Sep 26, 2023

IFRS Foundation
7 West ferry Circus
Canary Wharf
London E14 4HD, United Kingdom

RE: Request for Information: Post-implementation Review of IFRS 9 Financial Instruments Impairment

Dear Colleagues,

The Saudi Organization for Chartered and Professional Accountants (SOCPA) appreciates the efforts of the IASB and welcomes the opportunity to comment on the Request for Information: *Post-implementation Review of IFRS 9 Financial Instruments Impairment.*

Our detailed comments on the questions raised in the RFI are attached in the appendix to this letter.

Please feel free to contact Dr. Abdulrahman Alrazeen at (razeena@socpa.org.sa) for any clarification or further information.

Sincerely,

Dr. Ahmad Almeghames

SOCPA Chief Executive Officer

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Appendix: SOCPA Comments on: Request for Information: Post-implementation Review of IFRS 9 Financial Instruments Impairment

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?**

Please provide information about the effects of the changes to the impairment requirements introduced by IFRS 9, including the ongoing costs and benefits of preparing, auditing, enforcing or using information about financial instruments.

This question aims to help the IASB understand respondents' overall views and experiences relating to the IFRS 9 impairment requirements. Sections 2–9 seek more detailed information on specific requirements.

SOCPA Comments:

(a) SOCPA agrees the impairment requirements in IFRS 9 result in more timely recognition of credit losses compared to IAS 39 as IAS 39 required entities to recognize impairment losses only when there was objective evidence of impairment, such as a default by the borrower. As IFRS 9 requires entities to recognize expected credit losses (ECLs) on all financial assets for which there has been a significant increase in credit risk since initial recognition. This results in a more accurate and timely reflection of the financial position of the entity although there are concerns about the timing of actual loss occurrence and the level of subjectivity and complexity of measuring such loss. It also encourages entities to incorporate forward-looking information into their risk management processes, potentially leading to more effective risk mitigation strategies.

However, there is an associated significant cost with application and continuous maintenance of the ECL model relating to:

1. Data Collection and Management: Data required needs to be organized, cleaned, and updated regularly, which requires dedicated resources and possibly investments in data management systems.
2. Advanced Analytics and Modelling: Designing, testing, and maintaining the models demand specialized skills and ongoing monitoring.
3. Internal Controls: Monitoring and evaluating the effectiveness of controls require ongoing efforts and resources.
4. IT Infrastructure and Systems: This could involve purchasing or developing software to manage data storage, retrieval, and analysis efficiently.
5. Technology Upgrades.

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6. Data Quality Assurance: This involves regular checks for data accuracy, completeness, and reliability.
7. Audit Costs: Auditors need to assess the reasonableness of an entity's ECL estimates, leading to additional audit procedures and potentially higher audit fees.
8. Expertise and Training: Companies need to invest in training their staff to apply the ECL model effectively.
9. Disclosure and Reporting: Preparing disclosures demands additional time and resources, as entities need to ensure that the information is clear, consistent, and comprehensive.
10. Sensitivity Analysis: Conducting such analysis requires additional resources and expertise.

The following would be the benefits as a result of application of IFRS 9 impairment model:

1. More accurate representation.
2. Timely information.
3. Consistency and comparability.
4. Transparency.
5. Risk management.
6. Decision making.

The above was also confirmed when information was collected during an outreach carried out by SOCPA involving its constituents. Additionally, some constituents believed that the complexity of IFRS 9 ECL model sometimes added to the level of complexity beyond the multiple models used under IAS 39 with considerable amounts of expert judgement needed for application of IFRS 9 ECL model.

(b) SOCPA agrees the impairment requirements in IFRS 9 result in 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.

The expected credit loss (ECL) approach used in IFRS 9 is a more forward-looking approach than the incurred loss approach used in IAS 39. The ECL approach also requires entities to consider a broader range of factors when assessing credit risk, including macroeconomic conditions, industry trends, and the borrower's financial performance. This provides users of financial statements with a more comprehensive understanding of the risks that an entity faces.

IFRS 9 also requires entities to disclose more information about their impairment losses, including the amount of losses recognized, the factors that contributed to the losses, and the methods used to estimate the losses. This additional disclosure helps users of financial statements to better understand the impact of credit risk on an entity's financial performance and helps them to make more informed decisions by having access to more timely and comprehensive information about an entity's credit risk exposure and potential future cash flow implications.

In addition to the benefits identified in 1 (a) above, the following would be benefits as a result of providing information about credit risk:

1. Improved decision making.

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2. Transparency: enables users to assess the quality of an entity's credit risk management practices.

SOCPA, based on information collected during an outreach carried out by SOCPA noted that certain constituents believed information provided under the ECL model can overload users and make comparatives across organisations extremely difficult or impossible e.g. Purchased or Originated Credit-Impaired financial assets (POCI) vs Stage 3. Additionally, constituents believed level of stage 2 was not clear across institutions given ability to have different Significant Increases in Credit Risk (SICR) triggers.

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?

Please explain whether requiring entities to recognise at least 12-month expected credit losses throughout the life of the instrument and lifetime expected credit losses if there has been a significant increase in credit risk achieves the IASB's objective of entities providing useful information about changes in credit risk and resulting economic losses. If not, please explain what you think are the fundamental questions (fatal flaws) about the clarity and suitability of the core objectives or principles of the general approach.

(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?

If, in your view, the ongoing costs of applying the general approach to particular financial instruments are significantly greater than expected or the benefits of the resulting information to users of financial statements are significantly lower than expected, please explain your cost–benefit assessment for those instruments.

SOCPA Comments:

(a) SOCPA believes there are a number of fundamental questions (fatal flaws) about the general approach prescribed by IFRS 9. Some of these questions include:

- Is the 12-month expected credit loss (ECL) horizon appropriate for all financial instruments? For example, some financial instruments, such as long-term loans, may have a longer expected life than 12 months.
- Is the requirement to recognize 12-month ECLs throughout the life of the instrument too conservative? This could lead to entities recognizing impairment losses even when the credit risk of the instrument has not actually increased.
- Is the requirement to recognize lifetime ECLs if there has been a significant increase in credit risk too simplistic? This could lead to entities recognizing impairment losses even when the increase in credit risk is not permanent.
- Is the ECL approach too complex and costly to implement? This could make it difficult for smaller entities to comply with the standard.

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SOCPA considers the IASB's objective of entities providing useful information about changes in credit risk and resulting economic losses is not fully achieved by requiring entities to recognize at least 12-month ECLs throughout the life of the instrument and lifetime ECLs if there has been a significant increase in credit risk. This is because the 12-month ECL horizon may not be appropriate for all financial instruments, and the requirement to recognize lifetime ECLs if there has been a significant increase in credit risk may be too simplistic.

In addition, the ECL approach is complex and costly to implement, which could make it difficult for smaller entities to comply with the standard.

SOCPA, based on information collected during an outreach carried out by SOCPA noted that the majority of the constituents agreed with the aspects highlighted above.

(b) SOCPA believes the adoption of the general approach outlined in IFRS 9 comes with both costs and benefits, which can vary based on the complexity and characteristics of these instruments.

The general approach also may not offer as much insight into the timing of credit losses as the earlier models. Under IFRS 9, entities estimate lifetime expected credit losses (LECL), representing the present value of all projected credit losses over the instrument's lifespan. However, this doesn't provide clear information about when these losses might occur. In contrast, IAS 39 required entities to estimate the time it takes for a loan to default. s.

For example, under IFRS 9, if a loan's LECL is $10,000, the entity records a loss allowance of $10,000 immediately, but without indicating when this loss might transpire. In the earlier IAS 39, estimating that the loan would default in 5 years would communicate a $10,000 loss expected in 5 years.

This lack of timing information in the general approach can hinder users' ability to assess the implications of credit losses on an entity's future cash flows.

The applicability of the general approach varies based on financial instruments. For instruments with high uncertainty, like loans in emerging markets, the costs of applying the approach are often greater due to the complex and time-consuming nature of required judgments and estimates. Similarly, the resulting information's benefits for users are likely to be lower, given the approach's limited insight into timing. On the other hand, simpler instruments such as trade receivables might incur lower costs with higher benefits, as the approach's demands are less intricate.

Overall, the cost-benefit balance of the general approach depends on the specific characteristics of financial instruments.

SOCPA, based on information collected during an outreach carried out by SOCPA noted that the majority of the constituents agreed with the aspects highlighted above.

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?

Please explain whether the principle-based approach of assessing significant increases in credit risk achieves the IASB’s objective of recognising lifetime expected credit losses on all financial instruments for which there has been a significant increase in credit risk since initial recognition.

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If not, please explain what you think are the fundamental questions (fatal flaws) about the clarity and suitability of the core objectives or principles of the assessment of significant increases in credit risk.

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

Please explain whether the requirements provide an adequate basis for entities to apply the assessment consistently to all financial instruments within the scope of impairment requirements in IFRS 9.

If diversity in application exists for particular financial instruments or fact patterns, please explain and provide supporting evidence about how pervasive that diversity is and explain what causes it. Please also explain how the diversity affects entities' financial statements and the usefulness of the resulting information to users of financial statements.

If you have identified diversity in application of the assessment, please provide your suggestions for resolving that diversity.

In responding to (a) and (b), please include information about **applying judgement** in determining significant increases in credit risk (see Spotlight 3).

SOCPA Comments:

(a) SOCPA believes that there are a number of fundamental questions about the assessment of significant increases in credit risk (SICR) in IFRS 9. These include:

- What constitutes a significant increase in credit risk? The standard does not provide a clear definition of what this means, which leaves it open to interpretation by different entities.
- How should entities assess SICR? The standard provides a number of factors that entities should consider, but it does not provide any specific guidance on how to weight these 2factors or how to make the assessment. Example: when assessing the SICR criteria, an entity might use qualitative and non-statistical quantitative information without any specific guidance on whether or when to revise the criteria.
- What is the impact of SICR on the timing of loss recognition? The standard requires entities to recognize lifetime expected credit losses (LECL) on financial instruments for which there has been a SICR. However, it is not clear whether this means that entities should recognize the full LECL immediately, or whether they can defer some of the loss recognition over time.

SOCPA considers that the principle-based approach of assessing SICR may not achieve the IASB's objective of recognizing LECL on all financial instruments for which there has been a significant increase in credit risk since initial recognition. This is because the principle-based approach leaves a lot of discretion to entities in how they assess SICR.

In addition, the principle-based approach can be difficult to apply in practice, especially for complex financial instruments. This can lead to errors in the assessment of SICR, which can misstate the financial statements.

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The following are some of the fundamental questions (fatal flaws) about the clarity and suitability of the core objectives or principles of the assessment of significant increases in credit risk:

1. The definition of SICR is not clear and could be interpreted differently by different entities.
2. The standard does not provide specific guidance on how to weight the factors that should be considered when assessing SICR.
3. The standard does not provide clear guidance on the timing of loss recognition for financial instruments for which there has been a SICR.
4. The principle-based approach can be difficult to apply in practice, especially for complex financial instruments.

These fundamental questions and flaws can make it difficult for entities to assess SICR in a consistent and accurate manner.

SOCPA, based on information collected during an outreach carried out by SOCPA noted that the majority of the constituents agreed with the aspects highlighted above.

(b) SOCPA believes whether the assessment of significant increases in credit risk (SICR) as required by IFRS 9 can be applied consistently is a complex question. As given in our response to question 3(a), 1-4 above there are a number of factors that could affect the consistency of the assessment.

In addition, the diversity of entities and the different circumstances they face can also lead to different assessments of SICR. For example, a bank may be more likely to assess a SICR for a loan to a company in a struggling industry than a company in a more stable industry.

The diversity in the application of the assessment of SICR can affect entities' financial statements and the usefulness of the resulting information to users of financial statements. For example, if two entities with similar financial instruments make different assessments of SICR, this could lead to different levels of provisioning for credit losses.

SOCPA suggests that the IASB provide more specific guidance on the assessment of SICR to resolve the diversity in the application of the assessment of SICR.

SOCPA, based on information collected during an outreach carried out by SOCPA noted that the majority of the constituents agreed with the aspects highlighted above.

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?

Please explain whether the requirements for measuring expected credit losses achieve the IASB's objective of providing users of financial statements with useful information about the amount, timing and uncertainty of an entity's future cash flows. If not, please explain what you think are the fundamental questions (fatal flaws) about the clarity and suitability of the core objectives or principles of the measurement requirements.

(b) Can the measurement requirements be applied consistently? Why or why not?

Please explain whether the requirements provide an adequate basis for entities to measure expected credit losses consistently for all financial instruments within the scope of impairment requirements in IFRS 9.

If diversity in application exists for particular financial instruments or fact patterns, please explain and provide supporting evidence about how pervasive that diversity is and explain what causes it. Please also explain how the diversity affects entities' financial statements and the usefulness of the resulting information to users of financial statements.

If you have identified diversity in application of the requirements, please provide your suggestions for resolving that diversity.

In responding to (a) and (b), please include information about **forward-looking scenarios** (see Spotlight 4.1), **post-model adjustments or management overlays** (see Spotlight 4.2) and **off-balance-sheet exposures** (see Spotlight 4.3), as relevant.

SOCPA Comments:

(a) SOCPA is aware that the requirements for measuring expected credit losses (ECLs) under IFRS 9 have been met with some criticisms. These criticisms mainly revolve around the objective of providing users of financial statements with useful information about the amount, timing, and uncertainty of an entity's future cash flows.

Some of the fundamental questions or concerns raised:

- IFRS 9 requires entities to recognize lifetime ECLs (LECLs) immediately upon identification of a significant increase in credit risk (SICR). This has been criticized for not providing enough information about the timing of credit losses. For example, an entity may recognize a large LECL for a loan, but it is not clear when this loss will actually occur. This can make it difficult for users of financial statements to assess the impact of credit losses on the entity's future cash flows.
- The requirements for estimating ECLs involve significant judgment and estimation. This complexity can lead to inconsistent application of the requirements across entities, even within the same entity over different reporting periods. The use of forward-looking information, historical data, and macroeconomic factors to estimate credit losses can be challenging and introduce a high degree of uncertainty.
- The standard does not specify how far into the future entities should project ECLs. The lifetime approach adopted by IFRS 9 assumes that credit losses need to be estimated for the entire life of a financial instrument. Determining the appropriate period for loss projection can be challenging and uncertain.
- Critics argue that the LECL approach might not provide sufficient predictive ability for users to make informed decisions. While the intention is to capture expected credit losses early, the lack of clarity on the timing of these losses reduces the usefulness of the information for assessing an entity's future cash flows and financial health.
- The use of macroeconomic factors and assumptions to estimate credit losses introduces additional complexity and uncertainty. The interpretation and integration of these factors can vary and impact the reliability of credit loss estimates.

Forward-looking scenarios:

Forward-looking projections are based on assumptions about future events. SOCPA believes this leads to challenges in estimating credit losses accurately. The reliability of these projections and their implications for decision-making are therefore questionable.

Post-model adjustments or management overlays:

These adjustments are made to the results of credit loss models, and they can introduce subjectivity and potentially lead to inconsistencies in the application of the standard across different entities. Therefore, SOCPA has concerns that management overlays could undermine the comparability and transparency of financial statements.

Off-balance-sheet exposures:

SOCPA believes the estimation of credit losses for these exposures can be challenging due to the lack of historical data and the reliance on forward-looking information. This raises questions about the accuracy and reliability of the credit loss estimates for such instruments.

Based on information collected during an outreach carried out by SOCPA with constituents, it was stated that the macroeconomic models used to compute ECL has been unstable (requiring frequent redevelopment) due to its inability to capture the complex interaction between the state of the economy and the retail accounts going into default. Hence, any guidance on the usage of simplified' approach, i.e. scalar multiplier on PDs, in order to incorporate the FEG component will be helpful.

(b) SOCPA considers the consistent application of the measurement requirements for expected credit losses (ECLs) can be challenging due to the inherent complexities involved in estimating ECLs. The requirements may not always provide an adequate basis for entities to measure ECLs consistently for all financial instruments within the scope of impairment requirements.

There are several factors that can affect the consistency of the application of the ECL measurement requirements:

- Estimating ECLs involves subjective judgments, reliance on historical data, and the use of forward-looking scenarios. Different entities may interpret and apply these aspects differently.
- The wide variety of financial instruments with differing characteristics makes consistent application difficult. Instruments with complex structures, unique terms, or exposure to specific industries may require diverse estimation methods.
- Incorporating forward-looking scenarios introduces additional uncertainty. Entities may vary in their approaches to selecting and weighting macroeconomic factors.
- The option for entities to include management overlays or adjustments further contributes to inconsistency.
- The estimation of ECLs for off-balance-sheet exposures, such as loan commitments and financial guarantees, can be challenging due to the lack of historical data.

Diversity in application:

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Diversity in the application of IFRS 9's ECL measurement requirements has been observed, particularly for more complex instruments and situations. Entities may apply different methods to incorporate forward-looking information, make management adjustments, or estimate ECLs for off-balance-sheet exposures.

The lack of consistency in applying the requirements can result in varying ECL estimates across entities, leading to differences in reported financial performance and position.

To address diversity in application, the following steps could be considered:

- The IASB could provide additional guidance and examples, particularly for more complex financial instruments, to promote more consistent application.
- Requiring entities to disclose their estimation methods, assumptions, and any management adjustments can enhance transparency and allow users to understand the basis of ECL estimates.

SOCPA, based on information collected during an outreach carried out by SOCPA noted that the majority of the constituents agreed with the aspects highlighted above.

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?

Does applying the simplified approach achieve the IASB's objective of reducing the costs and complexities of applying IFRS 9 impairment requirements to trade receivables, contract assets and lease receivables? If not, please explain what you think are the fundamental questions (fatal flaws) about the clarity and suitability of the core objectives or principles of the simplified approach.

(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?

If, in your view, the ongoing costs of applying the simplified approach are significantly greater than expected, or the benefits of the resulting information to users of financial statements are significantly lower than expected, please explain your cost–benefit assessment.

SOCPA Comments:

(a) SOCPA believes that there are some fundamental questions (fatal flaws) about the simplified approach in IFRS 9. These include:

- The simplified approach does not consider the risk of interest rate changes. This means that the ECLs are calculated as if the interest rate will remain constant over the life of the financial instrument.
- The simplified approach does not consider the effect of collateral. Collateral can reduce the amount of the loss that an entity incurs if a borrower defaults.

- The simplified approach does not consider the time value of money. This means that the ECLs are calculated as if the amount of the loss will be incurred all at once, rather than over time.

  Therefore, SOCPA believes the IASB's objective of reducing the costs and complexities of applying IFRS 9 impairment requirements to trade receivables, contract assets and lease receivables is not fully achieved by the simplified approach and the simplified approach does not always provide a reliable estimate of ECLs.

SOCPA, based on information collected during an outreach carried out by SOCPA noted that the majority of the constituents agreed with the aspects highlighted above.

(b) SOCPA believes the ongoing costs of applying the simplified approach are not significantly greater than expected. These costs include: the cost of developing and implementing the necessary systems and processes, the cost of gathering and maintaining the data needed to calculate ECLs and the cost of auditing and monitoring the entity's compliance with the simplified approach. However, the benefits of the resulting information to users of financial statements may be lower than expected. While it is less complex than the general approach, which can reduce the time and resources needed to measure ECLs, the simplified approach does not take into account all of the factors that can affect the value of trade receivables, contract assets, and lease receivables.

SOCPA, based on information collected during an outreach carried out by SOCPA noted that the majority of the constituents agreed with the aspects highlighted above.

Question 6—Purchased or originated credit-impaired financial asset

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

Please explain whether the requirements can be applied consistently to these types of financial assets and lead to accounting outcomes that faithfully reflect the underlying economic substance of these transactions.

If there are specific application questions about these requirements, please describe the fact pattern and:

(a) explain how the IFRS 9 requirements are applied;
(b) explain the effects of applying the requirements (for example, the quantitative effect on an entity’s financial statements or an operational effect);
(c) explain how pervasive the fact pattern is; and
(d) support your feedback with evidence.

SOCPA Comments:

SOCPA believes the requirements in IFRS 9 for purchased or originated credit-impaired financial assets (POCI) can be applied consistently, however, there are some specific application questions that may need to be addressed.

- How should the DCF method be applied to assets with irregular cash flows?
- Estimating credit impairment – How should the future cash flows be predicted?
- How is the creditworthiness of borrowers assessed?
- How should the probability of default be estimated for assets that are not publicly traded?
- How should the expected timing and amount of cash flows be estimated for assets that are subject to prepayment?

SOCPA wishes to highlight that these are just a few examples of the specific application questions that may need to be addressed when applying the IFRS 9 requirements for POCI. The specific application questions that need to be addressed will vary depending on the facts and circumstances of each case.

The pervasiveness of the fact pattern is also a factor to consider when applying the IFRS 9 requirements for POCI. For example, if the fact pattern is common to many financial institutions, then the effects of applying the requirements will be more pervasive.

Based on information collected during an outreach carried out by SOCPA with constituents, it was stated that the requirements under IFRS 9 requires all instruments to be initially recorded at fair value whether acquired separately or as part of an acquisition. As a result, the calculated fair value embeds the lifetime ECL as reported under stage 3 equivalent to the amount booked at inception. The area where consistency can help is when a POCI asset recovers and had it been a stage 3 asset could be moved out of the stage 3 to stage 2. In contrast once a POCI is always a POCI. This creates an inconsistency between the stage 3 and POCI potentially for similar assets.

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?

If there are specific questions about how to apply the impairment requirements alongside other requirements, please explain what causes the ambiguity and how that ambiguity affects entities' financial statements and the usefulness of the resulting information to users of financial statements. Please describe the fact pattern and:

(a) indicate the requirements in IFRS 9 or in other IFRS Accounting Standards to which your comments relate;
(b) explain the effects of applying the requirements (for example, the quantitative effect on an entity's financial statements or an operational effect);
(c) explain how pervasive the fact pattern is; and
(d) support your feedback with evidence.

In responding to this question, please include information about matters described in this section of the document.

SOCPA Comments:

SOCPA believes that the impairment requirements in IFRS 9 are generally clear and can be applied consistently. However, there are some specific areas where the guidance is less clear or where there is potential for ambiguity.

One area of ambiguity is the interaction between the impairment requirements and the hedge accounting requirements in IFRS 9. For example, IFRS 9 allows an entity to designate a hedging relationship in which a financial asset is hedged against a risk of default. However, the impairment requirements in IFRS 9 do not specifically address how to account for impairment losses on the hedged financial asset.

The ambiguity in the impairment requirements in IFRS 9 can affect entities' financial statements in a number of ways. For example, it can lead to different entities applying the requirements in different ways, which can make it difficult to compare financial statements. It can also lead to entities recognizing impairment losses that are not actually necessary, or failing to recognize impairment losses that are necessary. This can reduce the usefulness of the information in financial statements for users.

To address the ambiguity in the impairment requirements, the IASB could provide additional guidance on how to apply the requirements in specific situations. This would help to ensure that entities apply the requirements in a consistent manner.

Based on information collected during an outreach carried out by SOCPA with constituents, it was stated that the requirements under IFRS 9 had no clear guidance on the presentation of modification gains/losses as opposed to impairment. They were of the view that additional guidance to address this area would be very beneficial to preparers.

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? Please explain whether the combination of the relief from restating comparative information and the requirement for transition disclosures achieved an appropriate balance between reducing costs for preparers of financial statements and providing useful information to users of financial statements.

Please explain any unexpected effects or challenges preparers of financial statements faced applying the impairment requirements retrospectively. How were those challenges overcome?

SOCPA Comments:

The combination of relief from restating comparative information and the requirement for transition disclosures was intended to strike a balance between reducing costs for preparers and providing useful information to users. The relief from restating comparative information allowed entities to avoid the costly and complex process of restating prior periods.

However, the retrospective application of the impairment requirements, presented challenges for preparers. One of the main challenges was the availability and reliability of historical data required for the calculation of expected credit losses. Many entities had to enhance their data collection and management processes to meet the new requirements. They also sought guidance from external experts and engaged in extensive training and education programs to ensure a proper understanding and application of the new impairment requirements.

SOCPA, based on information collected during an outreach carried out by SOCPA noted that the majority of the constituents agreed with the aspects highlighted above.

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?

Please explain whether the combination of disclosure objectives and minimum disclosure requirements for credit risk achieves an appropriate balance between users of financial statements receiving:

(i) comparable information—that is, the same requirements apply to all entities so that users receive comparable information about the risks to which entities are exposed; and

(ii) relevant information—that is, the disclosures provided depend on the extent of an entity's use of financial instruments and the extent to which it assumes associated risks.

If an appropriate balance is not achieved, please explain what you think are the fundamental questions (fatal flaws) about the clarity and suitability of the core objectives or principles of the disclosure requirements.

(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?

If, in your view, the ongoing costs of providing specific credit risk disclosures are significantly greater than expected or the benefits of the resulting information to users of financial statements are significantly lower than expected, please explain your cost–benefit assessment for those disclosures. Please provide your suggestions for resolving the matter you have identified.

If, in your view, the IASB should add specific disclosure requirements for credit risk, please describe those requirements and explain how they will provide useful information to users of financial statements.

Please also explain whether entities' credit risk disclosures are compatible with digital reporting, specifically whether users of financial statements can effectively extract, compare and analyse credit risk information digitally.

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SOCPA Comments:

(a) SOCPA believes there are certain fundamental questions that need to be addressed regarding the disclosure requirements for credit risk in IFRS 7.

One of the fundamental questions about the disclosure requirements is whether they achieve an appropriate balance between providing comparable information and relevant information. On the one hand, the requirements are designed to ensure that users of financial statements receive comparable information about the risks to which entities are exposed. This is important because it allows users to compare the financial statements of different entities and assess their relative riskiness. On the other hand, the requirements also need to be relevant to the specific risks that an entity faces. If the requirements are too general, they may not provide users with the information they need to make informed decisions.

Another fundamental question about the disclosure requirements is whether they are clear and suitable. The requirements are complex and can be difficult to understand. Additionally, the requirements may not be suitable for all entities. For example, the requirements may be too detailed for small entities that do not have significant exposure to credit risk.

SOCPA, based on information collected during an outreach carried out by SOCPA noted that the majority of the constituents agreed with the aspects highlighted above.

(b) SOCPA believes the costs of applying the disclosure requirements in IFRS 7 for credit risk and auditing and enforcing their application and the benefits to users of financial statements can vary among entities and jurisdictions.

However, the ongoing costs of providing credit risk disclosures are significantly greater than expected benefits of the resulting information to users of financial statements in the following specific instances.

- **Granular Portfolio Details:** Requiring entities to disclose detailed information about individual loans, counterparties, and credit exposures can demand substantial resources for data collection, analysis, and presentation.
- **Scenario Analysis:** Mandating disclosure of various credit risk scenarios (e.g., economic downturn, changes in market conditions) and their potential impacts on an entity's credit risk exposure can involve complex modelling and a significant allocation of resources.

Cost-Benefit Assessments:

- Granular Portfolio Details:
  - ✓ Costs: Gathering and maintaining data at a granular level necessitates robust data infrastructure and ongoing maintenance. It can also raise concerns about data privacy and confidentiality.
  - ✓ Benefits: Investors and creditors can gain deeper insights into the distribution of credit risk across an entity's portfolio. However, the incremental value of disclosing highly detailed data might not always justify the associated costs.
- Scenario Analysis:
  - ✓ Costs: Developing and presenting scenario analyses can require specialized expertise in financial modelling and forecasting. Resource allocation might be substantial, especially for entities with complex portfolios.

- ✓ Benefits: Users can better understand an entity's susceptibility to various economic conditions. However, the complexity and uncertainty inherent in scenario analysis might hinder users' ability to interpret and apply the disclosed information effectively.

Suggestions for IASB Consideration:

- Focus on Key Indicators:
  - ✓ Emphasize the disclosure of key indicators that provide meaningful insights into an entity's credit risk profile. This could include concentration of credit risk, credit loss history, and credit risk management strategies.
- Standardized Templates:
  - ✓ Introduce standardized reporting templates for specific credit risk disclosures. This approach could simplify reporting for entities and facilitate easier comparison for users.
- Narrative Disclosures:
  - ✓ Allow entities to provide narrative explanations alongside quantitative data. This would enable entities to provide context and insights that might not be easily conveyed through numbers alone.
- Streamlined Scenario Analysis:
  - ✓ If scenario analysis is deemed beneficial, consider allowing entities to disclose a limited number of key scenarios rather than an exhaustive range. Focus on scenarios that are most relevant and impactful.

SOCPA also believes the IASB could consider adding specific requirements that address any identified gaps in the disclosure of credit risk information. These requirements should focus on providing useful information to users, such as:

- Information on the credit quality of financial assets, including credit ratings, credit risk concentrations, and credit risk mitigation strategies.
- Information on the entity's credit risk management policies and procedures, including the assessment of credit risk, monitoring of credit exposures, and management of credit risk concentrations.
- Disclosure of significant changes in credit risk exposures and the impact on financial performance and position.

Regarding digital reporting, the compatibility of entities' credit risk disclosures with digital reporting depends on the availability and structure of the data. If entities provide their credit risk information in a structured and machine-readable format, users of financial statements can effectively extract, compare, and analyze the information digitally. Encouraging entities to adopt standardized and structured reporting formats can enhance the compatibility of credit risk disclosures with digital reporting and facilitate more efficient analysis by users.

SOCPA, based on information collected during an outreach carried out by SOCPA noted that the majority of the constituents agreed with the aspects highlighted above.

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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?
Please explain why those matters should be considered in the context of this post-implementation review and the pervasiveness of any matter raised. Please provide examples and supporting evidence.

(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.

SOCPA Comments:

(a) SOCPA believes the IASB could examine the consistency and comparability of ECL estimates across entities, industries, and jurisdictions. This assessment could help identify any significant divergences in practice and explore potential reasons behind such variations. It could also consider whether additional guidance or standardization is needed.

Additionally, the IASB could specifically examine the impact of the impairment requirements on financial institutions, such as banks and insurance companies. This assessment could consider the unique characteristics and challenges faced by these entities in implementing the requirements, including the interaction with regulatory frameworks and capital adequacy requirements.

SOCPA, based on information collected during an outreach carried out by SOCPA noted that certain constituents believed the requirement "has no reasonable expectation of recovering" in paragraph 5.4.4 of IFRS 9 needs further application guidance as it has been interpreted in many different ways when it has been practically applied.

Also, certain constituents believed that there was a need for additional guidance on calculating ECL on intragroup loans.

Additionally, constituents believed there was diversity in practice with regard to write offs with some entities increasing the ECL provision whereas some write-off against the asset. They believed guidance should be issued to ensure there is consistency in how entities account for and present, write-offs.

(b) SOCPA believes the IASB could consider the following to improve the understandability and accessibility of the impairment requirements in IFRS 9 when developing its future IFRS Accounting Standards.

- The impairment requirements in IFRS 9 are complex and can be difficult to understand, even for experienced accountants.
- The impairment requirements in IFRS 9 are not always consistent with the underlying economics of credit risk.
- The impairment requirements in IFRS 9 are not always clear and unambiguous. This can lead to different interpretations of the requirements, which can make it difficult for entities to apply the requirements consistently.

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The above can be addressed if the IASB incorporates the following to its future IFRS Accounting Standards:

- Simplify the requirements in order to make them easier to understand and apply. This could be done by reducing the number of factors that need to be considered, or by providing more guidance on how to apply the requirements.
- Could make the requirements more consistent with the underlying economics of credit risk by taking into account the time value of money and other factors that affect the amount of impairment that is expected to occur.
- Could provide more clarity and guidance on the requirements in order to reduce the number of different interpretations. This could be done by providing more examples, or by issuing more detailed guidance.

SOCPA, based on information collected during an outreach carried out by SOCPA noted that the majority of the constituents agreed with the aspects highlighted above.

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