*
Total judgemental adjustments (B)	**x**	**x**	**x**
Total reported ECL (A + B)	**x**	**x**	**x**

** The line items included in this example disclosure are for illustrative purposes only, the material judgemental adjustments disclosed for a particular bank would depend on the specific facts and circumstances.*
*** The column headers included in this example disclosure are for illustrative purposes only and are based on an entity that solely operates in the UK where it offers retail mortgages and corporate loans.*

The objective of the table is to quantify management's material judgemental adjustments, identified as part of the bank's relevant governance processes, and illustrate their relevance in the context of the reported ECL. The amount recorded as 'ECL before judgemental adjustments' is the aggregate of the modelled ECL plus any non-judgemental adjustments and enables reconciliation from the 'Judgemental adjustments' to the 'Total reported ECL'. The amount recorded under 'Other judgemental adjustments' includes any judgemental adjustments that may not be individually material but are so on an aggregate basis.

III. Impact of PMAs vs modelled outcomes with reasons - example as per the DECL report B.8 Example 2 – Qualitative disclosure

Recommendations on a comprehensive set of IFRS 9 ECL disclosures

	Modelled ECL £m	Individually assessed £m	Judgements due to COVID-19[1] £m	Other judgements £m	Total ECL £m
At 31 December 2021					
UK mortgages	**292**	**–**	**67**	**478**	**837**
Credit cards	**436**	**–**	**94**	**(9)**	**521**
Other Retail	**801**	**–**	**57**	**50**	**908**
Commercial Banking	**281**	**905**	**161**	**(14)**	**1,333**
Other	**43**	**–**	**400**	**–**	**443**
Total	**1,853**	**905**	**779**	**505**	**4,042**
At 31 December 2020					
UK mortgages	481	–	36	510	1,027
Credit cards	851	–	128	(56)	923
Other Retail	1,209	–	193	43	1,445
Commercial Banking	1,051	1,222	131	(2)	2,402
Other	50	–	400	–	450
Total	3,642	1,222	888	495	6,247

The bank also includes qualitative disclosure (an extract from the 2020 annual report is shown below) on the nature of material adjustments made to the modelled ECL, including an explanation of the circumstances under which the adjustment may be unwound and timeframe for such an event.

Other: £400 million

Central overlay in respect of economic uncertainty: £400 million

An important element of the methodology used to calculate the Group's ECL allowance is the determination of a base case economic scenario, predicated on certain conditioning assumptions, from which alternative scenarios are derived using stochastic shocks. The rapid evolution of the pandemic and significant changes that this has brought about could continue into 2021 and may partially invalidate the conditioning assumptions that underpin the Group's base case scenario. Management believes that the risks to the conditioning assumptions around the base case scenario are markedly to the downside, reflecting notably the potential for a material delay in the vaccination programme or reduction in its effectiveness from further virus mutation and the corresponding delayed withdrawal of restrictions on social interaction or introduction of further lockdowns. The Group's ECL allowances are required to reflect an unbiased probability-weighted view of all possible future outcomes and therefore management believes that an adjustment is required to capture these additional risks.

An adjustment of £400 million has been made to increase the Group's ECL allowances to reflect this increased uncertainty around the conditioning assumptions. This equates to a 1 percentage point increase in unemployment allied with a 5 per cent lower HPI in 2021, reflecting a more immediate and therefore greater ECL impact than the gradual increase reflected in the stated univariate sensitivity. It is proportionate to the level of volatility seen in forecasts as the pandemic has unfolded and is also equivalent to a 10 per cent re-weighting from the upside to the severe downside scenario. The adjustment, which has not been allocated to a specific portfolio, has been allocated against Stage 1 assets given the downside risks are largely considered to relate to exposures with currently low default probabilities, the majority of which are in Stage 1. Through 2021 the scale of the uncertainty is expected to diminish and the need for this adjustment will then be reassessed.

IV. Example as per the DECL report F.5 Example 1 – Stage 2 analysis -SICR triggers

The purpose of this disclosure is to explain the different reasons why exposures are in stage 2 at the balance sheet date. Exposures in stage 2 often meet a number of the possible criteria ('reasons') for which a transfer to stage 2 would occur but, as the sum of the exposures and ECL provisions shown in the table need to be the aggregate exposures and ECL provision, the table can reflect only one of those reasons.

While the disclosure looks at the reason for an exposure being in stage 2 at the balance sheet date, banks may also in addition disclose the original reason for the stage 2 transfer to provide additional insight into stage allocation methodology.

This disclosure helps users to better understand changes in credit quality during the reporting period.

F.5 Example 1 – Stage 2 analysis

31 December 20XX

Loans and advances to customers[1]

£m GCA = gross carrying amount				**PD movement**	**Forbearance support provided**	**Probation ary period**	**Other qualitative reasons**	**>30 days past due**	**Total**
UK	Drawn	Retail – mortgages	GCA	X	X	X	X	X	**X**
			ECL	X	X	X	X	X	**X**
			Coverage	X%	X%	X%	X%	X%	**X%**
		Retail – credit cards	GCA	X	X	X	X	X	**X**
			ECL	X	X	X	X	X	**X**
			Coverage	X%	X%	X%	X%	X%	**X%**
		Retail – other	GCA	X	X	X	X	X	**X**
			ECL	X	X	X	X	X	**X**
			Coverage	X%	X%	X%	X%	X%	**X%**
		Corporate loans	GCA	X	X	X	X	X	**X**
			ECL	X	X	X	X	X	**X**
			Coverage	X%	X%	X%	X%	X%	**X%**
Rest of the World (drawn)[2]			GCA	X	X	X	X	X	**X**
			ECL	X	X	X	X	X	**X**
			Coverage	X%	X%	X%	X%	X%	**X%**
Total (drawn)[2]			***GCA***	***X***	***X***	***X***	***X***	***X***	**X**
			ECL	***X***	***X***	***X***	***X***	***X***	**X**
			Coverage	***X%***	***X%***	***X%***	***X%***	***X%***	**X%**
Undrawn[2]			***ECL***	***X***	***X***	***X***	***X***	***X***	**X**
Total reported			**GCA**	**X**	**X**	**X**	**X**	**X**	**X**
			ECL	**X**	**X**	**X**	**X**	**X**	**X**

[1]Depending on materiality, disclosures for product groupings other than loans and advances to customers may also be provided.

[2]In this illustrative example, the preparer has provided the analysis of the stage 2 population of loans and advances to customers by reason for inclusion in stage 2 as at the balance sheet date) in accordance with the DECL Groupings. If an entity elects to present the information in accordance with the DECL Groupings, then depending on materiality, in some cases, the Rest of the World (drawn) and undrawn balances may be further disaggregated by product groupings and/or geography. In other cases, it may be appropriate to provide their respective relevant total amounts to reconcile to the total reported GCA and ECL amounts.

V. Extract from EY's illustrative financial statements- Good Bank 2022[5]
-Illustration of SICR triggers, including 30 days past due

Analysis of stage 2 loans reflecting the criteria for inclusion in stage 2

An analysis of stage 2 balances at the reporting date reflecting the reasons for inclusion in stage 2 by class of loans and advances to customers (gross carrying amount and corresponding ECL) is presented below. For the purposes of this analysis, where balances satisfy more than one criterion for determining a significant increase in credit risk, the corresponding gross carrying amount and ECL have been assigned in the order of the categories presented, for example, accounts with PD deterioration may also trigger backstops, but are only reported under "PD movement".

The indicators of significant increases in credit risk (SICR) are explained in Note 48.2.3.5.

In $ million	**Corporate lending**		**Small business lending**		**Consumer lending**		**Residential mortgages**		**Total Stage 2**	
31 December 2022	**Gross carrying amount**	**ECL**	**Gross carrying amount**	**ECL**	**Gross carrying amount**	**ECL**	**Gross carrying amount**	**ECL**	**Gross carrying amount**	**ECL**
Less than 30 dpd	1,857	81	1,262	93	5,307	210	1,150	61	**9,576**	**445**
- *PD movement*	703	33	860	69	3,178	138	214	18	**4,955**	**258**
- *Forbearance support provided*	1,075	44	202	10	1,029	19	792	32	**3,098**	**105**
- *Other qualitative reasons*	79	4	200	14	1,100	53	144	11	**1,523**	**82**
More than 30 dpd	206	36	198	15	564	27	103	10	**1,071**	**88**
Total	**2,063**	**117**	**1,460**	**108**	**5,871**	**237**	**1,253**	**71**	**10,647**	**533**

In $ million	**Corporate lending**		**Small business lending**		**Consumer lending**		**Residential mortgages**		**Total**	
31 December 2021	**Gross carrying amount**	**ECL**	**Gross carrying amount**	**ECL**	**Gross carrying amount**	**ECL**	**Gross carrying amount**	**ECL**	**Gross carrying amount**	**ECL**
Less than 30 dpd	1,894	75	1,371	69	5,726	203	1,795	77	**10,786**	**424**
- *PD movement*	513	24	863	40	2,651	96	711	39	**4,738**	**199**
- *Forbearance support provided*	1,163	42	197	12	1,009	34	773	25	**3,142**	**113**
- *Other qualitative reasons*	218	9	311	17	2,066	73	311	13	**2,906**	**112**
More than 30 dpd	309	13	173	9	334	23	133	11	**949**	**56**
Total	**2,203**	**88**	**1,544**	**78**	**6,060**	**226**	**1,928**	**88**	**11,735**	**480**

[5] EY Good Bank (International) Limited Consolidated financial statements 31 December 2022

VI. Sensitivity analysis – example as per DECL G.4 Example 1 – Quantitative information: example of a table showing the gross exposure and the effect on ECL resulting from applying a 100% weighting to selected scenarios (at least for central, upside and downside).

Recommendations on a comprehensive set of IFRS 9 ECL disclosures

G.4 Example 1 – Quantitative information: example of a table showing the gross exposure and the effect on ECL resulting from applying a 100% weighting to selected scenarios (at least for central, upside and downside).

31 December 20XX	Scenarios			
	Weighted	**Upside**	**Central**	**Downside**
Stage 1 Gross Exposure (£m)				
Retail - mortgages	11,889	12,554	12,158	11,233
Retail - credit cards	7,924	8,368	8,103	7,487
Retail - other	5,945	6,279	6,080	5,618
Corporate loans	19,806	20,910	20,249	18,709
Stage 1 ECL (£m)				
Retail - mortgages	2	1	2	8
Retail - credit cards	135	142	138	129
Retail - other	90	95	92	85
Corporate loans	270	285	276	255
Stage 1 Coverage (%)				
Retail - mortgages	0.0	0.0	0.0	0.1
Retail - credit cards	1.7	1.7	1.7	1.7
Retail - other	1.5	1.5	1.5	1.5
Corporate loans	1.4	1.4	1.4	1.4
Stage 2 Gross Exposure (£m)				
Retail - mortgages	1,326	661	1,057	1,982
Retail - credit cards	884	440	705	1,321
Retail - other	664	330	529	991
Corporate loans	2,204	1,101	1,761	3,302
Stage 2 ECL (£m)				
Retail - mortgages	30	10	27	62
Retail - credit cards	153	80	125	214
Retail - other	50	30	42	60
Corporate loans	300	101	247	499
Stage 2 Coverage (%)				
Retail - mortgages	2.3	1.5	2.6	3.1
Retail - credit cards	17.3	18.2	17.7	16.2
Retail - other	7.5	9.1	7.9	6.1
Corporate loans	13.6	9.2	14.0	15.1
Stage 3 Gross Exposure (£m)				
Retail - mortgages	120	120	120	120
Retail - credit cards	406	406	406	406
Retail - other	55	55	55	55
Stage 3 ECL (£m)				
Retail - mortgages	18	15	20	30
Retail - credit cards	307	265	315	399
Retail - other	30	25	29	41
Stage 3 Coverage (%)				
Retail - mortgages	15.0	12.5	16.7	25.0
Retail - credit cards	75.6	65.3	77.6	98.3
Retail - other	54.5	45.5	52.7	74.5
Total Gross Exposure (£m)				
Retail – mortgages	13,335	13,335	13,335	13,335
Retail - credit cards	9,214	9,214	9,214	9,214
Retail - other	6,664	6,664	6,664	6,664
Corporate loans	22,010	22,010	22,010	22,010
Total Gross Exposure (£m)	**51,223**	**51,223**	**51,223**	**51,223**
Total ECL (£m)				
Retail - mortgages	50	26	49	100
Retail - credit cards	595	487	578	742
Retail - other	170	150	163	186
Corporate loans	570	386	523	754
Total ECL (£m)	**1,385**	**1,049**	**1,313**	**1,782**

Reconciliation from reported ECL to sensitised weighted ECL*	**ECL £m**
Loans and advances to customers	2,014
Loan commitments and other off-balance sheet exposures to customers	58
Total ECL on gross exposures to customers	2,072
Items excluded from macro-economic sensitivity analysis:	
ECL on corporate loan stage 3 exposures not materiality sensitive	(139)
Judgemental adjustments made outside the ECL model (see further, note X)	(548)
Total weighted ECL included in sensitivity analysis	1,385

Recommendations on a comprehensive set of IFRS 9 ECL disclosures

Reconciliation from reported gross exposure to sensitised gross exposure	**£m**
Gross carrying amount of loans and advances to customers	37,601
Total undrawn loan commitments and other off-balance sheet exposures to customers	13,907
Total gross exposures to customers	51,508
Items excluded from macro-economic sensitivity analysis:	
Gross exposure corporate loan stage 3 exposures not materiality sensitive	(285)
Total gross exposure included in sensitivity analysis	51,223

**The reconciliations to reported Gross Exposure and ECL should include line items and detail as appropriate. In addition, narrative should be given to explain reconciling items to the extent not obvious from the line description. For judgemental adjustments the reconciliation may cross refer to the disclosures made under recommendation B.8 explaining the judgemental adjustments. A note to this table should explain how the judgemental adjustments might change under different scenarios (see 6th bullet below).*

VII. DECL - Good practice example Recommendation F.1
-Disclosure of credit risk exposure by credit risk rating grades showing both the gross carrying amounts, and the associated ECLs, allowing calculation of coverage ratios

Recommendations on a comprehensive set of IFRS 9 ECL disclosures

Wholesale lending – credit risk profile by obligor grade for loans and advances at amortised cost

		Gross carrying amount					Allowance for ECL						
	Basel one-year PD range	Stage 1	Stage 2	Stage 3	POCI	Total	Stage 1	Stage 2	Stage 3	POCI	Total	ECL coverage	Mapped external rating
	%	$m	$m	$m	$m	$m	$m	$m	$m	$m	$m	%	
Corporate and commercial		400,894	98,911	13,460	274	513,539	(665)	(1,874)	(5,601)	(64)	(8,204)	1.6	
– CRR 1	0.000 to 0.053	40,583	599	–	–	41,182	(7)	(1)	–	–	(8)	–	AA- and above
– CRR 2	0.054 to 0.169	78,794	4,843	–	–	83,637	(26)	(43)	–	–	(69)	0.1	A+ to A-
– CRR 3	0.170 to 0.740	139,739	19,199	–	–	158,938	(165)	(145)	–	–	(310)	0.2	BBB+ to BBB-
– CRR 4	0.741 to 1.927	91,268	23,365	–	–	114,633	(218)	(258)	–	–	(476)	0.4	BB+ to BB-
– CRR 5	1.928 to 4.914	45,850	28,375	–	–	74,225	(185)	(424)	–	–	(609)	0.8	BB- to B
– CRR 6	4.915 to 8.860	3,280	11,197	–	–	14,477	(22)	(242)	–	–	(264)	1.8	B-
– CRR 7	8.861 to 15.000	1,101	4,406	–	–	5,507	(24)	(167)	–	–	(191)	3.5	CCC+
– CRR 8	15.001 to 99.999	279	6,927	–	4	7,210	(18)	(594)	–	–	(612)	8.5	CCC to C
– CRR 9/10	100.000	–	–	13,460	270	13,730	–	–	(5,601)	(64)	(5,665)	41.3	D
Non-bank financial institutions		61,086	3,874	395	–	65,355	(44)	(26)	(40)	–	(110)	0.2	
– CRR 1	0.000 to 0.053	14,370	122	–	–	14,492	(2)	(1)	–	–	(3)	–	AA- and above
– CRR 2	0.054 to 0.169	16,438	43	–	–	16,481	(5)	–	–	–	(5)	–	A+ to A-
– CRR 3	0.170 to 0.740	18,282	1,026	–	–	19,308	(11)	(4)	–	–	(15)	0.1	BBB+ to BBB-
– CRR 4	0.741 to 1.927	6,835	1,204	–	–	8,039	(15)	(11)	–	–	(26)	0.3	BB+ to BB-
– CRR 5	1.928 to 4.914	5,053	1,297	–	–	6,350	(11)	(4)	–	–	(15)	0.2	BB- to B
– CRR 6	4.915 to 8.860	102	98	–	–	200	–	(5)	–	–	(5)	2.5	B-
– CRR 7	8.861 to 15.000	5	25	–	–	30	–	(1)	–	–	(1)	3.3	CCC+
– CRR 8	15.001 to 99.999	1	59	–	–	60	–	–	–	–	–	–	CCC to C
– CRR 9/10	100.000	–	–	395	–	395	–	–	(40)	–	(40)	10.1	D
Banks		81,636	1,517	–	–	83,153	(14)	(3)	–	–	(17)	–	
– CRR 1	0.000 to 0.053	61,275	10	–	–	61,285	(4)	–	–	–	(4)	–	AA- and above
– CRR 2	0.054 to 0.169	11,628	65	–	–	11,693	(3)	–	–	–	(3)	–	A+ to A-
– CRR 3	0.170 to 0.740	3,935	102	–	–	4,037	(2)	–	–	–	(2)	–	BBB+ to BBB-
– CRR 4	0.741 to 1.927	4,232	180	–	–	4,412	(5)	–	–	–	(5)	0.1	BB+ to BB-
– CRR 5	1.928 to 4.914	556	52	–	–	608	–	(1)	–	–	(1)	0.2	BB- to B
– CRR 6	4.915 to 8.860	9	541	–	–	550	–	–	–	–	–	–	B-
– CRR 7	8.861 to 15.000	1	564	–	–	565	–	–	–	–	–	–	CCC+
– CRR 8	15.001 to 99.999	–	3	–	–	3	–	(2)	–	–	(2)	66.7	CCC to C
– CRR 9/10	100.000	–	–	–	–	–	–	–	–	–	–	–	D
At 31 Dec 2021		543,616	104,302	13,855	274	662,047	(723)	(1,903)	(5,641)	(64)	(8,331)	1.3	

Personal lending – credit risk profile by internal PD band for loans and advances to customers at amortised cost

		Gross carrying amount				Allowance for ECL				
	PD range[1]	Stage 1	Stage 2	Stage 3	Total	Stage 1	Stage 2	Stage 3	Total	ECL coverage
	%	$m	$m	$m	$m	$m	$m	$m	$m	%
First lien residential mortgages		360,686	7,637	3,045	371,368	(128)	(131)	(416)	(675)	0.2
– Band 1	0.000 to 0.250	310,042	451	–	310,493	(30)	(5)	–	(35)	–
– Band 2	0.251 to 0.500	19,741	203	–	19,944	(7)	(2)	–	(9)	–
– Band 3	0.501 to 1.500	25,835	1,936	–	27,771	(79)	(8)	–	(87)	0.3
– Band 4	1.501 to 5.000	4,976	2,657	–	7,633	(12)	(30)	–	(42)	0.6
– Band 5	5.001 to 20.000	88	1,416	–	1,504	–	(35)	–	(35)	2.3
– Band 6	20.001 to 99.999	4	974	–	978	–	(51)	–	(51)	5.2
– Band 7	100.000	–	–	3,045	3,045	–	–	(416)	(416)	13.7
Other personal lending		96,270	8,802	1,897	106,969	(530)	(1,088)	(810)	(2,428)	2.3
– Band 1	0.000 to 0.250	45,049	187	–	45,236	(50)	(13)	–	(63)	0.1
– Band 2	0.251 to 0.500	12,625	605	–	13,230	(27)	(6)	–	(33)	0.2
– Band 3	0.501 to 1.500	22,791	1,518	–	24,309	(102)	(30)	–	(132)	0.5
– Band 4	1.501 to 5.000	13,006	2,360	–	15,366	(213)	(108)	–	(321)	2.1
– Band 5	5.001 to 20.000	2,732	3,257	–	5,989	(138)	(554)	–	(692)	11.6
– Band 6	20.001 to 99.999	67	875	–	942	–	(377)	–	(377)	40.0
– Band 7	100.000	–	–	1,897	1,897	–	–	(810)	(810)	42.7
At 31 Dec 2021		456,956	16,439	4,942	478,337	(658)	(1,219)	(1,226)	(3,103)	0.6

1 12-month point in time adjusted for multiple economic scenarios.

VIII. DECL Recommendation C.4
-Explanation regarding inputs and assumptions used when determining the probability-weighted outcome of ECL which takes into consideration a range of possible outcomes.

In addition, the following extract from the 2020/21 annual report for Nationwide Building Society was identified as an example of good practice as it clearly discloses the economic variables across the forward-looking economic scenarios.

Economic variables

	Rate/annual growth rate at December 2021-2026						5-year average (note i)	Dec-21 to peak (notes ii and iii)	Dec-21 to trough (notes ii and iii)
	Actual	Forecast							
	2021	2022	2023	2024	2025	2026			
4 April 2022	%	%	%	%	%	%	%	%	%
GDP growth									
Upside scenario	8.3	4.2	2.5	2.0	2.0	2.0	2.5	13.4	1.5
Base case scenario	8.3	2.3	1.7	1.5	1.4	1.4	1.7	8.6	0.7
Downside scenario	8.3	2.5	(3.9)	1.7	2.2	2.2	0.9	4.6	(1.5)
Severe downside scenario	8.3	(4.5)	2.6	2.0	1.9	1.6	0.7	3.6	(4.5)
HPI growth									
Upside scenario	10.6	6.1	3.7	4.0	3.8	3.8	4.3	23.2	2.0
Base case scenario	10.6	3.5	2.4	2.8	3.2	3.2	3.1	16.2	1.5
Downside scenario	10.6	1.5	(10.6)	(8.4)	5.6	5.0	(1.6)	2.0	(16.9)
Severe downside scenario	10.6	(1.8)	(23.6)	(5.5)	3.7	7.7	(4.6)	1.2	(29.2)
Unemployment									
Upside scenario	4.1	3.5	3.6	3.9	3.9	3.9	3.8	3.9	3.5
Base case scenario	4.1	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.0
Downside scenario	4.1	4.7	6.9	5.3	5.0	4.9	5.3	7.0	3.6
Severe downside scenario	4.1	9.4	8.2	6.2	5.5	5.3	6.7	10.0	4.1
Consumer price inflation									
Upside scenario	5.4	5.0	1.6	1.9	2.0	2.0	2.9	7.5	1.3
Base case scenario	5.4	5.0	1.8	1.7	2.0	2.0	2.9	7.5	1.6
Downside scenario	5.4	10.0	1.0	0.3	0.3	1.2	3.1	10.0	0.3
Severe downside scenario	5.4	3.0	(0.2)	0.0	0.0	0.1	1.2	7.0	(0.4)

IX. Recommendation C.4 from the DECL report showing the weightings assigned to the macroeconomic scenarios.

Recommendation C.4

The following extract from the 2021 annual report for Santander UK shows disclosure of the weightings assigned to forward-looking economic scenario for both the current period and the previous reporting period. The Taskforce noted that this enabled users to clearly understand how weightings have changed over periods – this was noted to be particularly valuable where the macro-economic outlook changed significantly between reporting periods

Scenario weights

Given the change to the base case in Q4 2021, we undertook a full review of the probability weights applied to all the scenarios. The setting of probability weights needs to consider both the probability of the economic scenarios occurring while ensuring that the scenarios capture the non-linear distribution of losses across a reasonable range. To support the initial assessment of how likely a scenario is to occur, we typically undertake a Monte Carlo analysis which would ascertain the likelihood of a five-year average GDP forecast growth rate occurring based on the long run historically observed average. Creating a standard distribution bell curve around this long run average allows us to estimate the probability of a given GDP scenario occurring and therefore assign a probability weight to that scenario. However, a key challenge with this approach in a stressed environment like the one seen in 2020 is that extreme GDP forecasts occur.

Due to the extreme falls in growth, in 2020 we changed the time period that we looked at for the Monte Carlo analysis to 2007-2012 in order to capture the very low period of growth, similar to those seen in 2020. However, this time period is no longer appropriate as the economy recovers resulting in large upswings in growth. As such, we have assessed various periods of growth, similar to the action we took in 2020, and the most relevant period would be to include the entire data set given that the number of growth periods since 1948 far outweighs the downswings. In this case, the base case sits at the 10th percentile with such a growth rate occurring, historically, nearly half the time (43%) implying that a weight of between 40-50% remains appropriate. Under the longer period, the Downside 3 scenario now sits in the 50th percentile since the number of significant quarterly growth periods is increasing as we move through 2021. However, this still suggests that a low weight remains appropriate.

We also need to consider the UK economic and political environment when applying weights. Although the economic recovery has started, it is clear that the roadmap will need to be altered in order to deal with any increasing infection rates caused by new variants, particularly as they are appearing regularly and vaccines may need to evolve further to deal with potential resistance to them. As such, we remain of the view that the risks are still biased to the downside and include: emergence of further variants that are resistant to existing vaccines leading to further lockdowns - at present the Omicron variant is an example of where uncertainty is affecting the UK economy via self-imposed restrictions as well as those mandated by the UK Government; a substantial increase in inflation; continuing weak investment; a larger negative impact from the EU trade deal than assumed; and the increasing possibility of a second Scottish referendum which may bring disruption to any recovery in the latter years of the forecast. As such, it remains appropriate to reflect this with a 50% weight for the downside scenarios.

The scenario weights we applied for 2021 and 2020 were:

Scenario weights	Upside 1 %	Base case %	Downside 1 %	Downside 2 %	Downside 3 %
2021	5	45	25	20	5

Scenario weights	Upside 1 %	Base case %	Downside 1 %	Downside 2 %	Downside 3 %
2020	5	45	15	25	10

X. Extract from EY's illustrative financial statements- Good Bank 2022
Disclosure of scenario weightings, together with inputs and assumptions (both current year, and forecasted inputs).

48.2. Credit risk *continued*

48.2.4. Analysis of inputs to the ECL model under multiple economic scenarios per geographic regions continued

48.2.4.1. Goodland

IFRS 7.35G(a)
EDTF 2
EDTF 3

31 December 2022

Key drivers	ECL Scenario	Assigned Weightings	2022	2023	2024	2025	2026	Long term rate
		%	%	%	%	%	%	%
GDP growth %[1]								
	Upside	30	1.5	3.0	2.8	2.3	2.1	1.4
	Base case	40	1.0	1.3	1.4	1.3	1.2	1.4
	Downside 1	15	(1.4)	(2.5)	(1.4)	(1.0)	(0.5)	1.4
	Downside 2	15	(2.5)	(4.0)	(2.8)	(2.1)	(1.5)	1.4
Unemployment rates %[2]								
	Upside	30	4.7	4.3	4.2	4.2	4.0	4.8
	Base case	40	5.5	5.8	5.6	5.4	5.2	4.8
	Downside 1	15	6.1	7.3	7.5	7.6	7.7	4.8
	Downside 2	15	7.0	8.3	8.8	9.0	9.2	4.8
Central Bank base rates %[2]								
	Upside	30	2.8	2.8	3.0	3.2	3.3	6.0
	Base case	40	2.5	2.5	2.4	2.3	2.3	6.0
	Downside 1	15	2.3	2.1	2.0	2.1	2.1	6.0
	Downside 2	15	2.1	1.8	1.9	1.5	0.5	6.0
House price index %[1]								
	Upside	30	0.9	2.1	2.0	1.8	1.7	2.7
	Base case	40	0.5	1.1	1.5	2.0	2.0	2.7
	Downside 1	15	(0.5)	(1.1)	(0.9)	(0.8)	(0.6)	2.7
	Downside 2	15	(1.5)	(2.4)	(2.0)	(1.9)	(1.6)	2.7

[1] GDP Growth and the house price index are expressed as an annual percentage change.

[2] Unemployment rates and central bank base rates are expressed as a percentage as at the end of the forecast year.

XI. Extract from EY's illustrative financial statements- Good Bank 2022 -Analysis of inputs to the ECL model under multiple economic scenarios.

48. Risk management *continued*

48.2. Credit risk *continued*

48.2.4. Analysis of inputs to the ECL model under multiple economic scenarios per geographic regions continued

48.2.4.1. Goodland continued

Since the beginning of the year, as the Bank has reassessed the key economic indicators used in its ECL models, the expected GDP growth rate over the next few years has been revised downwards, given the slowdown of Goodland's economy. Unemployment and house price assumptions follow a similar trend. Central Bank base rates have also been revised downwards for the short term, as part of the governmental response. Long-term expectations remain unchanged.

IAS 1.129
IFRS 7.35G(c)