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Erste Group Bank AG comments to “Consultation paper on amendments to the Guidelines on Financial Reporting (FINREP 10 March 2009)”

Ladies and Gentlemen,

Erste Group Bank AG thanks you for the opportunity to comment on the new proposal of Finrep. We welcome the intention to create uniform reporting format without national discretions to change the templates.

However we would like to highlight that reduction of quantitative data does not mean that also the reporting burden is decreased. The amended FINREP also requires a lot of new information which may be very burdensome. This is the case for counterparty breakdown of interest income and expenses. Counterparty breakdown and geographical breakdown for balance sheet items is better available in the (usually non-accounting) systems but here the requirements go too much into granularity. Other examples are reconciliations between CRD and IFRS scope of consolidation (Table 26) and additional split of information on derivatives. Providing such information would cause significant system changes and big projects with requirements for resources, time and budget would have to be performed.

We also note that significant changes are planned by IASB in the areas of financial instruments reporting and financial statements presentation. We understand that CEBS was invited by European Commission to amend the FINREP and appreciate the effort. However the changes planned for financial instruments are so big that many templates will have to be restructured when we know the outcome of the IASB project. Therefore we assume that additional round of public consultations will be needed.

Below you can find our comments to the questions raised by CEBS. Please, do not overlook our specific comments which present the most important message which we want to give. We placed them in separate Appendix of the letter. They are focused on bringing more clarity, removing the information which we think is not IFRS compliant and difficult to prepare from practical point of view. If you have any questions we stand ready to answer them.

We appreciate your considerations of comments and look forward to hearing from you.

Yours sincerely,

Mgr. Renata Harvankova
Head of Group Financial Statements

Answers to the questions

a. Do you think the revised FINREP Guidelines will reduce reporting burden?

Revised FINREP tends to reduce reporting burden. The main factor for this is that national discretions are removed. This will make possible that templates prepared by the parent bank and by its subsidiaries in other EU countries will be the same as regards the core information part. However national regulators may still require different non-core templates but here we admit that the harmonisation is hard to achieve by FINREP itself (Option 2 Maximum Data College model discusses harmonisation of the templates within the banking group but we do not support it because of the risk of multiplying the templates for all the banks in the group if reflecting the requirements of each national supervisor).

We welcome reduction of unnecessary cells and templates. However such positive effect is reduced by requiring new information which is not currently available. Collecting such information would often require significant system changes. We address these issues further in the answers and in the Appendix of the comment letter.

b. Do you think the revised FINREP Guidelines will make financial reporting in the EU more uniform?

As written in the answer to the question a. the revised FINREP is a significant movement to unifying the financial reporting in the EU. We support the Option 1 "Maximum data model" which was chosen by CEBS. However real effect will result from what templates will be chosen by national supervisors.

c. CEBS guidance is non-binding. However, the possibility has been discussed of making FINREP mandatory at the consolidated level, a step which lies beyond the responsibility of CEBS. In addition, some countries apply FINREP at the solo level as well. Against this background, we are interested in your views concerning:

i) The pros and cons of mandatory application of FINREP at the consolidated level by EU Member states.

Our subsidiaries in the countries where FINREP is not applied prepare now just information necessary for the parent company consolidated FINREP reporting. Mandatory application of FINREP by EU states in the group would be helpful only if FINREP was the only source of consolidated reporting for national supervisors. However if national supervisors required also non-FINREP consolidated financial reports mandatory FINREP would present additional reporting burden.

ii. The possibility of extending the use of the FINREP guidelines to the solo level. Are all of your subsidiaries allowed to use IFRS?

Application of FINREP on solo level makes sense only if IFRS serve as statutory national legislation for individual financial statements. In our group only two EU subsidiaries and one non-EU subsidiary use IFRS as statutory accounting legislation.

d. Do you expect there to be a link between the FINREP framework and the IFRS-GP taxonomy?

Yes we expect that there is a link between FINREP and the IFRS-GP taxonomy.

e. What do you think of the proposals concerning reporting frequencies and reporting deadlines? Do you have alternative options?

We agree with the reporting deadlines proposed by CEBS.

f. Do you have any comments on the proposals relating to versioning policy?

It is difficult to understand what this question asks. If it refers to the 3 main policy options we express our support to the Option 1 “Maximum data model” as we write in the answer to the question b.

g. What impact do you expect the revised Finrep framework will have on your reporting procedures?

It will depend on what templates will be required by regulators. We are concerned that much of the newly required information – tables 15a, 26, breakdown of notional amounts for derivatives, detailed breakdown of balance sheet items according to counterparties are impossible to prepare without significant system changes. We discuss these issues in Appendix of the comment letter.

h. Is the new information required added to the framework already available within your entity? Please specify reporting items that are not available?

It is demanding to compare current and proposed version of FINREP as regards the new information in detail and to check its availability. Much help could have been provided by CEBS if had marked the new information.

Table	Unavailable information
Table 3	Economic hedges derivatives
Table 3, 8	Split of notional amount of non-option derivatives according to positive and negative fair values
Table 3, 8	Other financial corporations counterparty for derivatives
Table 4	Line item “Debt securities”
Table 5 A, B, C	Counterparty breakdown of financial assets
Table 5 D	Geographical breakdown of financial assets by residence counterparties
Table 6	Breakdown of loans and advances according to the loan type
Table 7	Breakdown of the impaired and past due assets by counterparty and product
Table 10 A, C	Breakdown of financial liabilities by product, geographical breakdown by residence of counterparty
Table 11	Financial assets entirely derecognised
Table 14	Split is too detailed, we have only some information
Table 15 A	Counterparty breakdown of interest income and expenses
Table 15 B	Breakdown of gains and losses from financial assets and liabilities and hedge accounting (We admit that this information is required also by current FINREP but our regulator does not require it therefore it is new for us.)
Table 16 B	Breakdown of allowances movements according to counterparty
Table 18	Split is too detailed. We do not have the information which is new compared to current FINREP.
Table 20	Counterparty breakdown
Table 24	Not available

Table 25	Information on FV hierarchy for financial assets and liabilities not measured at FV
Table 26	The whole table

Reasons for unavailability of some information are discussed in the Appendix of the comment letter.

i. FINREP guidelines do seek to interpret IFRS. Are the references and instructions sufficient for completing in the templates? Please specify where more instructions are needed.

Our proposals for removing the unclarities can be found in the Appendix of the comment letter.

j. The Guidelines on FINREP (Annex 2) provide a definition of the counterparty breakdown. Section II. 29 (6) identifies two possible definitions regarding Retail exposures. Which option do you prefer, and why?

We prefer the option 2 which defines retail as “natural persons only”.

k. Do you think that all redundancies in the current framework have been eliminated?

Information which is impracticable to prepare or requires significant system changes is in our opinion redundant. Our comments on these issues can be found in the Appendix of the comment letter.

l. Do you support CEBS’s initiative of recommending IT best practices on cell definitions, as a complement to XBRL-related issues?

We support this initiative.

m. Do you have any comments on the work plan? Is your institution interested in collaborating on it?

In the opening part of the letter we expressed our concerns that there will be a need for significant changes of the proposed FINREP after the new standard on financial instruments is issued.

Appendix

Specific comments to the templates

1) Comment to

- Part 15 of Guidelines for implementation of FINREP

The table for collective impairment assessment process is not IAS 39 compliant in the step 1B because collective impairment is not allowed for individually impaired loans no matter if significant or not.

IAS 39.AG88 says

“Impairment losses recognised on a group basis represent an interim step pending the identification of impairment losses on individual assets in the group of financial assets that are collectively assessed for impairment. As soon as information is available that specifically identifies losses on individually impaired assets in a group, those assets are removed from the group.”

The table probably refers to the fact that for practical reasons individually insignificant loans which are impaired are not treated based on individual cash flow estimates but based on statistics collected on portfolio basis (like LGD). But if this was the intention some other wording is necessary. Maybe just name “individually insignificant impaired loans“ would be sufficient.

2) Comment to

- Part 19 of Guidelines for implementation of FINREP
- Table 15 Gains and losses recognised in the income statement

The name “gains and losses“ is not correct here because the table 15A under this heading breaks down the interest income and expenses. Gains and losses can never refer to interest income and expenses because the Framework in paragraphs 74-80 defines that gains / losses are subtype of income and expenses and may or may not arise in the course of ordinary activities. Interest income and expenses are always connected with ordinary activities of the banks so they always fall under revenue and expenses which are by nature different from gains / losses. Although borderlines here are not quite clear, IFRS never refer to interest items as gains / losses.

3) Comment to

- Part 19 of Guidelines for implementation of FINREP
- Table 2 Consolidated income statement
- Table 15A Interest income and expenses on derivatives

The possibility to recognise interest income and expenses on derivatives should be described further in the part 19 of Guidelines for implementation of FINREP.

The Table 2 Income statement contains line items

- interest income – derivatives – hedge accounting, interest rate risk
- interest expenses – derivatives – hedge accounting, interest rate risk

The table 15A splits interest from derivatives held for trading into income and expenses.

The hedge accounting interest income and expenses in the Income statement should be further described - for example "amounts transferred into interest income and expenses when cash flow hedge accounting is applied", "settlement payments from interest derivatives when fair value hedge accounting is applied".

The table 15A contains for derivatives held for trading wrong reference to IAS 18.35 (b). This paragraph requires to disclose the amount of interest revenue. IAS 18 requires in paragraph 30 that revenue from interest shall be recognised using the effective interest rate (EIR) as set out in IAS 39. However EIR cannot be calculated for derivatives using IAS 39 rules because derivatives like interest / FX swaps, forwards have no initial net carrying amount. If CEBS wants to bring clarity into this area it should define what can be considered as interest income or expenses from interest derivatives or FX (or also other derivatives?)

- are these just settlement payments or can also the whole fair value revaluation be reported here?
- can interest income and expenses flow also from open and matched positions (as defined in point 14 i, ii of the guidelines for implementation) or only from hedging derivatives (as defined in point 14 iii)?

Clarification is needed because IFRS do not contain any guidance what interest income and expenses are in relation to derivatives.

4) Comment to

- Table 1 Consolidated balance sheet, 1.1 Assets

The issue that debt securities and loans and advances have references to IAS 39.9 has been discussed already. But we have to keep on saying that these references are wrong. Debt securities and loans and advances are not defined in IAS 39.9.

In this new version of FINREP proposal we welcome the improvement that "debt instruments" were renamed to "debt securities". Now it is easier to derive that loans and advances are financial assets which are neither equity instruments nor debt securities. However in order to be quite clear it would be worth to write this explicitly in the Guidelines for implementation of FINREP and to cancel the wrong references.

5) Comment to

- Table 1 Consolidated balance sheet, 1.1. Assets. 1.2 Liabilities

The line items "Fair value hedge of interest rate risk" and "Cash flow hedge interest rate risk" both on asset and liability side refer to the IAS 39 paragraphs dealing with portfolio hedges. To avoid possible confusions such reference given directly in their names may be suitable – "Portfolio fair value hedge of interest rate risk", "Portfolio cash flow hedge of interest rate risk".

6) Comment to

- Table 1 Consolidated balance sheet 1.2 Liabilities

The line item "Share capital repayable on demand (e.g. cooperative shares)" has to be updated in the light of the IAS 32 amendment effective from 1st January 2009. It is very likely that most of such instruments will now meet the condition of equity instruments. If CEBS wants to keep this line

item then you should include the reference to IAS32.16A,16B. These paragraphs define when capital repayable on demand (puttable instrument) is treated as equity and not liability.

7) Comment to

**- Table 1 Consolidated balance sheet 1.2 Liabilities,
- Table 12 Provisions**

Split of provisions in the balance sheet and in the table 12 contains item “Pensions and other post retirement benefit obligations“ with reference to IAS 1.78(d) which requires to show separately provisions for employee benefits.

If the intention of this item was to include all employee benefits provisions it should be renamed. Current name has much narrower meaning.

If the intention was that only post-employment defined benefit plans are covered here, then it should be specified that other employee benefit provisions should be disclosed under “other provisions“.

It also has to be mentioned that the table 12 which shows movements in provisions is not suitable for post-employment defined benefit obligations and for other long-term employee benefits because they contain specific movements like interest cost, current service cost, expected return on plan assets, actuarial gains and losses... These movements are analysed in the table 19 (see also our comment No 17). Defined benefit liabilities from post-employment benefits and liabilities for other long-term employee benefits are specific kinds of provisions which can have also negative (asset) balance (when plan assets exist). Therefore FINREP should specify where they should be reported in the balance sheet and they should be excluded from the Table 12.

8) Comment to

-Table 2 Consolidated income statement

Line items for “Interest income - other assets” and “Interest expenses - other liabilities” should be explained.

As regards interest income from other assets – interest income items above this one cover all financial assets. Was the intention to report here interest income from non-financial assets? What cases should fall here?

As regards interest expense from other liabilities – interest expense items above cover all financial liabilities except for financial liabilities that arise when transfer does not qualify for derecognition or when continuing involvement approach applies. It means that this item may be relevant for interest expense from these financial liabilities. But do you also consider it to be relevant for interest expenses from non-financial liabilities like interest expenses from provisions or interest cost from post-employment defined benefit plans and long-term employee benefit plans or for other?

9) Comment to

- Table 2 Consolidated income statement

Referring to the line item „Gains (losses) on financial assets and financial liabilities held for trading, net“ do securities coming from securitisation of loans fall

- under interest rate instruments and related derivatives or

- under credit risk instruments and related derivatives?

The line item “Other (including hybrid derivatives)” should be renamed to “Other (including hybrid instruments)”.

10) Comment to

- **Table 3 Derivatives held for trading**
- **Table 8 Derivatives – hedge accounting**
- **Part 14 of Guidelines for implementation of FINREP**

We strongly object to the requirement that notional amount of derivatives is split into separate columns based on whether derivative has positive or negative fair value. IFRS do not require any disclosure about derivatives except for their fair values. However the notional amount is easy to obtain and this Finrep requirement has not caused practical difficulties so far.

The issue of split of notional amounts based on positive or negative fair values of derivatives was discussed in the January meeting at CEBS. Banking sector opposed it and no convincing reason was given from the side of supervisors why it was needed.

Such split will cause significant burden for accounting practice. So far the notional amount was posted once at the inception of the contract and did not change after. This new requirement would cause repostings from one account to another based on how fair value of the (non-option) derivative develops. Banks usually have huge amounts of derivative contracts and such change could not be handled manually. Therefore accounting system changes would be necessary. An all these difficulties would be caused by requirement

- which is not IFRS compliant and
- whose informatory value is more than questionable, probably useless.

11) Comment to

- **Table 4 Financial Assets designated at fair value through profit or loss: credit risk information**
- **Table 5C Counterparty breakdown for financial assets held for trading and financial assets designated at fair value through profit or loss**

a) The table 4 should be renamed into “Loans and receivables designated at fair value through profit or loss” because IFRS 7.9 requires these disclosures only for loans and receivables category. Therefore we also question why further breakdown into debt securities and loans and advances subitems is necessary.

b) The column “Amount of cumulative change in the fair values attributable to changes in the credit risk” in the table 5C should be specified that it relates only to loans and receivables which were designated at fair value through profit or loss. IFRS 7.9 is valid only for such types of assets.

12) Comment to

- **Table 7 Information on impairment and past due**
- **Table 16B „Allowances movements for credit losses“**

- a) the column “specific allowances for collectively assessed financial assets” should be renamed to reflect the facts which we mentioned in the comment No 1. Correct alternative might be “Specific allowances for individually insignificant financial assets”.
- b) equity instruments which may be impaired can belong only to available for sale (AFS) category or measured at cost category. Paragraphs IAS 39.67-70 specific for impairment of AFS financial assets and paragraph IAS 39.66 specific for financial assets carried at cost do not allow
- to distinguish individual and portfolio impairment and
 - to use separate allowance account for showing impairment.
- Such split into portfolio and individual impairment and using allowance account is allowed only for financial assets carried at amortised cost (IAS 39.63-65 and the whole AG part dealing with impairment AG84-AG92).

Therefore for equity instruments in the Table 7 only the columns “net carrying amount of the impaired assets” and “accumulated value adjustments recorded directly to the income statement (accumulated write-offs)” are relevant.

For the same reason the Table 16B cannot be relevant for equity instruments. IFRS 7.16 requires reconciliation of changes in separate allowance account only when it is really used for recording the impairment. However for equity instruments impairment must never use separate account. Impairment is always recorded directly against the asset account.

- c) the column “collateral and other credit enhancements received as security for the related impaired and past due assets (reference to IFRS 7.37 (c))” in the Table 7 should not be required as mandatory, because IFRS 7.37(c) does not require to give disclosures of collateral fair values when impracticable.

13) Comment to

-Table 14 Fee and commission income and expenses

What does the line item “Commissions to agents (acquisition costs)” include? Transaction costs connected with acquisitions of financial assets and incurrence of financial liabilities are part of the initial carrying amount and are not reported in P&L. IAS 39.13 explicitly says that commissions paid to agents are transaction costs.

14) Comment to

- Table 15B Breakdown of gains and losses

For better understandability the line items under “Gains and losses from hedge accounting” should be specified to what types of hedges they relate. Currently this results from the references but including such information directly in the names would be better.

- Fair value changes of the hedged item attributable to the hedged risk – *fair value hedges* (IFRS 7.24 (a) (ii))
- Fair value changes of the hedging derivatives (including discontinuation) – *fair value hedges* (IFRS 7.24 (a) (i))
- Fair value changes of the hedging derivatives – *cash flow hedges* (IFRS 7.24 (b))

Currently the third type of hedge – hedge of net investment in foreign operation is missing.

The line items names say only about hedging derivatives. But also non-derivative financial assets or liabilities can be in the position of hedging instruments for hedging the FX risk. Therefore hedging derivatives should be renamed into „hedging instruments“.

15) Comment to

- **Table 15B Breakdown of gains and losses**
- **Table 25B Information on unrealised gains and losses**

These tables require to show separately gains and losses. For the banks this is especially relevant for gains and losses from financial instruments. We have to stress that such split is not required by IFRS 7, because

- IFRS 7.20 requires to disclose net gains or net losses for financial instruments and
- IFRS 7.24 requires to disclose gains or losses from fair value hedges and ineffectiveness recognised in profit or loss for cash flow hedges and net investment hedges.

There is no requirement to use separate disclosures for gains and for losses.

When a bank accounts for the gains and losses from revaluation of financial instruments continuously it may use the system of postings from which such separate information about gains and losses cannot be tracked. This would be the case when

- for the same financial asset it posts for example gain 100 (when fair value went up by 100) for one month on one account and loss 20 for another month (when fair value decreased by 20) on another account. There are two separate accounts for gains and losses but they show the month-to-month +100 and -20 and not year-to-date information +80. Moreover in practice each asset does not have its own account for gains and losses and therefore such year-to-date information cannot be obtained simply by merging the gain and loss account; or
- One account both for gains and losses is used which shows the year-to-date gain or loss on individual asset level. But again postings on it merge many financial assets of the same or similar kind (like described above) and gain and loss balances are offset in this way.

To track such information the bank would have to handle each financial asset separately or would have to change the system of month-to-month (or day-to-date) postings of gains and losses. It might require significant system changes for the banks. Moreover banks which do not have this information do not even use it for internal purposes. Internal reporting based on net presentation of gains /losses is sufficient for them. Only information about financial instruments which are of particular interest for them is then searched individually.

The question is why should Finrep require information

- which is not required by IFRS,
- may not be tracked from accounting systems and
- when unavailable it is not even relevant for management decision making.

16) Comment to

- **Table 17 Repurchase agreements, reverse repurchase agreements and related agreements**

To be more understandable it should be specified to what values the particular tables relate

- Table A – carrying amount (of financial assets which were transferred but not derecognised)
- Table B – carrying amount of liability
- Table C – fair value of collateral when sold

- Table D – the carrying amount of assets (financing granted).
The reference to IFRS 7.15(a) is confusing here because this paragraph is about fair value of collateral held. If this table is about carrying amount of the assets (financing granted) then separate column for fair value of collateral held should be added.

17) Comment to

- Table 19 Defined benefit plans and employee benefits

Disclosures in this table are relevant for

- post employment defined benefit plans and
- other long-term employee benefits (although some line items are not relevant here like unrecognised actuarial gains/losses, unrecognised past service cost).

The scope of this table should be clearly defined because its current name is confusing.

18) Comment to

- Table 20 Loan commitments, financial guarantees and other commitments

The “doubtful” loan commitments and financial guarantees have to be defined. The possible definition might be that these are loan commitments and financial guarantees “for which provision on individual basis was created in accordance to IAS 37”.

19) Comment to

- Table 22 Statements of changes in equity

According to new IAS 1 statement of changes in equity is focused on owner changes in equity. This is reflected in the table. But the logical order of the line items would be that the comprehensive income for the year is the last line item just before closing balance. Currently it is placed in the middle of owner changes in equity.

20) Comment to

- Table 25A Information on fair value of financial instruments

- a) the columns for “Gross (before taxes) unrealised gains and losses (accumulated)” and further split into level 1, 2, 3 is not required by IFRS 7
- b) The table contains line items requiring to disclose fair value hierarchy for
 - loans and receivables,
 - held-to-maturity investments and
 - financial liabilities measured at amortised cost (with further sub-items),
i.e. for those financial instruments which are not recognised at fair value in the financial statements.
IFRS 7.27B requires to disclose fair value hierarchy only for fair value measurements recognised in the statement of financial position.

We strongly oppose that Finrep requires information that is outside the scope of IFRS. Preparing such information would be very burdensome for banks. If CEBS wants to collect such information anyway it should not use the heading Finrep which refers to IFRS.

21) Comment to

- Table 25D Hybrid financial instruments not designated at fair value through profit or loss

The column “Held for trading” is not relevant because under IAS 39.11 (c) if the hybrid instruments is measured at fair value through profit or loss (not only designated, but also when held for trading) the embedded derivative is not separated and no “rest of separable hybrid contracts” exists.

22) Comment to

- Table 14 Fee and commission income and expenses
- Table 15A Breakdown of interest income and expenses
- Table 16B Allowances movements for credit losses

Requiring further breakdown of income and expense items would result in significant system changes. A good example how to illustrate this issue is interest income and expenses. Contractual interest accruals run in the banks in very high frequency which is often daily. Interest income and expenses on top of this consist of amortisation of the difference between original carrying amount and principal which require even more computations with complicated algorithms. Such calculations relate to huge amount of transactions, thus they present big demands for accounting systems and are time consuming. They are calculated in the same way for similar transactions and results are aggregated on a high level. Requiring further split would mean programming new conditions in the systems with new demands for IT capacities.

23) Comment to

- Table 26 Reconciliation from CRD to IFRS scope of consolidation

This table is in our opinion impossible to prepare. When a regulator chooses scope of consolidation which it considers to be correct why it is interested in a information prepared under different scope of consolidation? For example when a bank prepares FINREP financial statements under CRD scope of consolidation it just cannot have IFRS scope of consolidation information available in FINREP structure. Even when it prepares and publishes its own IFRS consolidated financial statements they have different structure. Moreover the structure of FINREP financial statements is not suitable for insurance companies and other entities which are in the middle of reconciliations between the two scopes of consolidation.

24) Comment to

- Table 1.2 Liabilities

In the current FINREP balance sheet there is item “Financial liabilities associated with transferred financial assets” which disappeared from the proposed version. In the January meeting and May public hearing information was mentioned that such liabilities should be reported under respective portfolios. However according to IAS 39 there is no portfolio relevant for them because they present exception with specific measurement rules which does not belong to held for trading, fair value option or amortised cost measured financial liabilities (IAS 39.47b). We do not call for retaining the separate line item but it should be specified in the Guidelines for implementation

where such liabilities should be reported. For example measurement of liabilities from REPO transactions is straightforward and is equivalent to amortised cost of normal financial liabilities. More complex cases of such liabilities should be specified in a more detail (for continuing involvement approach even financial liabilities revaluated against AFS reserve may be relevant - IAS 39.31b if the transferred asset is an AFS instrument).

25) Comment to

- **Table 24 Asset management, custody and other service functions
Part 25 of Guidelines for implementation of FINREP**

What amounts should be reported here? Part 25 of Guidelines for implementation of FINREP dealing with off-balance says that table 24 provides information about business related to asset management, custody and other service functions and it further defines them. Table 24 requires disclosures of gross carrying amount for such activities. However off-balance sheet items have no carrying amounts. Therefore the guidelines should specify what amount should be reported here.