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Mouvement des Entreprises de France
MEDEF

A F E P

Association Française des Entreprises Privées

IASB
30 Cannon Street
London EC4M 6XH
UK

Paris, Apr. 1, 112011

Dear Sir or Madam,

Re: ***Supplement to ED/2009/12 "Financial Instruments: Impairment"***

We welcome the opportunity to comment on the Supplement to ED/2009/12 "Financial Instruments: Impairment" (the SD). The SD covers only a limited part of the matters covered by the ED, and our comments on it might be different if we were able to see the complete set of proposals on the impairment of financial assets held at amortised cost. Therefore, it is critical that constituents are given the opportunity to assess the overall proposals before the completion of the standard.

In our comment letter of 28 June 2010 on the ED we expressed our agreement with the general principle behind the IASB's proposed approach to amortised cost and impairment, but also our concerns with some of the aspects of the application of this approach. Our principle concerns were:

1. We did not agree with the transformation of the effective interest rate method into an integrated method which included an allocation of expected credit losses to accounting periods.

2. We thought that the timing of expected losses was extremely difficult to forecast and that it was more practical to assume that they occurred over the life of the portfolio using an averaging method.

3. We did not agree that the immediate recognition of the effect of all the subsequent changes in the estimated expected losses was consistent with the principle of an expected loss approach in which a large part of the losses will relate to future periods.

We welcome the proposals in the SD which respond to these concerns.

The impairment of open portfolios

In our view, one of the strong elements of the IASB's proposals in the ED was the focus on the link between the credit pricing of the asset, as incorporated into the interest rate, and the level of losses expected on the asset. The concerns mentioned above were in respect of the lack of practicality and the complexity of applying the ED's specific proposals. We think that some of the changes to the model now proposed in the SD respond to these concerns:

- We welcome the separation (decoupling) of the effective interest rate from the expected credit losses allocation. This substantially simplifies the calculations of the two elements of the impairment model of the ED, especially when the estimate of expected losses changes subsequently to the initial measurement. Separation also facilitates presentation and explanation of amounts.
- We agree with the use of the time-proportional expected credit losses method for recognition of credit losses for the good book as an operational simplification. As stated in our comment letter on the ED, the effect of changes should be recognized on a prospective basis unless they are incurred. Any incurred losses should not be deferred until future periods but covered by the allowance already built up.
- We think that these amendments make the approach more operational while representing an acceptable proxy for the principle of the approach in the ED.

However, we do not think that the requirement to use the higher of the time-proportional expected credit losses and the credit losses expected to occur within the foreseeable future (the floor) is consistent with the IASB's model. The use of this floor does not appear to respond to the principle proposed in the IASB's ED on impairment that the effective return should reflect an allocation of the [estimate of] expected credit losses over the expected life of the instrument. The floor is rather an acceleration of the recognition of losses on grounds which do not seem clear to us. This approach seems to break the link between the pricing of the financial asset and the expected losses it is intended to cover. We think that the use of the "higher of the time-proportional expected losses and the credit losses expected to occur within the foreseeable future period" would lead to the recognition of day-one losses in certain cases, such as for an individual asset or portfolios of short- to medium-term assets where the foreseeable future might cover most of the expected life of the assets.

We recognize that the purpose of the use of the floor proposed in the SD is to deal with situations in which losses appear to be arising earlier than expected, but we are convinced that this approach is not consistent with the principle of the IASB's ED. Furthermore, in our experience it is the economic cycle which is the principal driver of losses for many European constituents. Therefore, it is not desirable that this "early loss pattern" issue overrides the whole impairment model.

The requirement to transfer items to the bad book is, in our view, the equivalent of the use of a floor, and is more consistent with the principles of the ED. We therefore encourage the IASB to explore alternative ways of dealing with this issue while respecting the principle of allocating expected losses over the expected life of the assets.

We agree with the principle of the ED and paragraphs BC70 to BC73 of the SD, and thus disagree with the compromise over principles that now appears to have been reached with the FASB's approach. If, for reasons of expediency in the context of convergence, the Board decides to maintain the floor, we would recommend that the rather vague notion of the "foreseeable future" be replaced by a period of twelve months in all cases.

Other than our disagreement with the use of the floor in the good book, which should not be carried into the final standard, we think that the approach proposed in the SD deals adequately with the problem of the delayed recognition of the expected credit losses perceived in the current IAS 39 approach, and represents a good balance between principle and practicality. However, we would emphasise that it will be possible to judge the success of the amortised cost impairment model for financial instruments only when the complete model is near to completion and that detailed field-tests will be necessary to prove its robustness.

Extension of the decoupled, time-proportional allocation method to other financial assets at amortised cost

We think that a single impairment model for all financial assets carried at amortised cost is the best and simplest approach to aim for. Indeed, requiring two different approaches for essentially the same economic events would, in our view, be detrimental to comparability and understanding.

We therefore think that the use of this decoupled approach (again, without the floor) should be extended to closed portfolios and to individual non-current financial instruments. Such simplification will be particularly helpful to industrial and commercial corporates which may not have systems or management methods as sophisticated as those used by major financial institutions. This would be the "base-case" approach but should not preclude more sophisticated entities from refining the approach to achieve a representation of the return on financial assets which is more appropriate to their business, while respecting the objective of the future standard.

Please see our comments in respect of portfolios of listed debt securities below.

The "good book, bad book" approach

We support the use of the good book and the bad book for the purpose of determining the impairment allowance, as we think this simplifies the mechanism of the impairment approach by making a clean cut between assets that are performing "normally" and those that require more individual attention, and thus makes explanation of the accounting clearer. We think that the requirement for differentiation between the good book and the bad book is reasonably clear, but that it might be even clearer if the terms "good book" and "bad book" were introduced in paragraph 2 of the SD, as anticipated by paragraph IE9.

The use of the good book and the bad book provides useful information by virtue of the link it makes to the entity's credit management approach. The approach adopted by financial institutions will probably be different from that of industrial and commercial companies, because of their different business models and concerns. The guidance must therefore be adapted so that it can be applied to both types of entity. We therefore suggest that some of the Basis for Conclusion (extracts from BC49) is reintegrated in the body of the standard to make clear that risk management differs across entities and therefore the level of management judgement and subjectivity required may be more or less important. It could also be useful to specify that even though the requirement to differentiate assets between two different categories is mandatory, it does not mean that assets always have to be allocated to the bad book.

Inevitably the use of judgement to develop the criteria for differentiation will lead to some differences between entities, but we think that this is inherent in all approaches to impairment which require the use of judgement.

Portfolios of listed debt securities

As stated in our response to the ED, we did not believe that the proposed approach was appropriate for portfolios of listed debt securities, such as those held by Insurance companies, as the credit-worthiness of these portfolios is such that they rarely suffer from default. We think it would be inconsistent with the expected loss model of the ED if the market expectation inherent in the quoted prices should drive the estimation of the expected losses. Market data and credit-agency ratings should be used as potential indicators of credit loss trends, but it should always be the management of the entity which arrives at an entity-specific estimate of future credit losses based upon its judgement.

Information provided to users of financial statements should be relevant and useful while satisfying the cost/benefit challenge. This leads us to think that it is not justifiable to require a complex model to be implemented for such portfolios.

Consequently, we think that specific guidance should be included in the proposed standard to make the points above clear in the application guidance

One way of dealing with such high-quality assets while remaining within the new SD model might be to assign them to a particular good book in which no credit losses are expected. In the rare circumstance of collectability becoming significantly uncertain, the asset concerned could be transferred to the bad book and an appropriate allowance for impairment established.

Portfolios of trade receivables

We understand that the Board has tentatively decided to deal with short-term trade receivables within the scope of the revenue recognition project. Consistently with our response to the ED we agree with this decision. If the Board confirms this decision, and we believe that is the best approach, we think that the final standard should make it clear that none of the requirements of the SD apply to open portfolios of short-term trade receivables.

Presentation in the income statement (IASB only proposal)

We agree with the proposal to present in the income statement the interest revenue on an effective-interest-rate basis consistent with IAS 39 separately from the impairment losses. We think that this proposal enhances the clarity of the information presented and fits better with the use of an allowance account. We think that it is clearer to separate the return into only two distinct lines, that is, revenue on an effective interest rate basis and the effect of all impairment losses, as now proposed. We do not see the informational value in the presentation of a line that presents the original expected losses, as proposed in the ED, and this has the disadvantage of adding further lines to the face f the income statement. This information is more usefully disclosed in the notes to the financial statements where it can be better displayed and explained in detail.

We have noted a general trend in the Board's recent projects to require more and more line items to be presented on the face of the primary financial statements. We think that there is a high risk that this will result in a cluttering-up of the statements which will be detrimental to the clarity and ease of understanding of these. In our view, the purpose of the primary statements is to give a clear and succinct picture of the performance of the entity which can be used as a strong basis for communication between the management and the other users of the financial statements, and any superfluous detail can destroy such clear communication. The detail required by more sophisticated users should be provided in the notes.

Entities should be allowed to use their judgement as to the most appropriate presentation in the income statement. We think that the most useful presentational approach for financial institutions is to allow for flexibility to allow the entity to provide the information in the way that is most helpful to the user and in conformity with the economic sector and local regulatory requirements within which they have to operate. This will mean in some instances that an interest margin will be presented separately from the credit risk effect. On the other hand, there may be cases where a gross interest revenue figure is required to be disclosed as a performance indicator and this should be allowed as well.

Transfer of impairment allowance to bad book (IASB only proposal)

The proposal to transfer from the good book to the bad book an amount of the impairment allowance reflecting the age of the related transferred asset may add some complexity. Moreover, we think it is more consistent with the model proposed to assume that the allowance is built up for the purpose of covering the losses related to assets which have to be transferred to the bad book. We think that it is better to transfer from the good book's allowance account an amount which corresponds to the losses expected on the asset transferred to the bad book. We therefore do not support the IASB's proposal.

Please do not hesitate to contact us if you require any further explanation or comment on this topic.

Yours faithfully,

ACTEO	AFEP	MEDEF
Patrice MARTEAU Chairman	**Alexandre TESSIER** Director General	**Agnès LEPINAY** Director of economic and financial affairs