DUTCH ACCOUNTING STANDARDS BOARD (DASB)

RAAD VOOR DE JAARVERSLAGGEVING

Secretariat:
Antonio Vivaldistraat 2-8
Postbox 7984
1008 AD Amsterdam
The Netherlands

T +31 (0)20 301 03 91
F +31 (0)20 301 02 79
rj@rjnet.nl
www.rjnet.nl

EFRAG
Attn. EFRAG Technical Group
35 Square de Meeûs
B-1000 Brussels
Belgique

Our ref : AdK
Direct dial : Tel.: (+31) 20 301 0391 / Fax: (+31) 20 301 0302
Date : Amsterdam, 4 April 2011
Re : Comments on Supplementary Document Financial Instruments: Impairment

Dear members of the EFRAG Technical Expert Group,

The Dutch Accounting Standards Board (DASB) appreciates the opportunity to comment on your draft comment letter on the IASB's supplementary document on impairment issued on 31 January 2011 (the 'SD').

We refer to our letter to the IASB that is attached. In the appendix to that letter we have included our responses to the detailed questions of the SD.

As you can see in there we do not agree with the in our view insufficient time allocated to assess these complex proposals, which are also significantly different in comparison to the original ED. In our view this results in an inappropriate due process and we will write to the Trustees in that vein as well. Given your own draft responses we do not see why that point should not be brought over by EFRAG more forcefully as well.

In general we concur with most of your other draft responses to the questions in the SD, except for the following:

- We do not agree with your response to question 11 in respect of the flexibility related to using discounted amounts. We agree with the IASB proposal that either discounted or undiscounted amounts could be used and we also agree with the IASB that – if an entity uses discounted amounts – for practical reason any rate between the risk-free rate and the effective interest rate determined in accordance with IAS 39 can be used as the discount rate. However, we note that an entity should apply the elected allocation method consistently, and should also disclose the allocation method and the discount rate used.
- Regarding question 19Z we do not agree with the proposal, because of both the floor and the mechanism of transferring assets from the good book to the bad book, there is a general expectation that the proposals will simply result in a profit and loss account similar to the current incurred loss model – and potentially even more volatile – and a

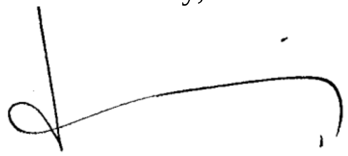
provision in the balance sheet that is built up but cannot be used, i.e. in reality a buffer. Would this indeed be the result, than we have significant doubts whether doubts whether:

- this outcome is in line with the key objectives of addressing the ‘too little, too late and too pro cyclical’ concerns of the incurred loss model;
- the benefits of implementing a complex model such as proposed in the SD will exceed the costs and efforts in such case.

In connection with your questions to the constituents we believe that almost all answers should be left to the IASB as these should be part of thorough field-testing.

We will be pleased to give you any further information that you may require.

Yours sincerely,



Hans de Munnik
Chairman Dutch Accounting Standards Board

Appendix: Comment Letter to the IASB

DUTCH ACCOUNTING STANDARDS BOARD (DASB)

RAAD VOOR DE JAARVERSLAGGEVING

Secretariat:
Antonio Vivaldistraat 2-8
Postbox 7984
1008 AD Amsterdam
The Netherlands

T +31 (0)20 301 03 91
F +31 (0)20 301 02 79
rj@rjnet.nl
www.rjnet.nl

International Accounting
Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

Our ref : AdK
Direct dial : Tel.: (+31) 20 301 0391 / Fax: (+31) 20 301 0302
Date : Amsterdam, 4 April 2011
Re : Comments on Supplementary Document Financial Instruments: Impairment

Dear members of the International Accounting Standards Board,

The Dutch Accounting Standards Board appreciates the opportunity to comment on your supplementary document on impairment issued on 31 January 2011 (the 'SD'). Whilst we support a common approach for credit impairment under IFRS and US GAAP and are glad to see that the SD includes such a joint proposal, we also have a number of significant concerns.

Due process
Our major problem is with the approach taken in this project for the reasons below:

- The proposals in the SD are far reaching (especially for the financial industry) and include many new elements (including for instance the 'floor') compared to the original proposals in the IASB Exposure Draft Financial Instruments: Amortised Cost and Impairment (the 'ED'). In our view a 60-day comment period is insufficient to absorb these proposals and to allow for your constituents to understand the complexities of these proposals in detail. More time is needed for a full impact assessment, also given the potential interaction with other (proposed) standards.
- The replacement of IAS 39 by IFRS 9 is designed as a phased approach. With this SD, the impairment phase is now further divided into separate components. The SD only addresses one element (open portfolios) and leaves many other elements of the ED open. Furthermore, there are several other matters that are not addressed in either the ED or the SD and relationships with other standards that still need to be addressed in order to have a final standard that is complete and coherent with other (proposed) standards.
- The timelines of the IASB and the FASB for finalising the entire financial instruments standard differ. Even though the SD includes a joint proposal, the fact that the IASB intends to finalise the standard at a much earlier date than the FASB may still result in significant differences.

In our view the self-imposed 30 June 2011 deadline for this and certain other standards should not override the need for an appropriate due process. The quality of the process and of the resulting standard should be of primary concern. In our opinion, the IASB should therefore allow more time for that process including its own assessment of comments received. That would be achieved by electing to run this project in parallel with the FASB timeline with the additional benefit that the likelihood of a common outcome would be much greater as well.

We will be expressing these concerns on the due process in a separate letter to the Trustees of the IFRS Foundation, too.

Other comments
Our detailed responses to your questions can be found in the Appendix to this letter, but we believe it to be important to raise two other significant issues we have with the proposals as they stand.

One of the elements that has been introduced in the SD is the so-called ‘floor’ in the impairment allowance based on a ‘foreseeable future period’. We believe that an expected loss impairment model should reflect the link between the pricing of the asset and the expected credit losses. The mechanism of a floor does not reflect this link. We believe that a floor is not necessary to achieve the proposed objective of the SD to reflect initial expected credit losses over the life of the portfolio. When a proper estimate is made of the time-proportional amount – including a periodical recalibration of such estimate – and a proper transition of loans from the good book to the bad book is applied, we believe that the introduction of the floor concept is unnecessary. We understand that the floor is intended to address early loss emergence scenarios, but we are not convinced that a floor is needed in this respect and believe that alternative approaches should be investigated. In addition, we note that the foreseeable future period is not defined and that is remains very unclear how this concept should be interpreted, another reason in our view do away with this concept when finalising the standard. We understand that the floor concept is a result of combining earlier IASB and FASB proposals into one converged proposal. However, attempting to join two fundamentally different models into one, in our view does not necessarily result in a sound standard. Convergence may be important, but high quality standards are even more important.

The proposals in the SD are rather complex and we believe that robust and satisfactory field-testing is necessary to better understand both the practicability of the proposals and the outcome of the proposals for various products and in various parts of the economic cycle. Such field-testing should be performed on an overall, complete proposal and not on a piece-meal basis for different parts of the final standard. We are particularly concerned that, because of both the floor and the mechanism of transferring assets from the good book to the bad book, there is a general expectation that the proposals will simply result in a profit and loss account similar to the current incurred loss model – and potentially even more volatile – and a provision in the balance sheet that is built up but cannot be used, i.e. in reality a buffer. Would this indeed be the result, than we have significant doubts whether:
- this outcome is in line with the key objectives of addressing the ‘too little, too late and too pro cyclical’ concerns of the incurred loss model;
- the benefits of implementing a complex model such as proposed in the SD will exceed the costs and efforts in such case.

We will be pleased to provide any further information that you may require.

Yours sincerely,

Hans de Munnik
Chairman Dutch Accounting Standards Board

Appendix A to Comments on the IASB's supplementary document on impairment

Question 1
Do you believe the approach for recognition of impairment described in this supplementary document deals with this weakness (ie delayed recognition of expected credit losses)? If not, how do you believe the proposed model should be revised and why?

The proposed approach in the SD addresses many of the concerns with the original proposals in the IASB Exposure Draft Financial Instruments: Amortised Cost and Impairment (the 'ED'). These include the possibility to apply the expected cash flow approach to open portfolios, the move to a proportional basis of the recording of catch ups when there is a change in the estimate of expected losses and the decoupling of interest revenues and the allocation of the expenses of loan losses. We note that the common approach of the SD is a compromise between the IASB and the FASB and, accordingly, new elements are introduced: the 'good book' and the 'bad book' as well as the application of the 'floor'.

We believe that the proposed approach for an impairment model with full provision for all expected losses on financial assets in the bad book and the recording of the higher of the time-proportional amount and the floor for the good book will result in earlier recognition of credit losses than the current incurred losses models. At least it could result in a once-only higher level of provision for credit losses when the proposed approached will be implemented.

The proposals in the SD are rather complex and we believe that robust and satisfactory field-testing is necessary to better understand both the practicability of the proposals and the outcome of the proposals for various products and in various parts of the economic cycle. Such field-testing should be performed on an overall, complete proposal and not on a piece-meal basis for different parts of the final standard. We specifically note in this respect the expectation that (because of both the floor and the mechanism of transferring assets from the good book to the bad book) there is an expectation that the proposals may simply result in a profit and loss account similar to the current incurred loss model (or even more volatile) and a provision in the balance sheet that is built but cannot be used (a 'buffer'). Would this indeed be the result, than we have significant doubts whether:

- this outcome is in line with the key objectives of addressing the 'too little, too late and too procyclical' concerns of the incurred loss model;
- what the quantitative impact is of the proposed approach among various entities, in respect of both the level of provisions and the volatility of the results;
- the benefits of implementing a complex model such as proposed in the SD will exceed the costs and efforts in such case.

Question 2
Is the impairment model proposed in the supplementary document at least as operational for closed portfolios and other instruments as it is for open portfolios? Why or why not?

Although the supplementary document seeks views on whether the proposed approach is suitable for open portfolios, the boards welcome any comments on its suitability for single assets and closed portfolios and also comments on how important it is to have a single impairment approach for all relevant financial assets.

We believe there is no conceptual reason why the impairment allowance for a group of single assets or assets in a closed portfolio should be different from that for a group of same assets in an open portfolio.

Question 3
Do you agree that for financial assets in the 'good book' it is appropriate to recognise the impairment allowance using the approach described above? Why, or why not?

Question 4
Would the proposed approach to determining the impairment allowance on a time-proportional basis be operational? Why, or why not?

Question 5
Would the proposed approach provide information that is useful for decision-making? If not, how would you modify the proposal?

We believe that it is appropriate to recognise the impairment allowance using the approach proposed in the SD, subject to robust and satisfactory field-testing. In addition, we believe that a floor is not necessary to achieve the proposed objective of the SD to reflect initial expected credit losses. When a proper estimate is made of the time-proportional amount – including a periodically recalibration of such estimate – and a proper transition of loans from the good book to the bad book is applied, we believe that the floor is useless. We also refer to our answer to the questions 9 and 10.

Question 6
Is the requirement to differentiate between the two groups (ie 'good book' and 'bad book') for the purpose of determining the impairment allowance clearly described? If not, how could it be described more clearly?

Question 7
Is the requirement to differentiate between the two groups (ie 'good book' and 'bad book') for the purpose of determining the impairment allowance operational and/or auditable? If not, how could it be made more operational and/or auditable?

Question 8
Do you agree with that proposed requirement to differentiate between the two groups (ie 'good book' and 'bad book') for the purpose of determining the impairment allowance? If not, what requirement would you propose and why?

Taking these questions in reverse order, we agree with the requirement to differentiate between the two groups, and to recognise all expected losses on assets in the bad book. Ignoring the application of the floor, the proposed approach would allocate future expected losses over the expected life of any portfolio on a time-proportional basis. We believe however that the criteria to determine when assets should be transferred from the good book to the bad book (and vice versa) should be clearer (e.g. through additional guidance and/or examples) when finalising the standard. This could be even more relevant for entities outside the financial services industry.

Question 9

The boards are seeking comment with respect to the minimum allowance amount (floor) that would be required under this model. Specifically, on the following issues:

(a) Do you agree with the proposal to require a floor for the impairment allowance related to the 'good book'? Why or why not?

(b) Alternatively, do you believe that an entity should be required to invoke a floor for the impairment allowance amount related to the 'good book' only in circumstances in which there is evidence of an early loss pattern?

(c) If you agree with a proposed minimum allowance amount, do you further agree that it should be determined on the basis of losses expected to occur within the foreseeable future (and no less than twelve months)? Why or why not? If you disagree, how would you prefer the minimum allowance to be determined and why?

(d) For the foreseeable future, would the period considered in developing the expected loss estimate change on the basis of changes in economic conditions?

(e) Do you believe that the foreseeable future period (for purposes of a credit impairment model) is typically a period greater than twelve months? Why or why not? Please provide data to support your response, including details of particular portfolios for which you believe this will be the case.

(f) If you agree that the foreseeable future is typically a period greater than twelve months, in order to facilitate comparability, do you believe that a 'ceiling' should be established for determining the amount of credit impairment to be recognised under the 'floor' requirement (for example, no more than three years after an entity's reporting date)? If so, please provide data and/or reasons to support your response.

Question 10

Do you believe that the floor will typically be equal to or higher than the amount calculated in accordance with paragraph 2.1(a)(i)? Please provide data and/or reasons to support your response, including details of particular portfolios for which you believe this will be the case.

No, we do not agree with the proposal to require a floor for the impairment allowance related to the good book. We believe that an expected loss impairment model should reflect the link between the pricing of the asset and the expected credit losses. The mechanism of a floor does not reflect this link. We believe that a floor is not necessary to achieve the proposed objective of the SD to reflect initial expected credit losses over the life of the portfolio. When a proper estimate is made of the time-proportional amount – including a periodically recalibration of such estimate – and a proper transition of loans from the good book to the bad book is applied, we believe that the floor is unnecessary. We understand that the floor is intended to address early loss emergence scenarios, although we are not convinced that a floor is needed in this respect and we believe that alternative approaches should be investigated. In addition, we note that the foreseeable future period is not defined and that is remains very unclear how this concept should be interpreted. This further illustrates that the foreseeable future floor should not be maintained when finalising the standard. Finally, we note our concern that the floor appears to result from combining earlier IASB and FASB proposals into one converged proposal. In our opinion, convergence is important, but high quality standards are even more important. Combining two fundamentally different models, resulting in the time proportionate model with a foreseeable future floor, does not achieve this objective.

Question 11
The boards are seeking comment with respect to the flexibility related to using discounted amounts. Specifically, on the following issues:
(a) Do you agree with the flexibility permitted to use either a discounted or undiscounted estimate when applying the approach described in paragraph B8(a)? Why or why not?
(b) Do you agree with permitting flexibility in the selection of a discount rate when using a discounted expected loss amount? Why or why not?

Yes, we agree. We note that the estimate of the timing of cash flows under the proposed model is rather complex and subjective. We agree with the IASB proposal that either discounted or undiscounted amounts could be used and we also agree with the IASB that – if an entity uses discounted amounts – for practical reason any rate between the risk-free rate and the effective interest rate determined in accordance with IAS 39 can be used as the discount rate. However, we note that an entity should apply the elected allocation method consistently, and should also disclose the allocation method and the discount rate used.

Question 12
Would you prefer the IASB approach for open portfolios of financial assets measured at amortised cost to the common proposal in this document? Why or why not? If you would not prefer this specific IASB approach, do you prefer the general concept of the IASB approach (ie to recognise expected credit losses over the life of the assets)? Why or why not?

Yes, we prefer the IASB approach rather than the FASB approach.

Question 13
Would you prefer the FASB approach for assets in the scope of this document to the common proposal in this document? Why or why not? If you would not prefer this specific FASB approach, do you prefer the general concept of this FASB approach (ie to recognise currently credit losses expected to occur in the foreseeable future at or after the first reporting date after initial recognition of the financial assets)? Why or why not?

No, we do not support the FASB approach model because it does not reflect the economics of lending transactions. In addition, referring to our answer to the questions 9 and 10 we have concerns on about the application of the concept of 'foreseeable future'.

Question 14Z
Do you agree that the determination of the effective interest rate should be separate from the consideration of expected losses, as opposed to the original IASB proposal which incorporated expected credit losses in the calculation of the effective interest rate? Why or why not?

Yes, we agree that for open portfolios the effective interest rate should be determined separately from the expected losses, to ensure that the method is at least operational.

Question 15Z
Should all loan commitments that are not accounted for at fair value through profit or loss (whether within the scope of IAS 39 and IFRS 9 or IAS 37) be subject to the impairment requirements proposed in the supplementary document? Why or why not?

Question 16Z
Would the proposed requirements be operational if applied to loan commitments and financial guarantee contracts? Why or why not?

Yes, we agree that all loans commitment that are not accounted for at fair value through profit or loss should be subject to the impairment requirements proposed in the SD.

Question 17Z
Do you agree with the proposed presentation requirements? If not, what presentation would you prefer instead and why?

Yes, we agree the proposed presentation requirements once the standard will be final based on the proposal. We accept the presentation proposals in the SD in the context of the common model.

Question 18Z
(a) Do you agree with the proposed disclosure requirements? If not, what disclosure requirement do you disagree with and why?
(b) What other disclosures would you prefer (whether in addition to or instead of the proposed disclosures) for the proposed impairment model and why?

Yes, we agree as we accept the disclosure proposals in the SD in the context of the common model, noting that additional field-testing should be performed in order to determine whether the proposed disclosure requirements are operational. In addition, we note that the term 'actual outcomes' as included in Z12 is not defined and might not be clear and that this term should be defined when finalising the standard.

Question 19Z
Do you agree with the proposal to transfer an amount of the related allowance reflecting the age of the financial asset when transferring financial assets between the two groups? Why or why not? If not, would you instead prefer to transfer all or none of the expected credit loss of the financial asset?

No, we do not agree, because of both the floor and the mechanism of transferring assets from the good book to the bad book, there is a general expectation that the proposals will simply result in a profit and loss account similar to the current incurred loss model – and potentially even more volatile – and a provision in the balance sheet that is built up but cannot be used, i.e. in reality a buffer. Would this indeed be the result, than we have significant doubts whether doubts whether:

- this outcome is in line with the key objectives of addressing the 'too little, too late and too pro cyclical' concerns of the incurred loss model;
- the benefits of implementing a complex model such as proposed in the SD will exceed the costs and efforts in such case.