



**Deloitte.**

Fifth Global IFRS  
Banking Survey  
Finding your way

September 2015



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# Preface

We are delighted to welcome you to our *Fifth Global IFRS Banking Survey*, the culmination of several months' work by Deloitte around the world.

With IFRS 9 published and the FASB's CECL project expected to come to a conclusion by the end of this year, we wanted to find out more about how banks are approaching the implementation of IFRS 9/FASB's CECL model impairment requirements in their organisations.

In this context, our global financial services industry group has collated the views of 59 major banks, to keep you informed of how the industry is responding to accounting and regulatory change.

Our previous surveys have stimulated discussions with a range of key stakeholders. We hope this survey will once again provide you with insights into current thinking and help develop market consensus where appropriate, through supporting conversations amongst and between institutions, investors, regulators and standard setters.

We are extremely grateful to all the institutions and individuals who have participated in this survey and thank you warmly for your contributions. We hope you find this report valuable. If you wish to discuss any of the themes raised by our research, please do contact one of us or your usual Deloitte contact. We look forward to working with you as you implement IFRS 9.

Regards

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# Key findings

Most global banks estimate new IFRS 9/FASB CECL rules on credit exposures will result in **loan loss provisions increasing by up to 50%** across asset classes.\*

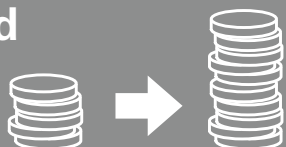


## Key implementation challenges include:

- Clarity around acceptable interpretation of the new rules;
- Internal co-ordination between finance, credit, risk, and IT functions; and
- Availability of data.



Total anticipated implementation budgets have **doubled** in the year since our previous survey.



**Three fifths** of banks think they **do not have enough technical resources** to deliver their IFRS 9/FASB CECL project and a quarter of these further doubt that there will be sufficient skills available in the market to cover any shortfall.



## Three quarters

of banks surveyed expect bank accounts to be more useful for regulators under the new rules.



**Two fifths** of banks surveyed believe **banking supervisors** would be most influential in interpreting the new rules, with a third expecting auditors to be key.



Despite discouragement from the BCBS, **three quarters** of respondents expect to use one or more of the operational simplifications available.



**85%** of banks surveyed anticipate their expected credit loss provisions to exceed those calculated under Basel rules, mostly driven by the provision of lifetime expected losses under 'stage II'.



\*Please note that a third of the participants in the survey did not know the answer to this question. Furthermore, responses given are high level estimates that do not necessarily reflect the transition impact in 2018

### About this survey

This survey includes the views of 59 banks from Europe, the Middle East & Africa, Asia Pacific and the Americas (42 of which are IFRS reporters).

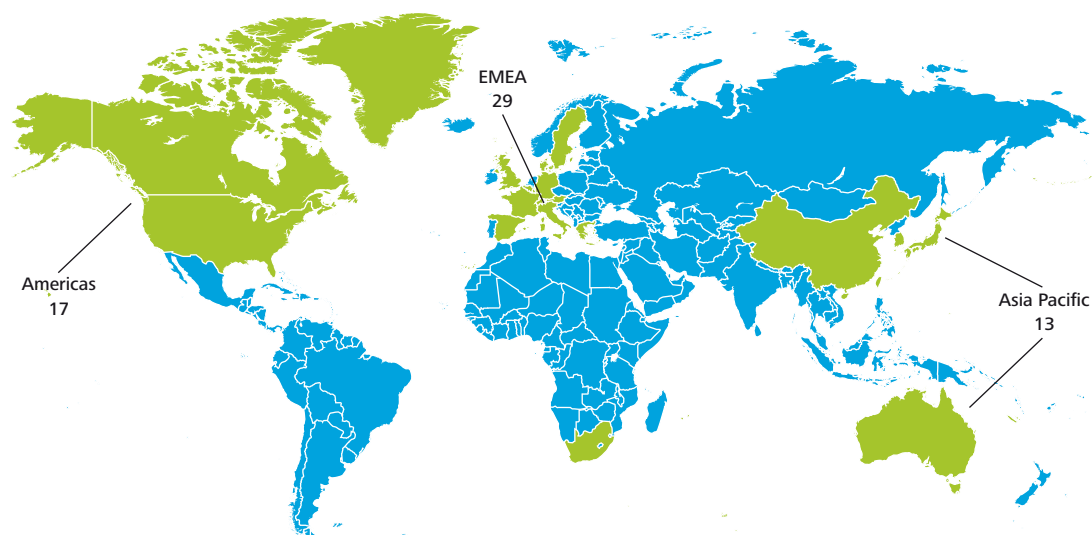
We received responses from 17 of the 30 global systemically important banks (G-SIBs) determined by the Financial Stability Board (FSB), including 12 of the 18 G-SIBs who are International Financial Reporting Standard (IFRS) reporters.

In most instances, responses have been coordinated from the accounting policy or finance area although many respondents have sought the views of other key areas of the bank such as the credit risk department.

This is the fifth time we have surveyed the world's major banks on IFRS 9 and related changes. Findings from our previous surveys were published in *IFRS 9 Impairment Survey 2011*, *Second Global IFRS Banking Survey – Q1 2012*, *Third Global IFRS Banking Survey* and *Fourth Global IFRS Banking Survey*. Our growing dataset means we are now able to examine how views of accounting standards are changing over time.

In the analysis that follows, we highlight the most interesting trends. In the charts in this report, we refer to the previous surveys in order of publication as the 1st, 2nd, 3rd and 4th respectively.

Figure 1. Geographical spread of respondents



Throughout the document, references are made to IFRS 9 and the FASB's Current Expected Credit Loss (CECL) model. While the IFRS 9 Standard was published in July 2014, the CECL model amendments proposed by the FASB are still in draft stage but will result, as in the case of IFRS 9, in a change from the existing incurred loss model to an expected credit loss model. Original questions in the survey sent to the US participants made reference to the FASB's CECL model while questions for the rest of participants referred to IFRS 9.

For questions requiring respondents to rank their options, percentages shown in the graphs reflect the weighting applied in order to incorporate respondents' preferences.

# Where are we now?

## An outline of developments since the previous Global IFRS Banking Survey

The International Accounting Standards Board (IASB) published the finalised version of IFRS 9 *Financial Instruments* in July 2014. This was the culmination of a number of years of work in reforming financial instruments accounting under IFRS. Critical to this project was the replacement of the impairment requirements previously included in IAS 39 *Financial Instruments: Recognition and Measurement*. In short, the incurred loss impairment model in IAS 39 was replaced with an expected loss impairment model in IFRS 9. The IASB were working jointly with the U.S. Financial Accounting Standard Board (FASB) with the aim of issuing converged standards. Unfortunately the Boards could not reach a consensus so the IASB finalised their standard, IFRS 9, in 2014 and the FASB is expected to publish their final standard in the fourth quarter of 2015. Although similar, the IASB and FASB's impairment approaches do differ, particularly in that the IASB's model generally requires that where there has not been a significant increase in credit risk, 12 months expected losses are provided for, whereas the measurement approach for FASB is solely based on lifetime expected credit losses.

Since IFRS 9 was published the IASB has set up the *IFRS Transition Resource Group for Impairment of Financial Instruments*. The aim of the group is to solicit, analyse and discuss stakeholder issues arising from the new impairment requirements, inform the IASB about implementation issues and provide a public forum for stakeholders to learn about the new impairment requirements from others involved in implementation. The first meeting was in April 2015 with two further meetings expected this year.<sup>1</sup>

Given the potential impact of the accounting reforms on future earnings, regulatory capital and financial stability, and their interaction with credit risk management, it is not surprising that prudential supervisors are closely monitoring the implementation of IFRS 9 in banks. In February 2015 the Basel Committee on Banking Supervision (BCBS) issued a consultative document, *Guidance on accounting for expected credit losses*.<sup>2</sup> The comment period has closed and the BCBS will deliberate feedback received with the aim of issuing final guidelines later in the year.

On disclosures, the Enhanced Disclosure Task Force (EDTF) are currently considering the implication of expected credit losses (ECL) for their previous recommendation. Likewise, the European Securities and Markets Authority (ESMA) are expected, once IFRS 9 has been endorsed by the EU, to provide further guidance on disclosures by EU listed companies.

<sup>1</sup> The summary of the first meeting of IFRS Transition Resource Group can be consulted [here](#)

<sup>2</sup> The BCBS consultative document can be accessed [here](#)

# Interpreting the new rules

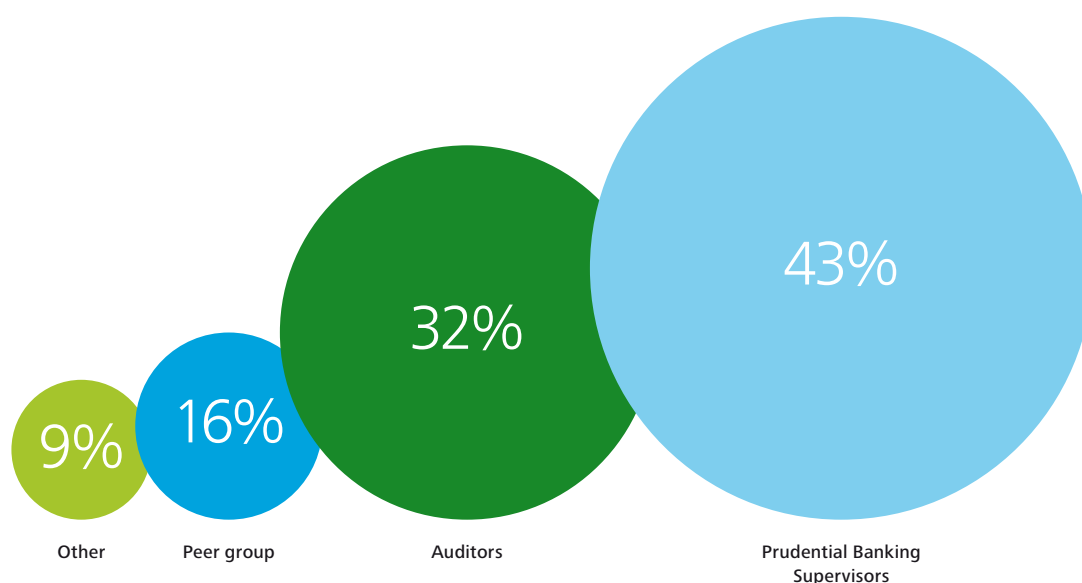
## Influential bodies

The new impairment requirements will require entities to make a significantly higher number of assumptions and judgements. Furthermore, entities will have to decide how to define key elements of their expected credit losses (ECL) model that will have an impact on their provision numbers.

We asked participants to indicate which bodies will be most influential when interpreting the IFRS 9 Standard for their implementation plan.

More than forty percent of respondents see the banking supervisors as the most influential body. This is likely to be as a result of supervisors' and regulators' reviews on quality of the loan portfolios, capital regulatory requirements and stress testing. Auditors are considered second most influential. The peer group was considered third most influential – due to banks wanting to follow best industry practices, avoiding being seen as outliers.

**Figure 2. Which of the following bodies will be most influential when interpreting the IFRS 9 Standard for your implementation plan?**

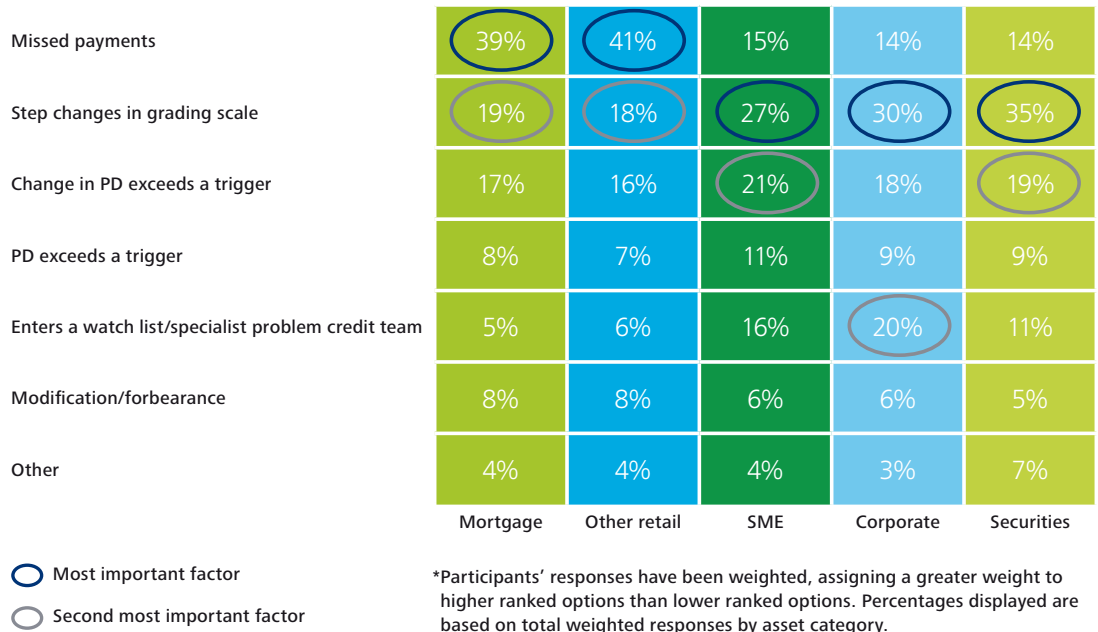


More than 40 percent of respondents see the banking supervisors as the most influential body.

## Significant deterioration

The definition to be used to measure significant increase of credit risk since origination is one of the key issues that entities will have to address. Depending on where this line is drawn, expected credit losses will be measured as 12 months or lifetime, leading to a different provision amount. We were interested in knowing which key measures participants expect to use for each of the different loan portfolios in their organisations.

**Figure 3. How do you expect to define and measure 'significant deterioration' in credit quality?**



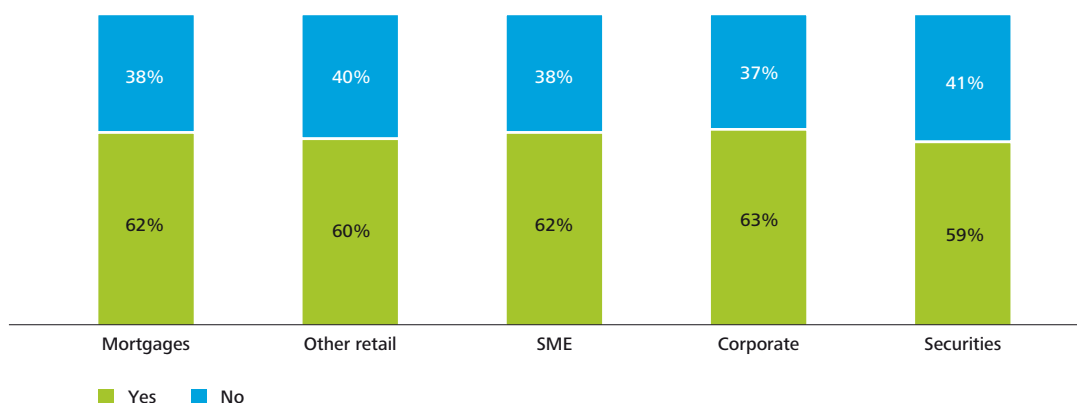
For mortgages and other retail loans, a large proportion of respondents expect to use "missed payments" as the key measure of significant deterioration, while for SME, corporate and securities, "steps changes in grading scale" will most likely be used.

We note that five participants expect to use "missed payments" as the *only* measure to define significant deterioration in mortgages and other retail portfolios. The view of the BCBS is that delinquency data should only be used on rare occasions and that lifetime expected credit losses are generally expected to be recognised *before* a missed payment occurs.

For the majority of the participants who consider "missed payments" as the key measure of "significant deterioration", the trigger will be 30 days past due across all portfolios including, surprisingly, securities. For those banks that selected "change in the PD exceeding a predefined trigger" as their key measure of significant deterioration, respondents were almost equally divided between those who will use a more sophisticated approach, using measures of internal default scale migration, and those with a simpler approach, using a multiple of the original probability of default (PD).



**Figure 4. Regardless of credit deterioration status, do you anticipate calculating both a 12 month expected loss and a Lifetime Expected Loss for all exposures?**



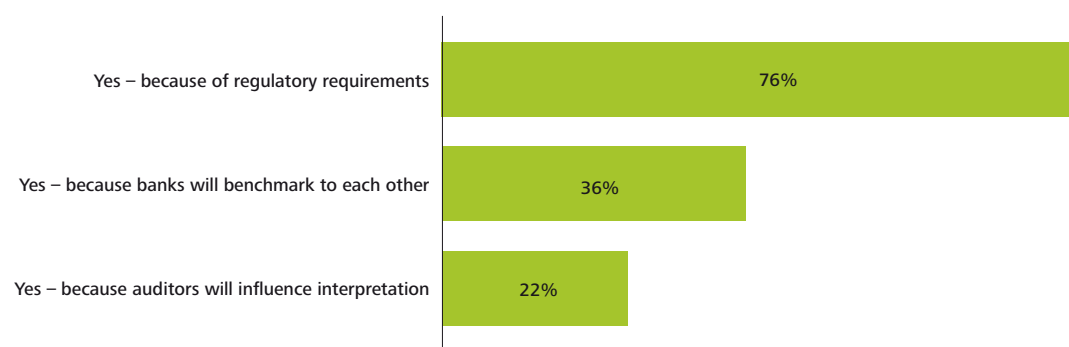
Surprisingly, opinion is divided on whether to calculate both a 12 month expected loss and a lifetime expected loss for all exposures or not; around forty percent of participants do not anticipate calculating both. This percentage is even greater in the Asia Pacific region, where sixty percent of participants will not be calculating both 12 month and lifetime expected losses (EMEA and the Americas results sit around thirty percent).

#### Definition of default

IFRS 9 does not define what 'default' means but emphasises that the definition used by the entities has to be aligned with the one used for credit risk management purposes. It includes, however, a rebuttable presumption that default does not occur later than when the financial asset is 90 days past due.

We were interested in knowing whether banks think there will be comparable definitions among their peer group.

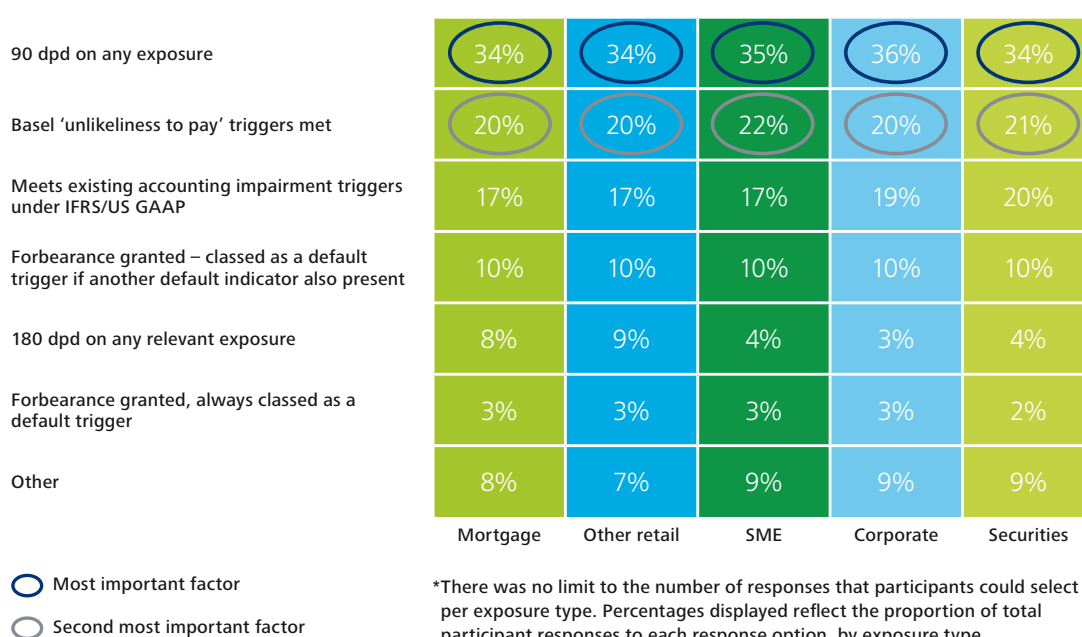
**Figure 5. IFRS 9 states that the default definition should be aligned with an entity's credit risk management practices. Do you think competitor banks will define default in a comparable manner?**



Ninety four percent of the banks think that default will be defined in a comparable manner, with others expecting a variety of practices and interpretations. Regulators are expected to play a key part in the interpretation of this area of IFRS 9 – most of those who think default will be defined in a comparable way believe consistency will be driven by regulatory requirements. Consistency is also likely to increase over time; for example, benchmarking between banks will become easier as the volume of published information grows.

It is remarkable the decrease in the percentage of participants not expecting banks to define default in a comparable manner from last year's results, where almost twenty percent had that view, to this year's, where only six percent expect different practices and interpretations in the default definition.

**Figure 6. By exposure type, how do you intend to define default for IFRS 9 purposes?**



In February 2015, the Basel Committee on Banking Supervision (BCBS) issued a consultative document, *Guidance on accounting for expected credit losses (GAECL)*. In the GAECL paper, the Committee expects banks to adopt a definition of default for accounting purposes that is 'guided by the definition used for regulatory purposes'. The responses of participants are consistent with this expectation, with '90 days past due (dpd)' as the most cited measure to define default, closely followed by Basel 'unlikelihood to pay' triggers. The Committee is still deliberating on the feedback received before issuing the definitive document.

#### **BCBS: Guidance on accounting for expected credit losses**

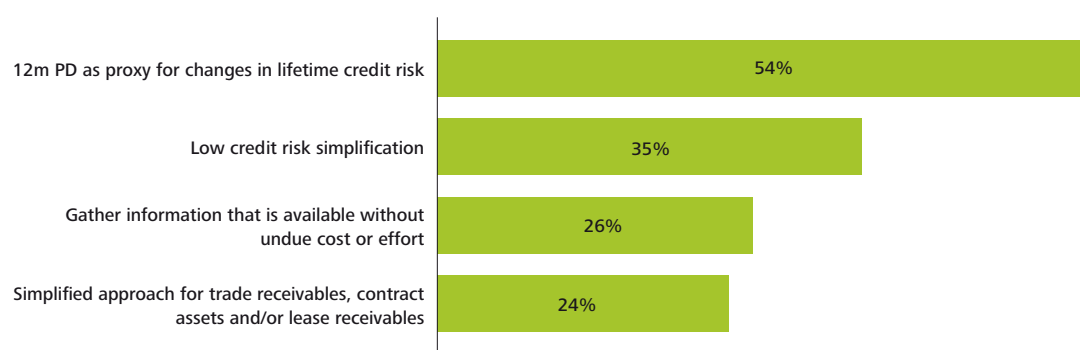
The Basel Committee on Banking Supervision (BCBS) published a consultation in February 2015 containing guidance on accounting for expected credit losses. The guidance sets out supervisory expectations for banks relating to sound credit risk practices associated with implementing and applying an Expected Credit Loss (ECL) accounting framework. Comprising 11 fundamental principles (eight for banks and three for regulators), the guidance also highlights three IFRS 9-specific requirements ("Loss allowance at an amount equal to 12-month ECL", "Assessment of significant increase in credit risk" and "Use of practical expedients") which banks need to consider during their design and build phases.

### Operational simplifications and rebuttable presumptions

The GAECL paper expects that internationally active banks and those banks more sophisticated in the business of lending will not make use of the practical expedients included in the IFRS 9 Standard. The GAECL paper considers that these are intended mainly for entities outside the banking industry.

We were interested in finding out the intention of the participants regarding the use of these operational simplifications.

**Figure 7. Do you expect to make significant use of the operational simplifications available under the IFRS 9 impairment model?**



Twenty six percent of participants do not expect to make significant use of any of the operational simplifications available under the IFRS 9 impairment model in line with BCBS expectations. However, a significant seventy four percent expect to use one or more of the practical expedients available in the Standard.

The operational simplification most expected to be used by these participants is the 12-month PD as proxy for changes in lifetime credit risk.

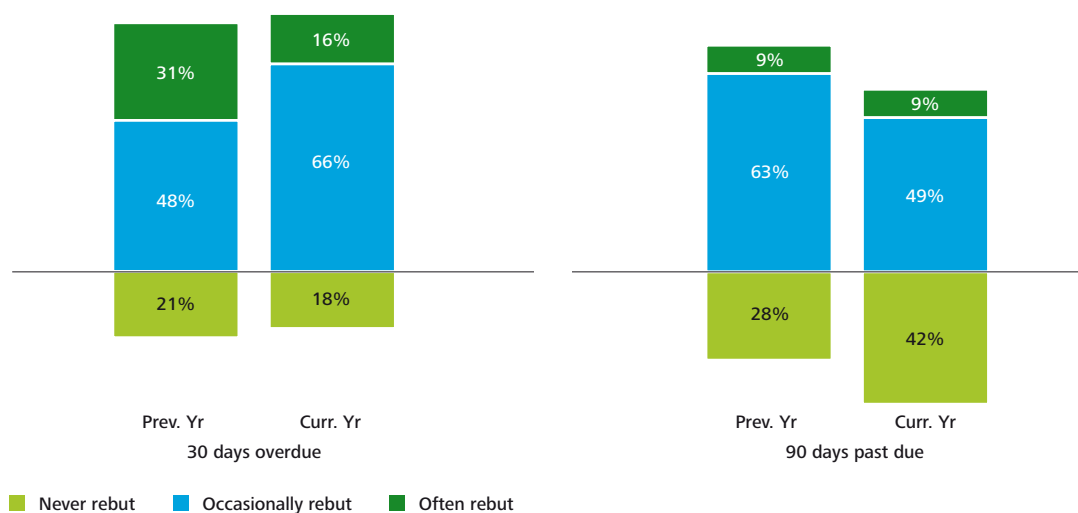
The second simplification most expected to be used is that of 'low credit risk', i.e. not assessing if a significant increase in credit risk has occurred where the credit risk of the loan is considered to be low at the reporting date. This is interesting, especially in light of the BCBS's expectation that "even when a bank assigns a low credit risk rating to an exposure, management should still assess whether credit risk has increased significantly".

Not surprisingly, eighty percent of the respondents that expect to make significant use of this simplification have internal ratings that indicate 'investment grade' across all or the majority of their asset classes. Other key indicators, besides investment grade, that participants expect to use to define low credit risk are 'days past due', 'probability of default', 'debt/capital ratio' and 'internal rating scales'.

The GAECL paper expects banks to use all reasonable and supportable information needed and considers that 'the cost of obtaining relevant information is not [...] likely to involve "undue cost or effort"', given their business.

74 percent of respondents expect to use one or more of the practical expedients available in the Standard.

**Figure 8. Do you expect to rebut the presumption that financial instruments (a) have significantly deteriorated if they are overdue by 30 days and (b) default does not occur later than 90 days past due?**



Sixteen percent of participants expect often to rebut the presumption that loans overdue by 30 days have deteriorated significantly. Those that expect to rebut this presumption have fallen significantly from when we last did our survey which is not surprising given the more conservative approach BCBS expects to see. There are still two thirds of participants that expect occasionally to rebut this presumption, presumably driven by banks experiencing subsequent payments on overdue loans.

Compared to last year banks are less likely to rebut the presumption that by 90 days past due a loan is in default, although nine percent do still expect to do this often and almost half occasionally.



# Impairment models and data

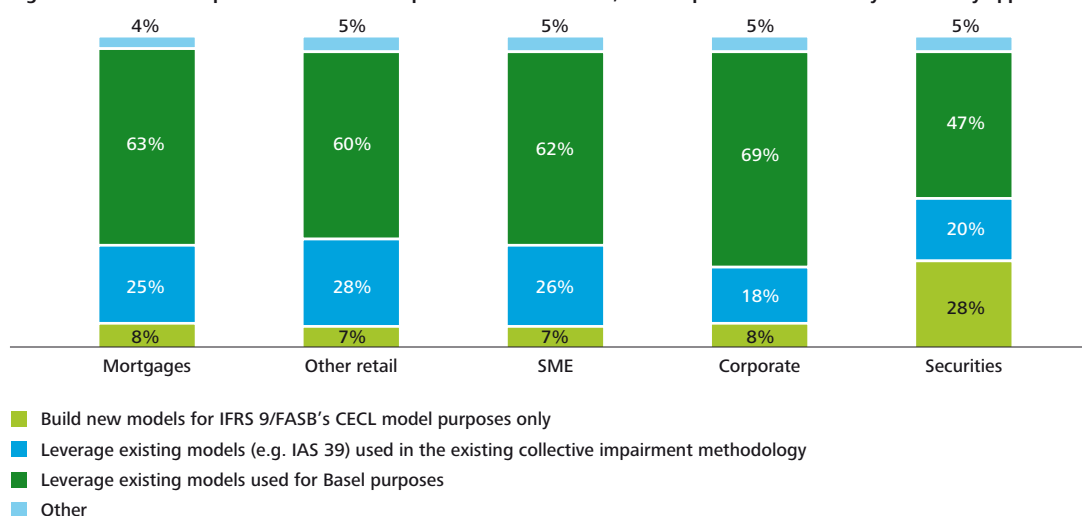
## Impairment models

Existing impairment models based on incurred losses will need to be replaced or the necessary changes implemented to be adapted to the new expected credit losses approach.

The majority of respondents have told us that they are planning to leverage existing models in their organisations to develop their IFRS 9 impairment models, especially existing models used for Basel purposes. Less than ten percent of the participants expect to build new models for IFRS 9 purposes only, with the exception of the securities portfolio. Interestingly, twenty eight percent of participants will not use any previous models for their securities portfolios and will build new ones for IFRS 9 purposes only.

In terms of the level of sophistication that these new or leveraged models will have, almost half of the respondents are planning to implement sophisticated IFRS 9 impairment models, using marginal PDs, complex behavioural measures, extensive macroeconomic factors, Exposure at Default (EAD) and Loss Given Default (LGD), behavioural profiles, etc., with the balance of respondents aiming for intermediate or simple models.

**Figure 9. In terms of impairment model development to deliver IFRS 9, which option best describes your delivery approach?**

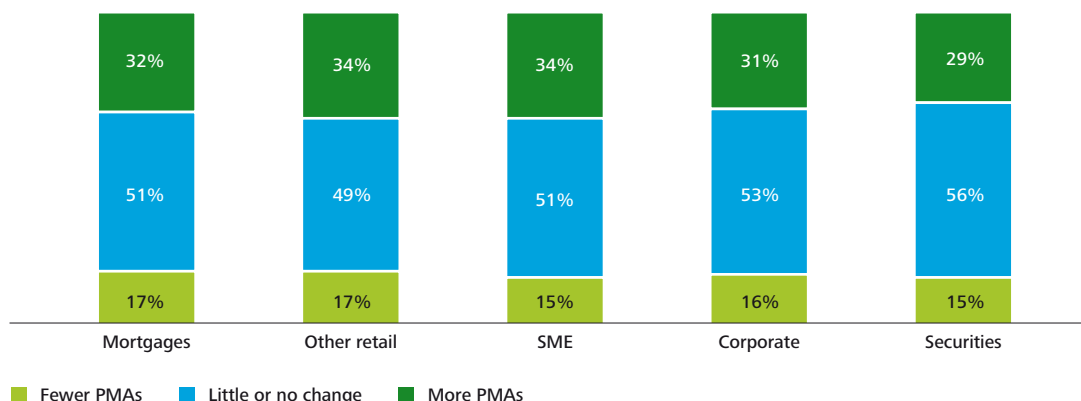


## Post-model adjustments

The majority of respondents do not expect to have an increase in the number of post model adjustments (PMAs) under IFRS 9/CECL when compared to now. Banks believe that the new accounting requirements will increase the number of areas of judgement; however, they expect to be able to have improved and well-controlled governance where that judgement is applied.

Nevertheless, there is a significant minority of respondents that anticipate having an increase in the number of PMAs given the increase in judgemental interpretations that are expected to arise. Some banks estimate that models will not be able adequately to capture all the forward looking information that the ECL calculation requires. Some of the respondents however think that these overlays will decrease as time passes.

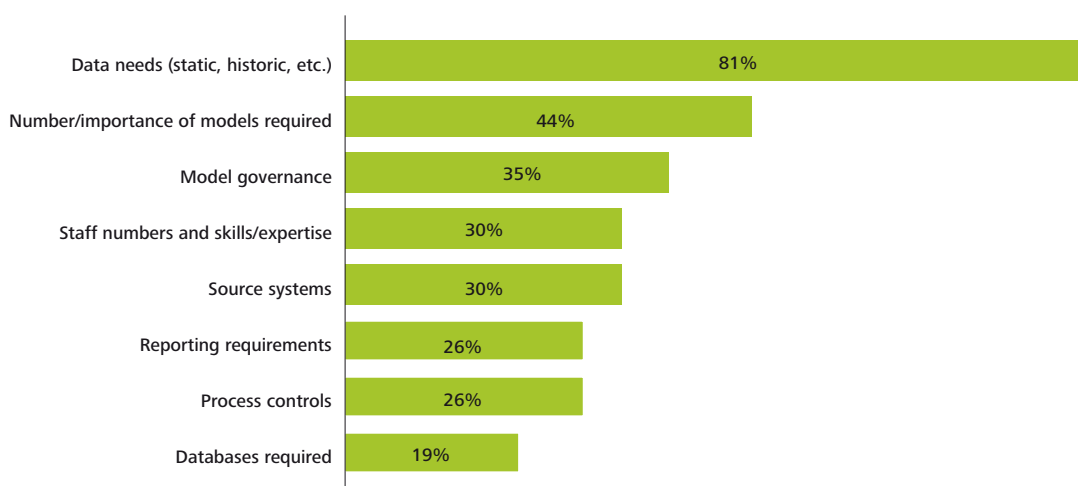
**Figure 10. As IFRS 9 increases the complexity of impairment calculations and introduces additional areas for judgement, do you expect this to change the number of post model adjustments ("overlays") held when compared to IAS 39?**



### Model challenges

Banks see data needs as the biggest model risk challenge under IFRS 9. The number and importance of models required and their governance, while important, are secondary concerns. Banks also note source systems, staff numbers and skills and expertise as areas that will likely pose a challenge. In the case of the former, increased data needs are likely to tie directly to increased database requirements and in the case of the latter, demands on staff may include significant time to develop, support and document assumptions that are integral to modelling IFRS 9.

**Figure 11. Which three factors do you see as the biggest model risk challenges under IFRS 9?**



### Data collection

We asked participants to indicate the key data collection challenges that they expect to face when designing and implementing their IFRS 9 project plan. As we would expect, the major challenge is the availability of historical data. Clearly, banks are concerned they will not be able to gather the necessary data for the estimation of PDs for the lifetime period.

#### Powered by data

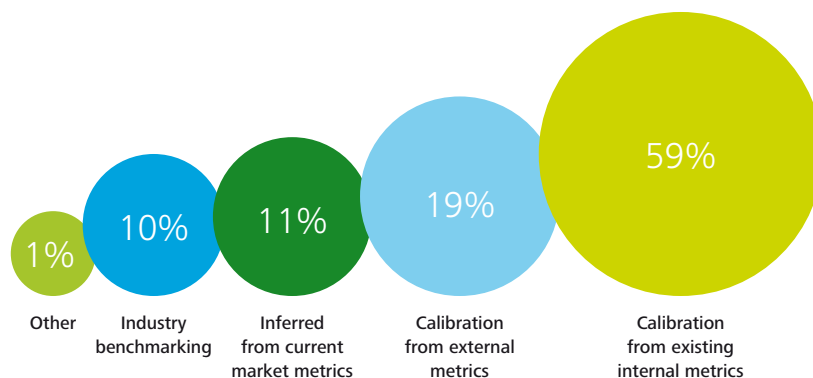
Banks may face their biggest data challenge yet as they prepare to implement changes to accounting for financial instruments. For all institutions IFRS 9 is a fundamental change in the way they measure impairment of financial assets. The robustness, quality and accuracy of data that support impairment measurement will be critical in management, regulators and auditors accepting this new approach.

As well as introducing the need to model losses across the lifetime of an asset; data and their quality, availability and collation will be at the forefront of implementation efforts. The scale of change and difficulty of implementation will be determined by the quality of each bank's data management practices. The following notes some of the challenges banks may have with regards to the data necessary to project the future expected losses and align their model with IFRS 9:

- **Modelling data history:** incomplete data history makes developing a robust and forward-looking expected loss model and achieving effective portfolio segmentation more difficult.
- **Forbearance data:** rich and complete forbearance data will be highly beneficial to IFRS 9 implementation. Data quality standards have improved, driven in part by Basel's focus but there is still room for improvement, supported by a stronger control environment.
- **Consistency and completeness of risk limit data:** these are too often incomplete, inconsistent and not subject to the same controls as balance data. Historic data may sometimes only be obtainable from paper files or by the use of proxies. This will be particularly problematic for manually underwritten and watch list or high risk accounts.
- **Single customer view:** a 'single customer view' is essential to effective credit risk management. IFRS 9 places more emphasis on this concept; data collation and validation will be essential, with data quality under-pinning the successful implementation of a useable single customer data source.
- **Lifetime PD information:** the lifetime modelling of credit risk and deteriorations thereof will be dependent on historic risk grades and expectations of performance across these risk grades. This presents potential issues both in terms of data completeness but also the richness of the data history, especially in a retail environment where it is not uncommon to have assets with term structures beyond 10 years (mortgages).
- **LGD information:** data concerning historic LGD rates, profiles and recovery curves will be an area with particular focus given collateral modelling requirements for IFRS 9 will be more granular than under IAS 39.
- **Behavioural lifetime information:** IFRS 9 introduces the concept of lifetime and behavioural information, unusual in credit risk assessment until now, but well established in insurance. High quality historic default, attrition and recoveries data will be necessary for effective modelling over lifetime.

Overcoming these challenges has the potential for business-wide benefits by allowing better management of financial assets, synergies through consolidation of data and improvements in technology and analytics. These data related improvements across the overall business can have a significant positive impact on the business and allow for more informed decision-making.

**Figure 12. Where Probability of Default (PD) and Loss Given Default (LGD) are used, how do you expect to approach data gathering?**



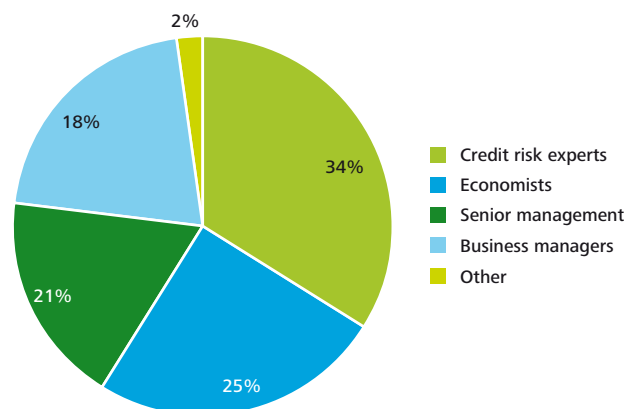
Banks' proposed approach to data gathering where they use PD and LGD will be primarily led by their existing internal metrics, followed by external metrics and inferred from current market metrics.

#### Forward-looking information and macroeconomics

The new impairment rules will require banks to incorporate into their expected credit loss calculations all relevant information, including forward-looking information and macroeconomic factors, so the recognition of the expected credit losses is not delayed.

Banks have told us that they will rely in the first place on credit risk experts when selecting forward looking information relevant to the bank's credit risk profile. Economists are cited as the second key experts expected to be involved in this process.

**Figure 13. When selecting forward looking information relevant to the bank's credit risk profile, who will be the key experts involved?**

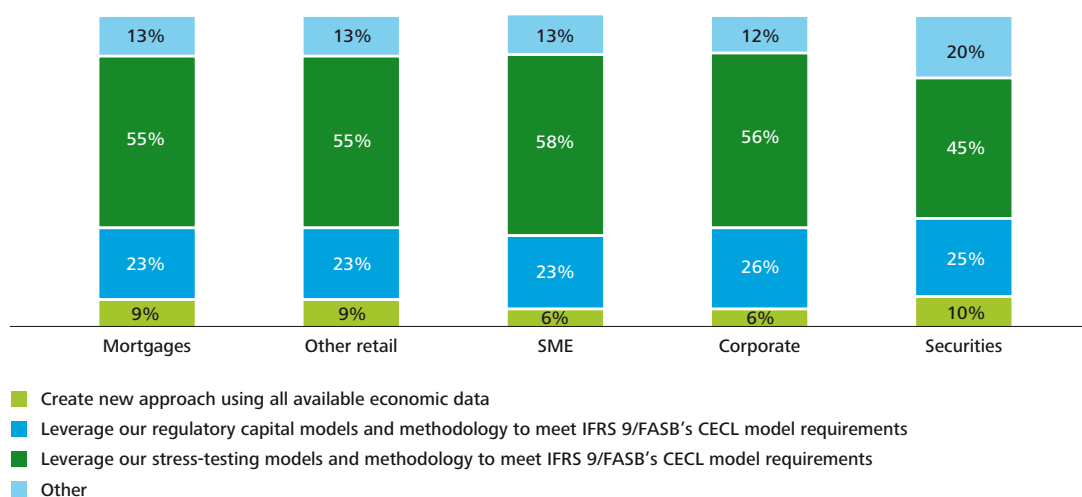




We were interested as well in finding out whether banks were planning to create new approaches to forecast future economic conditions or if they were expecting to leverage existing models in their organisations.

Not surprisingly, given the scale and volume of changes that banks will have to face to implement the new impairment requirements, across all portfolios, fewer than ten percent of respondents are considering implementing a new approach using all available economic data. The majority of banks will leverage their existing models and methodology, either those used for stress-testing (around fifty five percent of respondents) or their regulatory capital models (around twenty five percent of respondents).

**Figure 14. How do you intend to forecast future economic conditions?**



## Data challenges

**Figure 15. What are your biggest concerns about using credit risk management systems and data for financial reporting purposes?**



Consistent with the results of the fourth survey, when it comes to using credit risk management systems and data for financial reporting purposes, reconciling financial reporting and credit data continues to be the area of greatest concern with data quality being second; the gap however between these first two concerns has noticeably narrowed and concern is shifting to quality of audit trail and governance.

These findings are consistent with the recent Asset Quality Review (AQR) exercises and ECB stress testing where the following key areas of challenge were noted:

- sourcing and reconciliation of data;
- strong quantitative modelling;
- design of an appropriate and effective governance structure throughout the organisation;
- clear communication and understanding of underlying methodology and assumptions; and
- lack of resource availability, in particular amongst key teams and subject matter experts.

#### **Auditing challenges**

IFRS 9 represents a challenge for preparers, investors, securities regulators, prudential supervisors and auditors. For the latter, the transition to the inclusion of expected credit losses in audited financial statements will lead to new audit approaches being developed, using appropriately skilled and experienced auditors to execute impairment audits, and auditors applying consistent approaches across organisations (both banks and audit firms).

The audit of estimates based on forecast economic data is not new to financial reporting but IFRS 9 greatly broadens the scope of this work. Assessing the robustness of judgements, including the governance and controls around judgements that are used as a basis for estimating expected losses, will be a critical part of auditing the implementation of IFRS 9.

The measurement of expected credit losses will have to include historical, current and forecast information. A sound assessment of the policies, processes and controls of the entity around this area to ensure that all reasonable and supportable information is considered will have to be performed.

Auditors will play a key part in achieving an effective implementation of IFRS 9 through a consistent audit approach – together with prudential supervisors and securities regulators – across multiple geographies. However, national competent authorities also have an essential role in this process, where taking as consistent as approach as they can, jurisdiction by jurisdiction, will be fundamental in minimising the differences across geographies and will help banks trying to apply a consistent approach when implementing the new requirements across their international organisations.

The previously referenced BCBS' GAECL paper includes principles around supervisory practices. However, it is important to highlight that the opinion of statutory auditors is expressed by reference to an accounting framework as issued by local or international standard setters (local GAAP, IFRS or US GAAP). Because the BCBS guidance is not part of those accounting frameworks, there may be situations in which statutory auditors issue an unqualified audit opinion on a bank where there is not full compliance with the guidance, or where compliance with the guidance has not been assessed as it is not part of the scope of a statutory audit.

A consistent supervisory approach as a result of the joint work of national supervisors and the BCBS will be a crucial step towards the effective implementation of IFRS 9.

We were interested in knowing whether the AQR exercise carried out in Europe or the Comprehensive Capital Analysis and Review (CCAR) performed by the Federal Reserve Board helped in any way to improve data quality of participants. Sixty four percent of respondents believe that these assessments have been or will be helpful in improving their data quality. Examples include the alignment of credit risk assessment driven by the cooperation between business units or the greater coherence between banks in different countries with different regulators.

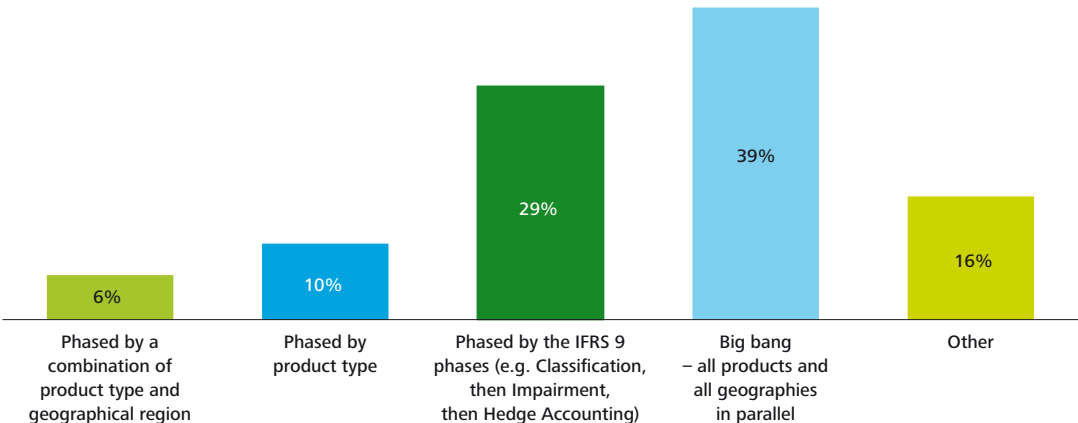
Lessons learned from these exercises may provide banks practical insights on the collection, integrity and effective use of data.

We also asked participants whether they anticipate any changes to the way they calculate and use EIR under IFRS 9 when compared to IAS 39 – in contemplation that the introduction of IFRS 9 might allow them to reconsider the validity of their historic approach. A vast majority of participants do not expect to make any changes in this area.

# Implementing your IFRS 9/CECL programme

## Approach and challenges

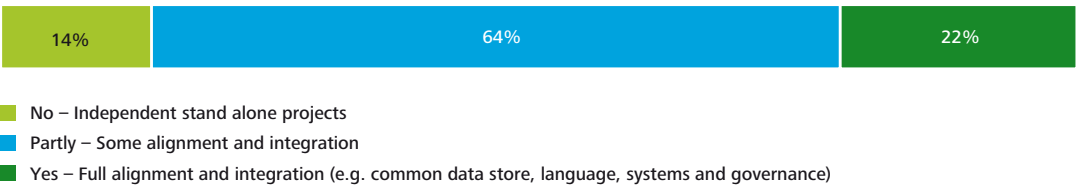
Figure 16. Which approach best describes your IFRS 9 implementation project plan?



The most popular approach amongst the respondents is to implement all phases, including all products and geographies, at the same time, with phasing by the IFRS 9 phases (e.g. classification, then impairment, then hedge accounting) not far behind in second.

Not surprisingly, the majority of the largest banks surveyed are planning to implement all products and phases at the same time, while smaller banks are more inclined to phase the project by the IFRS 9 phases.

Figure 17. Will you use IFRS 9 as a catalyst to align between accounting impairment and regulatory capital processes?

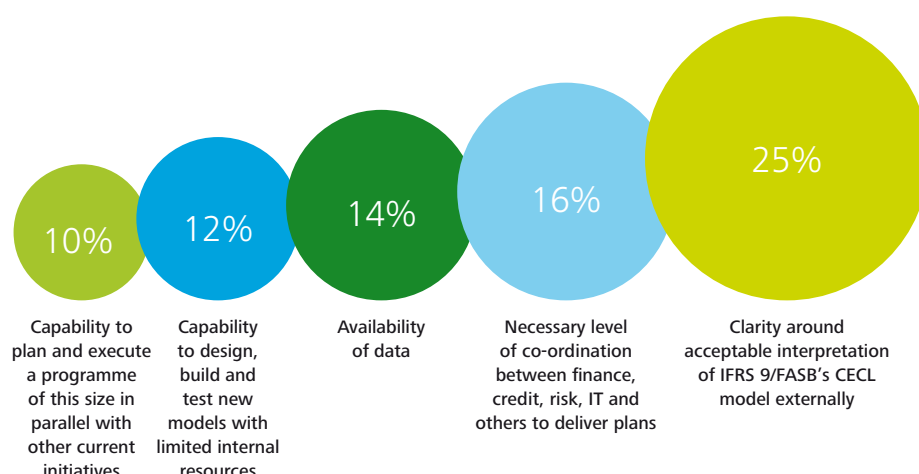


The vast majority of respondents believe that there is a clear relationship between accounting impairment and regulatory capital processes under IFRS 9: twenty two percent will consider full alignment and integration and sixty four percent will involve partial implementation. Only fourteen percent of all respondents see the two processes as mutually exclusive projects.

We were interested in finding out which elements respondents within the “partial alignment” group are expecting to align and interrelate. Half of this group does not know yet since the scope of the alignment is yet to be defined, with others consistently citing data, systems and governance.



Figure 18. What do you see as the 3 biggest challenges to implementing your IFRS 9 programme?

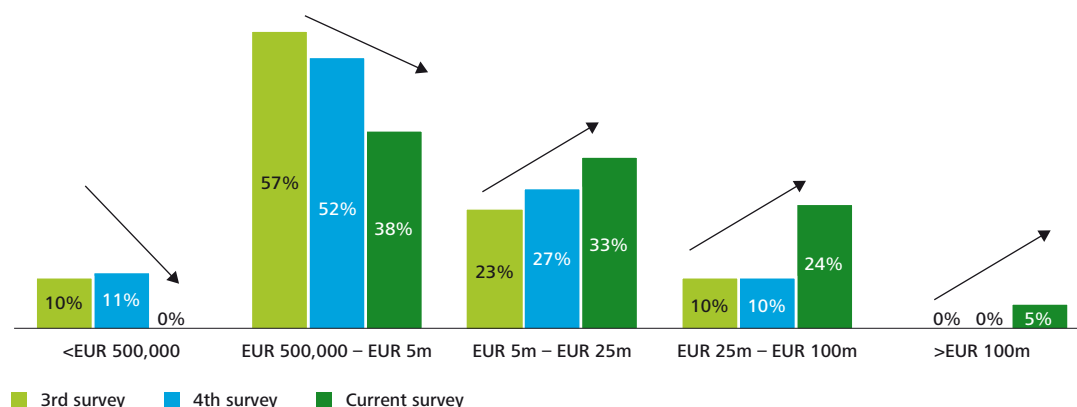


A quarter of banks believe the biggest challenge faced while implementing their IFRS 9 programmes will be the interpretation of IFRS 9 requirements. This is unsurprising given the high degree of complexity and judgement required under IFRS 9. Integration between business areas is considered the second largest challenge faced. IFRS 9 requires more integrated processes and controls among key areas of the business. Data availability is deemed third most significant. IFRS 9 has a much larger data requirement than IAS 39 both in terms of historical data and data quality and reliability for projections. There are also concerns over the amount of resources required both to implement and to validate new models and to execute the IFRS 9 projects in conjunction with other initiatives.

### Project management

We asked participants to indicate their estimated costs for their initial implementation of IFRS 9 as well as the ongoing costs once IFRS 9 is applied.

Figure 19. What is your estimated total budget (including all internal and external costs) to change to a fully compliant IFRS 9 programme?



A quarter of banks believe the biggest challenge will be the interpretation of IFRS 9 requirements.

## The average of budgets has doubled in the year to €25m.

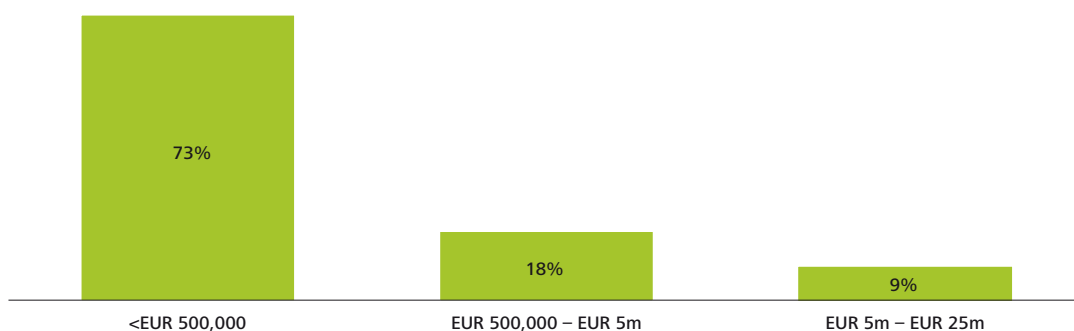
Sixty four percent of respondents indicated that they did not know what their estimated total budget was to change to a fully compliant IFRS 9 programme. The average of budgets this year has doubled in the year to €25 million up from €12 million last year (and €11 million in 2013) which is likely to be as a result of banks revising their estimates of the amount of effort involved both with the release of the finalised standard, and reflecting banks' expectations given experience in other regulatory exercises including the recent stress tests.

There is a predictable trend in terms of budgets, where the largest banks with total assets over €300 million expect to have to invest more than €5 million, while banks whose total assets are below that figure have, overall, estimated budgets between €500,000 and €5 million.

By regions, banks in EMEA have the highest anticipated budgets for their IFRS 9 programmes, with an average of almost €40 million. On the opposite side, the averaged budgets for banks in the Americas are in the region of €6 million, presumably affected by the fact that the FASB's CECL model has not been yet published.

In terms of the business as usual incremental costs after the implementation process, banks' responses varied. Only 11 participants provided an indication as to the anticipated total annual additional incremental cost of running their IFRS 9 solution, once it is part of business as usual, as compared to their current IAS 39 model. Seventy three percent believe that the total annual additional incremental cost of running their IFRS 9 solution once it is part of their business as usual will be less than €500,000 when compared to their current impairment model whereas eighteen percent (two banks) think that this annual incremental cost will be between €500,000 and €5 million, and the remaining bank think that it will be between €5 million and €25 million. The fact that not all respondents have replied to this question indicates a degree of uncertainty regarding total cost; consistent with the revisions to total budgeted costs as discussed above, estimating these costs is difficult and such estimate is likely to evolve as entities develop their IFRS 9 implementation plans.

**Figure 20. What do you anticipate the total annual additional incremental cost will be of running your IFRS 9 solution (once it is part of your business as usual) when compared to your current IAS 39 model?**

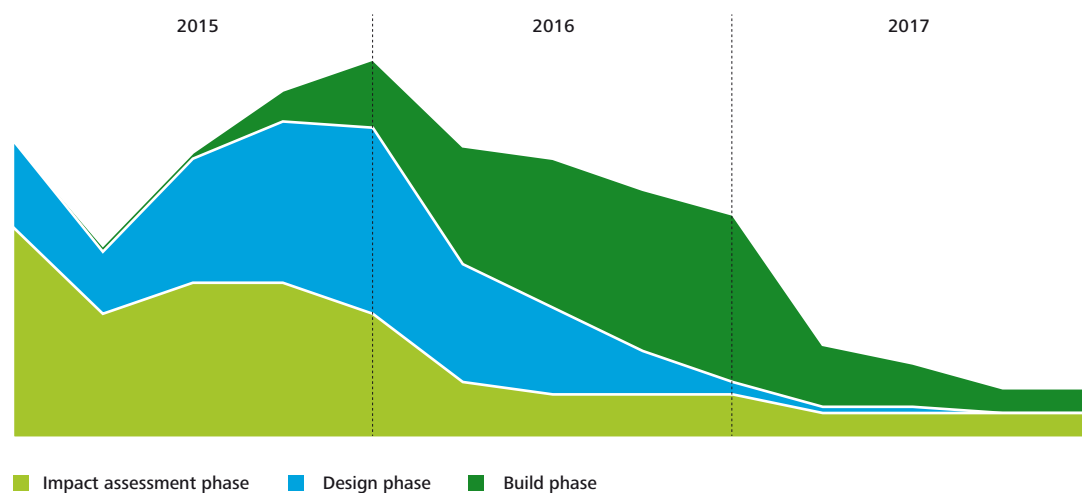


In terms of timing, twenty percent of respondents report having already completed the impact assessment phase prior to 2015. An additional fifty three percent of respondents anticipate completing this phase by the end of 2015

As may be expected, banks are not as far along on the design phase with only ten percent reporting having completed this phase prior to 2015, and an additional sixty percent anticipating completion by the end of 2015. Finally in respect of the build phase, while none of the respondents reports having completed this phase prior to 2015, thirteen percent anticipate completing this phase during 2015 with a further sixty nine percent anticipating completion by the end of 2016. Completion of the build phase prior to 2017 will enable banks to carry out a dry run of their models during 2017 prior to the IFRS 9 effective date. Seven banks reported not knowing when any of the three phases would be started and consequently end; a further three respondents have varying plans to start respective phases however have no planned end date.

Given banks indicated in our fourth survey that they require 3 years implementation time, where plans are not in place already, a timeline for implementation is considered critical.

**Figure 21. When do you anticipate starting and finishing (or when have you already started or finished) the following project phases relating to your IFRS 9 impairment implementation plan?**



#### A closer look: IFRS 9 adoption in Canada

Canadian Domestic Systemically Important Banks (“D-SIBs”) are required by the Office of the Superintendent of Financial Institutions (“OSFI”) to adopt the requirements of IFRS 9 as at 1 November, 2017, with published IFRS 9 figures to be produced as at January 31, 2018, the first quarter of IFRS 9 adoption.

In anticipation of this, the Canadian D-SIBs are well on their way through the assessment phase of the impact from IFRS 9 and related standards. This assessment phase includes:

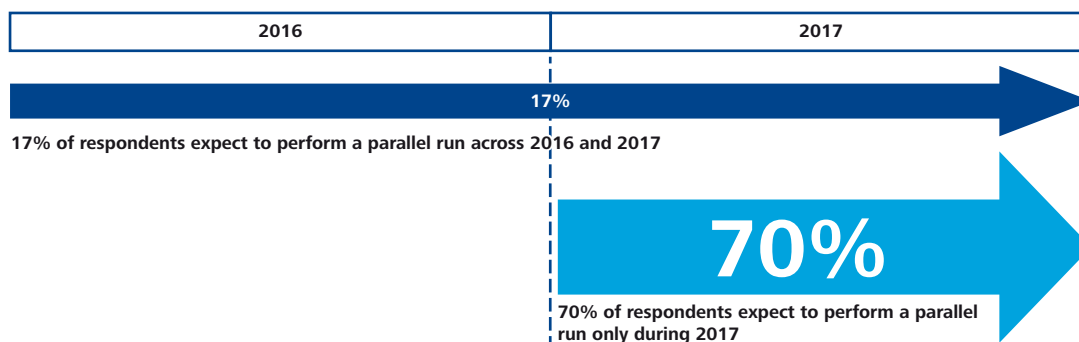
- Determination of key target state decisions required in the near term to obtain consensus for the purpose of creating an IFRS 9 implementation plan.
- Monitoring of best practices through peer experience both within and outside Canada to operationalise target state requirements such as the monitoring mechanism for the deterioration of credit risk, methodologies to incorporate macroeconomic factors into financial reporting impairment assumptions and tracking of data requirements at the asset versus portfolio level.

The majority of respondents are planning to have a one-year parallel run between their IFRS 9/CECL approach and their existing approach, with a minority allowing time in their project’s timelines for a two-years parallel run. This means banks have only one year and a half to design, build and test their new models (half year for those who are planning a two-years parallel run).

It is noticeable that thirteen percent of respondents think they will not perform a parallel run and they will calculate IFRS 9 real numbers for the first time at the effective date.

Respondents that favoured a parallel run across both 2016 and 2017 are almost entirely from the Americas and Asia Pacific regions, with only one respondent from the EMEA region.

Figure 22. To what extent are you considering a parallel run between your IFRS 9 approach and the existing IAS 39 approach?



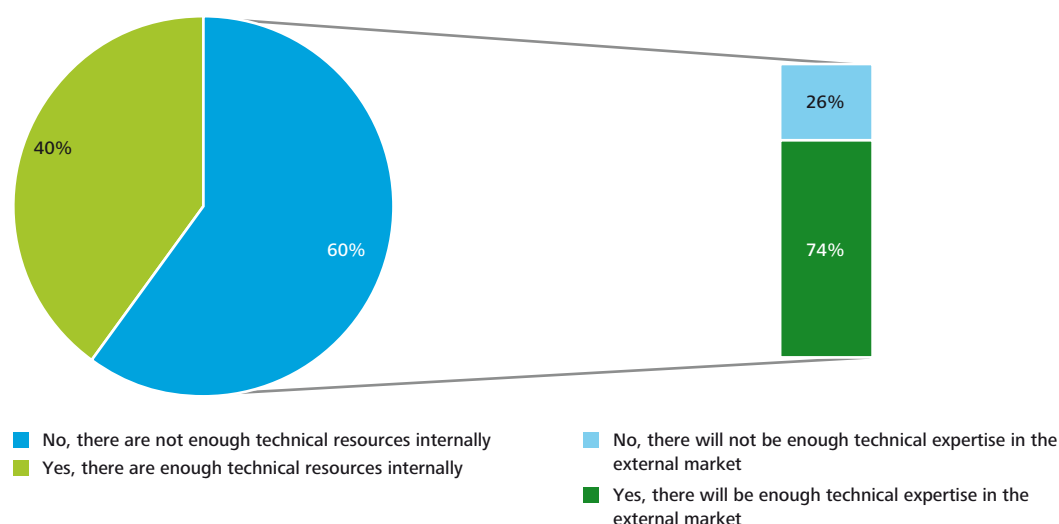
13% of the participants have no plans to implement a parallel run.

## Responsibilities and Resources

We asked participants to express their views on the technical resources available to deliver their IFRS 9 projects. Sixty percent of banks have told us that they believe there are not enough technical resources inside their organisations to deliver their IFRS 9 projects. Three quarters of these expect this shortfall of technical expertise to be available in the external market. However, it is of note that the remaining twenty six percent of respondents do not believe that there will be enough resources in the external market.

The expected shortage of internal expertise is consistent with the implementation challenges noted in the fourth survey as well as findings coming out of recent AQR and stress testing exercises.

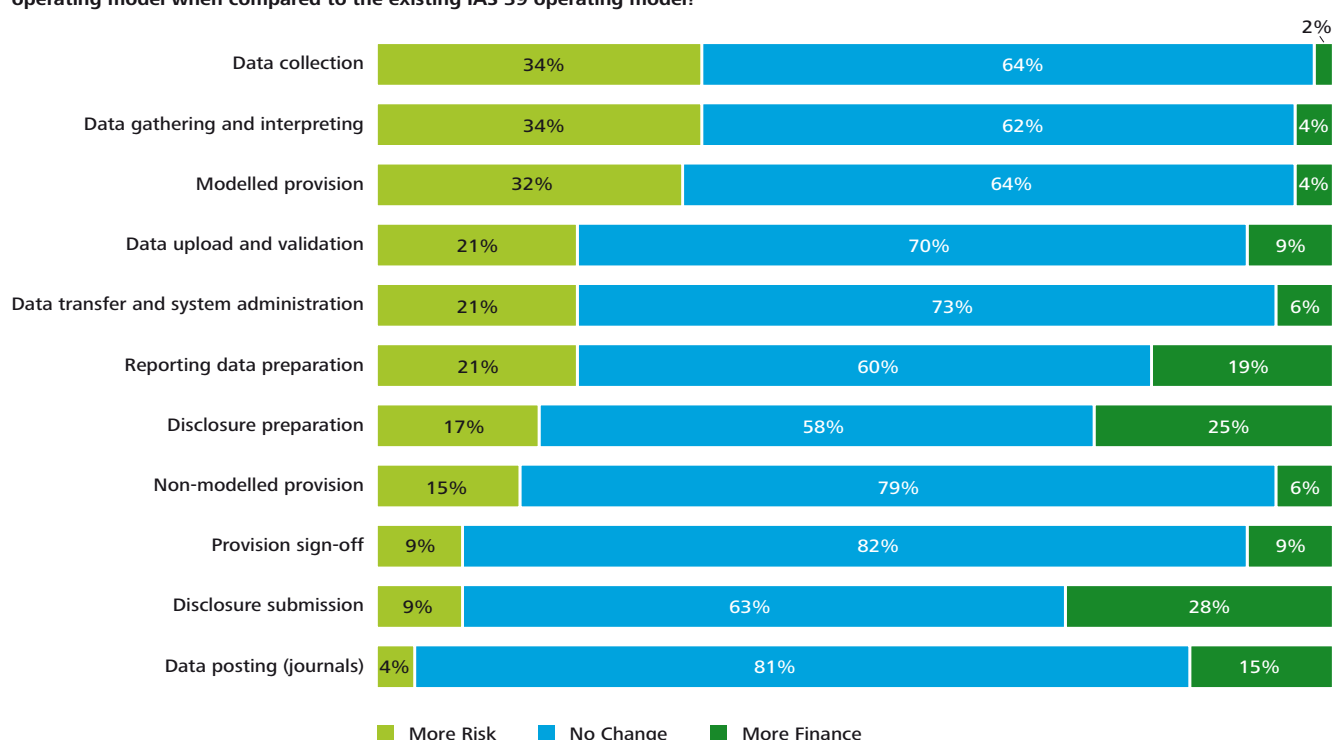
**Figure 23. Do you believe there are enough technical resources available inside your organisation to deliver your IFRS 9 project? If 'no', do you think there will be enough technical expertise in the external market to cover any shortfall of internal resources across the industry?**



60 percent of banks believe there are not enough technical resources inside their organisations to deliver their IFRS 9 projects.

IFRS 9 will lead to Risk and Finance working more closely together. We wanted to better understand bank's views on how IFRS 9 will change the distribution of tasks between the two groups.

**Figure 24. To what extent do you think the division of labour between Risk and Finance will change under the new IFRS 9 impairment operating model when compared to the existing IAS 39 operating model?**



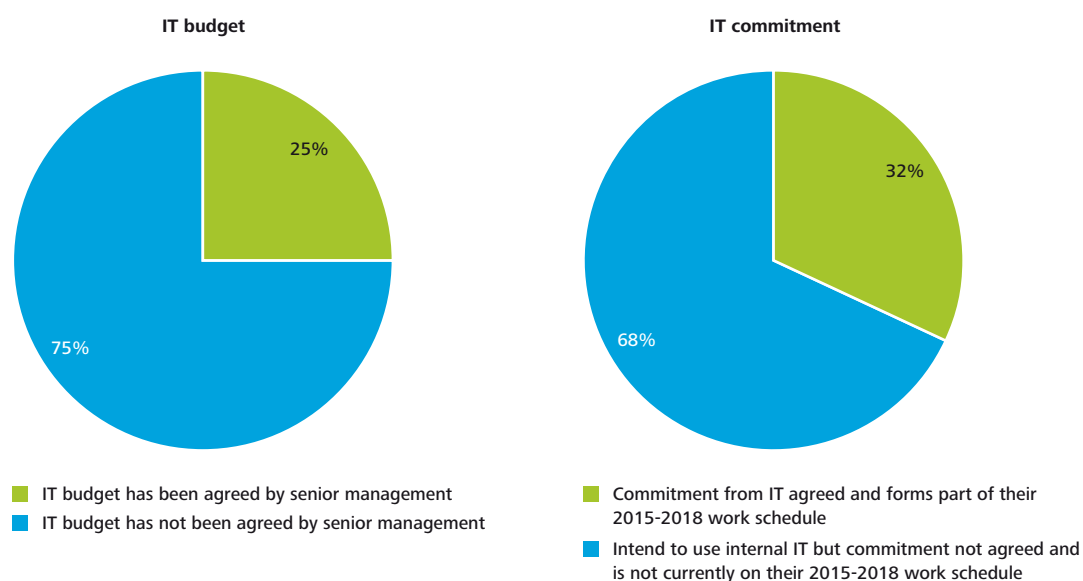
While the majority of respondents expect no change overall in the division of labour between Risk and Finance, just over a third of respondents expect a shift in responsibility to Risk in the areas of data collection and data gathering and interpreting and just under a third expect a shift in responsibility towards Risk for the modelling of the provision. Notably there is a shift of responsibility for disclosure preparation and disclosure submission where a greater involvement of Finance is expected.

These shifts in responsibility may demand more effective coordination amongst Finance and Risk especially in cases where reconciliation of data between Finance and Risk is required.

Virtually all banks report that currently the Risk/Credit Risk function has the greater role in calculating provision numbers.

## Systems/IT

Figure 25. IFRS 9 is likely to require new systems or enhancements to existing systems. Which option best describe the position of IT in your IFRS 9 delivery plan? (where internal IT function will be used)



Given the expectation of IT system changes across the majority of banks as indicated in our fourth survey, results indicate this will likely become a focus area. All respondents expect to have their IT function involved in their IFRS 9 project, alone or together with external third party vendors.

Focusing on banks' internal IT function, only twenty five percent reported having an IT budget agreed to by senior management and only thirty two percent reported having a commitment from IT that is agreed to and incorporated into the IT group's 2015-2018 work schedule.

Given expected internal constraints both amongst technical and IT resources, finalising budgets and securing adequate external resources would appear to be a key success factor for a bank's IFRS 9 project.



**Figure 26. Where system build/enhancements form part of your IFRS 9/CECL implementation plan, how flexible will this solution be in meeting additional regulatory requirements (e.g. US GAAP; EBA Forbearance; BCBS239; Basel 3; CRD4)?**



- No flexibility. Solution caters for known requirements only
- Some flexibility. Solution allows changes to existing specification only, but new requirements will be addressed via system 'bolt-ons'
- Very flexible (industry leading). Solution designed to incorporate all known regulatory requirements and new requirements can easily be added

Solutions that offer some flexibility via system "bolt-ons" are expected in sixty eight percent of cases. Only twenty one percent of respondents plan to implement an industry leading solution where new requirements can be added on easily and eleven percent have chosen a solution that offers no flexibility and caters to known requirements only.

Looking at the results by geography, the vast majority of banks that are planning to have a 'very flexible' solution are within the EMEA region, while almost all the banks that answered "no flexibility" are based in Asia Pacific.

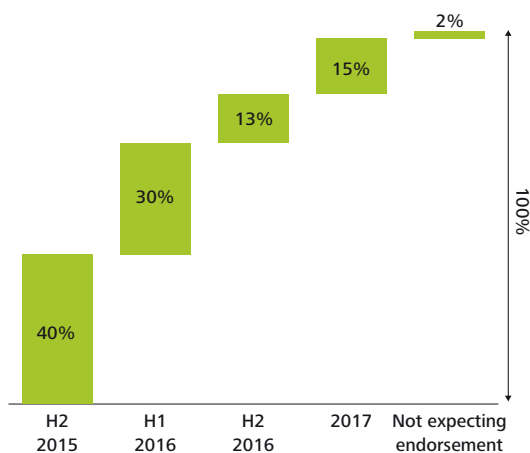
It appears that, perhaps consistent with the increasing expected cost of implementing banks' IFRS 9 solution, banks have settled on a solution that supports current requirements with flexibility to add on new requirements as needed.

# Other considerations

## EU Endorsement

At the time of sending the survey to participants, EFRAG's draft endorsement advice had not been published. Without this information that is now available, we asked their views on expected timings of endorsement in the EU. We were interested in knowing whether the uncertainty of EU endorsement would cause the postponement of part of their IFRS 9 project.

Figure 27. When do you expect IFRS 9 to be endorsed for use in Europe?

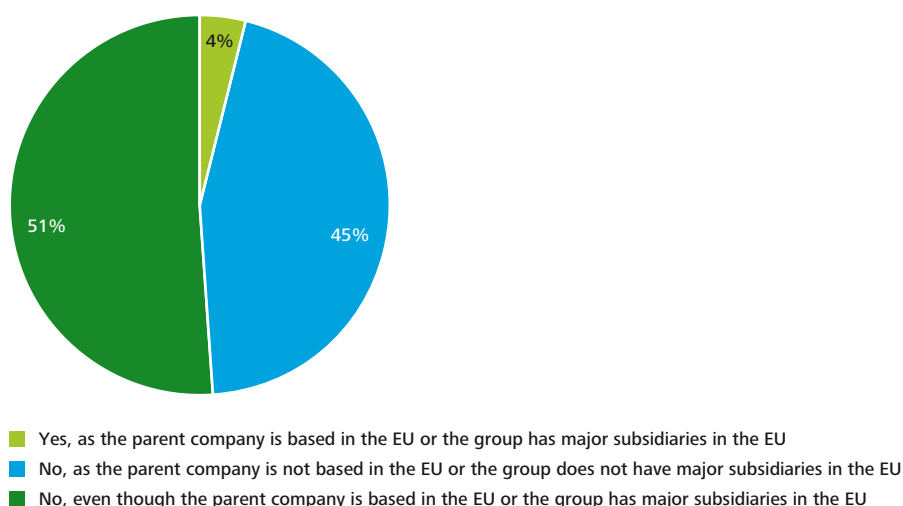


More than two thirds of respondents expected endorsement of IFRS 9 to take place between the second half of 2015 and the first half of 2016, with the remainder expecting a later date towards the second half of 2016 or 2017. It should be noted that all respondents except one expect IFRS 9 to be endorsed for use in the EU.

The majority of banks (ninety three percent) directly affected by the EU endorsement of IFRS 9 (either because the parent company or a significant subsidiary is based in the EU) have told us that they will not postpone their IFRS 9 implementation project as a result of uncertainty in the timing of endorsement. Clearly, banks are concerned about the tight deadlines: in their own words "The already limited time for implementation does not allow for any postponement" and "IFRS 9 needs to progress now to ensure a high quality implementation with a 2017 parallel run".

Additionally, banks with subsidiaries in both the EU and in other regions have remarked that even if IFRS 9 were not endorsed in the EU they would still have to calculate expected credit losses in their outside-EU subsidiaries and, therefore, they too will not be postponing their IFRS 9 implementation plans.

**Figure 28. Will the uncertainty around timing of EU endorsement of IFRS 9 result in the postponement of a significant portion of your IFRS 9 implementation project?**



### Using the new information

**Figure 29. Will financial statement users be better able to compare banks globally under IFRS 9 than under IAS 39 with respect to impairment of financial assets?**



Views are mixed whether the impairment requirements under IFRS 9 will lead to more or less comparability in financial results across banks. Almost half of the participants believing that financial statements will be less comparable under the new standard, with the other half believing there will be no change or an improvement in comparability. This is broadly consistent with the results of our fourth survey.

We have noted in the responses received that one of the key factors that drive banks' views on financial statements' comparability is the increment in judgemental areas, such as forward-looking information and the transfer criteria between stages 1 and 2. IFRS 9 being principles-based and the fact that FASB and IASB did not reach convergence are other reasons noted by respondents.

The extensive disclosure requirements are expected to improve comparability slightly, but will not, in participants' views, solve the problem.

The EDTF is developing guidance for banks' credit risk disclosures in the light of ECL approaches under IFRS 9 and forthcoming CECL. Even though it will probably aid comparability, challenges will likely remain given the differences in approach permitted under IFRS and US GAAP.

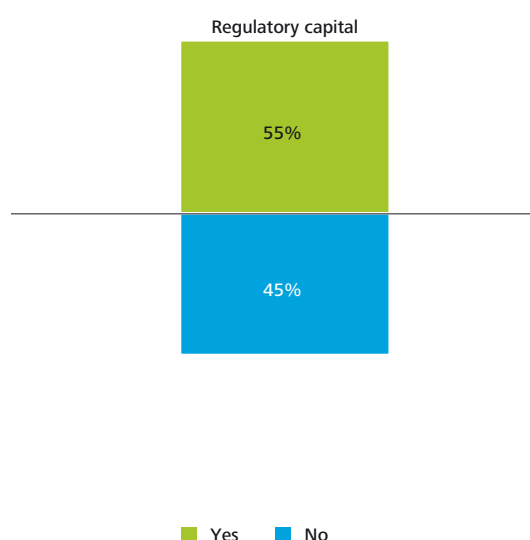
**Figure 30. Do you think regulators will find IFRS 9 information more appropriate for supervision purposes than that prepared under IAS 39 regarding Impairment requirements?**



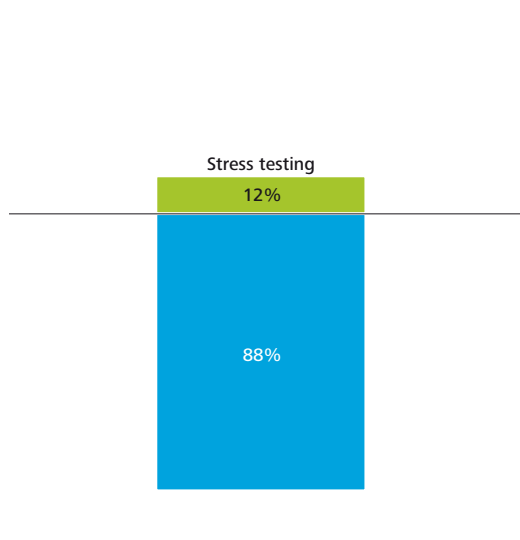
Despite some negative responses on the comparability of financial statements, the vast majority of respondents (seventy six percent) are of the impression that regulators will find IFRS 9 information more appropriate for supervision purposes, as opposed to only nine percent who believe the opposite. The views of banks in this area are similar to that of last year's survey.

### Estimating ECL before 2018

**Figure 31. Are you planning to incorporate your IFRS 9 impairment estimates for regulatory capital planning purposes?**



**Figure 32. Has your regulator requested that you include your IFRS 9 impairment numbers into your stress testing scenarios through 2018?**

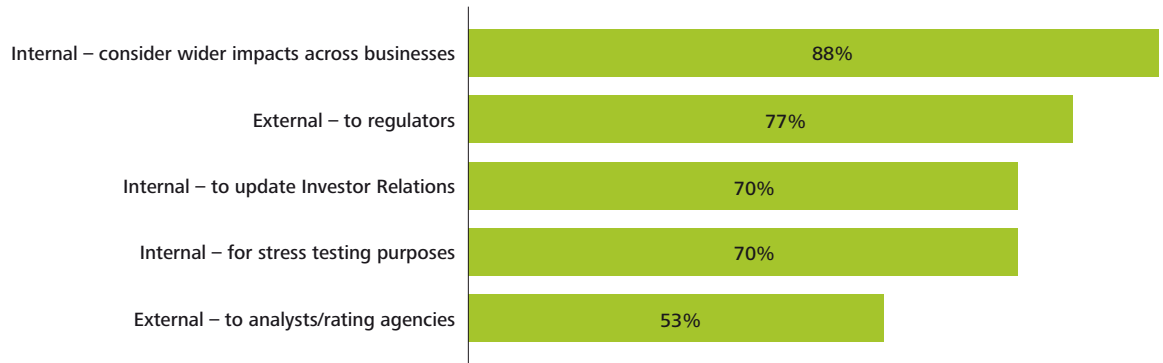


More than half of the respondents are planning to incorporate IFRS 9 impairment estimates for regulatory capital purposes. This is a good indicator of the significance placed on the IFRS 9 impairment estimates by banks.

Yet only a minority of the banks have been asked by their regulators to include IFRS 9 impairment numbers into their stress testing scenarios. It is interesting to note that the majority of banks are already planning on incorporating impairment numbers for regulatory capital planning purposes, even without the majority having a formal requirement for stress testing purposes.

The vast majority of respondents are of the impression that regulators will find IFRS 9 information more appropriate for supervision purposes.

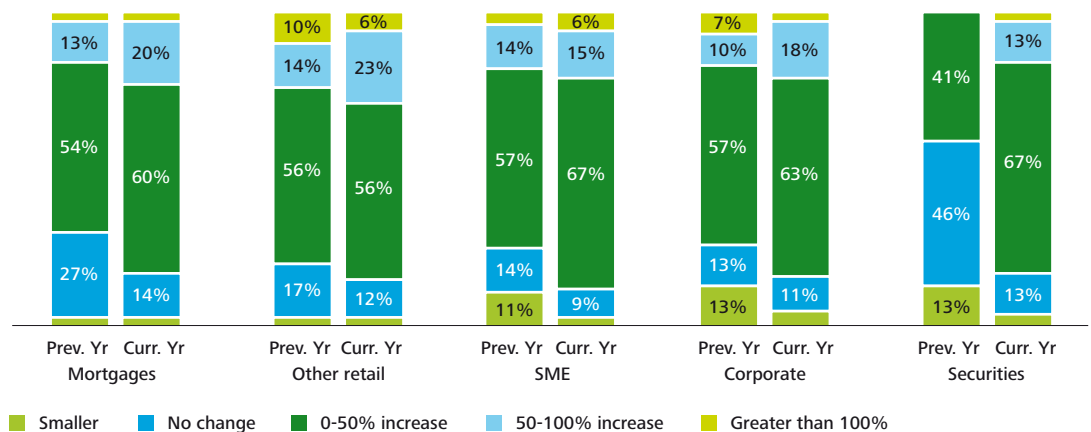
**Figure 33. Do you expect to have to estimate your expected loss provisions under IFRS 9 before 2018 for communication with:**



Almost all banks (ninety six percent) anticipate estimating their expected credit loss provisions under IFRS 9 before the 2018 effective date. The majority of banks expect to communicate this estimate to each of the internal and external groups and stakeholders listed above.

### How will impairment provisions change?

**Figure 34. Assuming today's credit environment were to apply, how is your bank's total impairment provision in the balance-sheet likely to change on transition to IFRS 9?**



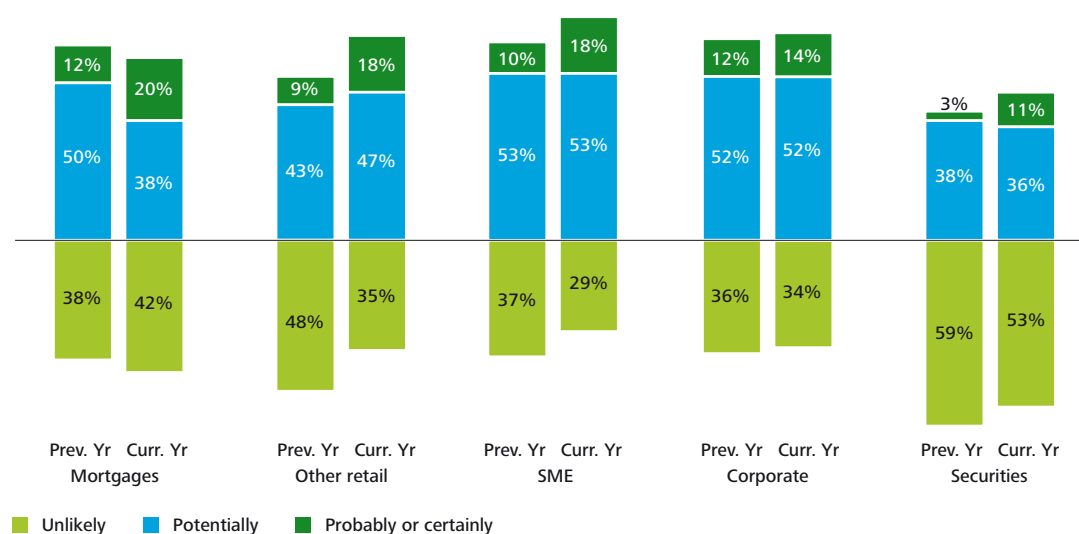
\* Responses given are high level estimates that do not consider 2018 economic conditions and do not necessarily reflect the transition impact in 2018

The majority of banks expect impairment provision to increase by up to 50 percent.

Across each category, the majority of banks consistently report they do not expect the total impairment provision in the balance sheet to change by more than fifty percent. These expectations remain broadly consistent with the results from the fourth survey. Across all categories, and in particular in the areas of mortgages and securities, banks expect additional change to the total impairment provision in the balance sheet on transition to IFRS 9 as is shown by the decrease in the percentage of respondents indicating "no change" in the current year as compared to the previous year. This may in part be due to results of the recent AQR exercises which indicated that in some cases higher levels of provisions are required and also due to the realisation that a provision for impairment will apply to all securities where under IAS 39 impairment of securities was less common.

## The impact of IFRS 9 on product pricing

Figure 35. Do you think moving to an expected loss impairment model will affect the pricing of the following products?



We have been asking banks since the launch of our survey in 2011 if IFRS 9 will impact the pricing of the products they offer given it is expected that additional provisions for impairment will negatively impact regulatory capital. With the exception of mortgages, where there was a slight increase in the percentage of respondents that considered an impact on pricing to be unlikely, banks are increasingly of the view that pricing will be impacted on moving to an expected loss impairment model. One bank noted that the “expected loss impairment model will necessarily be taken into account when implementing a new product”; another respondent noted that “enhancements to risk models [were] already impacting [...] pricing” and that pricing may be more favourable under an expected loss impairment model where it reflects “efficient pricing of risk”.

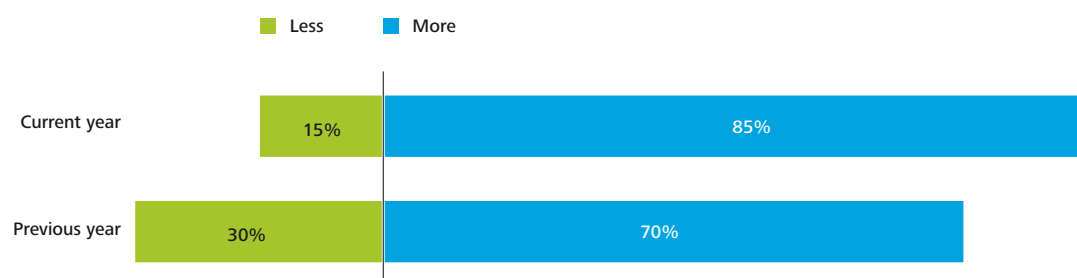
While a number of respondents noted pricing would likely to be less favourable for customers, a number of banks also noted this was dependent on understanding the full impact of IFRS 9 to capital requirements including any regulatory measures that may offset potential negative capital implications. As such impact is not yet fully known, neither is the full implication on pricing and the business.

## Interaction between loan impairment and regulatory capital

Consistent with the fourth survey, we wanted to understand banks’ views on the linkage between Internal Ratings Based (IRB) approaches under Basel and IFRS 9 approaches to Expected Credit Losses (ECL) as we believe the current relationship, whereby Basel regulatory measure of EL is in nearly all cases higher than the current level of impairment provision taken under IAS 39, will change under IFRS 9. As not all of the banks in our survey are within the Basel framework and of those not all of them use an IRB approach, our analysis of figures 36 and 37 is based on replies from approximately eighty percent of our survey population. The comparative figure from the fourth survey reflects replies from half of the survey population in the previous year.

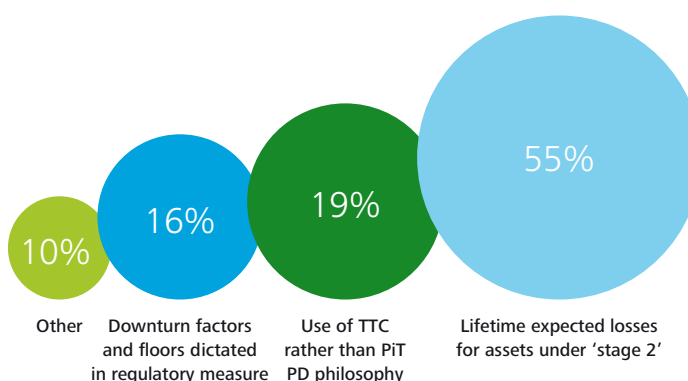
85 percent of respondents anticipate the ECL provision will exceed that under the Basel IRB regulatory capital approach.

**Figure 36. Do you expect your IFRS 9 expected credit loss provision to be more or less than your existing expected loss calculation under the Basel Internal Ratings Based regulatory capital approach?**



With the publication of the final standard, eighty five percent of respondents, up from seventy percent in the previous year, anticipate the expected credit loss provision will exceed that under the Basel IRB regulatory capital approach, and therefore lead to an increased core tier one capital requirement for banks under current capital rules.

**Figure 37. What do you see as the biggest contributing factors to differences between Internal Rating Based expected loss and IFRS 9?**



The majority of responses point to lifetime expected losses for assets under 'stage 2' as being the biggest contributing factor to differences between IRB EL and IFRS 9. Underperforming stage 2 assets are those exhibiting a significant credit risk increase since initial recognition but for which there is no objective evidence of impairment; the lifetime expected credit losses on these assets is recognised at this point, and therefore sooner, under IFRS 9. One bank noted that "the incorporated "forward looking" and macro-economic factors will have significant impact on the calculation and will introduce a big difference with the regulatory perspective".

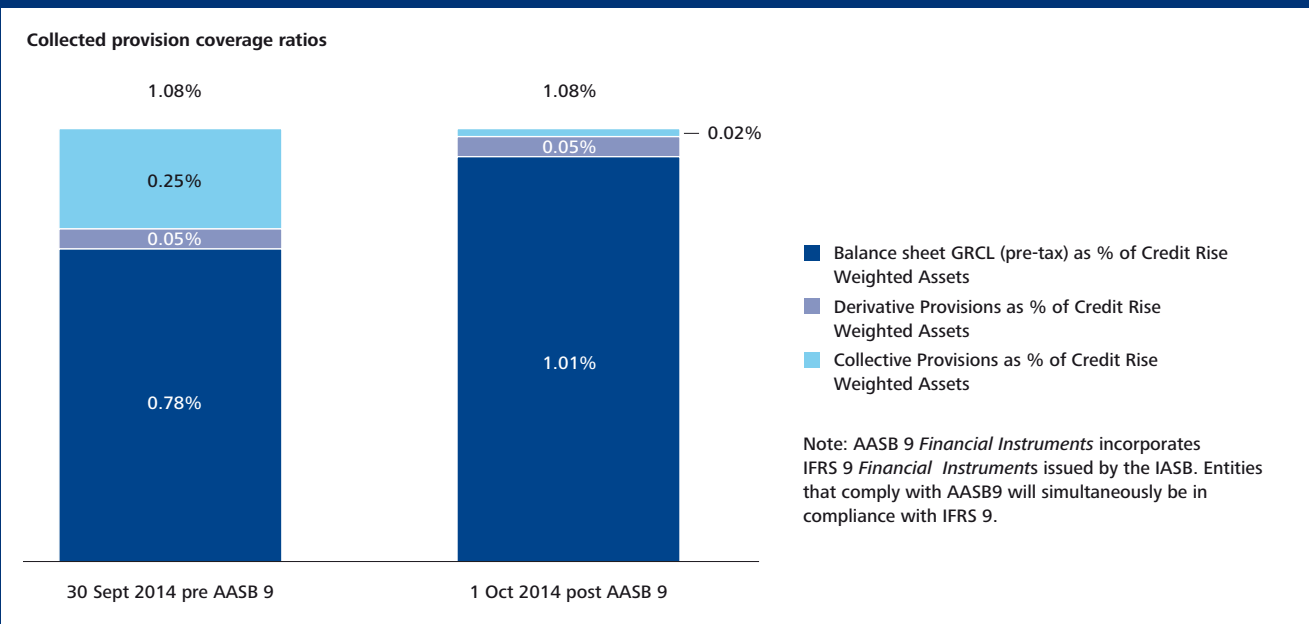
The majority of responses point to lifetime ECL for assets under stage 2 being the biggest contributing factor to differences between IRB EL and IFRS 9.



### A closer look: IFRS 9 adoption in Australia

One of the first major banks globally to early adopt IFRS 9 is Australian. National Australia Bank (NAB) adopted IFRS 9 on 1 October 2014 and in March 2015 they released a detailed investor presentation explaining the impact of transitioning from IAS 39 to IFRS 9. Interestingly, whilst the transition resulted in an additional AUD\$725m (EUR 510m) of provisions taken through retained earnings, there was no impact on regulatory capital (other than a deferred tax asset adjustment). This is because in Australia the regulator requires an additional amount to be set aside in a General Reserve for Credit Losses (GRCL) over and above accounting provisions. As the basis for calculating this amount is largely separate to the accounting provisions, it simply resulted in a reallocation from GRCL to accounting provisions.

One insight into how NAB adopted IFRS 9 is the use of an “economic forecast” adjustment on top of the base IFRS 9 provision calculation. The chart below is an extract from NAB’s Investor Presentation of their 2014 Full Year Results. It shows how they believe the IFRS 9 provision will change when compared to IAS 39.



It is not yet clear how implementation will affect other Australian banks.

### Tax impact

Eighty six percent of respondents do not know how the tax authorities will treat the changes arising from the adoption of IFRS 9. A number of respondents assume that, consistent with current tax legislation in their respective jurisdictions, taxes will be based on realised charges as opposed to provisions. However, further clarity in this area would be helpful.

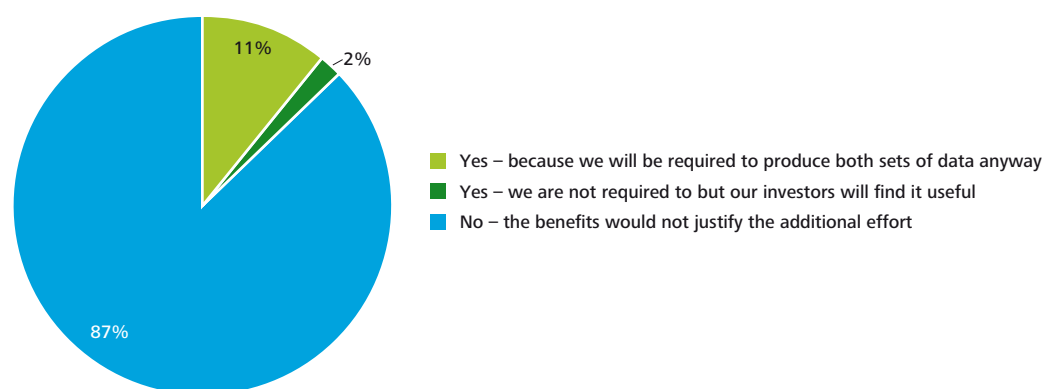
#### Tax treatment in the UK

In the UK, Change of Accounting Practice (COAP) regulations prescribe, in general, that accounting policy change adjustments related to loans and derivatives are recognised evenly to Profit and Losses over a 10 year period. The exception was in cases where debt is due to be repaid within the current period (typically 12 months from the balance sheet date); in such cases entities recognised the adjustments in full in the year of change.

As part of ensuring alignment between tax and accounting requirements, and with the aim of both minimising any possible accounting presentation distortion and protecting HMRC from volatility in tax receipts on entities' transition to IFRS 9, the HMRC has amended the COAP to remove the exception for current period debt. As a result, all adjustments resulting from entities' transitions to IFRS 9 impairment guidance will be recognised evenly over 10 years.

### Disclosing FASB's lifetime ECL

Figure 38. In addition to recording and measuring credit losses in line with the IASB's IFRS 9 requirements, would you consider disclosing the lifetime expected losses that the FASB may require?



The majority of respondents believe that the benefits do not outweigh the additional effort of disclosing the lifetime expected losses that the FASB may require. This presents an additional strain on capabilities and resources. Eleven percent of the banks are required to produce both sets of data for regulatory purposes. Only one bank considered it would voluntarily disclose the impairment measurement under the forthcoming FASB standard, principally for the benefit of the bank's investors.

#### FASB's CECL

The Financial Accounting Standards Board (FASB) is drafting a final Accounting Standard Update (ASU) which will amend U.S. GAAP on impairment for financial assets. The proposed amendments, which are referred to as Current Expected Credit Loss (CECL), will result in a shift from the existing incurred loss model to an expected credit loss model.

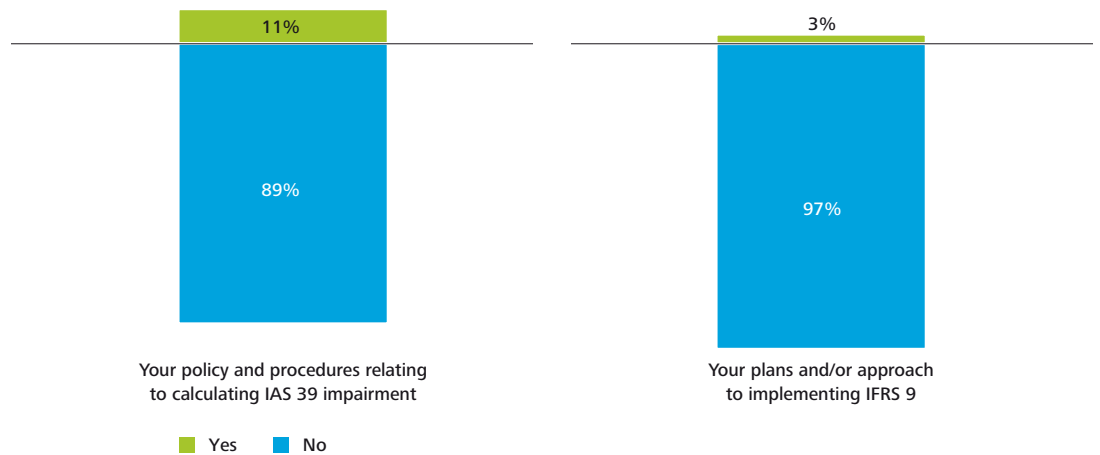
Some of the notable differences that exist between the likely CECL and IFRS 9 include:

- **Measurement:** CECL is a single measurement approach where the allowance reflects an estimate of all contractual cash flows not expected to be collected. This differs from IFRS 9 which is a dual measurement approach: for financial assets in the first stage IFRS 9 measures only 12-months of expected losses, and for financial assets in the second stage IFRS 9 measures lifetime expected losses.
- **Purchased Credit-Impaired (PCI) Assets:** Under CECL, upon acquiring a PCI asset, an entity would recognise as its allowance for expected credit losses the amount of contractual cash flows not expected to be collected as an adjustment that increases the cost basis of the asset. The allowance for PCI assets is subsequently measured consistently with how an entity measures expected credit losses for originated and purchased non-credit impaired assets. Interest income recognition is based on purchase price plus the initial allowance accreting to the contractual cash flows. IFRS 9 allowance for PCI assets is based on the cumulative change (from the original expectation at acquisition) in lifetime expected credit losses. Interest income recognition is based on applying the credit-adjusted effective interest rate to the amortised cost of the financial asset (rather than contractual cash flows).

The detailed application aspects of CECL will result in different outcomes in relation to recognition and measurement of credit impairment for financial assets compared to IFRS 9, contributing to the lack of a level playing field between banks following the different reporting frameworks.

### ECB findings from the AQR

Figure 39. Following the publication of the European Central Bank (ECB) findings from the Asset Quality Review (AQR), have you changed:



Nearly ninety percent of respondents made no changes to their policies and procedures as a result of the ECB findings from the AQR. Almost all respondents have indicated their plans and/or approach to implementing IFRS 9 have not changed following the ECB findings from the AQR.

### More to come

As banks progress with their implementation of IFRS 9, more and more detailed questions will arise and we look forward to exploring these further in our next survey.

# List of acronyms

AASB	Australian Accounting Standards Board	FASB	Financial Accounting Standards Board
ASU	Accounting Standard Update	FSB	Financial Stability Board
AQR	Asset Quality Review	GAAP	Generally Accepted Accounting Principles
BCBS	Basel Committee on Banking Supervision	GAECL	Guidance on accounting for expected credit losses
CCAR	Comprehensive Capital Analysis and Review	GRCL	General Reserve for Credit Losses
CECL	Current Expected Credit Losses	G-SIB	Global Systemically Important Bank
COAP	Change of Accounting Practice	HMRC	Her Majesty's Revenue and Customs
CRD	Capital Requirements Directive	IASB	International Accounting Standards Board
DPD	Days Past Due	IAS	International Accounting Standard
D-SIB	Domestic Systemically Important Bank	IBNR	Incurred But Not Reported
DTTL	Deloitte Touche Tohmatsu Ltd	IFRS	International Financial Reporting Standard
EAD	Exposure at Default	IRB	Internal-Ratings Based
EBA	European Banking Authority	LGD	Loss Given Default
ECB	European Central Bank	NAB	National Australia Bank
ECL	Expected Credit Losses	OSFI	Office of the Superintendent of Financial Institutions
EDTF	Enhanced Disclosure Task Force	PCI	Purchased Credit-Impaired
EFRAG	European Financial Reporting Advisory Group	PD	Probability of Default
EIR	Effective Interest Rate	PMA	Post-Model Adjustments
EL	Expected Losses	RWA	Risk-Weighted Assets
EMEA	Europe, Middle East and Africa	SEC	Securities and Exchange Commission
ESMA	European Securities and Markets Authority	SME	Small and Medium-sized Enterprise
EU	European Union		

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# Notes



# Notes



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