American Bankers Association
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Basel Committee on Banking Supervision
Bank for International Settlements

Via website submission: http://www.bis.org/bcbs/commentupload.htm

Re: Consultative Document: *Regulatory Treatment of Accounting Provisions – Interim Approach and Transitional Arrangements*

To Whom It May Concern:

The American Bankers Association (ABA[1]) appreciates the opportunity to comment on the Consultative Document *Regulatory Treatment of Accounting Provisions – Interim Approach and Transitional Arrangements* (CD). The CD recognizes that the implementation of Accounting Standards Update 2016-13 (the CECL Standard, which is effective in 2020, with early adoption available) in the U.S. and International Financial Reporting Standard No. 9 (IFRS 9, which is effective in 2018) for some other countries can have significant implications to bank capital. Higher and more volatile credit loss accounting provisions are anticipated, and the current differences in practice worldwide related to regulatory loss provisioning are seen to increase. As a result, the Basel Committee is considering various alternatives to the current loss provisioning framework for regulatory capital[2].

Due to the limited time until the effective date of IFRS 9, the CD proposes a transition process for regulatory capital purposes for both IFRS 9 and CECL. The CD would retain current regulatory treatment of credit loss provisions for regulatory capital purposes; however, it would effectively amortize the incremental increase resulting from the implementation of the new accounting standards into regulatory capital over a three to five year transitional period.

ABA supports the Committee's efforts to address the appropriateness of credit loss provisions through a regulatory transition period and a possible revision to the ongoing capital framework. This is a critical and challenging issue, as a final regulatory capital structure, in its attempt to efficiently ensure safety and soundness, should neither be so complicated that it will impede an individual bank's ability to serve its customers nor put certain banks at a competitive disadvantage.

[1] The American Bankers Association is the voice of the nation's $16 trillion banking industry, which is composed of small, regional and large banks that together employ more than 2 million people, safeguard $12 trillion in deposits and extend more than $8 trillion in loans..

[2] The alternatives are detailed in the Basel Committee Discussion Paper: *Regulatory Treatment of Accounting Provisions.*

A Transition Approach Should be Simple

ABA believes simplicity is critical for transitioning to these new accounting standards. Thus, we support Transition Approach #1, in which the monetary difference in CET1 capital at the effective date (calculated under current accounting and under the new standards) is spread over the proposed transition period. Transition Approach #2, which is based on a percentage difference (as opposed to monetary units), introduces unnecessary complexities for both banks and supervisors, as future loan growth and acquisitions would affect how the initial difference is eventually recognized into CET1 capital.

Transition Approach #3, which phases in recognition of IFRS 9 Stage 1 and 2 provisions, is solely targeted for non-U.S. preparers. As such, we believe this is an inappropriate solution to consider for U.S. banks, and we prefer a transition approach that is applied to both accounting models.

The "dynamic" nature of Approach #3, whereby Stage 1 and Stage 2 accounting provisions recorded both on and *after* the effective date are amortized into regulatory capital during the transition period, makes Approach #3 appealing outside the U.S. For U.S. application of Approach #3, we believe a practical expedient could be explored that assumes that all CECL accounting provisions for nonaccrual loans would qualify as Stage 1 and Stage 2 provisions under Approach #3, thereby allowing both IFRS 9 and CECL preparers to apply Approach #3. However, it is likely that significant current U.S. accounting provisions (those provisions recorded prior to CECL) already qualify as Stage 1 and 2 provisions under IFRS 9, which would distort the actual transitional difference in CET1 capital. Identifying the incremental CET1 impact of the new standard will be arduous for individual banks, especially if it is required on an ongoing basis.[3] Therefore, ABA believes the simplicity of Approach #1 is preferable and should be adopted.

A Significant Transition Timeframe is Necessary

ABA recommends that a timeframe of no less than five years be used for this transition. In addition to the increased allowances that are anticipated under the new standards, there are two important reasons for our proposed time period.

1. Banking institutions have no proven experience in forecasting long-term future macroeconomic conditions and then effectively quantifying the impacts on a life-of-loan basis. In fact, proficiency in such skills should not be expected to be attained for many years, if ever. As a result, volatility in expected credit loss estimates – both at the effective date and subsequent measurement dates – will cause any transition to be challenging.

[3] As noted during the November 15 outreach meeting conducted by the Basel Committee Task Force on Expected Loss Provisioning, certain provisions may decrease with the implementation of IFRS 9 and it is possible they could decrease under CECL. Of course, any decrease upon implementation should not be spread over the transition period.

2. Banks that have small portfolios will need greater transition time because those portfolios are naturally susceptible to short-term results beyond normal ranges of expected losses experienced in large portfolios. Since most loans will probably be adequately seasoned or resolved after 5 years, a similar transition period is appropriate.

Level Playing Field Issues Will Persist

ABA supports the Committee's intention to attain a level playing field among banks, large and small, located in various jurisdictions. The challenges of creating a level playing field are numerous and significant, both on a short-term and a long-term basis. Any efforts to attain the level playing field should, however, ultimately result in a long-term solution. We note that the Committee's discussion paper on the *Regulatory Treatment of Accounting Provisions* primarily addresses such long-term concerns.

As the Committee considers any specific transition approach (or approaches), it is generally known that CECL requirements for lifetime credit loss estimates will naturally result in higher accounting provisions that those in IFRS 9. Additionally, current practice differences with incurred credit loss models have resulted in significantly larger loss provisions in the U.S. that impact CET1 capital. Therefore, there is understandably much concern related to a level playing field.

While IFRS 9 becomes effective up to two years before CECL, the current uneven playing field may not be levelled during that interim period, as many in the U.S. believe that loss provisioning for banks implementing IFRS 9 will be lower than current (incurred loss) U.S. provisions. In fact, based on the then-current and forecasted economic states, it is possible to have larger increases in accounting provisions for U.S. banks during 2018 (the year of IFRS 9 implementation) compared to banks elsewhere.

Further, differences in general and specific provisioning practices for regulatory capital purposes further complicate level playing field issues. Although our preference might be to level the playing field sooner rather than later, it could complicate the transition process and may be an impractical goal. As a result, ABA recommends the Committee focus on transition and provide no further guidance in this CD to attempt to fill in any gaps during the transition period. Consistent application of the simplest transition approach should be the focus of the Committee.

Thank you for your attention to these matters and for considering our views. Please feel free to contact me (mgullette@aba.com; 202-663-4986) if you would like to discuss our views.

Sincerely,

Michael L. Gullette