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PIR IFRS 9 Impairment

Credit risk disclosures – feedback analysis

Objective

1 The objective of this session is to seek EFRAG FR TEG views on the IASB staff feedback analysis and recommendations and the IASB tentative decisions on credit risk disclosures.

Summary of the feedback received

2 Most stakeholders were of the view that that there are **no fatal flaws** with the objectives of credit risk disclosure requirements in IFRS 7 and that the combination of disclosure objectives and specific requirements is the right approach.

3 However, most stakeholders (including investors) reported **diversity in the information provided** and some attributed such diversity to the objective-based nature of the requirements and lack of sufficient specific disclosure requirements.

4 Stakeholders who raised concerns about diversity further explained that the quantity, quality, and the level of disaggregation of information vary significantly in practice which reduces comparability and limits the usefulness of information to investors. These stakeholders noted that they do not expect uniformity in the credit risk management approaches but greater consistency in how entities disclose information about them.

5 Many stakeholders (except some preparers) said that **greater consistency in practice could be achieved by adding or amending the specific disclosure requirements, accompanied by application guidance and illustrative examples in IFRS 7.**

6 Some stakeholders asked the IASB to consider the proportionality and balance between larger financial and smaller non-financial entities. In this context, some stakeholders, including CMAC members, suggested that the IASB **only enhance the disclosure requirements for financial entities and consider reducing the requirements for non-financial entities.**

7 In contrast, **some preparers (mostly financial entities) said that the IFRS 7 requirements are sufficient** and, in their view, strike the right balance between costs for preparers and benefits to investors. These stakeholders raised concerns that any potential improvements would involve significant costs for preparers to implement which would exceed any incremental benefit to be gained by investors.

8 Some stakeholders noted the positive effects that the regulatory or industry group recommendations in some jurisdictions have had on the disclosure quality. For example, the recommendations by the UK regulators about disclosures[1], have resulted in banks providing more consistent and high quality ECL disclosures.

9 Detailed feedback and stakeholders' suggestions to disclosure improvements related to:

(a) classes of financial instruments and level of aggregation; and

(b) more specific disclosure requirements about:

(i) sensitivity analysis;

(ii) post-model adjustments or management overlays (PMAs);

(iii) significant increases in credit risk (SICR);

(iv) forward-looking information; and

(v) reconciliation of the ECL allowance and changes in gross carrying amount of assets.

Classes of financial instruments and level of aggregation

10 **Respondents suggested either to specify the class of financial instruments** that is appropriate to the nature of information required by each disclosure requirement or to provide application guidance to support greater consistency in how entities decide the appropriate level of aggregating financial instruments into classes.

11 There was, however, no consensus among these stakeholders about what generally is an appropriate level of aggregation.

Sensitivity analysis

12 Most stakeholders noted that IFRS 7 has no specific requirements to disclose sensitivity analysis for credit risk and there is significant inconsistency for the entities that disclose this information in how they provide sensitivity analysis.

13 **Respondents suggested to add specific requirements for an ECL sensitivity analysis** to enable investors to evaluate the effects of future uncertainties on ECL.

Post-model adjustments or management overlays (PMAs)

14 Most stakeholders reported that there is often very limited information about PMAs in financial statements, even when such adjustments represent a material proportion of the total ECL allowance. Therefore, they **suggested to add more specific requirements about PMAs**, such as the amount of PMAs as at reporting period, the reasons that led an entity to using PMAs and plans for unwinding of such PMAs to enhance the usefulness of information for investors.

[1] Three UK regulators, the Financial Conduct Authority, the Financial Reporting Council and the Prudential Regulatory Authority jointly established a UK taskforce on disclosures of ECL which publishes reports with recommendations for a comprehensive set of ECL disclosures. These reports include recommendations on information to be provided on judgemental areas of ECL, along with illustrative best practice examples.

Significant increases in credit risk (SICR)

15 Many stakeholders said that disclosures do not sufficiently explain the approach an entity uses, and the most relevant factors it applies to determine if SICR occurs. These stakeholders also reported significant inconsistency in the level of detail in the information disclosed.

16 Therefore, they **suggested to specify 'baseline' information** an entity is required to provide about the approaches it has **used to determine SICR**. They also suggested **to specify the format of the required disclosure** to facilitate investor analysis.

Forward-looking information

17 Some stakeholders said that there is diversity in the information entities disclose about the forward-looking scenarios and their probability weightings.

18 Therefore, respondents suggested **to add a specific disclosure requirement about the forward-looking scenarios used in estimating ECL, probability weightings assigned to each scenario and any changes in such weightings**.

Reconciliation of the ECL allowance and changes in gross carrying amount of assets

19 Some stakeholders (including investors) said that the reconciliation from the opening balance to the closing balance of the ECL allowance is one of the most useful credit risk disclosures. However, despite the requirement in paragraph 35I of IFRS 7, the entities do not appropriately explain how the changes in the gross carrying amount of financial instruments contributed to the changes in the ECL allowance during the period.

20 Therefore, they suggested **to require the disclosure of the gross carrying amounts of financial instruments to be provided alongside the reconciliation of the ECL allowance, and that such information is provided in tabular format.**

Reducing disclosure burden for non-financial entities

21 Some stakeholders suggested **reducing the disclosure burden for non-financial entities** because the volume of required disclosures can sometimes be disproportionate to the nature of their business and their exposure to credit risk.

22 In particular, they suggested to:

(a) simplify requirements about write-off policies or collateral management for financial instruments in scope of the simplified approach (e.g. trade receivables); and

(b) scope out of disclosure requirements financial instruments which they perceive as 'low risk' (such as corporate bonds, sovereign debt or intragroup instruments).

IASB staff analysis

Classes of financial instruments and level of aggregation

23 The IASB staff notes that concept of class of financial instruments is not unique and applies across IFRS 7. Therefore, any deliberation about this concept would require consideration that is broader than the scope of this PIR being the credit risk disclosures.

24 Paragraph B3 of IFRS 7 further reinforces the principle set out in paragraph 6 of IFRS 7 that an entity decides the appropriate level of aggregation.

25 In the IASB staff view, **prescribing a level of aggregation for disclosure requirements would mean moving away from the principle in paragraph 6 of IFRS 7** and might result in disaggregation and level of disclosure that does not reflect the nature of the information disclosed and that does not take into account the characteristics of financial instruments.

26 Instead, the IASB staff is of the view that **specifying the format (e.g. tabular) and nature (e.g. quantitative) of some specific disclosure requirements for which there is significant diversity may be more effective** in supporting greater consistency in the information disclosed. The IASB staff note that this level of specificity is already present in some IFRS 7 requirements.

27 **On the reconciliation with a line item in financial statements**, the IASB staff emphasise that paragraph 6 of IFRS 7 already requires that, in deciding the appropriate level of aggregation / disclosure, an entity shall provide sufficient information to permit reconciliation to the line items presented in the statement of financial position. Therefore, in the IASB staff view, **no further requirements are needed for this matter**.

Sensitivity analysis

28 The IASB staff note that paragraph 125 of IAS 1[2] requires an entity to disclose the assumptions it makes about the future, and other major sources of estimation uncertainty at the end of the reporting period, that have a significant risk of resulting in a material adjustment to the carrying amounts of assets and liabilities within the next financial year. These requirements also apply to estimation uncertainty arising from ECL.

29 The IASB staff acknowledge that the fact that a specific requirement for sensitivity analysis is included in IFRS 7 for market risk (see paragraphs 40–41 of IFRS 7) and not for credit risk might contribute to the concerns raised by stakeholders.

30 Given the evidence gathered and the extent of estimation uncertainty inherent in estimating ECL, the IASB staff agree that **information about the sensitivity of the ECL allowance to particular risk variables or assumptions could be useful information**.

Post-model adjustments or management overlays (PMAs)

31 Paragraph 35B(b) of IFRS 7 requires disclosure of information about the amounts in the financial statements arising from expected credit losses. Such requirements, therefore, apply to the ECL amounts, regardless of the method or approach used in estimating such amounts.

32 Furthermore, paragraph 35A of IFRS 7 sets out the scope of credit risk disclosures, noting that an entity shall apply credit risk disclosure requirements (i.e. paragraphs 35F–35N of IFRS 7) to financial instruments to which the impairment requirements in IFRS 9 are applied. Paragraph 35G of IFRS 7 then requires an entity to disclose the basis of inputs and assumptions and the estimation techniques used to measure ECL, changes in the estimation techniques or significant assumptions made during the reporting period and the reason for those changes. Therefore, in the IASB staff view, **there is no ambiguity as to whether IFRS 7 credit risk disclosure requirements would apply to ECL amounts determined through a PMA.**

[2] In April 2024 the IASB issued IFRS 18 *Presentation and Disclosure in Financial Statements* which replaces IAS 1. Paragraph 125 of IAS 1 is carried forward to paragraph 31A of IAS 8 *Basis of Preparation of Financial Statements*.

33 Accordingly, the IASB staff **would not suggest to add disclosure requirements that would target PMAs specifically**. This is because the disclosure requirements in IFRS 7 are method / approach agnostic and **prescribing requirements that would apply to a particular method would be inconsistent with the disclosure objectives and requirements in IFRS 7**.

34 However, to acknowledge the feedback received, the IASB staff would **suggest exploring potential amendments to IFRS 7 about disclosure of the information on management judgements, including judgemental adjustments, made in estimating ECL as at reporting period**. Such amendments might include specific additions to the current requirements and additional illustrative examples.

Determining SICR

35 The IASB staff notes that feedback indicates that stakeholders need not more but more structured information. For example, a disclosure that provides more useful and structured summary about factors an entity used to determine SICR (SICR triggers) and that would be provided in a consistent way to allow for comparison between periods and different entities.

36 The IASB staff acknowledge stakeholders' feedback that understanding what factors triggered SICR (e.g. most movements from stage 1 to stage 2) and being able to compare the key SICR triggers with other comparable entities might provide useful information to users of financial statements.

37 Consequently the IASB staff recommend **considering potential improvements to IFRS 7 in this area - for example, by specifying particular items of information that would satisfy the disclosure objective in paragraph 35F(a) of IFRS 7[3].**

Forward-looking information

38 The IASB staff note that paragraph 35B and 35G of IFRS 7 already require entities to disclose how forward-looking information has been used in determining ECL, but IFRS 7 does not specify items of information that would satisfy these objectives.

39 The IASB staff agree that **disclosure about forward-looking scenarios and related probability weightings** are important inputs and assumptions in determining ECL. Accordingly, information about them would assist investors in evaluating ECL approaches between different entities or reporting periods. Therefore, in the light of evidence gathered, **the IASB could consider potential improvements to IFRS 7 in this area**.

Reconciliation of the ECL allowance and changes in gross carrying amounts

40 As explained in paragraphs BC48P−BC48S of IFRS 7, the IASB has previously considered requiring the reconciliation of the gross carrying amount of financial instruments alongside the reconciliation of the ECL allowance. However, in response to preparers' feedback about the operational burden of such reconciliation, the IASB clarified that the objective is to provide information about the key drivers for changes in the gross amount to the extent that it contributes to changes in ECL.

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[3] Paragraph 35F(a) of IFRS 7 requires an entity to disclose information that enables investors to understand and evaluate how an entity determined whether the credit risk of financial instruments has increased significantly since initial recognition.

41 In the light of the feedback about the diversity in the outcomes, the IASB staff think that **the IASB could consider potential improvements to current requirements in paragraph 35I of IFRS 7 as part of targeted improvements to IFRS 7**. However, the IASB would need to carefully consider such improvements in the light of preparers' concerns in paragraphs BC48P−BC48S of the Basis for Conclusions on IFRS 7.

Reducing disclosure burden for non-financial entities

42 In the IASB staff view, the IASB **could consider whether there is potential for simplifications as part of the targeted improvements to credit risk disclosures**, including **performing outreach** to obtain further evidence for identifying such areas.

43 The IASB could consider **limiting the potential new requirements only to financial instruments to which the general approach applies** (i.e. not require such information for financial instruments in scope of the simplified approach).

44 In context of reduced disclosure for non-financial entities, the IASB staff note that recently issued IFRS 19 *Subsidiaries without Public Accountability: Disclosures* permits an eligible subsidiary to apply IFRS Accounting Standards with reduced disclosure requirements. Applying this Standard would also help address concerns in this area for some entities.

EFRAG comment letter

45 The feedback the IASB received is mostly in line with the EFRAG comment letter.

46 EFRAG has been informed that the level of disclosures provided is not always sufficient to understand the high level of uncertainty arising from the level of judgement required by IFRS 9 for recognition of ECL. Stakeholders indicated that analysis of banks' credit risk disclosures showed a significant diversity in practice with different levels of detail about the assumptions taken, credit risk management policies, methodologies and models applied.

47 At the same time, some constituents are of the view that there are no fatal flaws in IFRS 7 disclosure requirements and that they together with disclosure objectives provide an adequate basis for entities to be able to provide sufficient credit risk disclosures, resulting in relevant information. These stakeholders have indicated that the regulatory institutions have an important role in ensuring comparability of information.

48 EFRAG, considering the credit risk disclosures as a medium priority issue, recommended that more guidance in the form of illustrative examples and/or educational material would be helpful to enhance the quality and comparability of credit risk disclosures. EFRAG further highlighted that this guidance should not undermine but support the principle-based approach of the Standard.

IASB discussions and tentative decision

49 Based on the above analysis, **the IASB staff recommend to classify as medium priority the matters raised by stakeholders about credit risk disclosures and to add a project to the research pipeline to make targeted improvements to the disclosure requirements in IFRS 7 about credit risk.**

50 The **IASB members generally agreed with the IASB staff recommendations** but highlighted the importance of proportionality and scalability of the required information. They also

highlighted that no additional disclosure requirements should be added, but the existing ones enhanced and made more consistent.

51 Some IASB members expressed concerns that sensitivity analysis of ECL can be very burdensome and costly. Others questioned whether medium priority was appropriate as it makes the resulting research project go before the next agenda consultation.

52 13 of 14 IASB members agreed with the IASB staff recommendation.

EFRAG Secretariat analysis

53 The EFRAG Secretariat agrees with the IASB tentative decision which is in line with the EFRAG recommendation in its comment letter.

54 However, like the IASB members, the EFRAG Secretariat considers important not to undermine objective-based approach of the Standard and keep the disclosure requirements proportionate.

EFRAG FIWG feedback

55 EFRAG FIWG discussed this topic at its meeting on 13 June 2024 and noted the importance of not overprescribing the disclosure requirements. The ECL models are still new and recently had to incorporate a lot of new risks, such as COVID, political instability, etc. Members were of the view that it is important to keep the objectives-based nature of the standard to be able to encompass different ECL and business models in place in different jurisdictions.

56 A member suggested that market discipline is a better solution than changing a wording in IFRS 7 which is a good objectives-based standard enabling to provide right disclosure.

57 Members were of the view that ECL sensitivity disclosures can be extremely costly and burdensome. Changing one or more parameters will require to rerun the model. In addition, some parameters are correlated between them and changing only one will not provide complete information.

58 It was noted that a lot of guidance on ECL disclosure already exists, such as Enhanced Disclosure Task Force requirements, and the key aspects are already captured by IFRS 7. Therefore, minimum targeted improvements should be sufficient.

Questions to EFRAG FR TEG

59 Does EFRAG FR TEG agree with the IASB staff analysis and the IASB tentative decision to classify as medium priority the matters raised by stakeholders about credit risk disclosures and to add a project to the research pipeline to make targeted improvements to the disclosure requirements in IFRS 7 about credit risk?

60 Does EFRAG FR TEG have any comments on the EFRAG Secretariat analysis?

Appendix A – IASB staff assessment against PIR criteria

Step 1 - Is further action needed?

61 Evidence gathered (i.e. majority of comment letter feedback, outreach, including feedback from CMAC members, and staff and academics research) demonstrate the same problem - inconsistency in particular disclosures that entities provide about credit risk.

62 Based on the analysis of the feedback and research evidence, the IASB staff agree with stakeholders' feedback that some targeted improvements to IFRS 7 might support greater consistency in credit risk disclosure. The IASB staff note that, in most cases, the disclosure objectives in IFRS 7 already require broader information in the areas that stakeholders have suggested more specific information is required.

63 Therefore, in most cases, potential improvements would be consistent with the current disclosure objectives, hence largely incremental to current requirements. For example, such improvements could, in some cases, be in the form of additional specific information required to support the disclosure objectives in IFRS 7, or in other cases it could be specifying the format or nature of the specific disclosure. The IASB could identify particular disclosure areas (for example, sensitivity analysis, judgemental adjustments, determining SICR). In the IASB staff view, illustrative examples alone would not appropriately address the problem because examples are non-authoritative.

64 The IASB staff assess that **most of the PIR criteria for taking action are present. Accordingly, they recommend the IASB take action relating credit risk disclosures.**

Step 2 - Is the finding high, medium or low priority?

65 According to the below analysis the IASB staff concluded that **most of the prioritisation characteristics are present to a large extent** and the benefits of any action are expected to exceed the costs. The evidence gathered however **does not suggest that solutions are needed urgently.**

66 Therefore, in accordance with the PIR framework, the IASB staff recommend the IASB classify matters relating credit risk disclosure **as medium priority and thus, add a project for this matter to its research pipeline.**

Does the matter have substantial consequences?

67 The IASB staff agree with stakeholders' feedback that because of the measurement uncertainty and inherently high level of judgement involved, the ECL model relies on high quality disclosures. This is consistent with the IASB's rationale for developing credit risk disclosure requirements to meet the additional information needs of investors that arise specifically from an expected and forward-looking credit losses model.

68 Therefore, inconsistency in disclosures about credit risk (particularly in areas that involve significant management judgement) might have substantial consequences for decision-useful information to investors.

Is the matter pervasive?

69 Credit risk disclosure requirements apply to financial instruments subject to impairment requirements of IFRS 9. Most entities have financial instruments that are subject to impairment. In this context, majority of feedback and all research evidence provide

evidence about inconsistency in disclosures for several areas. Therefore, the IASB staff assess that the matter is pervasive.

Can the matter be addressed by the IASB or the IFRS Interpretations Committee?

70 Yes, the IASB could consider targeted improvements to IFRS 7 to support greater consistency in credit risk disclosures. In addition to potential specific disclosure requirements, the IASB could also consider specifying the format and nature of particular requirements.

71 Nonetheless, the IASB staff note that due to the principle-based nature of the ECL model and the related objective-based credit risk disclosure requirements, the role of parties such as auditors and regulators will remain important to support decision-useful credit risk disclosures, including greater consistency in how entities provide such disclosures.

Would the benefits of any action be expected to outweigh the costs?

72 In the IASB staff view, the benefits relating the usefulness of information to investors would be expected to outweigh the costs for preparers. In reaching this view, was considered:

(a) *greater consistency in disclosure is needed for investors.* In this PIR, the IASB received feedback that the diversity in information arising from applying the requirements is reducing the usefulness of credit risk information to investors. If the disclosure objectives could be supported by specific information required for those main areas of diversity, greater consistency in credit risk disclosures would be achieved, making information more useful to investors. Furthermore, improvements relate to some of the most judgemental areas of the ECL model (e.g. SICR, PMAs, forward-looking scenarios)—greater consistency might assist investors in better evaluating such judgements.

(b) *potential enhancements largely consistent with current disclosure objectives.* As noted in the IASB staff analysis, most of the potential improvements requested from stakeholders relate to information arising from current disclosure objectives in IFRS 7. Therefore, most disclosure enhancements might be incremental to existing requirements, not necessarily brand-new requirements.

(c) *costs vs benefits to be considered in developing potential requirements*. In exploring potential improvements to credit risk disclosures, the IASB would need to achieve an appropriate balance between incremental benefits to investors and additional costs for preparers (for example, by considering whether specific requirements should only apply to financial instruments in scope of the general approach). Assessment of costs and benefits is consistent with the IASB's approach to developing any disclosure requirements.

Appendix B - Analysis of other comments

73 The following table summarises other disclosure comments identified by a few stakeholders. Based on the analysis, the I ASB staff conclude that no further action is needed in response to these comments.

Feedback	**Staff analysis**	**Conclusion**
Effect of climate-related risks in the measurement of ECL		
Some stakeholders suggested that the IASB provide guidance and illustrative examples for disclosures about how climate-related risks have been incorporated in estimating ECL.	The IASB staff note that, as part of the *Climate-related and other uncertainties in the financial statements* project, the IASB has tentatively decided to provide some examples, including a potential example illustrating disclosure requirements in IFRS 7 about the effects of climate-related risks on an entity's credit risk management practices and how these practices relate to measuring ECL. If the IASB were to add such an example to IFRS 7, we think that would address the feedback in this area.	**No further action.**
Other credit risk disclosures		
A few stakeholders also suggested specific disclosure requirements for other areas such as revolving credit facilities, modified financial instruments and ageing of trade receivables.	The IASB staff note that the PIR feedback does not suggest that these disclosure matters are prevalent. The IASB staff also note that IFRS 7 requirements broadly capture such information: • paragraph 35M of IFRS 7 requires information about loan commitments and trade receivables. • paragraph 35J of IFRS 7 requires information about modifications. Nonetheless, we note that the IASB's Amortised Cost Measurement project will consider requirements about modifications of financial instruments and might consider disclosure improvements.	**No further action.**

Appendix C – Analysis of current practice

74 To inform the IASB's response to the PIR feedback, the IASB staff did a desktop review of financial statements of 30 banks (20 global systemically important banks and 10 small-medium size banks) and 10 corporates, examining how entities disclosed credit risk information applying IFRS 7.

75 Our main findings are:

(a) *sensitivity analysis*. Not all banks in the sample disclosed sensitivity analysis for ECL. Among banks that provided such disclosure, most disclosed sensitivity analysis over changes in weightings of forward-looking scenarios and/or changes in key macroeconomic variables. Others disclosed sensitivity over other factors such as changes in probability of default or changes from stage 2 to stage 1. The disaggregation level at which disclosure was provided also varied—some banks disclosed information by each main portfolio; others did it at a different level or at the level of the total ECL amount.

(b) *PMAs.* Some banks provided no information about PMAs. The banks who provided such disclosure, the information about PMAs varied significantly - some provided brief and generic qualitative information (e.g. that PMAs were recognised due to rising inflation) without any accompanying detail about key inputs or assumptions used in determining the adjustment and no quantitative information. A few others disclosed detailed information about the reasons for PMAs and any changes thereof, and quantitative information such as PMA amounts by portfolio and by ECL stage.

(c) *determining SICR.* Almost all banks in our sample provided some information about their approach to determining SICR. However, the quantity and quality of the information disclosed varied significantly from bank to bank:

(i) some banks provided generic descriptions about factors they consider in determining SICR, repeated requirements of IFRS 9 with no entity-specific information (e.g. quantitative and qualitative factors considered with 30 days past due backstop);

(ii) a few banks provided summary information about the types of factors they consider but there was no portfolio specific information or explanation of the extent such factors contributed to the significant increases in credit risk during the reporting period; and

(iii) some other banks disclosed extensive quantitative and qualitative information about SICR triggers and disaggregated that information by portfolio. In addition, consistent with regulatory recommendations, some UK banks provided a structured summary, in a tabular format, showing decomposition of stage 2 assets setting out the reasons why a financial instrument was determined to have SICR (i.e. what portion of ECL were triggered by quantitative or qualitative factors and how much was triggered from financial instruments being 30 days past due).

(d) *reconciliation of the ECL allowance and gross carrying amount of assets.* Many of the banks in our sample provided some information about gross carrying amounts; a few however did not disclose such information despite it being required by paragraph 35I of IFRS 7. There were significant differences in how banks explained how the changes in the gross carrying amounts of financial instruments contributed to the changes in the loss allowance:

(i) some banks provided a reconciliation of the gross carrying amount and loss allowance in a tabular format, consistent with the illustrative example IG20B accompanying IFRS 7;

(ii) a few banks provided a reconciliation of the gross carrying amount and loss allowance as separate columns within the same table and disaggregated such information by ECL stages; and

(iii) other banks provided narrative explanations with a few key figures about changes in the gross carrying amounts but without no clear link to the changes in ECL that were reported in a different disclosure. Therefore, in such cases it was challenging to evaluate to what extent changes in the gross carrying amount contributed to changes in ECL.

(e) *trade receivables.* Corporates in our sample generally applied the simplified approach to recognise ECL and used the provision matrix for ECL of trade receivables as a practical expedient. However, some corporates did not disclose provision matrix even though they stated that they used such a matrix and did not provide any other disclosures about credit quality of their receivables despite it being required by paragraphs 35M-35N of IFRS 7.

(f) *other credit risk disclosures of corporates*. For the corporates in our sample, we did not identify extensive information was being provided about credit risk. For example, none of the corporates in our sample provided any information about write-off policies or information about collateral management.