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Dear Madam, dear Sir

Exposure Draft Investments in Debt Instruments (Proposed Amendments to IFRS 7)

The Committee of European Banking Supervisors (CEBS), comprised of high level representatives from banking supervisory authorities and central banks of the European Union, welcomes the opportunity to comment on the Exposure Draft Investments in Debt Instruments (ED). Our comments are set out below and in the Appendix.

Banking supervisory authorities and central banks have a strong interest in promoting sound and high quality accounting and disclosure standards for the banking and financial industry, as well as transparent and comparable financial statements that would strengthen market discipline.

As highlighted in previous comments CEBS regards disclosures about financial instruments to be an important factor in ensuring that users of financial statements can make well-informed investment decisions. Decision-relevant disclosure should also result in better transparency and thus strengthen market discipline mechanisms, which supervisors regard as an important tool to promote international financial stability and to enhance the soundness of the financial system.

As regards the additional disclosures put forward in the ED we take note that they are intended to address comments made by some participants in the context of the public round-table meetings held by the IASB and the US Financial Accounting Standards Board (FASB) in November and December 2008 in response to the global financial crisis.

In particular there were requests for disaggregated information about impairment losses of available-for-sale debt instruments, especially of the incurred credit-loss portion of the total impairment loss, i.e. the loss amount that would be recognised under the impairment model applied to debt instruments measured at amortised cost.

CEBS questions the added value and the objectives of the proposal to require entities to disclose profits or losses as though all investments in debt instruments had been (i) classified as at fair value through profit or loss and (ii) accounted for at amortized cost. These disclosures have no clear connection to the requested breakdown of available-for-sale debt impairment as recorded on the balance sheet. Furthermore, such a requirement may confuse users and is quite different to seeking to identify the components of an amount actually recognised on the balance sheet, in this instance AFS debt impairment.

CEBS is of the view that these and other additional disclosure requirements do not adequately address the issue raised by CEBS and some other stakeholders. Indeed, as you will remember, CEBS in its June 2008 [Report on issues regarding the valuation of complex and illiquid financial instruments](#), called on the IASB to consider impairment - and specifically possible changes to impairment rules for assets classified as available for sale – in the context of measurement. For this reason (and others, noted below) we are not sure that the disclosures as proposed by the IASB achieve what was requested by those users. In particular, CEBS and some other stakeholders consider that a change in measurement is required so that AFS debt impairment would only reflect incurred credit losses.

The relevant part of the CEBS report (paragraphs 40 to 44) is set out in the annex. In brief, we believe that impairment of available-for-sale debt assets should relate only to the lower (discounted) expected future cash flows as a result of a loss event post-initial recognition. It should not be measured as the difference between the carrying amount in the most recent statement of financial position and the latest fair value.

CEBS therefore urges the IASB to couple the introduction of the proposed disclosures with an amendment to IAS 39 whereby the impairment of debt instruments in the available-for-sale category is limited solely to the credit component, in a manner consistent with the rules applicable to instruments at amortised cost.

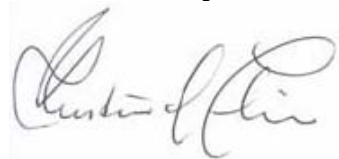
In addition, to promote timely recognition of impairment CEBS urges the IASB to allow for the reversal of impairment losses of available-for-sale equity instruments (up to the original carrying amount). Furthermore this would help in aligning the treatment of equity instruments and debt instruments.

Turning to the proposed disclosures, we do not believe that these will provide the clear analysis of the components of available-for-sale debt impairment which participants in the Roundtables, CEBS and others have called for. Specifically, it seems unduly convoluted for users to have to estimate the non-credit portion of impairment by comparing figures for amortised cost and fair value. In addition, the proposed tables do not include figures for credit-related impairment. The appendix to this letter sets out further CEBS comments on the disclosures proposed in the ED.

Additionally, we encourage the IASB to ensure together with the FASB that the final provisions require consistent disclosures using the same terminology.

The comments put forward in this letter and the related appendix have been coordinated by CEBS's Expert Group on Financial Information (EGFI) chaired by Mr. Didier Elbaum (Deputy Secretary General, Commission Bancaire) - in charge of monitoring any developments in the accounting area and of preparing related CEBS positions - and in particular by its Subgroup on Accounting under the direction of Mr. Ian Michael of the UK FSA. If you have any questions regarding our comments, please contact Mr. Elbaum (+33.1.4292.5801) or Mr. Michael (+ 44.20.7066.7098).

Yours sincerely,



Kerstin af Jochnick
Chair, Committee of European Banking Supervisors

APPENDIX

Question 1

The exposure draft proposes in paragraph 30A(a) to require entities to disclose the pre-tax profit or loss as though all investments in debt instruments (other than those classified as at fair value through profit or loss) had been (i) classified as at fair value through profit or loss and (ii) accounted for at amortised cost.

Do you agree with that proposal? If not, why? What would you propose instead, and why?

Question 2

The exposure draft proposes to require disclosing the pre-tax profit or loss amount that would have resulted under two alternative classification assumptions.

Should reconciliations be required between profit or loss and the profit or loss that would have resulted under the two scenarios? If so, why and what level of detail should be required for such reconciliations?

CEBS questions the added value of the proposal to require entities to disclose the pre-tax profits or loss as though all investments in debt instruments (other than those classified as at fair value through profit or loss) had been (i) classified as at fair value through profit or loss and (ii) accounted for at amortised cost.

However, if the IASB wishes to maintain this information CEBS suggests, in order to allow users of financial statements to understand these amounts, that entities be required to provide these pre-tax profits or loss broken down by category that the debt instruments are attributed to (i.e. available for sale, loans and receivables and held to maturity).

Question 3

The exposure draft proposes in paragraph 30A(b) to require entities to disclose for all investments in debt instruments (other than those classified as at fair value through profit or loss) a summary of the different measurement bases of these instruments that sets out (i) the measurement as in the statement of financial position, (ii) fair value and (iii) amortised cost.

Do you agree with that proposal? If not, why? What would you propose instead, and why?

CEBS also questions the added value of the proposal to require entities to tabulate for all investments in debt instruments (other than those classified as at fair value through profit or loss) a summary of the different measurement bases of these instruments setting out (i) the measurement as in the statement of financial position, (ii) fair value and (iii) amortised cost.

If the IASB were to maintain this information requirement CEBS considers that this information should be required to incorporate a breakdown of the bases by categories (i.e. available for sale, loans and receivables and held to maturity).

We encourage the IASB, in future work, to consider further the selection of required disclosures. A comprehensive analysis of gains and losses would require disclosure of the amount recognised in profit and loss and directly in equity, during the period

and cumulatively, for all debt instruments, showing separately the amount attributable to changes in credit risk, changes in market conditions that give rise to market risk, and other factors.

In any event we consider that the key disclosure is the total impairment amount as well as the credit and non-credit loss portions of the impairment amount, for available for sale debt instruments.

Question 4

The exposure draft proposes a scope that excludes investments in debt instruments classified as at fair value through profit or loss.

Do you agree with that proposal? If not, would you propose including investments in debt instruments designated as at fair value through profit or loss or those classified as held for trading or both, and if so, why?

For reasons of further enhanced transparency consideration should be given to requiring entities to cover also debt instruments as at fair value through profit or loss with a breakdown of those instruments designated at fair value through profit or loss and those classified as held for trading. However, it is unlikely that firms have the systems in place to produce those disclosures at present.

Question 5

Do you agree with the proposed effective date? If not, why? What would you propose instead, and why?

CEBS agrees that the change should be made quickly but careful consultation with preparers is required to determine the earliest feasible implementation date.

Question 6

Are the transition requirements appropriate? If not, why? What would you propose instead, and why?

See question 5.

Annex - Excerpt from the CEBS June 2008 report on issues relating to the valuation of complex and illiquid financial instruments.

40. *There are practical differences in IAS 39 between the mechanics and determination of impairment for available for sale financial instruments and impairment for financial instruments at amortised cost. Impairment for instruments at amortised cost is related to the occurrence of a (credit) loss event and is estimated using the original effective interest rate (i.e. without taking into account subsequent variations in interest rates). Impairment for available for sale assets incorporates the entire latent losses at the time of impairment, including when such latent losses are due to other market factors than credit risk.*

41. *When equity instruments in the available for sale category are impaired, such impairment cannot be reversed.*

42. *In order to avoid institutions refraining from timely recognition of impairment, **consideration should be given to a possible change to impairment rules applicable to available for sale instruments, notably:***

- ***to allow for the reversal of 'write-downs' of equity instruments through profit or loss (up to the original carrying amount); indeed, allowing banks to reverse impairment when the situation of the entity improves could help to alleviate problems of timely recognition and 'under-impairment' for equity classified as available for sale; and***
- ***to limit impairment of debt instruments in the available for sale category to the sole credit component, in a manner consistent with the rules applicable to instruments at amortised cost.** [Emphasis added]*

43. *Timely recognition of impairment is particularly critical from a prudential point of view, due to the prudential filters applying to assets available for sale:*

- *for equities, unrealised losses should be deducted (after tax) from original own funds and unrealised gains should only partially be included in additional own funds before tax;*
- *for loans and receivables, the unrealised gains and losses, apart from those related to impairment, are neutralised in own funds (after tax); and*
- *other available for sale assets (i.e. debt securities, financial instruments subject to interest rate risk) can be treated (consistently) as equities or as loans and receivables.*

44. *The prudential filters that are in place for available-for-sale assets have proved effective. However CEBS holds the view that it is crucial to underline the importance for banks to proceed with timely recognition of impairment to ensure that the deterioration of assets credit quality is reflected on a timely basis in institutions' balance sheets and results and, not least, in their regulatory capital.*