Banc Ceannais na hÉireann
Central Bank of Ireland
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The Central Bank of Ireland Impairment Provisioning and Disclosure Guidelines

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1. Application of Guidelines

1.1. Introduction

This paper sets out the Central Bank of Ireland's ("the Central Bank") best practice guidelines regarding the policies, procedures and disclosures which the State supported Covered Institutions (hereinafter referred to as the "Covered Institutions")[1] should adopt for loans and receivables financial assets (and held to maturity financial assets where applicable) that are subject to impairment review in accordance with the requirements of International Accounting Standard 39 Financial Instruments: *Recognition and Measurement* ("IAS 39").

These guidelines should be read in conjunction with the existing Central Bank's regulatory document entitled "Impairment Provisions for Credit Exposures".

The paper has three principal objectives. Covered Institutions should:

1. Recognise their incurred loan losses as early as possible within the context of International Financial Reporting Standards ("IFRS");
2. Adopt a sufficiently conservative[2] and comparable approach to the measurement of impairment provisions across all loan portfolios; and
3. Significantly improve the number and granularity of their asset quality and credit risk management disclosures which will enhance users understanding of their asset quality profiles and credit risk management practices.

The Central Bank considers that the combination of a sufficiently conservative approach to impairment provisioning together with significantly enhanced disclosures on asset quality and credit risk will assist in the restoration of investor confidence in the Irish banking sector.

In 2011, the Central Bank identified the need to publish best practice guidelines to support Covered Institutions in the development and application of their impairment provisioning frameworks. The guidelines highlighted the need for the provisioning frameworks to be appropriate to the current economic circumstances with appropriately conservative impairment triggers being adopted requiring the earlier completion of impairment reviews and an appropriately conservative approach to the measurement of provisions across all loan portfolios.

As part of its supervisory engagement the Central Bank will be discussing the implementation of these guidelines with the Covered Institutions. In addition, it will be conducting work on the prudential implications of their provisioning approaches by assessing the specific parameters that they are applying against benchmarks that take account of peer practices and other information to ensure a cautious and conservative approach.

[1] The term "Covered Institutions" refers to the Covered Institutions that have received financial support under the Covered Institutions (Financial Support) Act 2008.

[2] Refer to IFRS Framework paragraph 37 which states that the inclusion of a degree of caution in the exercise of judgements is needed in making estimates required under conditions of uncertainty.

1.2. Review of Impairment Provisioning and Disclosure Guidelines

The Central Bank has performed a review of the level of compliance with the disclosure requirements in the financial statements of the Covered Institutions as at 31 December 2011 and 31 December 2012 respectively. As part of this review the Central Bank also considered how the 2011 Impairment Provisioning and Disclosure Guidelines (the Guidelines) document could be improved. As a result of this review the Central Bank has decided to make the following changes to the Guidelines:

(i) The Guidelines have been streamlined principally by removing duplication with the Central Bank's Impairment Provisions for Credit Exposures[3] which all credit institutions are required to comply with;

(ii) The insertion of a definition of a "Non-Performing Loan";

(iii) A new section has been added to clarify the concept of "Cured Loans";

(iv) A clarification has been included confirming that all disclosures are required to be included within the Covered Institutions financial statements notwithstanding whether this information is provided in other disclosures published by the Covered Institution; and

(v) Disclosures have been removed which the Central Bank's review concluded did not provide relevant information such as the requirement to disclose the loss on sale resulting from disposal of collateral and the related weighted average LTV as a sale price percentage.

1.3. Who needs to apply these guidelines?

This paper applies to all Covered Institutions. While this paper has the status of guidance, the Central Bank considers that the guidelines contained herein represent an appropriate basis, especially taking into account current economic conditions, for the development and application of impairment provisioning frameworks. As such, the Central Bank would be minded to interpret material deviations from this guidance as running counter to the detail and spirit of these guidelines. The Central Bank will, as a matter of course, scrutinise the Covered Institutions' application of these guidelines as part of our on-going supervision.

The Central Bank expects Covered Institutions to implement these guidelines (including the amendments resulting from the Review) in the 2013 annual reports.

The Central Bank deems these guidelines as best practice and would strongly encourage all credit institutions to implement these guidelines.

Consideration will also be given to the application of these guidelines to Credit Unions as part of the on-going work by the Registrar of Credit Unions to develop provisioning guidelines for the Credit Union sector.

[3] http://www.centralbank.ie/regulation/industry-sectors/credit-institutions/supervisory-disclosures/Documents/Regulatory%20Doc%20on%20Impairment%20Provisions%20for%20Credit%20Exposures.pdf

1.4. Impairment Provisioning – a conservative approach

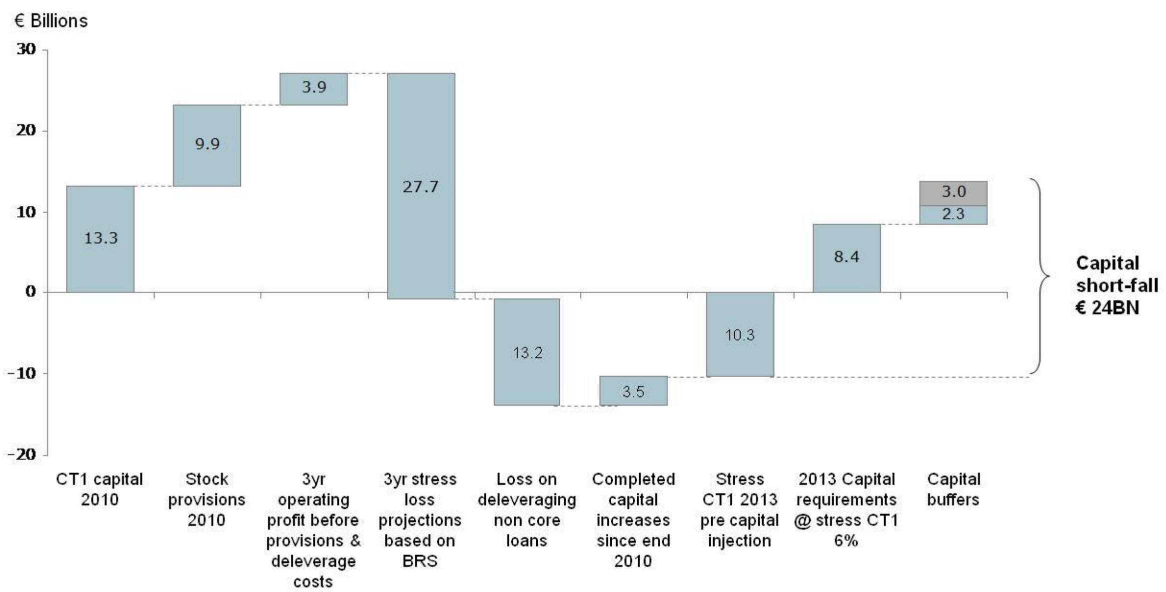
IAS 39 and in particular the incurred loss approach to impairment provisioning for financial assets, has been the subject of much discussion and some criticism. This has resulted in the International Accounting Standards Board ("IASB") accelerating its work programme to replace IAS 39 in its entirety.

The Central Bank recognises that the level of impairment provisions are lower under the incurred loss approach to impairment provisioning than those which would have been recognised under an expected loss approach. However, the Central Bank believes that the provision gap between the two approaches could have been narrower, and that provisions could have been recognised earlier and measured appropriately conservatively by some Covered Institutions had they:

- Adopted appropriately conservative impairment triggers to their loan portfolios;
- Used appropriately conservative estimates and assumptions relating to the condition and the evolution in property prices;
- Used appropriately conservative assumptions relating to the future domestic and international macroeconomic conditions; and
- Used appropriately conservative assumptions in calculating provisions on forborne loans.

This issue was brought into sharper focus when the Central Bank published "The Financial Measures Programme" dated 31 March 2011[4] ("FMP") which identified that expected losses in the Irish banking system greatly exceeded the stock of impairment provisions the Covered Institutions held at that time (Chart 1).

Chart 1: Process for calculating capital requirements (FMP)



[4] http://www.centralbank.ie/regulation/industry-sectors/credit-institutions/documents/the financial measures programme report.pdf

1.5. IFRS 9 Financial Instruments (Replacement of IAS 39)

IFRS 9 Financial Instruments ("IFRS 9") will eventually replace IAS 39 and work on its development is currently underway. IFRS 9 is being developed in three phases:

- Phase 1 Classification and measurement;
- Phase 2 Amortised cost and impairment of financial assets; and
- Phase 3 Hedge accounting.

At the time of writing Phases 1 and 2 are subject to revised proposals and have been re-exposed. Phase 3, hedge accounting, has been split into two projects, Hedge Accounting and Accounting for Macro Hedging. It is expected that Phases 1 and 2 will be re-deliberated by the end of 2013.

The mandatory effective date of IFRS 9 is anticipated as being 1 January 2015. The European Union has indicated that it will only consider endorsing IFRS 9 when all three phases are complete.

2. The Central Bank Review

To achieve the principal objectives of earlier recognition of incurred losses and improved transparency around asset quality and credit risk profiles the Central Bank has:

- Reviewed and analysed the Covered Institutions[5] impairment provisioning frameworks.
- Reviewed the Covered Institutions' impairment disclosures and benchmarked them against international best practice.
- Designed an enhanced template for disclosures in respect of the credit impairment disclosures, taking specific account of circumstances in the Irish market.
- Analysed the key management judgements, estimates and assumptions used by Covered Institutions in their impairment provisioning frameworks.
- Considered current issues such as forbearance measures, deteriorating loan-to-value ratios, weaker outlook for global growth, developments in the Basel Accord, CRD IV and IFRS.
- Undertaken a quantitative impact assessment study ("QIS") in respect of certain impairment provisioning inputs and parameters.
- Reviewed the impairment provision guidelines and publications issued by other regulators and standard setters.
- Engaged with various stakeholders including the Covered Institutions, their auditors, professional bodies and other regulatory authorities both in Ireland and across Europe.
- Performed a review of the level of compliance with the disclosure requirements in the financial statements of the Covered Institutions as at 31 December 2011 and 31 December 2012 respectively.
- The Central Bank has also reviewed the Guidelines for the purpose of identifying areas which required clarification.
- In revising the Guidelines the Central Bank has given regard to the definitions set out in the European Banking Authority's Consultation Paper on supervisory reporting on forbearance and non-performing exposures issued on 26 March 2013[6].

[5] Allied Irish Banks plc, The Governor and Company of the Bank of Ireland, permanent tsb plc.

[6] http://www.eba.europa.eu/Publications/Consultation-Papers/All-consultations/2013/EBA-CP-2013-06.aspx

3. Guidelines for Impairment Provisioning

Covered Institutions apply IAS 39 which requires the use of an incurred loss approach for the calculation of impairment provisions. The standard's core principle with respect to impairment is that impairment provisions are recognised only when losses are incurred and not before then.

The approach however, allows for subjective interpretation in a number of important areas, such as:

- Impairment triggers for each loan asset portfolio; and
- The inputs used in the specific, collective and incurred but not reported category ("IBNR") impairment provisioning calculations.

In order to recognise an impairment provision on a loan asset IAS 39 requires that:

- There must be one or more objective events ('impairment triggers') that have occurred; and
- The event is likely to have a negative impact on the estimated future cash flows of the loan asset.

The Central Bank expects that the following areas of Impairment Provisioning Frameworks are carefully considered by the boards of Covered Institutions:

1. **Core loan portfolios:**
    - Impairment triggers;
    - Characteristics of loan pools;
    - Forbearance measures;
    - Key management judgements, assumptions and estimates.

2. **Enhanced Asset Quality and Risk Disclosures**

An objective underpinning the FMP was to improve investor confidence in the Irish banking sector through enhanced asset quality and credit risk management disclosures.

The Central Bank has developed a comprehensive template of asset quality and credit risk management disclosures (Appendix 1) which has been tailored to reflect the circumstances of the Irish market and is consistent with the disclosure requirements of IFRS 7, other relevant IFRS standards and Pillar 3 of the Capital Requirements Directive ("CRD").

The Review highlighted that a number of disclosures, for various reasons, were not audited in the 2012 financial statements. The Central Bank expects that all of these disclosures will be disclosed in the financial statements and be audited.

3.1. Additional Senior Management responsibilities

Senior Management's responsibility for managing credit risk in the context of impairment provisioning includes, but is not limited to:

- Applying appropriate conservatism in the future cash flows and collateral value estimates used in impairment provision calculations. This should be supported by objective evidence, given current and expected future economic conditions at the reporting date;
- Applying appropriate conservatism to impairment assessments of forborne loans.
- Regularly reviewing and revising the key management judgements, assumptions and estimates used in the Institution's impairment provisioning;
- Appropriately disclosing key management judgements, estimates and assumptions;
- Disclosing a sensitivity analysis which considers factors such as changes to house price assumptions, GDP and unemployment rates;
- Providing the Central Bank with regular reports on the adequacy of impairment provisions and amounts written off.
- Estimate re-default rates for forborne and modified exposures and use to weight future contractual payments expected from clients as part of any impairment test.
- Deploy management information systems (MIS) that allow tagging, tracking and reporting of the following – breaches of threshold levels, internal grades, performing / non-performing status, age of arrears and LTV.

3.2. Identification of Triggers (all portfolios)

Under IAS 39 "Financial Instruments: Recognition and Measurement" an entity assesses at the end of each reporting period whether there is objective evidence that a loan or group of loans is impaired[7]. The standard states that a loan is impaired and impairment losses are incurred if there is "objective evidence" of impairment as a result of one or more events that occurred after the exposure was created ("the loss event") and that the loss event has an impact on the estimated future cash flows of the loans and these cash flows can be reliably estimated[8].

In reviewing the Covered Institutions' impairment provisioning frameworks (both in 2011 and 2012) and the 2012 disclosures the Central Bank observed that varying impairment triggers are being applied. Some Covered Institutions apply reasonably conservative triggers whilst others could apply conservative triggers much earlier to reflect the deterioration in the domestic and international economic environment.

[7] As required under IAS 39.58.

[8] Refer to IAS 39.59.

Review of impairment triggers

Covered Institutions should review and revise their existing impairment triggers for each loan asset portfolio to ensure that a trigger identifies a loss event as early as possible. This should result in the earliest possible recognition of losses within the IFRS framework.

If a Covered Institution has advanced multiple loans to a borrower, some of which are performing according to the contract, and others which are in default, all exposures to this borrower should be assessed for objective evidence of impairment.

Impairment triggers should be conservative and appropriate to each loan asset class.

A Covered Institution should assess all credit exposures for objective evidence of impairment based on current information and events at the date of the assessment. Such loss events should be considered on a portfolio by portfolio basis and objective evidence of such is not limited to:

Macroeconomic triggers

- National or local economic conditions that indicate a measureable decrease in estimated future cash flows of the loan asset class.
- An increase in the unemployment rate.
- A decrease in property prices for mortgages.
- An adverse change in industry conditions.

Mortgage portfolio triggers

- A loan asset meets the definition of a non-performing loan.
- A request for a forbearance measure from the borrower.
- Deterioration in the debt service capacity.
- A material decrease in rents received on a buy-to-let property.

Commercial Real Estate ("CRE") portfolio triggers

- A loan asset meets the definition of a non-performing loan.
- A request for a forbearance measure from the borrower.
- A material decrease in the property value.
- A material decrease in estimated future cash flows.
- The lack of an active market for the assets concerned.
- The absence of a market for refinancing options.
- A significant decline in the Institution's credit rating of the borrower.

Small Medium Enterprises (“SME”) portfolio triggers

- A loan asset meets the definition of a non-performing loan.
- A request for a forbearance measure from the borrower.
- Trading losses.
- Diversion of cash flows from earning assets to support non-earning assets.
- A material decrease in turnover or the loss of a major customer.
- A default or breach of contract.
- A significant decline in the Institution’s credit rating of the borrower.

In addition the following factors should be taken into consideration when assessing whether a loss event has occurred:

- Debt service capacity;
- Financial performance;
- Net worth and future prospects;
- The prospects for support from any financially responsible guarantors;
- The nature and degree of protection provided by the current and stabilised cash flow and value of any underlying collateral; and
- Country risk.

Disclosure of impairment triggers

Covered Institutions should disclose their impairment triggers for each loan asset portfolio and not simply disclose generic triggers extracted from accounting standards. For all loan asset portfolios, the Central Bank believes that, where applicable, when a loan is classified as non-performing this is indicative of an impairment trigger having occurred and the exposure should be assessed for impairment.

Supporting documentation

If there is objective evidence of impairment, the Covered Institution should document the type of objective evidence existing. If no objective evidence of impairment exists, the Covered Institution should document the steps taken in arriving at this conclusion.

3.3. Individually significant and non-significant exposures

Exposures should be assessed for objective evidence, measurement, and recognition of impairment on an individual basis for individually significant exposures. Where a Covered Institution has a number of individually significant exposures to one counterparty each loan should be individually assessed while also considering the overall position of the counterparty.

Exposures that are not individually significant may be assessed for impairment either on an individual or a group basis.

An impairment assessment should be performed for exposures for which there is objective evidence of impairment as follows:

- Individually significant exposures; and
- Exposures that are not individually significant.

If a Covered Institution determines that no objective evidence of impairment exists for an individually assessed exposure, whether significant or not, it includes this in a group of exposures with similar credit risk characteristics that are collectively assessed for impairment[9].

A collective assessment should be performed for exposures as follows:

- Exposures that have been individually assessed and were found not to be impaired on an individual basis; and
- Exposures that have not been individually assessed.

Portfolio impairment provisions are recognised for incurred losses not specifically identified but which experience in addition to observable data indicates losses are present in the portfolio of exposures at the date of collective assessment, i.e. incurred but not reported.

Supporting documentation

Covered Institutions should maintain supporting documentation on each individual exposure or group of exposures, including:

- Documentation of the rationale for determining whether an exposure should be assessed individually or collectively for impairment.
- Documentation of the rationale for determining appropriate groupings of exposures, including observable data supporting the conclusion that the exposures in each grouping have similar attributes or characteristics. This data must be assessed periodically as circumstances change or as new data that is more relevant and more directly representative of loss become available.
- Any adjustments to the impairment provisions for these factors should be supported by documentation that clearly demonstrates the estimated impact of changes in the factors on the historical loss experience.

[9] Refer to IAS 39.64

3.4. Individually assessed loans

The estimated recoverable amount and thus the amount of the provision required should be calculated using three different methods:

- The estimated recoverable amount is equal to the present value of the estimated future cash flows[10], discounted at the exposure's original effective interest rate;
- The estimated recoverable amount may be measured on the basis of an exposures fair value using an observable market price (e.g. on secondary markets); and
- The estimation of the recoverable amount of a collateralised exposure reflects the cash flows that may result from foreclosure where foreclosure is considered the likely course of action. The time, costs and difficulties involved in obtaining repayment through collateral or guarantees should be taken into account when determining the recoverable amount.

When conducting a specific assessment for impairment the Central Bank expects an appropriately conservative approach to the estimation of both the future cash flows and the collateral valuations. The estimates and assumptions should reflect the current economic challenges and the current view of the expected economic outlook. When determining the collateral valuations in the cash flow calculation, an appropriately conservative approach should be applied to both the expected timing and the amount of the proceeds. Where foreclosure proceedings have been initiated and the expected time to security realisation is prolonged and or delayed, the Central Bank expects that valuation of the underlying security should be reviewed on a regular basis.

Given that the valuation of collateral is a key consideration in determining impairment provisions the Central Bank expects that Credit Institutions will comply with the guidance and recommendations regarding collateral valuation contained in its 2012 publication "Valuation Processes in the Banking Crisis – Lessons Learned – Guiding the Future".

The Central Bank expects Covered Institutions to hold a recent independent valuation on collateral underlying residential mortgage loans, where the loan balance outstanding is in excess of €750,000. This threshold shall be reduced to €500,000 in 2014 and thereafter.

[10] Changes in the amount and timing of estimated cash flows may have a significant impact on the overall impairment provision and consequently the assumptions applied by the Credit Institution with respect to the timing of the cash flows must be based on reasonable supportable objective evidence.

3.5. Collectively assessed loans

3.5.1. Provisioning Methodology

The future cash flows of a group of exposures that are collectively evaluated for impairment are calculated on the basis of the estimated contractual cash flows the exposures in the group and historical loss experience for exposures with credit risk characteristics similar to those in the group.

Factors to take into consideration when determining the historical loss experience are:

- Analysis of impairment;
- Ageing of balances;
- Past loss experience;
- Forbearance measures applied;
- Current economic conditions; and
- Other relevant circumstances.

Covered Institutions that do not have the necessary historical loss experience for evaluating impairment shall use peer group experience[11] (for example, sourced from peer group information published by rating agencies) for a portfolio that is representative of the Covered Institution's own portfolio.

Historical loss experience should be adjusted to reflect the effects of current economic conditions that did not affect the period that the historical loss experience covers, and historical conditions that do not currently exist. Current factors to be considered that are likely to cause losses associated with the Covered Institution's portfolio to differ from historical experience, include, but are not limited to:

- Changes in lending policies and procedures, including underwriting standards and collection, the extension of forbearance measures, write-offs, and recovery practices;
- Changes in international, national and local economic and business conditions and developments, including the condition of various market segments;
- Changes in the trend, volume and severity of past due and adversely classified exposures, as well as trends in the volume of impaired exposures and restructurings;
- The existence and effect of any concentrations of credit, and changes in the level of such concentrations;
- The effect of external factors such as competition, legal and regulatory requirements on the level of estimated credit losses in the Covered Institution's current portfolio; and
- Changes in the risk profile of the portfolio as a whole.

[11] Refer to IAS39.AG89.

The Central Bank believes it is also necessary to ensure that other estimates and inputs included in collective impairment provisioning reflect an appropriate level of conservatism. For example:

- Conservative peak to trough house price assumptions should be used in relation to mortgage portfolios;
- Costs and timeframe involved in realising collateral;
- The Probability of Default ("PDs"), Loss Given Default ("LGD"), Cure Rates and Re-default rates should also be reflective of the credit characteristics of each appropriately stratified loan pool.

When senior management adjusts impairment provisions for these factors, there should be documentation that clearly demonstrates the estimated impact of changes in the factors on the historical loss experience.

The methodology and assumptions used for estimating cash flows should be reviewed regularly to reduce any differences between loss estimates and actual loss experience.

Exposures should be grouped on the basis of similar credit risk characteristics that are indicative of the counterparty's ability to repay according to the contractual terms. If a Covered Institution does not have a group of assets with similar risk characteristics, this assessment is not performed.

The following characteristics should be taken into consideration when grouping exposures:

- Asset type;
- Industry;
- Geographical location;
- Collateral type;
- Past-due status (age of arrears);
- Forbearance measures applied;
- LTV ratios,
- Employment status,
- Changes in net equity of collateral owned by the customer; and
- Other Relevant Factors.

The Central Bank expects that different Covered Institutions will apply different purpose-built models to calculate their collective impairment provisions. The Central Bank requires Covered Institutions to apply conservative and supportable assumptions within these models in line with the requirements set out in these guidelines.

The Central Bank considers that ageing of arrears and the number of repayments in arrears are key indicators of asset quality and are fundamental inputs into impairment provisioning frameworks. Accordingly, it is important that systems are capable of accurately capturing such data.

Back-testing

Covered Institutions should maintain supporting documentation, which shall be made available for review by the Central Bank, that:

- Sets out the inputs, calculations and outputs in support of each of the categories of assumptions made in relation to each cohort of loans;
- Sets out the rationale applied for determining these assumptions;
- Sets out the results of testing of these assumptions against actual loss experience; and
- Documents the policies and procedures which set out how the Covered Institutions set, monitor and assess these assumptions.

3.5.2. Performing Loans

Loans which are performing fall into the following categories:

Fully performing
Loans are not past due and do not present a risk of not being paid back in full without collateral realisation.

Performing in arrears

- Loans are between 1 – 30 days past due.
- Loans are between 31 – 60 days past due.
- Loans are between 61 – 90 days past due.

Such loans do not present a risk of not being paid back in full without collateral realisation.

For all exposures classified as performing a provision is estimated based on the probability of loans moving from the performing pool into the non-performing pool over a defined length of time (“emergence period”). This provision is referred to as the “IBNR”. The emergence period is critical to this calculation as it determines on a forward looking basis approximately how long it takes for non-performance to be identified and as such the longer the emergence period applied the higher the IBNR provision.

The emergence period should be linked to the definition of non-performing, and consideration must be given to ensure that sufficient time has been allowed for such non-performance to emerge. Covered institutions should document and evidence the rationale for the emergence period applied to each portfolio.

The Central Bank expects that when assessing IBNR in respect of fully performing loan portfolios that the Covered Institution applies a suitably conservative emergence period. The emergence period may differ by credit facility type and will be influenced by the frequency of the credit review cycle.

The Central Bank requires Covered Institutions to disclose the emergence period they apply in determining the IBNR and the rationale for using this emergence period.

Although classified as performing, the probability of a loan which is in arrears less than 90 days becoming impaired is higher than that of a fully performing loan. The Central Bank expects that Covered Institutions will assess these loans for impairment provisions using a conservative emergence period, higher PD, higher LGD and lower cure rates as arrears days worsen.

The Central Bank expects that all key assumptions will be back tested on a regular basis to ensure that they are appropriate and requires Covered Institutions to specify from which grade of their internal credit rating a borrower will be considered as non–performing.

3.5.3. Non-performing Loans

For the purposes of applying these guidelines non-performing loans (“NPL”) are defined as follows:

Non-performing loans are defined as:

(a) Loans more than 90 days past due.

(b) Loans which present a risk of not being paid back in full without collateral realisation, regardless of the existence of any past-due amount or the number of days past due.

The Central Bank considers that a loan which meets the definition of a NPL is considered to have met the requirements set out in IAS39.59 for there to be objective evidence of a loss event having occurred. Accordingly, such exposures should be reviewed for impairment on a specific or collective basis as appropriate.

The Central Bank expects that in respect of non-performing loans assumptions regarding collateral values, LTV ratios, workout periods and associated costs should be set conservatively, reviewed on a regular basis and adjusted to address any data limitations noted. Likewise cure rates are expected to be set lower as compared to cured loans. The Central Bank expects that all key assumptions will be back tested on a regular basis to ensure that they are appropriate.

The Central Bank expects that provisions are made with reference to the value of the underlying collateral in all cases.

3.5.4. Cured Loans

Loans may be considered to have ceased being non-performing when, simultaneously, the situation of the debtor has improved to the extent that full repayment, according to the original or when applicable the modified conditions, is likely to be made and the debtor does not have any amount past-due.

Cured loans represent loans that exited the non-performing category including forborne loans (see Section 3.5.6). The Central Bank believes that in respect of cured loans the PD will be significantly higher and cure rates significantly lower than for performing loans as these borrowers are more likely to re-default than loans which have never been classified as non-performing.

For the purposes of clarification, a modified loan with arrears capitalised may cure when full modified repayments (capital plus interest) are likely to be made and where the debtor does not have any amount past-due.

Inclusion in the cured loans category is only allowable if the loan is considered as performing which requires both that:

- The lender has made an analysis of the financial condition of the debtor to ensure it will be repaid (it becomes clear that the debtor can and will comply with the contract) and this analysis has been approved by the management of the lender; and
- The debtor has met repayments regularly which means: (i) it has paid more than an insignificant amount of principal and interest of the contract, including when applicable an amount equal to all amounts past-due before any forbearance measures were extended or all amounts that were written off by any forbearance measures; and (ii) a probation period has passed.
- The probation period shall end at one year since the date in which the first payment of principal is due in the debt contract with the latest forbearance measures without the debtor having any exposure classified as non-performing or totally or partially past due more than 30 days.

If the borrower exceeds 30 days past due on any of its exposures with the lender, or if any of its exposures is considered as non-performing, the probation period shall restart for the entire probation period time at the date the amount past-due is repaid or the exposures cease to be considered as non-performing. This criteria should be used to calculate re-default rates which are set conservatively and are evidence based.

The Central Bank would not expect an impairment provision reversal until there is demonstrable evidence that the forborne loans have the above characteristics and therefore the PD can be reduced.

The Central Bank requires Covered Institutions to disclose their rationale for applying the cure rates selected.

Cure rates must be evidence based and not skewed by forbearance measures which do not address the arrears position or are unsustainable forbearance measures which do not address the underlying repayment capacity issues. Until such a time in which the loan in forbearance returns to normal service status, or has passed the probation period after being modified, it should not be considered in computing cure rates. Similarly loans which have been granted interest only forbearance measures cannot be treated as cured and should not be included in computing cure rates.

Supporting documentation

Covered Institutions should maintain supporting documentation, which shall be made available for review by the Central Bank, which:

- Sets out the inputs, calculations and outputs in support of the cure rates applied in relation to each cohort of loans;
- Sets out the rationale applied for determining cure rates; and
- Documents the policies and procedures which set out how the Covered Institutions identify, monitor and assess whether non-performing loans have cured in accordance with the definition and guidance set out above.

3.5.5. Foreclosed Loans

Loans for which there is no likelihood of repayment resulting in the decision to foreclose.

For loans where the Covered Institution has taken the decision to foreclose cure rates should be set at 0. When determining the collateral valuations in the cash flow calculation, a conservative approach should be applied to both the expected timing and the amount of the proceeds.

Where foreclosure proceedings have been initiated and the expected time to security realisation is prolonged and/or delayed, the Central Bank expects that valuation of the underlying security should be reviewed on a regular basis.

3.5.6. Forbearance Measures

In the context of the challenging domestic and international economic climate, an increasing number of mortgages, personal and business borrowers are experiencing financial stress. In order to assist borrowers who are experiencing financial stress, Covered Institutions are applying forbearance measures, which if designed appropriately, can benefit both the Covered Institution and the borrower, as they may improve the ability of the borrower to repay their loans and therefore increase the probability of the Covered Institutions recovering the value of the loan asset.

Forbearance measures occur when a Credit Institution, for reasons relating to the actual or apparent financial stress of a borrower, grants a concession whether temporarily or permanently to that borrower. A concession may involve restructuring the contractual terms of a debt or payment in some form other than cash, such as an equity interest in the borrower. If the decision to make a concession is not related to the actual or apparent financial distress of the borrower, forbearance has not occurred.

During 2012 Covered Institutions developed strategies for the treatment of borrowers on a case-by-case basis, ranging from temporary forbearance, to longer-term modifications, and solutions involving change of ownership.

A policy of extending forbearance measures to borrowers experiencing financial stress has implications for the Covered Institutions' credit management practices and their associated impairment provision frameworks.

The Central Bank considers that the request for a forbearance measure from a borrower is an impairment trigger. Accordingly, such exposures should be reviewed for impairment on a specific or collective basis as appropriate.

The Central Bank considers that forbearance measures are reflective of the increasing underlying credit risk profiles of loan portfolios which therefore have a higher risk of default. Accordingly, these measures will have a negative impact on a Covered Institution's future level of impairments.

It is possible that over time, once sustainable solutions have been put in place, loans which are subject to forbearance measures will meet the definition of a cured loan as set out above. Whilst many borrowers will perform in accordance with the forbearance measures agreed, others may find that the concessions provided are insufficient to withstand the financial stress with which they are faced and default may ultimately still occur on the exposure. Hence, the Central Bank believes that there is a higher inherent risk attaching to forborne exposures in both the performing and non-performing loan portfolios.

The Central Bank believes that in respect of the forborne loan pools the PD will increase (as forborne borrowers are more likely to re-default/default), with a lower cure rate, in both performing loan and non-performing loan portfolios. As a result the Central Bank believes that performing forborne loan pools should be segregated by type of forbearance measure granted and the PDs should be reflective of the credit characteristics of each appropriately stratified loan pools.

Where a performing loan has been granted on an interest only forbearance measure the Central Bank expects it should have a highly conservative associated probability of moving to non-performing.

Renewal, refinancing, re-negotiation, restructuring or novation of a credit facility do not interrupt the aging of arrears unless the client pays all interest due by his own means without new financing provided by the bank for such purposes, directly or indirectly. The non-payment of interest as a result of the terms of modification of loans, including refinancing and renegotiation, is considered to be an indication of incurred loss having occurred. All loans thus modified shall therefore be subject to an impairment test on renewal.

Covered Institutions will need to develop MIS that have the capacity to monitor a borrower's performance on a forbearance measure. The MIS will also need to have the capability to track which forbearance measure was applied to each borrower and facilitate back-testing the key assumptions on a regular basis. Should there be an absence of data, given the untested nature of some forbearance measures, Covered Institutions should adopt appropriately conservative assumptions in calibrating the PDs.

Loan assets subject to forbearance measures should be separated into different pools in order to be able to comment on the sustainability of the forbearance measures over time.

If the exposure is below the threshold for specific assessment for impairment, forborne exposures should be collectively assessed for impairment provisioning.

IAS 39 requires that when collective assessment is used financial assets should be grouped on the basis of similar credit characteristics which indicate the borrower's ability to pay in accordance with the contractually agreed terms.

Cognisant of this requirement and the impact which forbearance measures may have on impairment provisioning, the Central Bank believes that:

- Loan pools which are subject to forbearance measures should be separated from the remaining non-forborne loan pools;
- Non-forborne loan pools may need to be further stratified. Such stratification should further sub-divide the pools where the loans exhibit similar risk characteristics.

When calculating the collective impairment provisions, particularly for mortgage portfolios, certain model inputs which are based on historic data may require management judgement to be applied to adjust historic data to reflect current economic circumstances and the granting of forbearance measures. For example, where a borrower is up to date with their revised terms, having previously received forbearance measures, the historic rate of transition to default may appear lower than the underlying risk profile of the loan pool.

3.5.7. Renegotiated Loans

The borrower is not in financial difficulty however terms of the loans have been renegotiated

As discussed above, forbearance only applies in relation to concessions made in relation to actual or apparent financial distress on the part of the borrower. From time to time the terms of a loan may be renegotiated to facilitate the on-going performance of that loan.

Renegotiated loans should be reviewed for impairment on an individual basis at the time that the loan is being renegotiated. Should the loan be found not to be impaired on an individual basis at that time it should be assessed collectively within a pool of loans with similar credit characteristics.

Renewal, refinancing, re-negotiation, restructuring or novation of a credit facility do not interrupt the aging of arrears unless the client pays all interest due by his own means without new financing provided by the bank for such purposes, directly or indirectly. The non-payment of interest as a result of the terms of modification of loans, including refinancing and renegotiation, is considered to be an indication of incurred loss having occurred. All loans thus modified shall therefore be subject to an impairment test on renewal.

3.6. Key management judgements, assumptions and estimates

The Central Bank recognises that impairment provisions are estimates which are determined based on informed management judgements as to what is an incurred loss based on the facts and circumstances pertaining at a point in time.

The Central Bank recognises that there will always be a range of possible outcomes for impairment provision estimates and that management can only make their judgements based on the facts and circumstances pertaining at a point in time and their assumptions relating to the future which maybe by either a pessimistic, neutral or an optimistic view.

It is acknowledged that it is inevitable in some cases, future events and developments may result in a different outcome in relation to estimates which is either positive or negative.

The Central Bank requires Covered Institutions to regularly review and revise their key judgements, assumptions and estimates relating to their impairment provisioning and these should be:

- Reflective of the current domestic and international macroeconomic environment and currently predicted future macroeconomic outlook;
- More conservative than those included in the historical impairment provisioning; and
- Disclosed in the annual report to allow users see in a more transparent way the impact that such key judgements, estimates and assumptions have on the impairment provisions.

The disclosure should include the key inputs and parameters used in the Covered Institutions mortgage impairment provisioning models and an explanation of significant changes in the inputs used from the prior year.

The Covered Institutions should disclose a sensitivity analysis of the impact of changes to the key assumptions and estimates on the impairment provisions.

Key facts and circumstances which impact impairment provisions include:

- Arrears data;
- Current economic data;

- Collateral asset values and LTV ratios;
- Historic cure rates;
- Interest rates;
- Historic emergence periods;
- Forbearance measures extended; and
- Workout costs and timelines.

Key assumptions relating to future events which impact impairment provisions include:

- Future economic activity and employment rates;
- Projected asset values over the work out period;
- Discounts on the disposal of repossessed assets;
- Gross Domestic Product (“GDP”);
- Unemployment rates;
- Institution specific asset foreclosure and disposal policies; and
- Future emergence periods.

The Central Bank requires that Covered Institutions document all key assumptions including explanations outlining why assumptions have been changed.

4. Disclosures

4.1. General disclosure requirements

IFRS 7 requires an entity to provide disclosures in their annual reports that help users evaluate the nature and extent of the risks arising from the financial instruments to which an entity is exposed and how they manage these risks.

Additionally, Covered Institutions are required to adhere to the CRD Pillar 3 disclosure requirements which requires disclosures to assist users assess key information about a Covered Institution's risk profile, capital structure and the level of capital held.

The European Banking Authority noted in its September 2011 update in relation to the Pillar 3 disclosures that "further efforts are necessary regarding the interrelationship between IFRS and Pillar 3 disclosures with a view to enable users to gain a better understanding of the overall profile of the bank as provided by both accounting and prudential information".

The Central Bank expects that over time, the financial disclosures will be further enhanced to reflect the changing nature of the risks faced by Credit Institutions and future IFRS developments.

Whilst it is not intended that the Covered Institutions' disclosures should follow the disclosure template's format, the Covered Institutions are expected to provide the granularity of these disclosures within their annual reports.

The Central Bank requires Covered Institutions to provide the following asset quality and credit risk management disclosures in their financial statements to enhance users' understanding of Covered Institutions' loan portfolios asset quality profile and credit risk management practices:

Quantitative disclosures:

- Loan origination profiles of the residential mortgage loan portfolios.
- Loan-to-value ratios segregated between private dwelling house (PDH) and buy-to- let in the mortgage loan portfolios.
- Quantitative disclosures of forbearance measures for residential mortgage loan portfolios.
- Impairment charges by individual and collective, by industry or geography.
- The impairment allowance segregated by the same groupings.
- The valuation of underlying collateral for residential mortgages loan portfolios.
- Loans and advances by asset quality.
- Internal grading profile.
- Ageing profile of the past due loans.
- Repossessed collateral.
- Disclosure of PDs, LGDs, cure rates and re-default rates by relevant segment, internal

grade and performing / cured / forborne / non-performing status.

- Interest income recognised arising from impaired, non-performing but not impaired and forborne loans.
- Interest income received arising from impaired, non-performing but not impaired and forborne loans

Qualitative disclosures:

- Triggers for impairment testing across all portfolios.
- The nature of key management judgements, estimates and assumptions used in the determination of impairment.
- The detailed methodologies for calculating impairment charges, including how the loan portfolios are stratified to reflect the differing credit characteristics.
- Disclosure of how the credit risks are managed should be included in the risk management section.
- Policy for write off of loans.
- Policy for reversal of loan portfolio impairments.
- Forbearance measures employed.
- Policy for debt to equity exchange (if applicable).
- The impairment charge sensitivities of changes to key assumptions.
- A detailed description of the cost of credit risk including disclosures of PDs, Exposure at Default ("EAD") and LGDs, cure rates.
- Description of the calculation of the present value of future cash flows when impairment is measured.
- Description of the emergence period used and why it is deemed appropriate.
- Policy detailing the indicative thresholds for deterioration to be taken into account when assessing whether a loss event has occurred.
- Policy specifying the internal credit grade from which a borrower is deemed to reach the non-performing status.

4.2. Specific disclosure relating to forbearance measures

IFRS 7 requires Covered Institutions to disclose information pertaining to the credit quality of their financial assets including assets that are neither past due nor impaired. Should the quantitative disclosures be unrepresentative of a Covered Institution's risk exposures, the Institution is required to provide additional information which is representative.

The Central Bank considers that the extent and nature of forbearance measures within the Irish banking sector is reflective of the increasing credit risk profiles of the loan portfolios and consistent with the objective of improving the transparency of a Covered Institution's underlying risks, the Central Bank therefore requires that there should be appropriate disclosures of forbearance measures which will assist users to better understand the Covered Institution's risks and the associated negative impact on the Institution's impairment provisioning.

The Central Bank expects all Covered Institutions to comply with the European Securities and Markets Authority's statement[12] on Forbearance issued on 20 December 2012.

The table below (taken from the appendix) is an example of one of the residential forbearance disclosures which will enhance transparency by disclosing the residential volume of loans to which forbearance measures have been applied.

31 December 20xx	**All Loans**		**Loans > 90 days in arrears and/or impaired**	
	Number	**Balance € million**	**Number**	**Balance € million**
Interest only				
Reduced payment (less than interest only)				
Reduced payment (greater than interest only)				
Payment moratorium				
Arrears capitalisation				
Term extension				
Hybrid (term extension and interest only)				
Other				
Total				

12 http://www.esma.europa.eu/news/ESMA-issues-statement-forbearance-practices

5. Future developments

In the recently released Mortgage Arrears Resolutions Targets document (March 2013)[13] the Central Bank sets out a provisioning approach which the Central Bank is minded to apply to Covered Institutions for years beginning on or after 2014.

The Central Bank is continuously collecting evidence on the overall performance of loan books. The work undertaken by the Central Bank, which will be provided to specific Covered Institutions and will provide sufficient experience to determine the relevant expected cash flows and the collateral value for loans that share similar credit risk characteristics. The Central Bank would expect that the specific Covered Institutions would use this experience in order that it can calculate the appropriate (collective) impairment charge for loans that are currently non-performing (as defined).

[13] http://www.centralbank.ie/press-area/press-releases/documents/approach%20to%20mortage%20arrears%20resolution%20-.pdf

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Appendices

Appendix 1 – Summarised Guidelines

<table>
<tr><th></th><th>Performing</th><th>Cured Loans</th><th>Non-Performing</th><th>Foreclosed</th></tr>
<tr><td>Risk</td><td colspan="4">Lower Higher</td></tr>
<tr><td rowspan="3">Definitions</td><td>Fully performing
Loans are not past due and do not present a risk of not being paid back in full without collateral realisation.</td><td rowspan="2">Loans may be considered to have ceased being non-performing when, simultaneously, the situation of the debtor has improved to the extent that full repayment, according to the original or when applicable the modified conditions, is likely to be made and the debtor does not have any amount past-due.</td><td rowspan="2">Loans more than 90 days past due.

Loans present a risk of not being paid back in full without collateral realisation, regardless of the existence of any past-due amount or the number of days past due.

Loans which have defaulted resulting in the decision to foreclose.</td><td rowspan="2">Loans for which there is no likelihood of repayment resulting in the decision to foreclose.</td></tr>
<tr><td>Performing in arrears
Loans are between 1 – 30 days past due.
Loans are between 31 – 60 days past due.
Loans are between 61 – 90 days past due.
Loans do not present a risk of not being paid back in full without collateral realisation.</td></tr>
<tr><td>Renegotiated loans
Borrower is not in financial difficulty however terms of the loans have been renegotiated</td><td colspan="3">Forbearance
Forbearance measures occur when a Covered Institution, for reasons relating to the actual or apparent financial stress of a borrower, grants a concession whether temporarily or permanently to that borrower. A concession may involve restructuring the contractual terms of a debt or payment in some form other than cash, such as an equity interest in the borrower. If the decision to make a concession is not related to the actual or apparent financial distress of the borrower, forbearance has not occurred.

Depending on the nature of the forbearance measure and whether it is sustainable the loan may fall into any of the categories listed above.</td></tr>
</table>

<table>
<tr><th></th><th>Performing</th><th>Cured Loans</th><th>Non-Performing</th><th>Foreclosed</th></tr>
<tr><td><u>Risk</u></td><td colspan="4">Lower → Higher</td></tr>
<tr><td rowspan="2"><u>Treatment</u></td><td><u>Fully performing</u>
Assess for IBNR using conservative emergence period.

<u>Performing in arrears</u>
Assess for provision using conservative emergence period, higher PD, higher LGD and lower cure rates as arrears days worsen.</td><td>The PD will be significantly higher and cure rates lower than for Performing in Arrears Loans as these borrowers are more likely to re-default than loans which have never been classified as non-performing.

Covered Institutions must demonstrate that the loans have continued to perform for a sufficient period of time prior to being considered as cured.</td><td>PD should be set at 1. Likewise, cure rates should be set conservatively lower than for cured loans.

When determining the collateral valuations in the calculation, an appropriately conservative approach should be applied to both the expected timing and the amount of the proceeds.</td><td>Cure rate should be set at 0.

When determining the collateral valuations in the calculation, an appropriately conservative approach should be applied to both the expected timing and the amount of the proceeds.

Where foreclosure proceedings have been initiated and the expected time to security realisation is prolonged and or delayed, the Central Bank expects that the valuation of the underlying security should be reviewed on a regular basis.</td></tr>
<tr><td><u>Renegotiated loans</u>
Review for impairment on an individual basis at the time that the loan has been renegotiated. Should the loan be found not to be impaired on an individual basis at that time it should be assessed collectively within a pool of loans with similar credit characteristics.</td><td colspan="3"><u>Forbearance</u>
A request for a forbearance measure from a borrower is an impairment trigger. Accordingly, such exposures should be reviewed for impairment on a specific or collective basis as appropriate.

The PD will increase and cure rates will fall in both performing loan and non-performing loan portfolios.</td></tr>
</table>

Appendix 2 – Illustrative Disclosure Template

To be applied by the Covered Institutions in their annual reports.

The template attached here is a representative template. The Central Bank recognises that individual Credit Institutions may prefer to present the disclosures in their own format. We also recognise that the Credit Institutions may tailor this template to relate to the specific portfolios held by them. The Credit Institutions, where possible, should provide comparative information. Any unaudited information should be disclosed as such by the Credit Institutions.

Disclosures	Additional	Enhanced[14]
Accounting policy for forbearance measures	✓	
Impairment charge sensitivity to critical accounting estimates	✓	
Impairment allowance split by product	✓	
Quantitative disclosures on forbearance measures (ROI only)	✓	
LTV ratios of mortgage lending	✓	
Loan origination profiles of residential mortgage loan portfolio	✓	
Accounting policy for debt for equity exchange	✓	
Detailed disclosures on Institution's non-core portfolios	✓	
Impairment charge (split by individual and collective)	✓	
Impairment charge (split by PDH and Buy-to-Let)		✓
Triggers for impairment testing across all portfolios		✓
Detailed methodologies for calculating impairment charges		✓
Disclosure of the internal grading profile		✓
Disclosure of how credit risk is managed		✓
Policy for write-off of loans		✓
Policy for reversal of loan portfolio impairments		✓
The nature of key management judgements, estimates and assumptions used in the determination of impairment		✓
Disclosure of cost of credit risk including disclosure of PDs, EADs and LGDs		✓
Disclosure of the cost of calculation of the present value of future cash flows when impairment is measured		✓
Repossessed Collateral		✓

[14] To the disclosures requirements in IFRS.

INCOME STATEMENT (extract)

For the year ended 31 December 20x2

	Note	20x2 € million	20x1 € million
Impairment losses on financial investments	2		

BALANCE SHEET (extract)

For the year ended 31 December 20x2

	Note	20x2 € million	20x1 € million
Loans and receivables			
Loans and advances to customers	3		

NOTES TO THE FINANCIAL STATEMENTS (extract)

1. Accounting policies *(extract)*

a. Impairment of loans and advances

A financial asset is considered to be impaired, and therefore its carrying amount is adjusted to reflect the effect of impairment, when there is objective evidence that events have occurred which give rise to an adverse impact on the cash flows that were estimated at the transaction date. Impairment provisions are calculated on individual loans and on groups of loans assessed collectively. Impairment losses are recorded as charges to the income statement. The carrying amount of impaired loans on the balance sheet is reduced through the use of impairment provision accounts. Losses expected from future events are not recognised.

Interest accrual is suspended when a loan is impaired. Collections relating to impaired loans and advances are used to recognise the accrued interest and the remainder, if any, to reduce the principal amount outstanding.

Individually assessed loans and advances

For all loans that are considered individually significant, Bank assesses on a case-by-case basis at each balance sheet date if there is any objective evidence that a loan is impaired. All loans more than 90 days past due or loans which present a risk of not being paid back in full without collateral realisation, regardless of the existence of any past-due amount or the number of days past due, are classified as impaired, unless the value of the supporting collateral is sufficient to repay the outstanding balance. Further examples of trigger events, that may lead to the initial recognition of impairment provision include:

Macroeconomic triggers

- National or local economic conditions that indicate a measureable decrease in estimated future cash flows of the loan asset class.
- An increase in the unemployment rate.
- A decrease in property prices for mortgages.
- An adverse change in industry conditions.

Mortgage portfolio triggers (examples only)

- A loan asset that is 90 days in arrears.
- A request for a forbearance measure from the borrower.
- Deterioration in the debt service capacity.
- A material decrease in rents received on a buy-to-let property.

Commercial Real Estate ("CRE") portfolio triggers (examples only)

- A request for a forbearance measure from the borrower.
- A material decrease in the property value.
- A material decrease in estimated future cash flows.
- The lack of an active market for the assets concerned.
- The absence of a market for refinancing options.
- A significant decline in the Institution's credit rating of the borrower.

Small Medium Enterprises ("SME") portfolio triggers (examples only)

- A request for a forbearance measure from the borrower.
- Trading losses.
- Diversion of cash flows from earning assets to support non-earning assets.
- A material decrease in turnover or the loss of a major customer.

- A default or breach of contract.
- A significant decline in the Covered Institution's credit rating of the borrower.

For those loans where objective evidence of impairment exists, impairment losses are determined considering the following factors:

- The bank's aggregate exposure to the customer;
- - viability of the customer's business model and their capacity to trade successfully out of financial difficulties and generate sufficient cash flow to service debt obligations;
- the amount and timing of expected receipts and recoveries;
- likely dividend available on liquidation or bankruptcy;
- the extent of other creditors' commitments ranking ahead of, or pari passu with, Bank and the likelihood
- of other creditors continuing to support the company;
- the complexity of determining the aggregate amount and ranking of all creditor claims and the extent to which legal and insurance uncertainties are evident;
- the realisable value of security (or other credit mitigants) and likelihood of successful repossession;
- the likely deduction of any costs involved in recovery of amounts outstanding; and
- - the ability of the borrower to obtain, and make payments in, the currency of the loan if not denominated in local currency

Impairment provisions are calculated by discounting the expected future cash flows of a loan at its original effective interest rate and comparing the resultant present value with the loan's current carrying amount. The impairment provisions on individually significant accounts are reviewed at least quarterly and more regularly when circumstances require. Refer note x in the Risk management section for key principles applied in respect of property collateral held by the Bank.

Collectively assessed loans and advances

Impairment is assessed on a collective basis in the following circumstances:

- to estimate losses which have been incurred but have not yet been identified on loans subject to individual assessment; and
- to estimate losses for homogeneous groups of loans that are considered individually insignificant.

Incurred but not yet identified impairment

Individually assessed loans for which no evidence of loss has been specifically identified on an individual basis are grouped together according to their credit risk characteristics (exposure to an industry or geographical location) for the purpose of calculating an estimated collective loss. This reflects impairment losses that Bank has incurred as a result of events occurring before the balance sheet date, which Bank is not able to identify on an individual loan basis, and that can be reliably estimated. These losses will only be individually identified in the future. As soon as information becomes available which identifies losses on individual loans within the group, those loans are removed from the group and assessed on an individual basis for impairment.

The collective impairment provision is determined after taking into account:

- historical loss experience in portfolios of similar credit risk characteristics (for example, by industry sector, loan grade or product);
- the estimated period between impairment occurring and the loss being identified and evidenced by the establishment of an appropriate provision against the individual loan; and
- management's experienced judgement as to whether current economic and credit conditions are such that the actual level of inherent losses at the balance sheet date is likely to be greater or less than that suggested by historical experience.

The period between a loss event occurring and its identification is estimated by local management for each identified portfolio.

Homogeneous groups of loans and advances

The bank should describe how they stratify the overall portfolio included for collective assessment into pools that reflect similar risk characteristics. In particular, describe how the bank separates out from the overall portfolio, the pool in which forbearance measures have been applied. Other metrics that are representative of the pool should take into account significantly different LTVs, debt on other account, or external bureau scores.

Statistical methods are used to determine impairment losses on a collective basis for homogeneous groups of loans that are not considered individually significant, because individual loan assessment is impracticable.

Losses in these groups of loans are recorded on an individual basis when individual loans are written off, at which point they are removed from the group. Two alternative methods are used to calculate provisions on a collective basis:

When describing models or methods used to calculate provisions, use separate comments about how models are calibrated to take account of forbearance activities.

When appropriate empirical information is available, the Bank utilises roll rate methodology. This methodology employs statistical analyses of historical data and experience of delinquency and default to estimate the amount of loans that will eventually be written off as a result of the events occurring before the balance sheet date which Bank is not able to identify on an individual loan basis, and that can be reliably estimated. Under this methodology, loans are grouped into ranges according to the number of days past due and statistical analysis is used to estimate the likelihood that loans in each range will progress through the various stages of delinquency, and ultimately prove irrecoverable. Current economic conditions are also evaluated when calculating the appropriate level of provision required covering inherent loss. The estimated loss is the difference between the present value of expected future cash flows, discounted at the original effective interest rate of the portfolio, and the carrying amount of the portfolio. In certain highly developed markets, sophisticated models also take into account:

- Behavioural and account management trends as revealed in, for example, bankruptcy and rescheduling statistics.
- When the portfolio size is small or when information is insufficient or not reliable enough to adopt a roll rate methodology, Bank adopts a formulaic approach.
- Additional risk factors may be identified as part of this process. These risk factors, where relevant, are taken into account when calculating the appropriate level of impairment provisions by adjusting the impairment provisions derived solely from historical loss experience. Roll rates, loss rates and the expected timing of future recoveries are regularly benchmarked against actual outcomes to ensure they remain appropriate.

Write-off of loans and advances

Loans (and the related impairment provisions) are normally written off, either partially or in full, when there is no realistic prospect of recovery. Where loans are secured, this is generally after receipt of any proceeds from the realisation of security. In circumstances where the net realisable value of any collateral has been determined and there is no reasonable expectation of further recovery, write off may be earlier.

Reversals of impairment

If the amount of an impairment loss decreases in a subsequent period, and the decrease can be related objectively to an event occurring after the impairment was recognised, the excess is written back by reducing the loan impairment provision account accordingly. The write-back is recognised in the income statement.

Reclassified loans and advances *(if applicable)*

Where financial assets have been reclassified out of the fair value through profit or loss category to the loans and receivables category, the effective interest rate determined at the date of reclassification is used to calculate any impairment losses. Following reclassification, where there is a subsequent increase in the estimates of future cash receipts as a result of increased recoverability of those cash receipts, the effect of that increase is recognised as an adjustment to the effective interest rate from the date of change in the estimate rather than as an adjustment to the carrying amount of the asset at the date of change in the estimate.

Forbearance measures

Forbearance based on sound conduct principles provides for sound prudential management. Forbearance provided should be based on an individual assessment of the customer.

In considering the forbearance measures employed, refer to note x in the risk management section of this document.

The forbearances measures disclosed by the Covered Institution should include measures employed for loans that are forborne due to financial stress.

Mortgages

The Covered Institution should provide details on what type of forbearance is being applied in both the PDH and Buy-to-Let categories. There should also be disclosed an assessment of the sustainability of individual forbearance measures.

CRE and SME

The Covered Institution should provide details on what type of forbearance is being applied in both the CRE and SME categories. There should also be disclosed an assessment of the sustainability of individual forbearance measures.

Debt for equity exchange (if material)

Securities acquired in exchange for loans in order to achieve an orderly realisation are accounted for as a disposal of the loan and an acquisition of equity securities. Where control is obtained over an entity as a result of the transaction, the entity is consolidated; where the Bank has significant influence over an entity as a result of the transaction, the investment is accounted for by the equity method of accounting. Any subsequent impairment of the assets or business acquired is treated as an impairment of the relevant asset or business and not as an impairment of the original instrument.

b. Significant accounting judgments, estimates and assumptions

Impairment losses on loans and advances
Management is required to exercise judgement in making assumptions and estimations when calculating loan impairment provisions on both individually and collectively assessed loans and advances.

The most significant judgemental area is the calculation of collective impairment provisions. They are subject to estimation uncertainty, in part because it is not practicable to identify losses on an individual loan basis because of the large number of individually insignificant loans in the portfolio.

The methods involve the use of statistically assessed historical information which is supplemented with significant management judgement to assess whether current economic and credit conditions are such that the actual level of inherent losses is likely to be greater or less than that suggested by historical experience. In normal circumstances, historical experience provides the most objective and relevant information from which to assess inherent loss within each portfolio, though sometimes it provides less relevant information about the inherent loss in a given portfolio at the balance sheet date, for example, when there have been changes in economic, regulatory or behavioural conditions which result in the most recent trends in portfolio risk factors being not fully reflected in the statistical models. In these circumstances, the risk factors are taken into account by adjusting the impairment provisions derived solely from historical loss experience.

Risk factors include loan portfolio growth, product mix, unemployment rates, bankruptcy trends, geographical concentrations, loan product features, economic conditions such as national and local trends in housing markets, the level of interest rates, portfolio seasoning, account management policies and practices, changes in laws and regulations, and other influences on customer payment patterns. The methodology and the assumptions used in calculating impairment losses are reviewed regularly in the light of differences between loss estimates and actual loss experience. For example, roll rates, loss rates and the expected timing of future recoveries are regularly benchmarked against actual outcomes to ensure they remain appropriate.

However, the exercise of judgement requires the use of assumptions which are highly subjective and very sensitive to the risk factors, in particular to changes in economic and credit conditions across a large number of geographical areas.

Given the relative size of the mortgage portfolio, the key variables include house price which determine the collateral value supporting loans in such portfolios and rates by which defaulted or delinquent accounts are assumed to return to performing status ('cure rate'). A x% favourable change in the cure rate will reduce the impairment charge by approximately €x million. The value of collateral is estimated by applying changes in house price indices to the original assessed value of the property. If average house prices were x% lower than those estimated at 31 December 20x1, the impairment charge would increase by approximately €x million.

The foreclosure costs and period influence the value of the collateral. A x% increase in foreclosure costs and an increase in one month in the foreclosure period will result in increasing the impairment charge by €x million.

A collective unimpaired provision is made for impairments that have been incurred but have not been separately identified at the balance sheet date. This provision is sensitive to changes in the time between the loss event and the date the impairment is specifically identified. This period is known as the loss emergence period. In the Wholesale division, an increase of one month in the loss emergence period in respect of the loan portfolio assessed for collective unimpaired provisions would result in an increase in the collective unimpaired provision of approximately €x million. The emergence period applied to x portfolio is months/year. This is deemed appropriate because it reflects our experience over the last number of years and has remained stable.

2. Loans and advances to customers

Loans and advances to customers	20x2 € million	20x0 € million
Agricultural, forestry and fishing		
Energy and water supply		
Manufacturing		
Mortgages		
Other Personal		
Property companies		
Financial, business and other services		
Construction		
Total loans and advances to customers before provision for impairment losses		
Impairment provision		
Net loans and advances to customers		
Core		
Non-Core		

3. Impairment losses on loans and advances

Impairment losses on loans and advances	20x2 € million	20x0 € million
Core		
Non-Core		
Total Impairment losses		

Split of impairment charge by nature of impairment provision is set out below:

Impairment Charge by nature of impairment provision	20x2 € million	20x0 € million
Individual		
Collective		
IBNR		
Total Impairment losses		

Impairment charge on loans and advances to customers by division	**20x2 € million**	**20x1 € million**
Retail		
Wholesale		
Wealth and International		
Total impairment charge		
Retail division		
Owner Occupier		
Ireland		
United Kingdom		
Buy-to-let		
Ireland		
United Kingdom		
Other		
Total impairment charge		

Retail's impairment charge decreased by €1,480 million to €2,747 million in 20x2 compared with 20x1 and was lower in both secured and unsecured portfolios. This improvement was driven primarily by the improved quality of new business and effective portfolio management, coupled with the continuing slow recovery of the economy. Across Retail in 20x2, there were fewer cases going into arrears. The impairment provision on loans and advances to customers, as an annualised percentage of average loans and advances to customers, decreased to 0.74 per cent from 1.11 per cent in 20x1.

Wholesale division	**20x2 € million**	**20x1 € million**
Corporate Markets		
Asset finance		
Total impairment charge		

Wholesale's impairment charge decreased by €6,237 million, or 62 per cent, compared to €10,683 million for 2009. Impairment charges as an annualised percentage of average loans and advances to customers reduced to 2.08 per cent from 5.92 per cent in 2009. Together with the stabilising UK environment in 20x1, a low interest rate environment helping to maintain defaults at a lower level and a number of write backs due to asset disposals, impairment charges have decreased substantially compared with 2009.

Wealth and International division	**20x2 € million**	**20x1 € million**
UK		
Ireland		
Total impairment charge		

Wealth and International's impairment charge increased by €2,661 million to €3,534 million in 20x2 compared with 20x1. Impairment charges as a percentage of average loans and advances to customers increased to 8.90 per cent from 6.04 per cent in 20x1.

Total Impairment charge on loans and advances to customers by geographical location	20x2 € million	20x1 € million
Republic of Ireland		
United Kingdom		
United States		
Total impairment charge		

Impairment provision for loans and advances to customers

A reconciliation of the provision for impairment losses for loans and advances is as follows (table for 20x1 not re- produced):

Total	Residential Mortgages	Other Personal	Property & Construction	SME & Other Commercial	Corporate			Total
At January 20x2								
Charge for the year (note 2)								
Unwinding of discount								
Recoveries								
Amounts written off								
Interest accrued on impaired loans and advances								
At December 20x2								

Core	Residential Mortgages	Other Personal	Property & Construction	SME & Other Commercial	Corporate			Total
At January 20x2								
Charge for the year (note 2)								
Unwinding of discount								
Recoveries								
Amounts written off								
Interest accrued on impaired loans and advances								
At December 20x2								

Non-Core	**Residential Mortgages**	**Other Personal**	**Property & Construction**	**SME & Other Commercial**	**Corporate**			**Total**
At January 20x2								
Charge for the year (note 2)								
Unwinding of discount								
Recoveries								
Amounts written off								
Interest accrued on impaired loans and advances								
At December 20x2								

Impaired loans for which provisions are held are further split in the table below:

Total	**Loans & Advances**	**Impaired Loans**	**Impaired loans and % of Total loans**	**Provision Individually Assessed**	**Provision Collectively Assessed**	**Total Impairment Provision**	**Provision as a % of impaired loans**	**Collateral Value**
Retail								
Wealth & International								
Wholesale								
Total Gross Lending								
Impairment Provision								
At 31 December 20x2								

A further Divisional split of Secured and Unsecured Lending in Retail Division is as follows *(by bank product line)*

Retail Division	**Loans & Advances**	**Impaired Loans**	**Impaired loans and % of Total loans**	**Provision Individually Assessed**	**Provision Collectively Assessed**	**Total Impairment Provision**	**Provision as a % of impaired loans**	**Collateral Value**
Owner Occupier								
Buy to let								
Credit Cards								
Personal Loans								
Bank Accounts								
Other, including joint ventures								
Unsecured								
Total Gross Lending								
Impairment Provision								
At 31 December 20x2								

Wealth & International	**Loans & Advances**	**Impaired Loans**	**Impaired loans and % of Total loans**	**Provision Individually Assessed**	**Provision Collectively Assessed**	**Total Impairment Provision**	**Provision as a % of impaired loans**	**Collateral Value**
Ireland								
UK								
Total Gross Lending								
Impairment Provision								
At 31 December 20x2								

Wholesale Division	Loans & Advances	Impaired Loans	Impaired loans and % of Total loans	Provision Individually Assessed	Provision Collectively Assessed	Total Impairment Provision	Provision as a % of impaired loans	Collateral Value
Corporate Markets:								
Corporate								
Commercial								
Wholesale equity								
Wholesale markets								
Total Corporate Markets								
Treasury and Trading Asset Finance								
Total Gross Lending								
Impairment Provision								
At 31 December 20x2								

RISK MANAGEMENT (extract)

The risk management disclosures in this section are focused only on impairment provisioning and related disclosures with respect to loans and receivables and available-for-sale investments. Accordingly, other credit risk disclosures not included in this extract are set out below:

- Overview of credit risk exposures.
- Credit risk organisation and structure.
- Techniques to mitigate credit risk.
- Concentrations of credit risk and maximum exposure to credit risk by class of financial instruments including financial guarantees and commitments.
- Disclosure by industry and geography, where material.
- Details of collateral and other credit enhancements.

As stated in the introduction, this extract provides relatively condensed information and extracts where applicable of best practice disclosures (as quoted via footnotes). In practice, more detailed information might be necessary to reflect the circumstances of each bank. In addition, further narrative may be required to explain changes in risks and risk management processes compared to the previous year.

Additionally, the general requirement of IFRS 7.34(a) is that the quantitative data on risk exposures should be based on information provided internally to key management personnel.

Please note that some of the comparatives tables are not re-produced in some instances due to the repetitive nature of these disclosures.

1. Measurement and internal ratings

The principal objective of credit risk measurement is to produce the most accurate possible quantitative assessment of the credit risk to which the Bank is exposed, from the level of individual facilities up to the total portfolio. Integral to this is the use of an internal ratings system. This system is comprised of three elements – probability of default, exposure at default and loss given default – which are listed and explained below. These parameters are fundamental in assessing the credit quality of loan exposures, with variants of these used for the calculation of regulatory and economic capital. The key building blocks of this process are:

- Probability of default (PD) – the likelihood of a borrower being unable to repay his obligations on his obligations ;
- Exposure at default (EAD) – the exposure to a borrower who is unable to repay his obligations, at the
- point of default
- Loss given default (LGD) – the loss associated with a defaulted loan or borrower.

Use of PD, LGD and EAD within Credit Risk management processes

The bank should disclose how often the methodology they use for calculating PD is reviewed.

Forbearance

The bank should separately disclose the PDs for non-performing and performing forborne loans.

As part of its credit risk management processes, Bank uses a rating scale that is built upon these concepts. More specifically, borrowers are graded on an internal grading scale in accordance with their likelihood of default. This grading is fundamental to credit sanctioning and approval, and to the on-going credit risk management of loan portfolios.

For example, Bank can assign an expected loss over the next 12 months to each customer by multiplying these three factors. We calculate probability of default (PD) by assessing the credit quality of borrowers and other counterparties. For the sake of illustration, suppose a customer has a 2% probability of defaulting over a 12- month period.

The exposure at default (EAD) is our estimate of what the outstanding balance will be if the customer does default. Supposing the current balance is €150,000, our models might predict a rise to €200,000 by then. Should customers default, some part of the exposure is usually recovered. The part that is not recovered, together with the economic costs associated with the recovery process, comprise the loss given default (LGD), which is expressed as a percentage of EAD. Supposing the LGD in this case is estimated to be 50%, the expected loss for this customer is: 2% x €200,000 x 50% or €2,000. To calculate probability of default (PD), Bank assesses the credit quality of borrowers and other counterparties and assigns them an internal risk rating. Multiple rating methodologies may be used to inform the overall rating decision on individual large credits, such as internal and external models, rating agency ratings and other market information. For smaller credits, a single source may suffice such as the result from an internal rating model. Bank recognises the need for two different expressions of PD depending on the purpose for which it is used. However, for the purposes of pricing and existing customer management, PDs should represent the best estimate of probability of default given the current position in the credit cycle. Hence, point-in-time (PIT) PDs are also required.

Each PD model outputs an estimate of default probability that is PIT, TTC or a hybrid (e.g. a 50:50 blend)[15]. Bespoke conversion techniques, appropriate to the portfolio in question, are then applied to convert the model output to pure PIT and TTC PD estimates. In deriving the appropriate conversion, industry and location of the counterparty and an understanding of the current and long-term credit conditions are considered. Both PIT and TTC PD estimates are recorded for each client.

The calculation of internal ratings differs between wholesale and retail customers. For wholesale portfolios, the rating system is constructed to ensure that a client receives the same rating regardless of the part of the business with which it is dealing. To achieve this, a model hierarchy is adopted which requires users to adopt a specific approach to rating each counterparty depending upon the nature of the business and its location. A range of methods are utilised for estimating wholesale counterparty PDs. These include bespoke grading models developed internally in the bank (internal models), vendor models such as MKMV Credit Edge and RiskCalc, and a conversion of external alphabet ratings from S&P, Moody's or Fitch. Retail models, especially those used for capital purposes, are almost exclusively built internally using the bank's data. In many cases bureau data is used to complement internal data. In addition, in some low data/low default environments, external developments may also be utilised.

A key element of the wholesale framework is the PD Master scale. This scale has been developed to distinguish meaningful differences in the probability of default risk throughout the risk range. In contrast to wholesale businesses, retail areas rarely bucket exposures into generic grades for account management purposes (although they may be used for reporting purposes). Instead, accounts are

[15] Dependent on individual methodologies in each institution and as such may not be applicable in all instances.

managed at a more granular and bespoke level.

Exposure at default (EAD) represents the expected level of usage of the credit facility should default occurs. At the point of default, the customer exposure can vary from the current position due to the combined effects of additional drawings, repayment of principal and interest and fees. EAD parameters are all derived from internal estimates and are determined from internal historical behaviour. The lower bound of EAD for regulatory capital purposes is the current balance at calculation of EAD. For derivative instruments, exposure in the event of default is the estimated cost of replacing contracts where counterparties have incurred obligations which they have failed to satisfy.

Should a customer default, some part of the exposure is usually recovered. The part that is not recovered, the actual loss, together with the economic costs associated with the recovery process, comprise the loss given default (LGD), which is expressed as a percentage of EAD. The Bank estimates average LGD using historical information. The level of LGD depends principally on: the type of collateral (if any); the seniority or subordination of the exposure; the industry in which the customer operates (if a business); the length of time taken for the recovery process and the timing of all associated cash flows; and the work-out expense. The outcome is also dependent on economic conditions that may determine, for example, the prices that can be realised for assets, whether a business can readily be refinanced or the availability of a repayment source for personal customers. For the purposes of regulatory capital an adjustment is made to the modelled LGD to account for the increased losses experienced under downturn conditions, giving a 'downturn LGD'.

Use of PD, LGD and EAD within Regulatory Capital and in Impairment Provisioning

The three parameters PD, LGD and EAD are key components in deriving the regulatory capital. As outlined above, the parameters are modelled in varying ways for different portfolios, in order to capture the differential credit risks within these portfolios. Parameters drawn from bank's internal models are used to determine the aggregate level of risk weighted assets, in accordance with the requirements of the Central Bank of Ireland and the Capital Requirements Directive, with PD's reflecting the likelihood of borrower default within a 1-year time horizon, and LGD's reflecting the 'down-turn' LGD outlined above.

These parameters also impact the provisioning process, but to a lesser degree, with collective provisioning models based upon movements between arrears and /or grading classifications. Where PD or LGD elements have been used for provisioning purposes, the time-horizon has necessarily been altered to reflect a period of greater than 1 year in accordance with existing accounting standards.

2. Distribution of EAD and expected loss

The table below sets out the distribution by industry of the outstanding credit exposure to customers in terms of EAD. PD, LGD and EL. The expected loss from customer exposure as can be seen from the table below can be considered as a medium-to-low risk profile.

31 December 20x2	**EAD € million**	**%**	**Average PD (%)**	**Average LGD (%)**	**EL**
Residential Mortgages: Owner Occupiers					
Residential Mortgages: Buy to Let Properties					
Wholesale lending: Commercial property					
Wholesale lending: Corporate					
Wholesale lending: SME					
Other consumer					
Total					

3. Monitoring weakness in portfolios

The bank should describe how they incorporate forbearance measures into their methods for monitoring weaknesses in portfolios.

Whilst the basic principles for monitoring weaknesses in wholesale and retail exposures are broadly similar, they will reflect the differing nature of the assets. As a matter of policy all facilities granted to corporate or wholesale customers are subject to a review on, at least, an annual basis, even when they are performing satisfactorily. Corporate accounts that are deemed to contain heightened levels of risk are recorded on graded early warning lists or watch lists comprising three categories graded in line with the perceived severity of the risk attached to the lending, and its probability of default.

These are updated monthly and circulated to the relevant risk control points. Once an account has been placed on watch list (WL) or early warning list (EWL), the exposure is carefully monitored and, where appropriate, exposure reductions are affected. Should an account become impaired, it will normally have passed through each of the three categories, which reflect the need for increasing caution and control. Where an obligor's financial health gives grounds for concern, it is immediately placed into the appropriate category. While all obligors, regardless of financial health, are subject to a full review of all facilities on, at least, an annual basis, more frequent interim reviews may be undertaken should circumstances dictate. Specialist recovery functions deal with clients in default, collection or insolvency. Their mandate is to maximise shareholder value via the orderly and timely recovery of impaired debts. Accounts can stay in recoveries for up to two years unless a longer-term strategy has been agreed.

Within the retail portfolios, which tend to comprise homogeneous assets, statistical techniques more readily allow potential weaknesses to be monitored on a portfolio basis. The approach is consistent with the bank's policy of raising a collective impairment provision as soon as objective evidence of impairment is identified. Retail accounts can be classified according to specified categories of arrears status (or cycle), which reflects the level of contractual payments which are overdue on a loan.

The probability of default increases with the number of contractual payments missed, thus raising the associated impairment requirement.

Once a loan has passed through the appropriate stages within the credit process it will enter recovery status, having been charged off. In most cases, charge-off will result in the account moving to a legal recovery function or debt sale. This will typically occur after an account has been treated by a collections function. However, in certain cases, an account may be charged off directly from a performing (up to date) status, such as in the case of insolvency or death.

4. Impairment provisioning

The accounting policy in respect of impairment on loans and advances to customers is set out in note 1. As property loans represent a significant concentration within the Bank's advances, some key principles have been applied in respect of property collateral held by the Bank. For impaired property exposures, cash flows will generally emanate from the development and/or disposal of the assets which comprise the collateral held by the bank. The Bank's preference is to work with the obligor to progress the realisation of the collateral although in some cases the bank will foreclose its security to protect its position. Bank typically holds various types of collateral as security for these loans, e.g. land, developments available for sale/rent and investment properties or a combination of these assets via cross collateralisation.

Where cash flows arising from the realisation of collateral held are included in impairment assessments, management typically rely on valuations or business appraisals from independent external professionals. However, in accordance with Internal Policy on Collateral Valuation, the Bank uses a number of methods to assist in reaching appropriate valuations for the collateral held, given the absence of a liquid market for property related assets in Ireland at present. These include: (a) consultations with valuers; (b) use of professional valuations; (c) use of internally developed residual value methodologies; (d) the application of local market knowledge in respect of the property and its location, and (e) use of internal guidelines. These are described below.

- Consultations with valuers would represent circumstances where local external valuers are asked to give verbal 'desk top' updates on their view of the assets' value. Consultation also takes place on general market conditions to help inform the bank's view on the particular property valuation. The valuers are external to the Bank and are familiar with the location and asset for which the valuation is being requested.
- Use of professional valuations would represent circumstances where external firms are requested to provide formal written valuations in respect of the property. Up to date external professional valuations are sought in circumstances where it is believed that sufficient transactional evidence is available to support an expert objective view. Historic valuations are also used as benchmarks to compare against current market conditions and assess peak to trough reductions. Available market indices for relevant assets, e.g. residential and investment property are also used in valuation assessments.
- The residual value methodology assesses the value in the land or property asset after meeting the incremental costs to complete the development. This approach looks at the cost of developing the asset to determine the residual value for the Bank, including covering the costs to complete and additional funding costs. The key factors considered include: (i) the development potential given the location of the asset; (ii) its current or likely near term planning status; (iii) levels of current and likely future demand; (iv) the relevant costs associated with the completion of the project; and (v) expected market prices of completed units. If, following internal considerations which may include consultations with valuers, it is concluded that the optimal value for the Bank will be obtained through the development/completion of the project; a residual value methodology is used. When, in the opinion of the Bank, the land is not likely to be developed or it is non-commercial to do so, agricultural/green field values may be applied.
- Application of local market knowledge would represent circumstances where the local bank management familiar with the property concerned, with local market conditions, and with knowledge of recent completed transactions would provide indications of the likely realisable value and a potential timeline for realisation.
- In valuing investment property, yields are applied to current rentals having considered current yields and estimated likely yields for a more normal market environment for relevant asset classes.

Applying one or a combination of the above methodologies, in line with bank's Valuation Policy, has resulted in a wide range of discounts to original collateral valuations, influenced by the nature, status and year of purchase of the asset. The frequency, and availability, of such up-to-date valuations remains a key factor within impairment provisions determination. Additionally, all relevant costs likely to be associated with the realisation of the collateral are taken into account in the cash flow forecasts. The spread of discounts is influenced by the type of collateral, e.g. land, developed land or investment property and also its location. The valuation arrived at is therefore a function of the nature of the asset, e.g. un-serviced land in a rural area will most likely suffer a greater reduction in value if purchased at the height of a property boom than a fully let investment property with strong lessees. The discounts to original collateral value, having applied our valuation methodologies to reflect current market conditions, can be as high as 95% for land assets where values have been marked down to agricultural/green field site values.

When assessing the level of provision required for property loans, apart from the value to be realised from the collateral, other cash flows, such as recourse to other assets or sponsor support, are also considered. The other key driver is the time it takes to receive the funds from the realisation of collateral.

While this depends on the type of collateral and the stage of its development, the period of time to realisation is typically two to seven years but sometimes this time period is exceeded. These estimates are frequently reassessed on a case by case basis.

5. Loans and advances by asset quality

	Retail		Wholesale	Wealth & International	Total	Split as:	
	Mortgage	Other				Core	Non Core
Neither past due nor impaired Past due but not impaired Impaired – no provisions required Impaired – Provisions held							
Gross							
Provision for impairment losses							
Net							

The impaired loans above are held on a non-accrual basis i.e. no accrual of interest. Total interest income that would have been recorded during the year ended 31 December 20x2 had interest on gross impaired loans been included in income amounted to €2million (20x1: €4million).

Loans and advances which are neither past due nor impaired:

	Retail	Wholesale	Wealth & International	Total	Split as:	
					Core	Non Core
Strong Satisfactory Higher Risk						
Total neither past due or impaired						

If it is the bank's practice to include in this table, those loans which have had their arrears capitalised, the bank should disclose that fact and explain the rationale.

Strong: There is a very high likelihood of the asset being recovered in full.
Satisfactory: whilst there is a high likelihood that the asset will be recovered and therefore, of no cause for concern to the Bank, the asset may not be collateralised, or may relate to retail facilities, such as credit card balances and unsecured loans, which have been classified as satisfactory, regardless of the fact that the output of internal grading models may have indicated a higher classification. At the lower end of this grade there are customers that are being more carefully monitored.
Higher risk: there is concern over the obligor's ability to make payments when due. However, these have not yet converted to actual delinquency. There may also be doubts over value of collateral or security provided. However, the borrower or counterparty is continuing to make payments when due and is expected to settle all outstanding amounts of principal and interest.

For the purpose of analysis of credit quality, the following internal measures of credit quality have been used:

Internal Credit Rating	Default Grade
Strong	1-3
	4-5
	6-8
	9-11
Satisfactory Quality	12-14
	15-19
High Risk	20-21

Loans and advances which are past due but not impaired:

	Retail		Wholesale	Wealth & International	Total
	Fair value of collateral	**Loan exposure**	**Loan exposure**	**Loan exposure**	
0-30 days 31-60 days 61-90 days 91-180 days 181-360 days > 360 days					
Total past due not impaired	**-**	**€**	**€**	**€**	
Fair value of collateral held	**€**	**-**	**N/A**	**N/A**	

A financial asset[16] is 'past due' if a counterparty has failed to make a payment when contractually due.

Collateral held against retail mortgage lending is principally comprised of residential properties; their fair value has been estimated based upon the last actual valuation, adjusted to take into account subsequent movement in house prices, after making allowance for indexation error and dilapidations. The resulting valuation has been limited to the principal amount of the outstanding advance in order to provide a clearer representation of the Bank's credit exposure.

In respect of wholesale and wealth and international lending decisions are based on an obligor's ability to repay from normal business operations rather than reliance on the disposal of any security provided. Collateral values for non-mortgage lending are assessed more rigorously at the time of loan origination or when taking enforcement action and may fluctuate, as in the case of floating charges, according to the level of assets held by the customer. Whilst collateral is reviewed on a regular basis in accordance with business unit credit policy, this varies according to the type of lending and collateral involved. It is therefore not practicable to estimate and aggregate current fair values of collateral for non-mortgage lending.

[16] A financial asset as defined in IAS 39(9)

6. Forbearance arrangements(ROI only)

In 20x2, the Central Bank recognise that the below tables will include forbearance due to financial stress and may include forbearance due to non- financial difficulties. Going forward, it is expected that the tables will only include forbearance due to financial stress.

Bank operates a number of mechanisms which are designed to assist borrowers experiencing credit and loan re- payment difficulties, which have been developed in accordance with existing codes of practice. These are set out below.

Residential Mortgages

In accordance with the 2010 Code of Conduct of Mortgage Arrears (CCMA), Bank has defined a Mortgage Resolution Process (MARP) for mortgages which are secured on the primary residence of borrowers (owner occupier mortgages). This process applies to Bank's assessments of both borrowers in arrears and borrowers who, though not in arrears, have informed Bank about impending credit difficulties and potential future arrears ('pre-arrears borrowers').

Within this process, a full financial assessment of a borrower's ability to pay, based upon both re-payment capacity and re-payment history, is performed by banks Arrears Management Unit in order to determine the most viable alternative re-payment or forbearance arrangement. Currently, Bank extends the following options to borrowers:

- Interest only payments for a period of up to 3 months;
- Interest and partial capital re-payment;
- Capital and /or interest moratorium
- Term extension
- Change of mortgage type (except in the case of tracker mortgages)
- Capitalisation of arrears and interest
- Deferred Interest scheme

The table below sets out the volume of loans to which forbearance arrangements have been applied.

The impaired balance noted represents the loan balances to which impairment charges have been raised due to either being 90 days or more in arrears, or showing evidence of impairment prior to reaching arrears of 90 days.

Residential Owner Occupier Mortgages

The incidence of the main type of forbearance arrangements for owner occupied residential mortgages only is analysed below:

31 December 20x2	All Loans		Loans > 90 days in arrearsand or impaired	
	Number	Balance € million	Number	Balance € million
Interest only				
Reduced payment (less than interest only)				
Reduced payment (greater than interest only)				
Payment moratorium				
Arrears capitalisation				
Term extension				
Hybrid (term extension and interest only)				
Other				
Total				

Residential buy to let Mortgages

The incidence of the main type of forbearance arrangements for buy to let residential mortgages only is analysed below:

31 December 20x2	All Loans		Loans > 90 days in arrears and or impaired	
	Number	Balance € million	Number	Balance € million
Interest only				
Reduced payment (less than interest only)				
Reduced payment (greater than interest only)				
Payment moratorium				
Arrears capitalisation				
Term extension				
Hybrid (term extension and interest only)				
Other				
Total				

Impairment charge on loans and advances to customers by division

The balances in the preceding tables denoted impaired loan balances. The table below lists the impairment charges in respect of these balances, by lending type.

	20x2 € million			20x1 € million		
	Total	Loans in Forbearance Performing	Loans in Forbearance Non-Performing	Total	Loans in Forbearance Performing	Loans in Forbearance Non-Performing
Retail						
- - Owner occupier						
- - Buy to let						
- - Other Consumer						
Total impairment charge						

7. Repossessed collateral

Overall repossessions

31 December 20x2	Number of repossessions	Balance outstanding
		€ million
Residential repossessions		
Owner occupier		
Buy to let		
Total residential repossessions		

In respect of retail portfolios, the Bank does not take physical possession of properties or other assets held as collateral and uses external agents to realise the value as soon as practicable, generally at auction, to settle indebtedness. Any surplus funds are returned to the borrower or are otherwise dealt with in accordance with appropriate insolvency regulations. In certain circumstances the Bank takes physical possession of assets held as collateral against wholesale lending. In such cases, the assets are carried on the Bank's balance sheet and are classified according to the Bank's accounting policies.

In the course of the year, 95% of properties repossessed by value for residential mortgages and 90% for wholesale were disposed of by 31 December 20x2 and the remaining 5% are in the process of disposal. The table below sets out details of the sales on disposal of re-possessed properties.

31 December 20x2	Number of disposals	Balance Outstanding at repossession	Gross sales proceeds	Costs to sell	Loss on sale*
		€m	€m	€m	€m
Residential					
Owner occupier					
Buy to let					
Total residential					
Wholesale repossessions					
Commercial real estate					

* Calculated as gross sale proceeds – (balance outstanding at repossession + costs to sell)

8. Loan-to-value ratio ('LTV') of mortgage lending *(index linked)*

Loan to value is the relationship between the loan and the appraised value of the mortgaged property.

Analysis by loan-to-value ratio of the Bank's residential mortgage lending which is neither past due nor impaired:	20x2 € million	20x1 € million
Less than 50%		
50%-70%		
71% to 80%		
81% to 90%		
91% to 100%		
101%-120%		
121% to 150%		
Greater than 150%		
Total		

Actual and average LTVs across principal mortgage portfolios

31 December 20x2	Owner occupier %	Buy to let %	Total %
Less than 50%			
50%-70%			
71% to 80%			
81% to 90%			
91% to 100%			
101%-120%			
121% to 150%			
Greater than 150%			
Total	100	100	100
Average LTV:			
Stock of residential mortgages at year end			
New residential mortgages during year			
Impaired mortgages in total			

Arrears profile of loans and advances which are past due but not impaired (only for residential mortgages)

31 December 20x2	Owner Occupier € million	Buy to let € million	Total € million
0-30 days			
31-60 days			
61-90 days			
91-180 days			
180-360 days			
Over 360 days			
Total loans and advances which are past due but not impaired			

Analysis by loan-to-value ratio of the Bank's residential mortgage lending which are 90 days past due

	Owner occupier %	Buy to let %	Total residential mortgage portfolio %	Total loan portfolio %
Less than 50%				
50%-70%				
71% to 80%				
81% to 90%				
91% to 100%				
101%-120%				
121% to 150%				
Greater than 150%				
Total				

*The 'Total Loan Portfolio' column represents the percentage of the aggregate portfolio within these LTV categories, and is not restricted to those exposures 90 days or more in arrears.

9. Loan origination profile of the residential mortgage loan portfolio as at 31 December 20x2 before provision for impairment

	Residential mortgage loan book		Impaired residential mortgage loan book	
	Number	Balance €million	Number	Balance €million
1996 and before				
1997				
1998				
1999				
2000				
2001				
2002				
2003				
2004				
2005				
2006				
2007				
2008				
2009				
20x1				
20x2				
Total				

Appendix 3 – Definitions

Past due (arrears): A financial asset is past due when a counterparty has failed to make a payment when contractually due (IFRS 7: Appendix A).

Loans where repayment of interest and/or principal is overdue by at least one day are past due. Renewal, refinancing, re-negotiation, restructuring or novation of a credit facility do not interrupt the aging of arrears unless the client pays all interest due by his own means without new financing provided by the bank for such purposes, directly or indirectly. In the case of overdrafts, past due days are counted once a borrower:

- has breached an advised limit;
- has been advised of a limit lower than the then current outstanding balance;
- has drawn credit without authorisation:
- has failed to provide funds that are sufficient to pay for the interest debited into the account from the overdraft or from other credit facilities of the client;
- the limit of the overdraft is augmented without the client satisfying the later condition; or
- the overdraft is consolidated into a longer tenor facility that effectively capitalises interest due on the overdraft.

When a borrower is past due, the entire exposure is reported as past due, rather than the amount of any excess or arrears.

Impairment exposure: A loan is impaired and impairment losses are incurred if, an only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated. (IAS39)

Forborne exposure: Forbearance measures occurs when a bank, for reasons relating to the actual or apparent financial stress of a borrower, grants a concession whether temporarily or permanently to that borrower. A concession may involve restructuring the contractual terms of a debt (such as a reduction in the interest rate or principal due, or an extension of the maturity date or any weakening of the security structure or adjustment/non enforcement of covenants) or payment in some form other than cash, such as an equity interest in the customer.

Interest income recognition on impaired exposures (IAS 39 AG93): IAS 39 requires impairment losses to be calculated based on discounted future cash flows (principal and interest). Given IAS 39 requires all cash flows (principal and interest) to be taken into account for calculating the impairment loss, IAS 39: AG93 does not allow for non-accrual of interest following impairment as it is unnecessary. Following impairment, IAS 39 requires interest revenue to be recognised using the contractual EIR (i.e. the rate that was used for discounting the future cash flows for the purpose of measuring the impairment loss) applied to the carrying amount (which is net of the impairment amount). **(**IASB Staff Paper 4C, week beginning 11 April 2011).

Non-accrual of interest: When the 'trigger event' occurs, if the loan is considered to be worthless and there are no future cash flows expected, the impairment provision would amount to the carrying value of the asset and there would be no further interest income recognised in this scenario.

Amortised cost of a financial instrument: The amount at which it was measured at initial recognition minus principal repayments, plus or minus the cumulative amortisation using the 'effective interest method' of any difference between that initial amount and the maturity amount, and minus any write-down (directly or through the use of an allowance account) for impairment or uncollectability. (IAS 39)

Carrying Amount of a loan: The principal amount of the loan, taking into account payments applied to reduce principal, and adjusted to reflect accrued but uncollected interest, write-offs, unamortised premium or discount, and unamortised loan fees and costs, and reduced by any impairment provision.

Credit risk concentration: Risk based on similar or positively correlated risk factors, which, in times of stress, have an adverse effect on the creditworthiness of each of the individual counterparties making up the concentration.

Contractual amounts due: Principal and interest payments outstanding as set out in the loan contract.

Effective interest rate: The rate that exactly discounts estimated future cash payments or receipts over the expected life of the instrument or, when appropriate, a shorter period, to the instrument's net carrying amount. (IAS 39)

Emergence Period: Spanning the time between the occurrence of a loss event and the date that loss event is identified.

Estimated Future Cash Flows: Forecasted principal and interest payments (not necessarily contractual amounts due) as well as any cash flows from foreclosure of collateral.

Exposure: The total potential loss which a Covered Institution could incur in the event of non-payment by a counterparty. An exposure includes an amount outstanding on a loan, both principal and interest.

Non-performing loan: Non –performing exposures are those that satisfy at least one of the following criteria:

- Loans that are more than 90 days past due;
- Loans which present a risk of not being paid back in full without collateral realisation, regardless of the existence of any past-due amount or the number of days past due.

Cured loans: Loans may be considered to have ceased being non-performing when, simultaneously, the situation of the debtor has improved to the extent that full repayment, according to the original or when applicable the modified conditions, is likely to be made and the debtor does not have any amount past-due.

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