May 31, 2013

Technical Director
Financial Accounting Standards Board
401 Merritt 7
PO Box 5116
Norwalk, CT 06856-5116

File Reference No. 2012-260, Proposed Accounting Standards Update: Financial Instruments – Credit Losses (Subtopic 825-15)

Dear Sir/Madam,

The Inter-American Development Bank (IDB or Bank) appreciates the opportunity to comment on this proposed accounting standards update (Proposal) on Financial Instruments – Credit Losses. The IDB is an international development institution with total assets of $91 billion. The IDB’s purpose is to further economic and social development of Latin America and the Caribbean. The vast majority of our loans outstanding are sovereign guaranteed, but we also hold some non-sovereign loans.

Overall, we are supportive of the FASB’s Proposal and believe that it adequately addresses many of the weaknesses identified in the existing US GAAP. We also view it as a welcome simplification of the existing impairment requirements bringing together the various impairment models currently included in US GAAP. However, we have some observations and comments about the Proposal and the process in general, that we would like to bring to the Board’s consideration before the Proposal is finalized.

First of all, we urge the FASB and the IASB to continue working together to bring US GAAP and IFRS as close to each other as possible. We are concerned that the recent developments in the Financial Instruments project in particular, including this Proposal, mean that convergence will not be achieved in the foreseeable future.

Second, while we appreciate the two Boards’ efforts to thoroughly consider many different possible solutions and all the feedback provided by different stake holders, we find it important that the project be advanced to the final standard stage as soon as possible, to allow reporting entities to move on with their financial reporting and potential system upgrades that may have been postponed in anticipation of the new standard.
Our responses to selected questions by the FASB are included in the Annex to this letter and our main comments about the Proposal are summarized below:

- We agree with the Board that an earlier recognition of credit losses will provide more decision-useful information.

- We commend the Board for simplifying the myriad of existing impairment models under US GAAP and believe that there is room for even more improvement. For example, we question the Board’s decision to exclude financial guarantees from the scope of this Proposal which seems counter-intuitive to the idea of bringing all impairment guidance together.

- We note that the proposed impairment model increases subjectivity of the reported numbers when compared to the existing US GAAP. This will most likely lead to implementation and comparability issues and might provide opportunities for income management. However, we agree with the Board that the Proposal results in the simplest expected credit loss model for users of the financial statements to understand and believe that overall, its benefits outweigh the foreseeable implementation issues.

Yours Sincerely,

Alberto Suria
Chief, Accounting Division
ANNEX – Responses to Selected Questions by the FASB

**Question 1:** Do you agree with the scope of financial assets that are included in this proposed Update? If not, which other financial assets do you believe should be included or excluded? Why?

We agree with the proposed scope except for the Board’s decision to scope out financial guarantees. By nature guarantees are similar to loans and provisioning for them is assessed together with allowance for loan losses. Including guarantees in the expected Insurance standard seems confusing and would contradict the Board’s efforts to bring all impairment guidance in one place.

**Question 2:** The proposed amendments would remove the initial recognition threshold that currently exists in U.S. GAAP and, instead, view credit losses as an issue of “measurement” as opposed to an issue of “recognition” because the credit losses relate to cash flows that are already recognized on the balance sheet. Do you believe that removing the initial recognition threshold that currently exists in U.S. GAAP so that credit losses are recognized earlier provides more decision-useful information?

It is our view that in general credit losses should be recognized earlier than under current US GAAP. We believe that removing the initial recognition threshold results in more decision-useful information.

**Question 3:** As a result of the proposed amendments, the net amortized cost on the balance sheet (that is, net of the allowance for expected credit losses) would reflect the present value of future cash flows expected to be collected, discounted at the effective interest rate. Do you agree that the net amortized cost (which reflects the present value of cash flows expected to be collected) results in more decision-useful information than currently exists under U.S. GAAP?

We believe that a net amortized cost that reflects the present value of future cash flows expected to be collected, as opposed to an incurred loss model, would result in more decision-useful information.

**Question 4:** The Board has twice considered credit loss models that would permit an entity not to recognize certain expected credit losses. In the January 2011 Supplementary Document, the Board considered a model that would permit an entity not to recognize some credit losses expected to occur beyond the foreseeable future. In the recent discussions on the three-bucket impairment model, the Board considered a model that would permit an entity only to recognize lifetime credit losses for loss events expected to occur within a 12-month horizon. Instead, the proposed amendments would require that at each reporting date an entity recognize an allowance for all expected credit losses. Do you believe that recognizing all expected credit losses provides more decision-useful information than recognizing only some of the expected credit losses? If not, how would you determine which expected credit losses should not be recognized (for example, 12 months or similar foreseeable future horizon, initial recognition threshold, and so forth)?

We believe that recognizing all expected credit losses provides more decision-useful information. Limiting the loss recognition to the first 12 months seems arbitrary and lacks theoretical basis. We also believe that including a threshold like that would increase subjectivity
of the numbers and potentially provide more income management opportunities than when there is no threshold.

**Question 5:** The proposed amendments would require that an estimate of expected credit losses be based on relevant information about past events, including historical loss experience with similar assets, current conditions, and reasonable and supportable forecasts that affect the expected collectability of the financial assets' remaining contractual cash flows. Do you believe that expected credit losses based on this information provide decision-useful information?

Refer to our answer to question 9.

**Question 8:** The proposed amendments would require that an entity place a financial asset on nonaccrual status when it is not probable that the entity will receive substantially all of the principal or substantially all of the interest. In such circumstances, the entity would be required to apply either the cost-recovery method or the cash-basis method, as described in paragraph 825-15-25-10. Do you believe that this approach provides decision-useful information?

We agree with the general approach above and believe that codifying the non-accrual policy followed by most entities as part of US GAAP will improve the existing financial reporting practice.

**Question 9:** The proposed amendments would require that an estimate of expected credit losses be based on relevant information about past events, including historical loss experience with similar assets, current conditions, and reasonable and supportable forecasts that affect the expected collectability of the financial assets' remaining contractual cash flows. Do you foresee any significant operability or auditing concerns or constraints in basing the estimate of expected credit losses on such information?

We agree with the Board that using relevant historical information in conjunction with information related to current economic conditions, and reasonable and supportable scenario analysis, is a good basis to estimate future losses.

**Question 10:** The Board expects that many entities initially will base their estimates on historical loss data for particular types of assets and then will update that historical data to reflect current conditions and reasonable and supportable forecasts of the future. Do entities currently have access to historical loss data and to data to update that historical information to reflect current conditions and reasonable and supportable forecasts of the future? If so, how would this data be utilized in implementing the proposed amendments? If not, is another form of data currently available that may allow the entity to achieve the objective of the proposed amendments until it has access to historical loss data or to specific data that reflects current conditions and reasonable and supportable forecasts?

**Question 11:** The proposed amendments would require that an estimate of expected credit losses always reflect both the possibility that a credit loss results and the possibility that no credit loss results. This proposal would prohibit an entity from estimating expected credit losses based solely on the most likely outcome (that is, the statistical mode). As described in the Implementation Guidance and Illustrations Section of Subtopic 825-15, the Board believes that many commonly used methods already implicitly satisfy this requirement. Do you foresee any significant operability or auditing concerns or constraints in having the estimate of expected credit losses always reflect both the possibility that a credit loss results and the possibility that no credit loss results?
Our answers to Questions 10 and 11:
We maintain historical loss data. We use this data, which is periodically updated, as a component in our ongoing assessment of the likelihood and risk of loss. Other factors taken into consideration are macro-economic factors, which in our considered judgment, may impact asset quality.

We suggest that the Board reconsider its decision to prohibit the use of the most likely outcome to assess expected credit losses. Our assessment of loan loss provisions is the product of a scenario analysis that tests a range of possible outcomes, with the expected credit loss based on the weighted average of the probable scenarios. However, we believe there could be situations where the likelihood of a scenario that results in no credit loss to the Bank, as the proposed amendment would require, could be remote compared to an alternative scenario that results in credit losses. In these cases, the use of the most likely scenario would result in better and more decision-useful information.

**Question 15:** The proposed amendments would require that an entity place a financial asset on nonaccrual status when it is not probable that the entity will receive substantially all of the principal or substantially all of the interest. In such circumstances, the entity would be required to apply either the cost-recovery method or the cash-basis method, as described in paragraph 825-15-25-10. Do you believe that this proposal will change current practice? Do you foresee any significant operability or auditing concerns with this proposed amendment?

We do not foresee this proposal to significantly change current practice.

**Question 17:** Do you believe the disclosure proposals in this proposed Update would provide decision-useful information? If not, what disclosures do you believe should (or should not) be required and why?

**Question 18:** Do you foresee any significant operability or auditing concerns or constraints in complying with the disclosure proposals in the proposed Update?

Our answers to Questions 17 and 18:
We believe the proposed roll forward disclosure requirements for certain debt instruments included in 825-15-50-(12-13) are too extensive and would not add much value to financial statements.

**Question 19:** Do you believe that the implementation guidance and illustrative examples included in this proposed Update are sufficient? If not, what additional guidance or examples are needed?

In general, we would like to see more illustrative examples with the detailed calculations behind the various treatments. In addition, we believe that some of the ideas and helpful clarifications included in the FAQ document published by the FASB staff on March 25, 2013 should be incorporated in the final standard.

**Question 20:** Do you agree with the transition provision in this proposed Update? If not, why?

We agree that a cumulative-effect adjustment to the statement of financial position is appropriate.
Question 23: Do you believe that the transition provision in this proposed Update is operable? If not, why?

We believe that the transition provision is operable.

Question 24: How much time would be needed to implement the proposed guidance? What type of system and process changes would be necessary to implement the proposed guidance?

We believe at least two years from the time the final standard is issued should be provided to implement the proposed guidance.