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Your ref., Your message of Our ref., person in charge Extension Date

 BSBV 115/Dr. Egger 3137 25 October 2016

**EBA Consultation on Draft Guidelines on credit risk management practices and accounting for expected credit losses**

The Division Bank and Insurance of the Austrian Federal Economic Chamber, as representative of the entire Austrian banking industry, appreciates the possibility to comment on the above cited consultation document and would like to submit the following position:

**General comments**

While we acknowledge and welcome the role that the European Banking Authority (EBA) plays in the international harmonisation of supervisory frameworks and rules, we believe it is up to the accounting standard setters to determine rules for financial statements within a given financial reporting framework. Preparers – in cooperation with their statutory auditors – have to ensure that financial statements are in line with the applicable financial reporting framework.

We note that EBA attempts to harmonise the calculation of expected losses, which could be seen as one of the crucial elements for the financial stability of the financial sector, but we would like to point out that EBA is an organisation charged with the harmonisation of the supervisory rules for international credit institutions, which is clearly different from setting accounting standards for preparers of financial statements.

We are concerned that EBA, by issuing guidance on accounting issues in financial reporting, could possibly come to be seen as an additional financial reporting standard setter.

***Question 1 (page 13): Is the scope of application of the guidelines appropriate and sufficiently clear?***

We understand the scope of application as being the FINREP category loans and advances and not debt securities, which contains credit risk relevant assets classified at AAC (at amortized cost) or FVOCI (fair value though other comprehensive income).

***Question 2 (page 15): Is the date of application of the guidelines of 1 January 2018 appropriate?***

In light of the need to have an IFRS 9 compliant bank at the beginning of January 2018 this would seem appropriate. However we would mention two aspects. Firstly, by this date we will have tested our systems for over a year, however this is no substitute for live testing which, in the past, has shown to provide significant insights. Furthermore, it will take time for new IFRS 9 related internal governance processes to establish themselves on an operating level, a process which can only really start after 1 January 2018. Secondly, we expect an emergence of new trends in best practice in critical areas such as significant increase of credit risk (SICR). In this respect we expect an increase in positive inputs during 2018, i.e. the disclosures of our peer banks, discussions with auditors and regulators. Also in case of major change request the application of the guidelines might be postponed to a later date or at least there should be sufficient transitional rules.

***Question 3 (page 16): Please provide any comments you may have on the appropriateness of the proposed proportionality approach.***

We very much welcome the inclusion of the proportionality approach as it reflects the real heterogeneity which exists in the European banking industry. In this respect we would strongly urge to explicitly include "less developed markets" as one of the criteria. One example of this is the use of forward looking information. The degree of availability and robustness of macroeconomic indicators varies from country to country. Another example is that the banks using STD or FIRB approach might need to additionally focus on development of some of the credit risk parameters during the implementation time.

***Questions 5 and 6 (page 63): Do you agree with the impact assessment and its conclusions, having regard to the baseline scenario used for this impact assessment? Please provide any additional information regarding the costs and benefits from the application of these guidelines. Please provide any additional comments on the draft guidelines***

We agree with the impact assessment and baseline scenario and welcome the strong intention of the regulator to create a level playing field. For us the benefits are clear and hence the appropriate level of funds has been devoted to the project.

**Other comments**

Para 27:

The word "relevant" is used in the context of "relevant and reasonable and supportable information". Reasonable and supportable is used in the IFRS standard however “relevant” has now been added and may lead to confusion.

Para 94:

In our view, additional segmentation only seems appropriate if the segmentation is forced by a new, so far unrecognised significant risk or if risk factors or their correlation have changed.

Para 102:

For small exposures which are monitored and controlled on a portfolio basis (in particular in the retail segment) a past due indicator may be appropriate given cost-benefit considerations. Many banks have statistical models that capture the connection between days past due and increased probability of default. For large exposures other factors will be considered, as these are monitored on an individual basis. However, this will usually not be possible for small loans, for which past due status may be an objective and comparable indicator.

Para 106/107:

This states that indicators as defined by IFRS 9.B5.5.17 (a)-(p) should each be considered when determining whether an exposure should move to bucket 2. IFRS 9 states that the factors mentioned “may be relevant”, but does not require entities to track all the factors for all loans. Point 106 refers to IFRS 9.B5.5.17 and the 16 classes of possible factors to be monitored when assessing changes in credit risk. Then point 107 picks out some and makes them more relevant than others. Also, the wording in point 107 is inconsistent with IFRS 9.B5.5.17, which will lead to additional diversity in practice. It seems that factors listed in point 107 generally lead to LEL. We do not see the need to establish these automatic moves to LEL as they might act as false incentives to banks (i.e., not to take additional collateral for an exposure when it would make economic sense, because it would lead to an automatic shift from bucket 1 to bucket 2). This paragraph should therefore either be rephrased or deleted.

Para 116:

Even with reference to IFRS 9 B5.5.1, it is not defined, what the word “group” means in this context. Thus, further clarification is needed. In our opinion a downgrading of a single counterparty within a group with shared credit risk characteristics should not automatically lead to transfer of the entire group to LEL.

Para 121:

It is not clear whether the "additional factors" mentioned here in relation to SICR are over and above the factors mentioned in IFRS 9.B5.5.17.

Para 129, 132 etc.:

It is not clear what is meant by "limited use" of the practical expedients and should be clearer i.e. they can be used or not. Otherwise this could lead to a situation that not using the practical expedients will introduce bias.

Para 130:

This imposes an additional burden of proof on the bank: the bank has to document and disclose why it has acted in a way that is permitted by IFRS 9, but is discouraged or forbidden by the guidelines.

Para 131:

Just as with any implementation of new systems or processes required by a new standard, the implementation of IFRS 9 should be subject to cost-benefit analysis, as generally stipulated in IFRS. It is not clear why "nevertheless" has been used at the beginning of this sentence. Furthermore it is not clear why the sentences quoted by IFRS 9 could be interpreted "restrictively". Also it is doubtful why it is considered that information for a high-quality application of IFRS 9 can be derived without ‘undue cost and effort’.

Para 132-134:

It is not clear under which circumstances use of the low credit risk exemption would be acceptable.

We ask you to give our remarks due consideration.

Yours sincerely,

Dr. Franz Rudorfer

Managing Director

Division Bank and Insurance