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Banks

Rising to the challenges of IFRS 9

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10 focus questions for management and audit committees

With just over a year to go before IFRS 9 is effective, banks face two immediate challenges: ensuring readiness for adoption in 2018 and providing the required disclosures for this year and next.

It is therefore unsurprising that the European Banking Authority (EBA) and the European Securities and Markets Authority (ESMA) have recently made announcements on these issues.

So as we approach the year end, I thought it would be helpful to share my insight and some practical guidance on implementing the standard, and responding to the regulators' expectations and those of the market.

Time is running out

A number of my clients have recently intensified their implementation efforts on IFRS 9. And they've found that the challenge is inversely proportional to the time left. So, if you haven't already kicked off your implementation project, I'd encourage you to engage – right now!

Even if your implementation project is underway, it's time to start thinking about communication, and what disclosures you're going to have to make.

Communicating with the market

The market is already expecting provisions for bad debts to be bigger under the new impairment requirements. But it's important that you help to set the expectations of analysts and investors, so that they aren't surprised by the actual figure when they see it.

Equally, they'll want to understand how IFRS 9 will impact your regulatory capital position.

The EBA's report included an impact assessment, which revealed that surveyed banks on average estimated an 18% increase in provisions and a 59 bps decrease in CET 1 ratios – but for some the impacts could be much larger.

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Responding to regulators' expectations

Prudential, securities and audit regulators are watching very closely. They are expecting robust, high-quality implementation of the new requirements and transparent disclosure of the impacts.

So what do you need to do about these two key challenges?

The readiness challenge

In terms of readiness for 2018, management need to ensure that implementation projects are appropriately designed and on schedule. And audit committees need to oversee management's efforts, by actively monitoring progress and requesting regular updates.

In its report, the EBA stressed that banks should not underestimate the work required and the need to involve audit committees and boards of directors. Banking supervisors will continue to show a keen interest in bank readiness – for example, the EBA is launching a second assessment exercise.

The disclosure challenge

Your disclosures in 2016 and 2017 will have to reflect progress made on implementation and the expected impact of IFRS 9. Both ESMA and the Enhanced Disclosure Task Force are encouraging a gradual and phased approach to disclosure in the run up to the 2018 implementation date.

In his recent blog post, Mark Vaessen goes into more detail on ESMA's recommended disclosures on IFRS 9 and the new revenue standard, IFRS 15.

Seeing the wood for the trees

Back in June, myself and the other IFRS 9 specialists from the six largest global accounting networks[1] contributed to published guidance on implementing the impairment requirements of IFRS 9. Although the guidance is aimed at larger banks, it contains principles and insights that smaller banks can use too.

The guidance includes **10 questions that audit committees can use** to focus discussions on IFRS 9 impairment plans, as well as more detailed information that management can use.

What should you do right now?

The need to engage with IFRS 9 becomes more pressing by the day. If you haven't engaged yet, I would encourage you to start straight away.

If you have started, then I suggest you make sure that plans are on track to address the key challenges of IFRS 9 and provide useful disclosures in the run-up to adoption.

To help make this happen, you might like to read our quick guide to the GPPC paper on impairment, which summarises the implementation challenges and key focus areas.

For more information on all aspects of IFRS 9, visit our web pages on Financial Instruments and IFRS for Banks or speak to your usual KPMG contact.

About the author

Chris Spall leads the global team that develops KPMG's guidance on financial instruments.

1 BDO, Deloitte, EY, Grant Thornton, KPMG and PwC; represented by the Global Public Policy Committee (GPPC).

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IFRS 9 for banks – 10 focus questions for audit committees

These questions will help audit committees focus their discussions with management on IFRS 9 implementation

Key decisions and interpretations of IFRS 9

1. What plans are in place to conclude on **key decisions**, build and test necessary **models and infrastructure**, execute **dry/parallel runs** and deliver high quality implementation by 2018?

2. What are the **key accounting interpretations and judgements** and why are they appropriate?

3. How will **implementation decisions** be **monitored** to ensure they remain appropriate?

Transparency

4. What **KPIs and management information** will be used to monitor drivers of ECLs and support **effective governance** over key judgements?

5. How will the **IFRS disclosure requirements** be met and how will those disclosures facilitate **comparability**?

Expected credit loss modelling

6. What are the **planned levels of sophistication** for different portfolios and **why are these appropriate**?

7. How will a ‘**significant increase in credit risk**’ be identified and **why are the chosen criteria appropriate**?

8. How will a representative range of **forward-looking scenarios** be used to capture non-linear and asymmetric impacts?

Systems and controls

9. Has the bank identified all **changes to existing systems and processes**, including data requirements and internal controls, to ensure they are appropriate for use under IFRS 9?

10. How will **reporting processes and controls** be documented and tested, particularly where systems and data sources have not previously been subject to audit?

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