Accounting Provisioning Under the Expected Credit Loss Framework: IFRS 9 in Emerging Markets and Developing Economies - A Set of Policy Recommendations

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# Abbreviations and Acronyms

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<th>Abbreviation</th>
<th>Full Form</th>
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<tbody>
<tr>
<td>BCB</td>
<td>Central Bank of Brazil</td>
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<tr>
<td>BOT</td>
<td>Bank of Thailand</td>
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<tr>
<td>CCB</td>
<td>capital conservation buffer</td>
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<td>CCyB</td>
<td>countercyclical buffer</td>
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<tr>
<td>CECL</td>
<td>current expected credit losses</td>
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<td>CET1</td>
<td>common equity tier 1</td>
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<tr>
<td>CFO</td>
<td>chief financial officer</td>
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<tr>
<td>CFRR</td>
<td>Centre for Financial Reporting Reform</td>
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<tr>
<td>COVID-19</td>
<td>the disease caused by the coronavirus</td>
</tr>
<tr>
<td>CP</td>
<td>Basel Core Principles on Effective Banking Supervision, 2012</td>
</tr>
<tr>
<td>EBA</td>
<td>European Banking Authority</td>
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<td>ECB</td>
<td>European Central Bank</td>
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<td>ECL</td>
<td>expected credit loss</td>
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<td>EMDEs</td>
<td>emerging markets and developing economies</td>
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<tr>
<td>ESMA</td>
<td>European Securities and Market Authority</td>
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<td>ESRB</td>
<td>European Systemic Risk Board</td>
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<td>EU</td>
<td>European Union</td>
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<tr>
<td>FASB</td>
<td>Financial Accounting Standards Board</td>
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<tr>
<td>FinSAC</td>
<td>World Bank Financial Sector Advisory Center</td>
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<tr>
<td>FSB</td>
<td>Financial Stability Board</td>
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<tr>
<td>FVTOCI</td>
<td>fair value through other comprehensive income</td>
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<tr>
<td>GAAP</td>
<td>generally accepted accounting practices</td>
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<td>GDP</td>
<td>gross domestic product</td>
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<td>G-SIBs</td>
<td>global systematically important banks</td>
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<td>IAS 39</td>
<td>International Accounting Standards 39</td>
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<td>IASB</td>
<td>International Accounting Standards Board</td>
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<td>IFRS</td>
<td>International Financial Reporting Standards</td>
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<tr>
<td>IFRS 9</td>
<td>International Financial Reporting Standards 9</td>
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<tr>
<td>IMF</td>
<td>International Monetary Fund</td>
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<tr>
<td>IRB</td>
<td>internal ratings-based</td>
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<tr>
<td>IRBA</td>
<td>Independent Regulatory Board for Auditors (South Africa)</td>
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<tr>
<td>IT</td>
<td>information technology</td>
</tr>
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<td>LGD</td>
<td>loss given default</td>
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<tr>
<td>Abbreviation</td>
<td>Definition</td>
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<td>LIC</td>
<td>low-income countries</td>
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<tr>
<td>MAS</td>
<td>Monetary Authority of Singapore</td>
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<td>NBRNM</td>
<td>National Bank of the Republic of North Macedonia</td>
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<tr>
<td>NBR</td>
<td>National Bank of Rwanda</td>
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<tr>
<td>nGAAP</td>
<td>national generally accepted accounting practices</td>
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<tr>
<td>NPE</td>
<td>non-performing exposure</td>
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<td>NPL</td>
<td>non-performing loan</td>
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<tr>
<td>PA</td>
<td>Prudential Authority (South Africa)</td>
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<tr>
<td>PD</td>
<td>probability of default</td>
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<tr>
<td>QIS</td>
<td>quantitative impact study</td>
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<td>PRA</td>
<td>Prudential Regulation Authority, United Kingdom</td>
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<td>ROSC</td>
<td>Reports on the Observance of Standards and Codes</td>
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<tr>
<td>RWA</td>
<td>risk-weighted asset</td>
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<tr>
<td>SARB</td>
<td>South Africa Reserve Bank</td>
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<tr>
<td>SPPI</td>
<td>solely payment of principal and interest</td>
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<tr>
<td>SSB</td>
<td>standard-setting body</td>
</tr>
<tr>
<td>stage 1</td>
<td>exposures without significant increase of credit risk since initial recognition</td>
</tr>
<tr>
<td>stage 2</td>
<td>exposures with significant increase of credit risk since initial recognition but not credit impaired</td>
</tr>
<tr>
<td>stage 3</td>
<td>exposures credit impaired</td>
</tr>
<tr>
<td>SICR</td>
<td>significant increase in credit risk</td>
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<tr>
<td>SupTech</td>
<td>supervisory technology</td>
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<tr>
<td>TFRS 9</td>
<td>Thai Financial Reporting Standards 9</td>
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<tr>
<td>UTP</td>
<td>unlikely to pay</td>
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Acknowledgments

This paper is a product of the Financial Stability and Integrity Global Unit in the World Bank Group’s Finance, Competitiveness, and Innovation Global Practice. It was prepared by Ezio Caruso (Senior Financial Sector Specialist at the Financial Stability and Integrity Unit, Task Team Leader), Katia D’Hulster (Lead Financial Sector Specialist in the East Asia and Pacific Region), Tatsiana Kliatskova (Young Professional in the South Asia Region), and Juan Ortiz (Senior Financial Sector Specialist at the Financial Sector Advisory Center). Alfonso Garcia Mora, Yira J. Mascaro and Jean Pesme provided overall guidance. We are grateful for the substantive feedback received from peer reviewers Miquel Dijkman, Krishnamurti Damodaran, and Henry Fortin (all from World Bank). We would also like to thank the National Bank of the Republic of North Macedonia, the Bank of Italy, the Central Bank of Brazil, the Bank of Thailand, the South Africa Reserve Bank, and the National Bank of Rwanda for their excellent cooperation. The team thanks Elizabeth Pontiff and Marcy Gessel of Publications Professionals LLC for editorial support and Diego Catto Val for design and layout assistance.

The findings, interpretations, and conclusions expressed in this paper are entirely those of the authors. They do not represent the views of the International Bank for Reconstruction and Development, World Bank and its affiliate organizations, or the executive directors of the World Bank or the governments they represent.
Executive Summary

In 2009, the G-20 in London recommended that accounting standard setters “strengthen accounting recognition of loan-loss provisions by incorporating a broader range of credit information” (G20 2009). In response, the International Accounting Standards Board (IASB) issued International Financial Reporting Standard 9 (IFRS 9) in July 2014. The new standard became effective in January 2018 and introduced an expected credit loss (ECL) approach, as opposed to the incurred credit loss under the International Accounting Standards 39 (IAS 39) that was in place at the time. IAS 39 (par. 59) permitted accounting provisioning only in case of “objective evidence of impairment” without admitting losses due to future events and hence resulted in “too little and too late” provisioning. By contrast, IFRS 9 anticipates the time of provisioning by requiring banks to recognize losses earlier in the credit cycle, even at origination stage.

This paper relies on a survey and bilateral meetings with prudential supervisors. We conducted a survey to (a) identify challenges faced by banks and supervisors in countries that implemented IFRS 9 and (b) in countries that have not yet implemented the new accounting framework, understand the reasons behind the decision to postpone the transition to IFRS 9. We sent the survey to 184 countries and economies across all regions and received 91 responses. Only 7 responses were from low-income countries, while 20 were from lower-middle-income countries (see table 1 for the complete income and regional breakdown). The limited number of responses from low-income countries should be kept in mind when interpreting our recommendations.

We also held bilateral meetings with six prudential supervisors (National Bank of the Republic of North Macedonia, Bank of Italy, Central Bank of Brazil, Bank of Thailand, South Africa Reserve Bank, and National Bank of Rwanda) to get an in-depth understanding of their IFRS 9 implementation challenges. These were selected to ensure a broader diversification of experience, either in terms of regions (Europe, Latin America, Africa, South East Asia) or of level of income (advanced and emerging economies). Based on the experience of the surveyed countries and their reflections on challenges and potential remedies that they used while implementing the IFRS 9 accounting framework, we identified a set of high level policy recommendations for prudential supervisors in emerging markets and developing economies (EMDEs) willing to transition to IFRS 9.

The survey (see section 2 of this paper for a full discussion) revealed several challenges that banks and supervisors faced with IFRS 9 implementation. Data availability and low data quality, modeling risk, and overreliance on managerial judgment were reported as the most important ones. According to the survey, respondents mostly apply IFRS, even though we found a high degree of heterogeneity on the edges of application. IFRS 9 is being used in 53 countries in our sample. In an additional 25 countries, IFRS 9 applies only to certain financial institutions, depending on factors such as the size of the financial institution, whether it is listed or not, and whether
financial statements are on a consolidated or individual basis. On the one hand, setting the same accounting standards for all financial institutions avoids two or multiple-tier accounting systems (listed vs. not listed banks, consolidated vs. individual accounts, large vs. small banks) and standardizes regulatory reporting. On the other hand, bilateral meetings showed that smaller banks might find it difficult to build up an in-house ECL model at a time when IFRS resources are in high demand and could decide to outsource the process, with limited capacity to manage the associated risks (reliance on a third party, conflict of interest of the provider, security of data, termination rights, and so forth). EMDEs also reported limited staff capacity as an important constraint for prudential supervisors, particularly for local banks. With the effect of IFRS 9 on banks being substantially different across jurisdictions, most supervisory authorities provided guidance to banks during the transition and implementation period to mitigate the IFRS 9 impact on banks.

Further, 13 out of 91 respondents have not yet implemented IFRS 9, but most of them plan to do so in the next one to three years. Some authorities suggested that their plans might be affected by the COVID-19 pandemic due to the prioritization of critical supervisory activities as well as the uncertain impact of IFRS 9 on banks. While this indicates that most respondents either have or will relatively soon implement IFRS 9, it is unclear if the remaining countries that did not respond to the survey (93) have or will implement IFRS 9, particularly low-income countries, which are a large share of nonresponding countries (67 percent).

The World Bank has played a leading role in encouraging the development of the International Financial Reporting Standards and their use around the world. Valuation practices consistent with accounting standards widely accepted internationally contribute to a robust assessment of credit, market, and liquidity risk. For EMDEs, this is important for attracting foreign investments. However, prudential supervisors should be adequately prepared before embarking on this journey (see section 3). To the extent permitted by law and regulations, prudential supervisors should exert sound judgement about proportionality: imposing IFRS application only on banks of a certain size (measured in terms of total assets or risk-weighted assets) adheres to the proportionality principle, but it might excessively fragment the accounting and reporting framework. On the opposite side, requiring all banks to apply IFRS might lead medium-small credit institutions to outsource the ECL calculation, without understanding the underlying model. Supervisors should always require a good understanding of the ECL model by banks, and rigorous governance and internal control processes for assessing external vendors They should formulate a comprehensive preparatory plan, strategizing the transition to IFRS 9 and raising awareness with banks’ boards and senior management on the significance of the challenges. It is important to set clear, timely, and comprehensive supervisory expectations on the ECL framework and ensure broad consistency between credit classification criteria and the IFRS staging process. Prudential supervisors should also strike a balance between flexibility and oversight on entry and exit criteria to and from stages 2 and 3 and should consider prudential backstops on provisioning. To mitigate procyclicality, supervisors should have in place macroprudential policies consisting of replenished capital buffers that could be released in time of stress. They should also make use of transitional arrangements.

The COVID-19 outbreak is the first real test of IFRS 9. Concerns about IFRS 9 procyclicality might result in further implementation delays, despite the flexibility embedded in a principle-based standard, as clarified by standard-setting bodies (SSBs), central banks, and prudential supervisors (see boxes 1, 2 and 3 for more information about IFRS and COVID-19). Countries might still postpone IFRS 9 given the difficulties of generating reasonable and supportable forecasts to estimate ECL under the uncertainty and course of the pandemic. A sound policy decision should be based on a broad ongoing assessment of the preconditions that ought to be in place for an effective IFRS 9 (and IFRS in general) implementation, including maturity and quality of the external audit profession, robust governance and risk management arrangements in banks, and credit risk modeling expertise in banks and with supervisory staff.

Prudential supervisors in EMDEs, particularly those that have already implemented IFRS 9, should also invest in credit-risk modeling capacity, both in terms of human resources and information technology (IT) tools. In this respect, supervisory technology (SupTech) solutions can be useful in addressing challenges related to data collection and ECL modeling. The ultimate goal is to ensure that banks’ methods for determining accounting allowances lead to an appropriate and comprehensive measurement of ECL. Those supervisors in EMDEs with more compelling budget constraints, can build up capacity on the ECL model mainly through online training platforms and technical assistance, but qualified resources remain crucial.

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1. Stage 1 is financial instruments for which credit risk has not increased significantly since initial recognition; stage 2 is instead those characterized by a significant increase of credit risk (SICR) since initial recognition. Stage 3 is impaired loans. For stage 1, ECL is calculated from default events that are possible within 12 months after the reporting period; for stage 2 and 3, loss allowance should reflect lifetime ECL, incorporating forward-looking information.
Introduction

1.1 What Is the International Financial Reporting Standard 9?

IFRS 9 Financial Instruments is the new international financial reporting standard. It was issued by the IASB in July 2014 and became effective in January 2018. IFRS 9 replaced IAS 39 Financial Instruments: Recognition and Measurement, which was considered too complex, inconsistent with the way entities manage their businesses and risks, and responsible for delaying the recognition of credit loss on loans until too late in the credit cycle.

IFRS 9 implemented three major changes (a) classification and measurement of financial instruments, (b) expected credit loss, and (c) hedge accounting. Classification and measurement of financial instruments is based on the entities’ business model and contractual cash flow characteristics. Entities are required to assess if the objective of holding a financial instrument is only to collect the contractual cash flow (hold to collect) or both to collect the contractual cash flow and sell the financial assets (hold to collect and sell), as well as whether the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest (SPPI). Financial instruments that pass both the business model and SPPI tests can be classified either at amortized cost or at fair value through other comprehensive income (FVTOCI) and are subject to impairment. Any financial asset that does not pass the SPPI or the business model test is always measured at fair value through profit and loss. Compared to IAS 39, the number of portfolios is reduced to three, and reclassifications are possible only when there is a change in the business model (very infrequent), limiting the dubious reclassification practices that occurred in the aftermath of the global financial crisis of 2007–2009.

2. For the full standard, see https://www.ifrs.org/issued-standards/list-of-standards/ifrs-9-financial-instruments/.
Change 1: IFRS 9 introduced a new framework for recognition and measurement of impairments in loans and receivables that are measured at amortized cost or FVTOCI, the expected credit loss (ECL). IAS 39 used an incurred loss approach, where loss was only recognized when a trigger event occurred. This resulted in a too little and too late recognition of loan losses. Under IFRS 9, banks are required to recognize losses earlier in the credit cycle, even at origination stage, updating them at each reporting date to reflect changes in credit risk. The recognition of impairment is not based anymore on a past event generating loss, but it is attributed to a potential credit loss. There is no need for objective evidence of impairment, because experience suggests that the determinants of credit losses begin to show up a considerable time before loans enter a cumulative delinquency. Therefore, the shift from an incurred credit loss approach to an expected credit loss approach affects the timing of the provisioning.

Change 2: ECL is allocated in three stages, with implications for the amount of accounting provisioning, particularly when there is a material deterioration in the asset quality. If the credit risk has not increased significantly since initial recognition, ECL is calculated from default events that are possible within 12 months after the reporting period (stage 1). If there is a significant increase of credit risk (SICR) since initial recognition (stage 2), loss allowance should reflect lifetime ECLs, incorporating forward-looking information (including macroeconomic variables such as gross domestic product [GDP] and unemployment rate). Stage 3 is credit-impaired loans.

Change 3: IFRS 9 allows more exposures to be hedged and establishes new criteria for hedge accounting that are somewhat less complex and more aligned with the way that entities manage their risks than under IAS 39. Companies that have rejected using hedge accounting in the past because of its complexity and those wishing to simplify, refine, or extend their existing hedge accounting may find the new hedging requirements more accommodating than those in IAS 39.

1.2 The Scope of the Paper and Its Methodology

This paper deals with the expected credit loss framework, with a particular focus on EMDEs. In 2020, EMDEs were facing challenges when dealing with IFRS 9 during the COVID-19 pandemic, given the unprecedented reversals in capital flows as global risk appetite declined. EMDEs are coping with weaker health care systems and more limited fiscal space to provide support.

This paper is based on a number of inputs, including academic research and literature reviews; a survey on implementation of IFRS 9 that was sent to the supervisory authorities (central banks, financial supervisory authorities, regulatory commissions) in 184 countries and territories; and bilateral meetings with six prudential supervisors: National Bank of the Republic of North Macedonia, Bank of Italy, Central Bank of Brazil, Bank of Thailand, South Africa Reserve Bank, and National Bank of Rwanda. While the survey provides a snapshot of the challenges that supervisors and banks faced when implementing or preparing for IFRS 9 implementation, the bilateral meetings with prudential supervisors allow for an in-depth understanding of IFRS 9 implementation challenges.

Based on the experiences of the surveyed countries while switching to the IFRS 9 accounting framework, the challenges they faced, and the remedies they used during the switch, we derived broad policy recommendations for prudential supervisors in EMDEs that have implemented or plan to implement IFRS 9. In addition, we paid specific attention to the interaction between COVID-19 and IFRS 9. Several stakeholders (supervisors, analysts, investment banks) emphasized the unintended consequences of IFRS 9, considering the current recession, the increased probability of default (PD) and, therefore, the higher loan loss provisions. This potential procyclical effect of accounting provisioning, in turn, would absorb available capital, subsequently decreasing the supply of credit that is much needed to support the real sector. In the paper, we reflect on two important questions, (a) how the pandemic affects SICR, and (b) how banks could estimate ECL in such an uncertain environment (see box 2).

The paper is organized as follows: Section 2 presents the survey results. Section 3 presents policy recommendations for supervisory authorities in countries that implemented IFRS 9 as well as in countries that are still in the process of IFRS 9 implementation. Section 4 offers conclusions.
The impact of IFRS 9 on financial stability can be examined from various angles. The most important change introduced by IFRS 9 is the shift from an ‘incurred’ to an ‘expected’ credit loss (ECL) approach for measuring impairment allowances. The new approach is based on recognition of ECL along three stages, reflecting the increasing credit risk from origination to default. Banks must base their unbiased, point-in-time estimates of ECLs on a broad range of credit-relevant information, including forward-looking macroeconomic variables. By contrast, under the previous accounting framework, the recognition of credit losses was primarily based on ‘realized’ (incurred losses) events.

It can be argued that IFRS 9 increases financial stability, because it pursues a fuller and more timely recognition of credit losses, enhancing the size of banks' loss-absorbing allowances and their responsiveness to information pointing to a deterioration in credit risk. Financial stability benefits from expediting loss recognition: if the downturn can be identified sufficiently early on, procyclicality of banks' provisioning may be reduced and the credit contraction in a downturn may be less severe.

However, the earlier recognition of impairments induces a significant ‘front-loading’, of credit losses, which is expected to impede banks’ ability to retain earnings. As earnings are a key component of Common Equity Tier 1 (CET1), in the short-term banks’ regulatory capital is expected to decrease. Nevertheless, it should be noted that IFRS 9 implementation is usually accompanied by transitional arrangements that allow for a gradual absorption of the impact of the first-time application of IFRS 9 by smoothing the impact on the capital ratio over a time horizon of up to five years.

It is also worth highlighting that banks might not be able or willing to anticipate the downturn (limitations in forecast assumptions, model risk, lack of incentives, shareholders’ expectations). The COVID-19 pandemic showed how crisis can suddenly occur. Then, the ECL approach might trigger an abrupt increase of impairment allowances, also in reaction to new and forward-looking information. As a result, IFRS 9 could have certain procyclical effects derived from the cyclical sensitivity of the credit risk parameters used for the estimation of ECLs and from the shifts of exposures between stages.
2.1 Implementation of IFRS 9 in Different Countries

At the beginning of March 2020, the World Bank launched a survey on the implementation of IFRS 9. The aim of the survey was twofold. First, the survey aimed to identify challenges faced by supervisors in countries that implemented IFRS 9. Second, for countries and economies that postponed transition to IFRS 9, the survey aimed to understand the reasons behind this decision. The survey was sent to the supervisory authorities (central banks, financial supervisory authorities, regulatory commissions) in 184 countries. Supervisory authorities reported also on behalf of the supervised banks, underlying the challenges faced by credit institutions with implementation and use of IFRS 9. The questionnaire is presented in the appendix.

Despite the COVID-19 outbreak, the participation rate was 49 percent. We received 91 responses: 36 are from high-income countries and economies, 28 from upper middle-income countries and economies, 20 from lower middle-income countries and economies, and 7 from low-income countries and economies. Geographical distribution of the respondents is as follows: 16 jurisdictions are from the African region, 14 from the East Asian and Pacific region, 33 from the European and Central Asian region, 17 from the Latin America and the Caribbean region, 7 from the Middle East and North African region, and 4 from the South Asian region (table 1). A list of countries that responded to the survey is presented in the appendix. It is worth emphasizing that a total of 57 out of 91 respondents indicated that they have powers to regulate and issue accounting rules.
When interpreting the aggregate results of the survey, it is worth taking into account the drawbacks of the survey design. First, the response rate might be affected by the COVID-19 outbreak as responses were collected during March–April 2020. Countries that especially suffered from the pandemic had other priorities, and, therefore, some of them did not answer the survey. In addition, responses to the survey questions might be affected by the pandemic. For example, some respondents indicated that their worries about the procyclicality of IFRS 9 became a major concern for bank supervisors at the beginning of the crisis. Second, survey responses might suffer from self-selection bias, that is, countries that answered the survey might be the ones that are particularly successful in implementing IFRS 9 or be the ones that would like to voice problems that they faced while implementing IFRS 9.

We believe that our aggregate results are sufficiently representative, as we got answers from a wide range of countries, that is, (a) countries from different geographical regions and income groups; (b) countries that implemented and countries that postponed implementation of IFRS 9; (c) countries that faced different scales of difficulties while implementing IFRS 9; and (d) countries that had different outcomes after implementing IFRS 9. However, we acknowledge that applicability of the findings to low-income countries might be limited given the relatively low number of respondents in this group, especially from Sub-Saharan Africa and Latin America.

Banks in countries covered by the survey are mostly required to apply IFRS or national accounting standards that are in a close compliance with IFRS. IFRS is in effect in 56 countries, while national accounting standards are applied by banks in 21 countries. In addition, 14 countries apply a mix of accounting standards depending on the type of financial institution, its size, listing status on a stock exchange, and reporting basis (that is, consolidated or individual).

**IFRS 9 is in effect in 53 countries in our sample.** In an additional 25 countries, IFRS 9 applies only to certain financial institutions. Varying by country, the applicability of IFRS 9 depends on the size of the financial institution, listing status on a stock exchange, and reporting basis being either consolidated or individual. In some countries, banks may apply IFRS 9 on a voluntary basis, depending on their preparedness. In 13 countries, IFRS 9 is not effective (figure 1).

**According to our survey, 62 percent of respondent supervisors have powers to regulate and issue accounting rules.** However, when accounting standard setters are separated from prudential supervisors, the interaction with each other is frequent, considering prudential supervisors’ interest in ensuring that banks’ financial statements reflect sound judgement of asset quality and prudent provisioning practices.

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4. Some countries apply national accounting standards, but they fully integrated IFRS 9 into their national accounting framework.
FIGURE 1 - Implementation of IFRS 9 by the Survey Respondents

Note: Countries colored in white did not provide responses to the survey. The map is based on the responses to the survey (i.e., self-declaration).
2.2 Major Challenges in Implementing IFRS 9

Most countries in our sample implemented IFRS 9 in 2018. While 65 jurisdictions implemented IFRS 9 in 2018, other countries postponed implementation to 2019–2024. In some countries, IFRS 9 is applied on a voluntary basis and will become mandatory in upcoming years.

The main challenges that supervisory authorities encountered with implementation of IFRS 9 are shown by figure 2. Survey participants highlighted the following difficulties: (a) modeling risk; (b) data availability and low data quality; and (c) limited staff capacity. In several instances, low data quality interacted with limited staff capacity, resulting in difficulties for the supervisor in adequately reviewing the banks’ model validation and adequacy of the data inputs. This often led to challenges in assessing the adequacy of loan loss provisioning and ensuring consistency of application of a principles-based accounting standard across institutions.

Supervisors reported that banks faced challenges in implementing IFRS 9. As shown by figure 3, the main challenges highlighted by the survey are (a) data availability and low data quality that make it difficult to set up and apply expected credit loss models; (b) modeling risk and overreliance on managerial judgment; and (c) burden due to the involvement of several business areas, such as budgeting, information technology, risk, finance, governance, and processes. Supervisors indicated that banks, and especially small banks, faced challenges with using forward-looking information for modeling the probability of default (PD), the significant increase of credit risk (SICR), and other parameters used for calculation of the expected credit losses (ECL). Further, in countries with a high presence of foreign capital in the banking sector, some foreign-owned banks received ECL models from their parent banks. While some respondents reported that such models were high quality, a few others suggested that models were often not country-specific and poorly reflected the host country’s environment.

Supervisors’ Challenges in Implementation of IFRS 9

<table>
<thead>
<tr>
<th>Challenge</th>
<th>Respondents who selected that option</th>
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<tr>
<td>Modelling Risk</td>
<td>69%</td>
</tr>
<tr>
<td>Data Availability and Low Data Quality</td>
<td>65%</td>
</tr>
<tr>
<td>Limited Staff Capacity</td>
<td>56%</td>
</tr>
<tr>
<td>Lack of Appropriate Analytical Tools</td>
<td>44%</td>
</tr>
<tr>
<td>Regulatory Treatment of Accounting Provisioning</td>
<td>32%</td>
</tr>
<tr>
<td>Difficulties with Constraining Managerial Judgement</td>
<td>29%</td>
</tr>
<tr>
<td>Other</td>
<td>16%</td>
</tr>
<tr>
<td>Lack of Enforcement from a Supervisor</td>
<td>5%</td>
</tr>
</tbody>
</table>

*Note: Percentages represent share of respondents who selected that option; the respondents could select all options that apply.*
Based on the supervisors’ responses, the challenges that banks faced with implementation of IFRS 9 vary across countries with different income levels. The top three challenges – data availability and low data quality, modelling risk and overreliance on management judgement, and burden due to the involvement of several business areas – are the same for all income groups. At the same time, survey participants from lower middle-income and low-income countries highlighted limited staff capacity and lack of appropriate analytical tools as important challenges with IFRS 9 implementation. In addition, overreliance on external vendors was named as a significant issue in low-income countries.

Most supervisory authorities (72 percent of respondents) provided guidance setting out expectations to banks during the implementation of IFRS 9. The supervisory authorities’ major activities were as follows: (a) performing a quantitative impact assessment of IFRS 9 on banks’ balance sheets and supervisory metrics prior to IFRS 9 implementation; (b) assessing banks’ preparedness for IFRS 9 implementation via bilateral meetings, questionnaires, and on-site visits, as well as a parallel run with previous accounting standards; and (c) issuing official guidelines and instructions on IFRS 9 implementation to ensure consistent and effective implementation of the standard. Among other tasks, supervisory authorities issued guidelines clarifying supervisory expectations with regard to disclosures for financial reporting; provisioning for regulatory purposes; credit risk management; measurement and classification of financial assets; and definition and modeling of SICR and PD. Additional clarification of supervisory expectations included organization of workshops and training sessions for capacity building in partnership with consulting firms and international organizations; preparation of macroeconomic scenarios for ECL modeling as well as dissemination of historical annual data (for example, on default rates of banks); and ongoing support via consultations and Q&As.

A total of 34 out of the 77 respondents who answered that IFRS 9 is effective or effective for some FIs indicated that IFRS 9 had no substantial material effect on banks’ profit and loss accounts or on key performance indicators. Twenty-two percent of respondents suggested that the effect on banks was positive and 34 percent of respondents pointed out a negative effect of IFRS 9 on banks (figure 4). With a few exceptions, respondents observed higher loan loss provisioning on performing loans at the time of adoption of IFRS 9, which made banks more resilient at the start of the current crisis. Further, the effect of IFRS 9 on asset quality, profitability, and capital ratios differ across jurisdictions. Some respondents said they saw no or only a marginal material effect on the above-mentioned indicators. In some cases, banks observed a significant decrease in their profitability and capital adequacy ratios due to a higher loan loss provisioning, though the negative effect was mostly temporary. In other cases, banks improved the quality of their assets by reducing impairment levels and optimizing their balance sheets. In addition, a greater operational and strategic alignment between the accounting and risk management functions was seen as a potential benefit for banks.

6. We report the results by income group only if there is a clear difference in responses by countries belonging to different income groups.
FIGURE 4 - Impact of IFRS 9 on Banks

Note: Figure 4 shows the data for question 10 of the survey: Do you observe any material effect of IFRS 9 on banks’ profit and loss account as well as on key performance indicators (asset quality, loans losses provisioning, capital ratios, and so forth)?

Most supervisory authorities undertook some measures to mitigate impact of IFRS 9 on banks. Sixty percent of respondents suggested that some mitigation tools are in place. First, most of the supervisors implemented transitional arrangements. Transitional arrangements allow for a gradual absorption of the impact of the first-time application of IFRS 9 by smoothing the impact on the capital ratio over a time horizon of up to five years (some countries opted for a shorter period, see section 3). The transitional arrangements are on a voluntary basis for banks, with the number of banks applying for them varying substantially across countries. Second, some supervisors applied prudential backstops, requiring minimum provisioning not only for financial assets already impaired (so called ‘stage 3’; for example, the European Union in relation to non-performing exposures) but also for credit exposures showing a significant increase of credit risk (SICR, so called ‘stage 2’) or even for loans at origination (‘stage 1’; for instance, Thailand and Singapore), which could mitigate the capital impact of a cyclical increase in accounting loss allowance during an economic downturn. Third, in some countries, banks were also required to have a parallel run of the two accounting standards to assess the potential impact of IFRS 9 prior to the final transition to the standard.
2.3 Reasons for Countries to Postpone Implementation of IFRS 9

In our sample, 13 countries did not implement IFRS 9 at all. Except for three countries, supervisory authorities plan to implement IFRS 9 in their jurisdictions in the next one to three years. In some cases, authorities suggested that their plans might be affected by the COVID-19 pandemic because of the need to prioritize critical supervisory activities and an uncertain impact of IFRS 9 on banks.

**FIGURE 5 - Reasons for Postponement of IFRS 9 Implementation**

<table>
<thead>
<tr>
<th>Reason</th>
<th>% Respondents</th>
</tr>
</thead>
<tbody>
<tr>
<td>Lack of appropriate models and analytical tools</td>
<td>69%</td>
</tr>
<tr>
<td>Data gaps</td>
<td>54%</td>
</tr>
<tr>
<td>Too high costs of transition</td>
<td>38%</td>
</tr>
<tr>
<td>Potential impact on the capital adequacy</td>
<td>38%</td>
</tr>
<tr>
<td>Potential negative impact on banks’ profitability</td>
<td>23%</td>
</tr>
</tbody>
</table>

Note: Percentages represent share of respondents who selected that option; the respondents could select all options that apply.

Supervisory authorities had country-specific reasons for postponement of IFRS 9 implementation. The main obstacles for IFRS 9 implementation include (a) a lack of appropriate models and analytical tools; (b) data gaps (figure 5). Interestingly, 69 percent of respondents identified other reasons not mentioned in the survey questionnaire. One of the obstacles is lack of legal basis for the transition to IFRS 9, including conversion of the standard to Islamic banking. Some countries postponed implementation of IFRS 9 to make necessary adjustments to regulations, a time-consuming process that, in some cases, requires technical expertise that may be hard to find. In addition, some survey participants indicated limited skills in ECL model development and validation as another challenge. Bank supervisors are concerned that they may not have the appropriate skills and expertise to challenge ECL models and, therefore, properly supervise financial institutions under new accounting standards. That, in turn, might harm banks’ safety and soundness. Moreover, some survey participants were concerned about the impact of IFRS 9 on financial institutions, including the procyclicality of provisioning (related to COVID-19). They indicated additional country-specific studies are required before transitioning to IFRS 9. In addition, supervisors in some developing economies are considering a more proportional approach to IFRS 9 implementation depending on the size and complexity of financial institutions.

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7. IFRS were designed with conventional finance in mind. Discounting cash flows and time value of money are generally calculated with reference to interest rate, which raises concern under the general prohibition of interest rate transactions dominating Islamic finance. Additionally, IFRS 9 incorporates the notion of “substance over the form,” which is critical for classification and measurement of financial assets. By contrast, Islamic legal form ultimately determines the accounting treatment. The International Accounting Standards Board set up an Islamic Finance Consultative Group, with the view to support IFRS implementation in the concerned jurisdictions.
BOX 2 - IFRS 9 and COVID-19

COVID-19 is the first real test of IFRS 9 since its inception in 2018. In the aftermath of the COVID-19 crisis (March–April 2020), regulators, supervisors, and SSBs were confronted with two main questions.

HOW DOES THE PANDEMIC AFFECT THE SIGNIFICANT INCREASE OF CREDIT RISK (SICR)?

The Basel Committee on Banking Supervision (BCBS 2020) agreed that the extraordinary support measures introduced in many jurisdictions to alleviate the financial and economic impact of COVID-19 should be considered by banks when they calculate their ECLs. Relief measures such as public guarantees or payment moratoriums, granted either by public authorities or by banks on a voluntary basis, should not automatically result in exposures moving from a 12-month ECL to a lifetime ECL measurement. The IASB expressed the same view (IASB 2020).

Several supervisors and regulators released public statements to clarify the impact of the pandemic on the IFRS 9 staging process. For example, the Prudential Regulation Authority, United Kingdom (PRA) outlined that banks should have reflected the temporary nature of the shock and fully consider the significant economic support measures announced by global fiscal and monetary authorities (IASB 2020). Banks’ forecasts should consider the relief measures made available to enable borrowers who are affected by the COVID-19 outbreak to resume regular payments. Extension of a mortgage repayment holiday should not automatically be, other things being equal, a sufficient condition to move participating borrowers into stage 2 ECL. The European Banking Authority (EBA 2020) pointed out that IFRS 9 offers a degree of flexibility, without dictating when a SICR has occurred. IFRS 9 requires an assessment based on quantitative and qualitative triggers, but it does not impose a strict automatism. Accordingly, the application of public or private moratoria aimed at addressing the adverse systemic economic impact of the COVID-19 pandemic should not be considered by themselves an automatic trigger to conclude that a SICR has occurred. The ‘Guidance on treatment of IFRS 9, capital requirements and relief measure due to Covid-19 pandemic by banks’, adopted by the National Bank of Rwanda (June 2020) considers ‘that the use of government endorsement payment holidays by a borrower would not on its own trigger the counting of days past due for the 30 days past due backstop used to determine SICR...’.

Being principle based, the IFRS 9 staging process certainly allows flexibility, but it might lead to unintended consequences. While a moratorium targeted at a wide range of borrowers and granted by force of law (or even on a voluntary basis) cannot mechanistically be considered a SICR, it might nevertheless signal an underperforming status. If read in conjunction with other exceptional measures adopted by prudential supervisors (postponement of on-site inspections, reduction of nonessential regulatory reporting, cancellation of stress tests), excessive flexibility might lead to a misapplication of accounting standards, which in the long run could affect financial stability. Banks could indeed exploit repayment holiday measures to keep borrowers who are not facing just temporary liquidity constraints in stage 1. When exerting judgment, the key challenge is to distinguish between borrowers whose credit standing would not be significantly affected by the current situation in the long term and those who would be unlikely to restore their creditworthiness. However, too much flexibility might open the door to manipulation of financial statements. Banks might be tempted to exploit the relaxation in supervisory standards to transfer financial assets benefitting from forbearance measures (for example, restructuring following a moratorium) to a better stage.

HOW COULD BANKS ESTIMATE ECL IN SUCH AN UNCERTAIN ENVIRONMENT?

Prudential and accounting SSBs emphasized that IFRS 9 requires the use of expert judgement. The BCBS (2020) recognized the high levels of uncertainty surrounding the forward-looking information relevant to estimating ECLs and expected banks’ evaluations to reflect the mitigating effect of the significant economic support and payment relief measures put in place by public authorities and the banking sector. The IASB (2020) clarified that IFRS 9 allows entities to adjust their approach to determining ECLs in different circumstances. Assumptions and linkages underlying the way...
ECLs have been implemented to date may no longer hold during the pandemic. Entities should not continue to apply their existing ECL methodology mechanically but rather develop estimates based on the best available information about past events, current conditions, and forecasts of economic conditions. Consideration should be given both to the effects of COVID-19 and to the significant government support measures being undertaken. It is likely to be difficult currently to incorporate the specific effects of COVID-19 and government support measures on a reasonable and supportable basis. However, changes in economic conditions should be reflected in macroeconomic scenarios applied by entities and in their weightings. If the effects of COVID-19 cannot be reflected in models, postmodel overlays or adjustments will need to be considered.

**Regulators underlined the uncertainties of the ECL estimate.** According to the European Securities and Markets Authority (ESMA 2020), issuers should assess the extent to which the high degree of uncertainty and any sudden changes in the short-term economic outlook are expected to result in impacts over the entire expected life of the financial instrument. The EBA (2020) emphasized that banks should consider the current exceptional circumstances when determining which information can be considered “reasonable and supportable,” as well as considering the nature of the shock (that is, whether it is expected to be temporary or not).

**Supervisors were concerned that, particularly in these times of pronounced uncertainty, IFRS 9 model outcomes may be excessively variable and procyclical.** The European Central Bank (ECB 2020b) recommended that banks facing uncertainty in generating reasonable and supportable forecasts, should give a greater weight to long-term stable outlook evidenced by experience when estimating long-term ECLs. In order to reduce inappropriate volatility in regulatory capital and financial statements, the ECB (2020b) set guidance on the use of forecasts to estimate the ECL during the COVID-19 pandemic. The Bank of England PRA (2020) emphasized that any changes made to ECL to estimate the overall impact of COVID-19 will be subject to very high levels of uncertainty as so little reasonable and supportable forward-looking information is available. This makes it even more important that ECL is implemented well, to reduce the risk of firms recognizing inappropriate levels of ECL, whose overstatement could prompt behavior that leads to unnecessary tightening in credit conditions. While acknowledging that markets have been trending significantly downward, and that steps being taken to contain the virus (including social distancing and business closures) could, if judged in isolation, have negative implications for borrowers’ ability to pay, the PRA emphasized that those factors should not be judged in isolation because governments and central banks globally have announced unprecedented interventions to minimize the impact on individuals and corporates. Given the unprecedented nature of the current situation and the significant uncertainties that exist, a greater reliance is being placed on overlays and the governance around them. Well-balanced judgements about ECL should reflect that the economic shock from the pandemic will likely be temporary, although its duration is uncertain. While it is plausible to assume that the economic consequences of the pandemic could mean that some borrowers will suffer a long-term deterioration in credit risk, many will need the support measures in the short-term but will not suffer a deterioration in their lifetime probability of default.
Policy Recommendations for Prudential Supervisors

3.1 Standard Setting Bodies and Accounting Framework

SSBs support the implementation of high-quality global accounting standards. The Basel “Core Principles for Effective Banking Supervision” (BCBS 2012) require that supervisors determine that banks and banking groups prepare financial statements in accordance with accounting policies and practices that are widely accepted internationally (CP 27, Essential Criteria 1). The Financial Stability Board (FSB 2009) recommended that standards setters give due consideration to approach alternative to the “incurred credit loss” for the recognition and measurement of loan loss provisioning that incorporate a broader range of available credit information and called on the IASB and the Financial Accounting Standards Board (FASB) to continue efforts to achieve a single set of high-quality global accounting standards (Meeting of the Financial Stability Board in London on September 25, 2015).

Valuation practices consistent with accounting standards that are widely accepted internationally contribute to a robust assessment of credit, market, and liquidity risk. For EMDEs this is critical to attract foreign investments. IFRS (a) bring transparency, by enhancing international comparability and quality of financial information; (b) strengthen accountability by reducing the information gap between those responsible for preparing and the users of financial statements; and (c) contribute to economic efficiency by helping investors identity risk and opportunities across the world, thus improving capital allocation.

As emphasized in the Memorandum of Understanding signed with the IFRS Foundation (2017)\(^8\), the World Bank considers reliable financial information a prerequisite for access to finance, while investors’ confidence in financial information is crucial to enhancing trust in capital markets and banks, as well as promoting economic prosperity in EMDEs. The World Bank has been a long-term supporter of work to develop a single set of high-quality global accounting standards, and it has played a leading role in encouraging the development and sound implementation of IFRS and their use around the world, including by assessing compliance using the Reports on the Observance of Standards and Codes.\(^9\) Several projects have been designed to provide EMDEs with technical assistance in this field; some loans are condi-

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tional on sound IFRS implementation as a tool to strengthen the financial sector.

The World Bank supports sound IFRS 9 implementation by its client countries and sees it as critical to ensure global consistency and a robust loan provisioning framework. The incurred credit loss model, which was in place in most jurisdictions before January 2018, might have delayed loss recognition and inflated banks’ capital. As recognized by the Basel Committee for Banking Supervision, ECL is “an important step forward in resolving the weakness identified during the financial crisis that credit loss recognition was too little, too late” (BCBS 2015c). IFRS 9 provides incentives for banks to follow sound credit risk management and vigorous provisioning practices. For these reasons, the WB recommends IFRS 9 implementation, as the expected credit loss is more prudent than the incurred loss model and makes the accounting framework more consistent with the prudential framework.

However, EMDEs supervisors need to be aware of the potential procyclical effect of IFRS 9 (see box 3).

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BOX 3 - Is IFRS 9 Procyclical?

In the aftermath of the pandemic, regulators, supervisors, and accounting standard setters released various statements reasonably aimed at limiting the procyclical effect of IFRS 9. The financial system might act as shock amplifier rather than a shock absorber, exacerbating the feedback mechanism between the real economy and the financial sector. For example, the IAS 39 accounting standards relied heavily on market valuations, which may be justified on transparency grounds, but they induced excessive procyclicality (Borio and Restoy 2020). Furthermore, under IAS 39 a provision for loan losses was recognized only if an impairment event had taken place (“incurred”) and banks failed to fully recognize existing credit losses at the beginning of the credit cycle. Earlier identification of credit losses, which is consistent both with transparency in financial statements and prudential objectives of safety and soundness, could potentially dampen cyclical moves and reduce procyclicality (FSB 2009).

Under IFRS 9, part of the impairment losses that typically occur during a downturn can be recognized at the early stage of the credit cycle, even at origination stage, and should be increased when first signs of the downturn arise, when banks are better able to shoulder losses. Anticipating the downturn might reduce procyclicality and the credit contraction could be less severe. Early loss recognition also reduces market concern about capital adequacy. Nevertheless, various factors might limit the banks’ ability and willingness to anticipate the downturn, including limitations in forecast assumption, model risk, lack of incentives, and shareholders’ expectations (Serrano 2019).

In addition, IFRS 9 might have procyclical effects stemming from cyclical variation in the input of ECL and the systematic shift from stage 1 to stage 2. The incremental credit loss implied by a negative phase of the business or credit cycle might decrease bank capital that, interacting with market confidence, could give rise to deleveraging pressures. The procyclicality of IFRS 9 is a controversial topic, including its comparison with the current expected credit losses (CECL) model (Buesa et al. 2019; ESRB, 2019a. A recent study from the European Systemic Risk Board (ESRB 2019a) supports the idea that IFRS 9 might be procyclical at the onset of the downturn, if the triggers to transfer financial assets to stage 2 are too high and hence banks are not able to anticipate the downturn far enough in advance. This might produce a material transfer of exposures from stage 1 to stage 2 (cliff effects) under already deteriorated economic conditions, which in turn might exacerbate the negative evolution of the business cycle and become a concern from a financial stability point of view.

However, the current prudential framework, compared to the framework in place at the time of the global financial crisis, incorporates several buffers (capital conservation buffer [CCB], countercyclical buffer [CCyB], and global systematically important banks [G-SIB]) that could mitigate procyclicality. A comprehensive discussion on procyclicality should be not isolated to IFRS 9, but needs to be widened to the Basel III framework, looking at that whole system (capital buffers, transitional arrangements, and so forth). It is therefore important that EMDEs introduce a macro-prudential framework consisting of buffers that could counteract IFRS 9 procyclical effects (see recommendation n. 6).
3.2 Recommendations for Prudential Supervisors in EMDEs That Have Not Yet Implemented IFRS 9

3.2.1. The Preparatory Phase

RECOMMENDATION N. 1:
Prudential Supervisor Should (i) Adequately Prepare IFRS 9 Implementation, (ii) Strategize the Transition to it, (iii) Raise Awareness with the Banks’ Board on the Degree of Challenges, and (iv) Decide about the Perimeter of Application of the Accounting Standards

Prudential supervisors and banks should be adequately prepared before embarking on IFRS 9 implementation. It requires material investment in new models, information technology infrastructures, data collection, risk management, governance, and human resources, which might be even more difficult to undertake during a period in which banks will be struggling with the fall out of the COVID-19 pandemic. In addition, lack of familiarity with modeling credit risk in banks and with prudential supervisors amplifies the degree of challenges.

Prudential Supervisors should formulate a comprehensive preparatory plan. Even though banking prudential supervisors might not necessarily be responsible for accounting standards, we recommend strengthening the cooperation among prudential supervisors and accounting standard setters, by fostering information sharing, understanding the interaction between prudential and accounting framework, and sharing perspectives on respective initiatives.

Prudential supervisors in EMDEs should strategize the transition to IFRS 9. It might be useful to embed the IFRS 9 implementation project into supervisory priorities and spell out the preconditions for an effective transition. During the preparatory phase we recommend prudential supervisors take stock of international standards, guidelines (BCBS 2015c, 2016, 2017a, 2020), and good practices, focusing on the interactions with the accounting framework, and verifying whether amendments are needed in the supervisory reporting systems.

Prudential supervisors must raise awareness with banks’ boards and senior management on the significance of the challenges. Scheduling regular meetings with banks’ specific functions (for example, risk management, chief financial officer, IT, board) might help assess the stage of preparedness by the concerned functions and quantify the expected impact of IFRS 9 on banks’ profitability, loan loss provisions, and capital. By involving the external auditor in bilateral and trilateral meetings, prudential supervisors might not only be able to better understand how auditors intend to fulfil their obligations, but also to corroborate banks’ estimates of IFRS 9 quantitative impact (see boxes 4 and 5).

>> BOX 4 - Thailand: Preparation for Implementing Thai Financial Reporting Standards 9 (TFRS 9)

In 2016, the Bank of Thailand (BOT) together with Thai financial institutions started preparing for the TFRS 9 implementation. BOT developed a strategy and policy and operational processes, as well as education and training for staff and stakeholders. The BOT engaged with a wide range of stakeholders, including ministries, regulators, banks, auditors, standard setters, and the real sector. The BOT and financial institutions also invested, developed, and adjusted systems and databases to support TFRS 9 implementation. The BOT surveyed the level of preparedness for TFRS 9 in banks and performed quantitative impact studies on ECL and classification and measurement. In 2018, the BOT started to actively oversee the banks’ implementation progress and issue regulations. Starting from the last quarter of 2018, banks were required to submit to BOT their TFRS 9 data for four consecutive quarters, until the third quarter of 2019. Early adoption was allowed, but none of the banks chose to proceed earlier.
BOX 5 - The Republic of North Macedonia: Preparation for Implementing IFRS 9

Implementation of IFRS 9 by the National Bank of the Republic of North Macedonia (NBRNM) involved several departments and was conducted under close collaboration with relevant stakeholders, such as banks, the Banking Association, and external auditors. During the preparatory phase, the NBRNM discussed necessary amendments to the regulations as well as possible effects of IFRS 9 implementation on the financial performance and business processes of the banks (third and fourth quarters of 2016). The NBRNM had an open discussion with the Banking Association, as well as the large banks and external auditors, to collect insights from the industry and gather additional guidelines that local subsidiaries of European Union (EU) banks received from their parent companies. The NBRNM also investigated the degree of banks’ preparedness, IFRS 9 challenges, and possible effects on banks’ reporting and balance sheets in the course of round tables and bilateral meetings. In 2017, the NBRNM received technical assistance from international organizations (World Bank Financial Sector Advisory Center and the Centre for Financial Reporting Reform, among others) and the EU supervisors (the Bank of Slovenia) to build capacity. In February 2017, the NBRNM presented its strategy to commercial banks and discussed the IFRS 9 implementation, including methodological issues.

The draft version of the NBRNM Decision on the methodology for credit risk management was enriched by the public consultation. However, the comments, despite being formally considered, were not published. During the implementation phase, a questionnaire was sent to the banks and savings houses regarding their activities for the implementation of the decision on credit risk management (February 2019). In addition, there is an ongoing communication with banks through Q&As that are published at the NBRNM website. The NBRNM also issues guidance on topics that it deems require further clarification.

Initially, there was a significant difference in preparedness and awareness about IFRS 9 by local banks and banks owned by EU parent banks. EU-owned banks were better prepared by relying on their banking group guidelines and being aware of the required data. At the same time, local banks and banks owned by parent banks outside the EU could leverage the NBRNM instructions. The NBRNM states that currently all banks have converged to a similar level of preparedness due to the introduction of changes to their regulatory and operational systems.

A key step of the preparatory phase is the decision about the perimeter of application of IFRS 9. This is somehow related to a proportionate application of accounting standards, that, similarly to the prudential standards, could take account of the size and complexity of banks. Considering the nexus between accounting provisioning and regulatory capital, the Basel Committee intervened several times on this matter (2015, 2017, 2020).

In line with the Core Principles for Effective of Banking Supervision (2012, pars. 17 and 31, also Core Principle 8), the Basel Committee guidance on credit risk and accounting for expected credit loss (BCBS 2015c) recognized that prudential supervisors may adopt a proportionate approach about the supervision and standards that they impose on banks. However, the committee also warned that the use of properly designed proportionate approaches should not jeopardize the high-quality implementation of the ECL accounting frameworks. Proportionality should enable banks to adopt sound allowance methodologies commensurate with size, complexity, structure, economic significance, and risk profile. In other words, proportionality should not result in laxity when calculating ECL.

When defining the perimeter of application of IFRS 9, EMDEs have two basic options: (a) requiring compliance of all banks for both individual and consolidated financial statements and (b) limiting application to banks’ consolidated accounts, or to listed banks, or to banks reaching a certain size and complexity. For example, in the European Union, IFRS are mandatory only for consolidated accounts of publicly traded companies; EU member states might permit or require IFRS standards also for (a) annual individual accounts of publicly traded companies and (b) consolidated and annual accounts of companies other than those publicly traded (Art. 4 and 5 [EU] Regulation no. 1606/2002; see box 6). In Rwanda, all banks are required to comply with IFRS (art. 46 Banking Law n. 47/2017), both for individual and consolidated financial statements, regardless of their status as listed or unlisted companies. In Brazil, IFRS are mandatory only for consolidated financial statements of banks in segments 1, 2 and 3, while smaller institutions might adopt them beginning in 2022 (see box 7).

Each policy option has its own advantages and disadvantages. Requiring IFRS for all banks avoids two-tier or multiple-
Tier accounting systems (listed/not listed banks, consolidated/individual accounts, large/small banks) and homogenizes regulatory reporting. However, smaller banks might find it difficult to build up an in-house ECL model at a time when IFRS resources are in high demand. This could result in excessive reliance on outsourcing with limited internal capacity to manage the associated risks (reliance on a third party, conflict of interest of the provider, security of data, termination rights, and so forth). Prudential supervisors need to be mindful of these risks and take appropriate actions to address them.

By contrast, imposing IFRS application only to banks of a certain size adheres to the proportionality principle, but might fragment the accounting and reporting framework and create cliff effects (for example, when a bank is just below the threshold). In such cases, we recommend also allowing small credit institutions belonging to banking groups to apply IFRS, to align the accounting and financial reporting framework within the financial conglomerate or banking group.

Limiting IFRS 9 application to listed banks should not result in opaque information by nonlisted banks on their asset quality and provisioning indicators. The Basel “Corporate Governance Principles for Banks” (BCBS 2015a) requires disclosure and transparency toward depositors, shareholders, and other stakeholders by all banks. Regardless of its listing on a stock exchange, a bank should disclose key information concerning risk exposures and risk management strategies (BCBS 2015a, par. 155). Furthermore, EMDEs that implemented the Basel II/III framework should be vigilant on the Pillar 3 framework,11 which sets out disclosure requirements on credit risk, composed of both qualitative and quantitative information, including accounting provisioning for credit loss (BCBS 2019b).

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BOX 6 - European Union: Proportionality in Application of IFRS 9

The EU regulatory framework does not prescribe IFRS 9 for banks’ individual accounts. In the European Union only consolidated accounts of publicly traded companies are required to be prepared in conformity with international accounting standards. Member states may permit or require that publicly traded companies also prepare their annual individual accounts in conformity with international accounting standards. Furthermore, member states have the same option in relation to companies other than those publicly traded (Art. 4 and 5 Regulation EU 1606/2002). Italy, which in the past had exerted both options and required all banks to prepare their individual and consolidated accounts according to IFRS (D. Lgs n. 38/2005), recently allowed nonlisted companies to prepare their financial statements according to national accounting standards (art. 1, sec. 1070 L. 145/2018).12

In substance, the European Union calibrated IFRS application to the size and complexity of companies, as well as to the duty of disclosure stemming from the status of listed entities. Assuming that publicly traded companies are more complex than nonlisted companies, listed companies’ consolidated accounts should follow IFRS standards to ensure a higher degree of transparency and comparability. This is an important policy option that EMDEs should contemplate before embarking on IFRS 9 implementation, considering the associated challenges for small, less complex, and nonlisted banks.

The banking sector does not deviate from this general rule. Indeed, the Regulation EU n. 575/2013 (Capital Requirement Regulation; CRR) Art. 24 states that the valuation of assets and off-balance sheet items is (“only”) affected in accordance with the applicable accounting framework. By way of derogation from paragraph 1, competent authorities may require that institutions effect the valuation of assets and off-balance sheet items and the determination of own funds in accordance with International Accounting Standards as applicable under Regulation (EC) No 1606/2002.

According to a recent study from the European Commission (2020b), banks that use national accounting standards for their financial statements instead of IFRS are mostly small, local retail banks. The proportion of total banking assets reported under generally accepted accounting principles (GAAP) is less than 5 percent of total banking assets, with the exception of Germany (52.1 percent) and Austria (22.7 percent). Even though many national accounting standards base the credit risk provisions only on losses already incurred, the overall impact on prudential ratios is considered limited, because the national accounting frameworks often already have other provisions, such as general credit risk provisioning, that limit the impacts of accounting differences in practice.

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11. See https://www.bis.org/basel_framework/standard/DIS.htm.
12. To date, no banks have moved to national accounting standards.
In Brazil, consolidated financial statements based on IFRS are required for publicly listed financial institutions and for financial institutions in segments 1, 2, and 3. Central Bank of Brazil (BCB) Resolution 4,776 of 2020 requires listed financial institutions and financial institutions in segment 1 (total assets above 10 percent of GDP or performing relevant international activity), segment 2 (total assets between 1 percent and 10 percent of GDP), and segment 3 (total assets between 0.1 percent and 1 percent of GDP) to disclose their consolidated financial statements in accordance with IFRS standards. Additionally, the BCB is the accounting regulator for the banking sector, pursuant to the Banking Law and Law 11941 of 2009. Circular BCB 1,273 of 1987, which established the COSIF (Financial Institution Accounting Regulatory Requirements), sets the local accounting standard for banks and requires financial institutions to publish financial statements and explanatory notes, along with the external auditor’s opinion. Additionally, financial institutions that are not obliged to publish consolidated financial statements, but want to do so for any reason, will have to comply with full IFRS rules. Consequently, about half of the banks prepare and publish financial statements that comply with IFRS. In addition, all banks prepare and publish solo financial statements that comply with the COSIF. For individual company’s financial statements, the auditor’s opinion refers to BRGAAP; the auditor’s report usually includes an explanatory paragraph describing the differences between BRGAAP and IFRS.

RECOMMENDATION N. 2: Prudential Supervisors in EMDES Should Invest in Credit Risk Modeling Capacity; However, they Should Refrain from Moving to the Internal Rating Based (IRB) Approach

Sixty-nine percent (69 percent) of respondents to our survey indicated that modeling risk was the major challenge when implementing IFRS 9. Prudential supervisors in EMDES often lack personnel skilled in quantitative analysis. This shortage is especially problematic for those EMDES that have approved the use of the advanced approaches in Basel II/III in their jurisdictions, which allow banks to rely on internal models for the determination of credit risk estimates and capital requirements (FSB, IMF, and WB 2011).

Human resources skilled in modeling credit risk are typically scarce and generally not available to prudential supervisors in EMDES for a variety of reasons, including more attractive compensation in the private sector. When Basel II introduced the internal model approaches (in 2004), many prudential supervisors in high-income countries and some in EDMEs hired the few qualified staff skilled in quantitative disciplines and built their risk model teams. Others supervisors in EMDES with more compelling budget constraints now have to compete with banks for scarce resources when dealing with IFRS 9 implementation. They can however still build up capacity on ECL model through online training platforms and technical assistance.

Experience from the field shows that in some cases staff skilled in modeling credit risk are appointed to the financial stability department, but synergies with prudential supervision are not always fully realized. This might depend on various reasons, for example because the financial stability unit is incorporated within the central bank, whereas the supervision is exerted by another authority, and limited coordination is in place. While there are jurisdictions where financial stability and prudential supervision work closely together, there is also evidence of an excessively rigid allocation of responsibilities. Prudential supervisors in EMDES should strive to overcome this silo approach and make the best use of qualified resources for tasks requiring quantitative skills (for example, valuation of the internal capital adequacy and assessment process, stress testing, and assessment of IFRS 9 models).

Supervisory technology (SupTech) solutions can be useful in addressing challenges related to data collection and ECL modeling. SupTech applications can enhance data collection and validation required for building up an ECL model. First, they allow for various forms of automated reporting, such as (a) submission of harmonized information by banks to supervisors and (b) extraction of relevant information from the IT systems of supervised banks. Second, various advanced methods, like big data analytics and machine learning, can be used to improve ECL modeling and validation. SupTech applications can also be used for analyzing huge amounts of data for forecasting and incorporating forward-looking information in ECL. Estimation of major parameters (PD, SICR, and LGD, for example) can be another possible application.

Prudential supervisors in EMDES might be tempted, in conjunction with IFRS 9 implementation, to allow banks...
to use internal models to calculate capital requirements. We discourage this choice. Particularly EMDEs with less internationally integrated financial systems and with substantial supervisory capacity constraints should first focus on reforms to ensure compliance with the Basel Core Principles and only then move to the more advanced capital standards at a pace tailored to their circumstances (FSB, IMF, WB 2011). Shortcomings are still observable in some EMDEs in fundamental areas (for example, independence of the supervisor, transactions with related parties, corporate governance, risk management and supervisory approach) (Adrian and Narain 2019).

Being based on historical data, internal models are generally considered to be more risk sensitive than the standardized approach. Despite input constraints and output floors aimed at ensuring conservativeness in model parameters and limits to the regulatory capital benefits, internal models can still play an important role, aligning the regulatory framework with the risk management practices and improving capital allocation. Nevertheless, there are various counterindications in the adoption of IRB approach by EMDEs.

Despite complementarities, there are several methodological differences between the IFRS 9 impairment model and the IRB approach. The literature emphasized the differences in the PD time horizon (one year versus lifetime), the different degree of conservativeness of the LGD (downturn/ubiais) and point in time versus through the cycle estimates (ESRB 2017; D’Hulster, Salomao-Garcia, and Letelier 2014). While internal models can be used as a starting point for estimating ECL for accounting purposes, moving to IRB approaches to reap synergies with IFRS 9 is not a good option for prudential supervisors in EMDEs who have not yet build the resources and capacity for credit risk modeling. Uncertainty and risks are attached to the use of models, including those stemming from risk weight manipulation. In our opinion, these risks might be exacerbated in those EMDEs where the supervisory capacity to understand models is immature.

3.2.2 The Implementation Phase

RECOMMENDATION N. 3:
Supervisors Need to Set Clear, Timely, and Comprehensive Expectations on ECL Framework, Ensuring Broad Consistency Between Credit Classification Criteria and the IFRS Staging Process

Guidance should be issued before IFRS 9 enters into force. IFRS 9 is principle based and applicable to all industries, not just banks. However, as banks’ lending generates credit risk, the application of IFRS 9 might require more detailed guidance than what is provided under applicable accounting standards (Baudino, Orlandi, and Zamil 2018). To be able to meet expectations on adoption, the banking industry should be familiar with supervisory expectations before the standard is applicable. Moreover, a parallel run between IFRS 9 estimated ECL and impairment calculation under the previous accounting framework is useful to test the IFRS 9 outcomes.

Modeling ECL involves multiple challenges and material discretion; supervisors might consider setting expectations on key parameters. Supervisors could require a minimum historical data time frame for the estimation of the PD. Where only limited data are available, prudential supervisors might require a greater margin of conservatism. Factoring off-balance-sheet commitments into provisioning is a key decision point (IFRS 9 B.5.5.30 and B.5.5.31), particularly in relation to the forward-looking information. The loss given default (LGD) is affected by the amount and the timing of the cash flow expected from the foreclosure of the collateral: supervisory haircuts should ideally be based on robust statistical evidence on the recovery rates.

The guidance should cover also the governance of the ECL model. IFRS 9 implementation requires the involvement of various hierarchical levels, including the board, which should approve the project governance, consider its impact in the banks’ strategic plan, and allocate enough budget. The guidance should emphasize the board’s responsibility for the oversight of the outcomes, the initial approval and the continuous implementation of the allowance methodology, the effectiveness of the internal control system around it, and the approval of the disclosure policy.

Credit classification criteria in place for prudential purposes are usually more granular than the IFRS 9 staging process. IFRS 9 envisages three stages for financial instruments assessed at amortized cost or at FVTOCI: (a) exposures without SICR since initial recognition (stage 1); (b) exposures with SICR but not credit impaired (stage 2); and (c) exposures credit impaired (stage 3). When measuring the loss allowance, banks should consider 12-month ECLs for stage 1, as opposed to lifetime ECLs for stages 2 and 3 (IFRS 5.5.3 and 5.5.5). From a prudential perspective, credit exposures are instead classified based on a broader range of quantitative (days past due) and qualitative criteria, which usually result in a greater stratification of borrowers.

It is recommended to ensure a high degree of consistency between accounting and prudential classification.
Alignment does not necessarily mean that the preexistent prudential credit classification criteria should be dismantled but rather that each bucket should find a univocal correspondence into one of the three IFRS 9 stages.

The granularity incorporated in the prudential perspective strengthens banks’ risk management practices as well as supervisors’ early intervention capacity; in parallel, a consistent implementation of internationally harmonized definitions for non-performing loans (NPLs) and forbearance increases comparability of asset quality. A well-stratified loan classification system provides banks with a wider set of information, which is useful during the various phases of the credit cycle (underwriting and approval, monitoring, matrix migration, reporting, and so forth). Prudential supervisors also benefit from this stratified information so as to detect adverse trends early, benchmark credit institutions, and accurately calibrate stress testing scenarios. To ensure international consistency, it is important that the BCBS guidelines to harmonize NPLs and forbearance definitions are implemented.

The IFRS 9 staging process enhances comparability of financial statements. Market participants are interested not only in the amount on non-performing or impaired assets, but also in the credit risk exposures which are more likely to migrate to the non-performing status. For loans experiencing a SICR, default is more likely than at initial recognition. Prudential supervisors and investors are keen to understand the assumptions and estimation techniques used by banks to determine whether the credit risk of financial instruments has changed, which indicators have been included (IFRS 9 par. B5.5.17), and how forward-looking the information is that has been used in determining the ECL.

Whereas few jurisdictions opted for a full alignment between prudential and accounting standards, others maintained preexisting prudential classification rules. For example, we analyzed the Thailand regulation and found that it opted for a full alignment between prudential and accounting standards, moving from five pre-existing risk categories (pass, special mention, substandard, doubtful of loss, and loss) to three (performing, underperforming, non-performing), which replicate the IFRS 9 staging (see box 9). This approach reduces potential discrepancies between the prudential and accounting perspectives. Yet, it might also result in losing information on past due vintage, considering that the stage 2 bucket might include credit exposures with different intrinsic risks of underperformance (days past due might vary from 31 to 90). We also analyzed the Brazilian regulation, which is at the opposite end: Brazil will likely retain for informative purposes its credit risk classification system, consisting of nine categories (from AA to H). As a result, the Central Bank of Brazil holds more granular information on past-due exposures (see box 8); nevertheless, it could be more difficult to reconcile the accounting framework with the prudential standards (stage 2 exposures, general provisioning added back to tier 2 capital).
According to BCB Resolution nº 2,682, loans and leasing operations must be classified according to their risk level in one of the categories described in table 2. Also, banks should consider lifetime ECL based, among other things, on the number of days past due together with certain characteristics of the borrower, including its financial situation and economic activity; collaterals pledged; leverage; ability to generate economic results; cash flows; quality of management; punctuality of payments; contingencies; credit limits; and nature of the transaction. For past due payments, banks should assess the risk category monthly; for other types of evaluation, each six months or annually.

The supervisor would intend to keep, for informative purposes only, these prudential classification categories also after IFRS 9 will be fully implemented for individual banks’ financial statements. The idea is that ECL will be calculated using IFRS9 methodology and, after this, fitted in the proper letter in accordance with its ECL level. While this will ensure more granular information on day-past-due, it could make it more challenging the reconciliation with the IFRS 9 staging (for example, clear identification of significant increase of credit risk)

The provisioning floors have been calibrated based on a statistical methodology. They will be likely kept as a prudential backstop. The fact they are provided in the secondary law (regulation) will make it easier for the supervisor to adjust it, if needed.

<table>
<thead>
<tr>
<th>Risk category</th>
<th>Minimum ECL</th>
<th>Days past due</th>
</tr>
</thead>
<tbody>
<tr>
<td>AA</td>
<td>&lt; 0.5%</td>
<td>None</td>
</tr>
<tr>
<td>A</td>
<td>&lt; 1.0%</td>
<td>None</td>
</tr>
<tr>
<td>B</td>
<td>&lt; 3.0%</td>
<td>15–30</td>
</tr>
<tr>
<td>C</td>
<td>&lt; 10.0%</td>
<td>31–60</td>
</tr>
<tr>
<td>D</td>
<td>&lt; 30.0%</td>
<td>61–90</td>
</tr>
<tr>
<td>E</td>
<td>&lt; 50.0%</td>
<td>91–120</td>
</tr>
<tr>
<td>F</td>
<td>&lt; 70.0%</td>
<td>121–150</td>
</tr>
<tr>
<td>G</td>
<td>&lt; 100.0%</td>
<td>151–180</td>
</tr>
<tr>
<td>H</td>
<td>100.0%</td>
<td>&gt; 180</td>
</tr>
</tbody>
</table>

Note: ECL = expected credit loss.
BOX 9 - Thailand: Credit Classification Criteria and IFRS 9 Staging

The BOT issued Notification FPG 23/2561: Regulation on Asset Classification and Provisioning of Financial Institutions. This regulation replaced the existing BOT regulation on loan loss provisioning, which set out more conservative provisioning requirements than IAS 39. The objective of this regulation is to ensure that financial institutions have adequate provisions for losses that may occur from their assets, especially loans that are the core assets of financial institutions. The regulation requires financial institutions to classify financial assets and commitments in three stages: (a) financial assets and commitments that are credit impaired (non-performing); (b) financial assets and commitments that have significant increase in credit risk (underperforming); and (c) financial assets and commitments that have no significant increase in credit risk (performing). It also requires setting aside provisions for expected credit losses and writing off assets in accordance with the financial reporting standards. The BOT thus moved from six to three credit categories, replicating the TFRS 9 staging.

The regulation provides criteria for classification in each of the three stages. The criteria for stage 3 classification include, among others, the 90 days past due criterion, as well as unlikely to pay. For stage 2, an exposure being more than 30 days past due automatically qualifies it for that stage, without the rebuttal present in IFRS 9. The regulation also allows the BOT to order classification of exposures in stage 2 or stage 3. According to TFRS 9 and IFRS 9, an entity shall accrue interest income on non-performing assets, and both Thai and International Standards require an entity to set aside provision against that accrued interest.

RECOMMENDATION N. 4:
Prudential Supervisors Should Consider Prudential Backstops on Provisioning

IFRS 9 amplifies management judgment and might give rise to undue discretion when dealing with model choices. To preserve adequate coverage of NPLs, supervisors in EMDEs could implement prudential backstops. The definition of ECL and the prescribed methodology to calculate it increases both discretion and uncertainty in modeling predictivity. This makes the provisioning outcome subject to higher variability, which could in turn undermine the comparability of reported capital adequacy across jurisdictions (Coehlo, Restoy, and Zamil 2020).

There are several tools to ensure, directly or indirectly, minimum prudential provisioning. For example, under Basel internal ratings-based (IRB) approaches, banks compare the total eligible provisions to the regulatory measure of expected losses and any shortfall is fully deducted, without considering tax effects, from Common Equity Tier (CET1) capital (the excess is instead added back to tier 2 capital, up to 0.6 percent of credit risk-weighted assets [RWAs]). Furthermore, in the European Union, Regulation (EU) 2019/630 introduced a minimum loss coverage for non-performing exposures originated after April 2019; if the coverage is lower than the minimum, the difference is deducted from CET1. Moreover, the Monetary Authority of Singapore (MAS) requires all locally incorporated domestic systemically important banks to maintain a minimum regulatory loss allowance of 1 percent of non-credit-impaired exposures (that is, stage 1 and 2 exposures), net of collaterals. This is done via an appropriation of retained earnings into a separate, nondistributable regulatory reserve account.

EMDEs that already have minimum provisioning levels might consider retaining them. The Basel Committee (2017a) does not discourage such regulatory practice, if deemed appropriate by a jurisdiction. Loan loss reserves for regulatory purposes could even be in excess of those that would be established pursuant to application of IFRS 9. Provisioning floors can be set directly by the law or by the supervisor. In the former case, it might take longer to adjust them; in the latter case, there is the risk that prudential supervisors could act under political or industry interference, particularly when their independence is limited. Retaining the existing floors could mitigate the risk inherent in the adoption of sophisticated ECL models (Restoy and Zamil 2017). Alternatively, when moving to IFRS 9 countries could consider introducing new floors for stage 1 and 2 financial assets, as the experience of Thailand suggests (see box 10).

13. ECL is an unbiased and probability-weighted amount that is determined by evaluating a range of possible outcomes; it should reflect the time value of money, as well as reasonable and supportable information that is available at the reporting date without undue cost or effort about past events, current conditions, and forecasts of future economic conditions (IFRS 9, 5.5.17).
3.2.3. The Monitoring Phase

RECOMMENDATION N. 5:
Prudential Supervisors Should Strike a Balance between Flexibility and Oversight on Entry and Exit Criteria to and from Stages 2 and 3

In the aftermath of COVID-19, many jurisdictions adopted various measures to facilitate loan restructuring. According to IFRS 9 (par. 5.5.12), if the contractual cash flows on a financial asset have been renegotiated or modified and the financial asset was not derecognized, an entity shall assess whether there has been a SICR by comparing (a) the risk of a default at the reporting date (based on the modified contractual terms) and (b) the risk of a default at initial recognition (based on the original, unmodified contractual terms).

The IASB (2020) clarified that the extension of payment holidays to all borrowers’ classes of financial instruments should not automatically result in all those instruments being considered to have suffered an SICR. Borrower relief measures can take various forms of restructuring, such as moratoria, payment holidays, and so forth (FinSAC 2020). In many cases, a judicious and prudent restructuring, accompanied by disclosure requirements ensuring market discipline, might effectively support temporary illiquid borrowers (IMF and World Bank Staff 2020). Nevertheless, in other circumstances restructuring could affect the net present value of the exposure, particularly for borrowers unlikely to restore their creditworthiness. Banks and borrowers might abuse these measures, also under the pressure of related parties.

Prudential supervisors should strictly monitor regressions from stage 2 to stage 1, which should be based on a history of up-to-date and timely payment performance against the modified contractual terms. If the contractual cash flows on a financial asset have been renegotiated or otherwise modified, but the financial asset is not derecognized, that financial asset is not automatically considered to have lower credit risk (IFRS 9, par. 5.5.27). The bank must assess whether there has been a SICR since initial recognition based on all reasonable and supportable information that is available without undue cost or effort. This includes historical and forward-looking information as well as an assessment of the credit risk over the expected life of the financial asset, which includes information about the circumstances that led to the modification.

IFRS 9 does not specify a probation period, but we recommend conservatism and compliance with prudential standards. To exit the forborne/restructured status, international guidelines require a probation period of not less than one year (BCBS 2017a, par. 40). According to IFRS 9, a borrower would need to demonstrate consistently good payment behavior over a period before the credit risk is considered to have decreased. Given its principle-based nature, IFRS 9 does not quantify the period; nevertheless, a history of missed or incomplete payments would not typically be erased by simply making one payment on time following a modification of the contractual terms (IFRS 9 par. 5.5.27).

We recommend setting timely write-off criteria to mitigate the risk that NPLs can be carried on the balance sheet for a long-time and to avoid distorting the coverage ratio. IFRS 9 does not set a timeline beyond which an impaired financial instrument should be written off. However, it requires an entity to directly reduce the gross carrying amount of a financial asset when there is no reasonable expectation of recovering a financial asset in its entirety or a portion thereof (par. B4.5.9). Further, IFRS 7 requires disclosure of write-off criteria. Even though there is no harmonized prudential standard on write-off, the literature emphasizes the benefit of timely write-offs of uncollectible loans (Gaston and Song 2014), and timely write-offs of unrecoverable loans has become a key supervisory focus in certain jurisdictions (ECB 2017a).

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14. BCBS (2015c) only prescribes that (a) robust and sound methodology for assessing credit risk and measuring the level of allowances generally will outline the bank’s policies and procedures on write-offs and recoveries (Principle 2) and that (b) supervisors should be satisfied that the bank is following policies and practices consistent with the ECL measurement principles, including that uncollectability is recognized in the appropriate period through allowances or write-offs (Principle 10).
The BOT Notification FPG 23/2561: Regulation on Asset Classification and Provisioning of Financial Institutions does not allow excess provisions that may have arisen as a result of transitioning to TFRS 9 to be reversed on day one of adoption. In cases where the provision according to TFRS 9 was less than the provision amount that a financial institution had set aside under the former regulation, the excess provision should not be reversed and recognized as income on the first day of TFRS 9 implementation. Yet, a financial institution must amortize this excess provision within five years by either the straight-line method or based on the financial institution’s plans by offsetting the excess provisions when set aside provisions for financial assets and commitments under the new regulation. In cases where the provision under TFRS 9 after the adoption but within five years is still less than the provision under the former regulation, a financial institution could gradually reverse excess provision and recognize it as income. Aggregate excess provisions were around 18 percent.

The BOT has also issued an additional regulation: Minimum Requirements on Provisions for Financial Institutions and Financial Business Groups. This regulation ensures that financial institutions have adequate provisions to support unexpected events, thus reducing capital fluctuations due to the cyclical provisions of TFRS 9. This regulation requires that financial institutions maintain a minimum provision of 1 percent of assets and off-balance-sheet items classified as performing (stage 1) and underperforming (stage 2). A financial institution maintains a 1 percent provision floor by appropriating a shortfall from capital (instead of recognizing provision in profit or loss, as occurs under TFRS 9).

The provisions for assets and commitments in stage 1 and stage 2 are classified as general provisions. These provisions may be included in tier 2 capital up to a limit of 1.25 percent of credit risk weighted assets for banks using standardized approach. For IRB banks, these provisions are part of eligible provisions, and any excess can be included up to a maximum of 0.6 percent of credit risk weighted assets in tier 2 capital. An excess means that the total eligible provisions are greater than regulatory expected loss.

RECOMMENDATION N. 6:
Prudential Supervisors Should Have Tools in Place to Mitigate Procyclicality

Minimum provisioning requirements that EMDEs have in place against nonimpaired loans might play a countercyclical role. However, it might be argued that these floors, which could often be higher than general provisioning in high-income countries, compensate for more volatile economies.

In addition, some EMDEs have neither formal, nor concretely replenished, prudential buffers, which were introduced to mitigate system-wide vulnerabilities and designed precisely to be used in times of stress. IFRS 9 was conceived to mitigate the procyclicality embedded in IAS 39, but it might have unintended consequences. The introduction of a gradual loss recognition under the three stages approach could reduce procyclicality at the cost of front-loading losses (Kund and Rugilo 2020). However, this might weaken capital adequacy, particularly at the beginning of a sudden adverse scenario, which might lead to a credit supply shock. It is therefore important that prudential supervisors, before introducing IFRS 9, have in place replenished prudential buffers (capital conservation, countercyclical, systemic) that, if needed, can be released to dampen the procyclical effects (see boxes 3 and 11).

EMDEs should take advantage of transitional arrangements that smooth the impact on capital and alleviate procyclicality. As clarified in 2017 by the Basel Committee, transitional arrangements must apply only to new provisioning (provisions that do not exist prior the adoption of an ECL accounting model) and must adjust CET1. Jurisdictions should choose between the static and dynamic approach.15 In our opinion, a dynamic approach might entail more flexibility, since it takes into account also the evolution of new expected credit loss. The transition period begins on the date when a bank adopts ECL accounting and cannot exceed five years. Jurisdictions must disclose details of transitional arrangements (BCBS 2019a, CAP90.7).

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15. The static approach permits only one calculation of the transitional adjustment; the dynamic approach allows periodic recalculation within the transition period.
Considering the COVID-19 pandemic, the committee amended transitional arrangements (April 2020). Modifications allowed jurisdictions to (a) apply the existing transitional arrangements, even if they were not initially implemented when banks first adopted the ECL model; (b) permit banks to switch from the static to the dynamic approach; and (c) use alternative methodologies to approximate the cumulative difference between provisions under the ECL accounting model and provisions under the prior incurred loss accounting model (BCBS 2020). Furthermore, irrespective of when a jurisdiction initially started to apply transitional arrangements, for 2020 and 2021 jurisdictions may allow banks to add back up to 100 percent of the transitional adjustment amount to CET1; the add-back amount must then be phased out on a straight line basis over the subsequent three years.

Transitional arrangements are voluntary, but banks should make use of them because the IFRS 9 impact could be higher than expected and result in an unexpected decline in capital ratios. In response to the great lockdown, some prudential supervisors recently allowed banks that at the time had not opted to adopt transitional measures to apply them (ECB 2020a).

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BOX 11 - Italy: Views on the Procyclicality of IFRS 9

The Bank of Italy emphasizes that IFRS 9 could amplify procyclicality. The Bank of Italy raised concerns about unintended consequences stemming from IFRS 9. As also confirmed by the recent COVID-19 pandemic, banks are not always able to anticipate a crisis, with the result that IFRS 9 can be highly procyclical at the beginning of a crisis. While IFRS 9 has a certain degree of flexibility that can help fixing procyclical risks to some extent, the COVID-19 experience has made clear the need for a post-implementation review of the standard to verify whether any modification is needed, according to the Bank of Italy.

The Bank of Italy quoted a recent study from ESRB (2019a), which supports the idea that IFRS 9 might be procyclical at the onset of the downturn, if the downturn is not anticipated far enough in advance and transfers of financial assets to stage 2 are too high. This situation might produce more pronounced “cliff effects” (material transfer of exposures from stage 1 to stage 2) under already deteriorated economic conditions. In those circumstances, a substantial increase in expected credit losses would occur when already entering the downturn, which, in turn, could exacerbate the negative evolution of the business cycle and become a concern from a financial stability point of view.
3.3 Recommendations for Prudential Supervisors in EMDEs That Have Already Transitioned to IFRS 9

Most of the recommendations discussed in this section might be also applicable to countries that have already implemented IFRS 9. Authorities may consider if a revision is warranted to introduce, for instance, proportionate application of accounting rules, the clear statement of supervisory expectations, or the use of prudential backstops.

**RECOMMENDATION N. 7:** Supervisors Should Oversee the Extent of Banks Reliance on Third Party Providers

To meet IFRS 9 requirements, we noted extensive intra- and extra-group outsourcing by banks in EMDEs. Local banks mainly hired consultants to build ECL models (see box 12). Subsidiaries of internationally active banks benefitted from the parent companies’ centralized functions (risk management, IT, budgeting, and so forth).

Outsourcing has the potential to reduce cost and transfer skills. However, it could impede the ability of banks to demonstrate to regulators that they are taking appropriate steps to manage their risks and comply with applicable regulations. For a local bank, purchasing an ECL model from an external vendor, without fully understanding the key drivers, is not advisable. Similarly, for a foreign owned bank, a mechanical implementation of ECL models, not tailored to the local environment, might have potential unintended consequences (for example, the use of forward-looking information derived from high-income countries, where the GDP growth rate is generally lower than that forecast in emerging markets, might lead to disproportionate ECL, triggering procyclical effects). It is important to ensure that foreign owned banks can exert their credit judgement.

**Supervisors in EMDEs should require that banks have a good understanding of the risk management and finance departments of the ECL model and rigorous governance and internal control processes for assessing external vendors.** Authorities need to verify that ECL models reflect the institution’s business model and risk profile and are well understood by the bank. Prudential supervisors should put emphasis on the banks’ board role to hold the senior management responsible for developing and maintaining sound ECL methodology, which should be comprehensively documented and independently validated (BCBS 2015c).

The supervisor should be satisfied that the methods employed by banks to determine accounting allowances lead to an appropriate measurement of ECL. To this end, prudential supervisors could compare model outcomes, to understand if differences in the level of provisioning are justified by the different degree of riskiness of the portfolio or, on the other hand, by questionable model choices.

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**BOX 12 - Rwanda: External Vendors**

One interesting point underlined by the National Bank of Rwanda (NBR) was the banks’ overreliance on external vendors. Six out of sixteen banks hired the same consultant to build up an ECL model. In general, purchasing models from external vendors without a full understanding of the provisioning key drivers (PD, LGD, exposure at default; EAD) is a material risk. Furthermore, in the case described by NBR, the reliance on the same provider by a large number of Rwandan banks posed additional challenges in terms of concentration risk and potential conflict of interest even though the NBR Regulation on outsourcing (n. 3/2018) clearly states that the board and senior management remain ultimately responsible for “outsourcing operations” and for managing risks inherent in such outsourcing relationships.

Cognizant of these risks, NBR required the relevant banks to have an external review of the work carried out by the consultant. Models should be tailored to reflect the institution’s risk profile and should be well understood by the institution itself. Lack of customization and poor governance around ECL models resulted in shortcomings that NBR was required to address.
RECOMMENDATION N. 8: Prudential Supervisors Should Know What to Expect from External Auditors

The quality of the external audit profession is an essential precondition for an effective implementation of IFRS 9 (and any accounting standards). International standards emphasize the crucial role played by the external auditors in the loan loss provisioning process. For example, the BCBS Core Principles for Effective Banking Supervision (2012) require that supervisory guidance or local audit standards determine that audits cover areas such as loan portfolio, loan loss provisions, and non-performing assets (BCBS 2012, Core Principle n. 27). Moreover, the Basel Committee (BCBS 2014) underlines the importance of effective communication channels between the supervisor and the external auditors and sets out expectations on external auditors’ knowledge, competency, objectivity, independence, professional skepticism, and quality control (BCBS 2014).

Objectivity and independence are prerequisites for audit quality. Auditor independence has been debated for decades. Bias and conflict of interests might arise from the simultaneous provision of consultancy services by audit firms in the context of IFRS 9 implementation, particularly to banks operating under the credit risk standardized approach. The Basel Core Principles for effective banking supervision envisage rotation of external auditors (either the firm or individuals within the firm) from time to time. In smaller financial systems, auditor rotation might be difficult to implement due to the limited number of banks and auditor concentration.

Consultant services by the audit firm (or the network of audit firms) to the audit client may affect a third party’s perception of the external auditor’s independence (BCBS 2014). Some jurisdictions, such as the European Union, introduced restrictions to nonaudit service and limits to the amount of consulting work that accounting firms could earn from audit clients (a fee cap). Restrictions and limits apply to “public interest entities,” which include listed companies, banks, and insurance undertakings. During the bilateral meetings, we identified cases where the prudential supervisor required banks to have an external review of the IFRS 9 implementation work carried out by the accounting firm operating as consultant (for example, Rwanda) or introduced joint audits (for example, South Africa, see box 13) (Groepe 2017). As is known, some of the most important accounting firms stopped offering consulting service to large audit clients (Jones 2019). Additional options to strengthen independence could consist of (a) enhancing governance arrangements of audit firms (such as greater disclosure and transparency of nonaudit fees and lengthening the required cooling-off periods for senior staff when transitioning to employment with audited clients) and (b) leveraging the role of the audit committee in monitoring and assessing external auditor independence.

External auditors should exert appropriate professional skepticism, by challenging management assumptions. The use of expert management judgement is not only a necessary component of the loan loss provisioning estimation but also an indicator of potentially higher risk of misstatement, since it involves a wide range of measurement uncertainty. Quantifying credit loss under IFRS 9 is not just subjective, but also complex, considering the level of uncertainty inherent in the “cash flow shortfall” estimation, as well as macroeconomic variables (GDP, unemployment, and so forth) needed to incorporate forward-looking information.

While it remains up to the auditor to set the audit scope and procedures, the Global Public Policy Committee (GPPC 2016, 2017) provided guidance for a sound implementation of IFRS 9. Potential areas of investigation to be agreed with the banks include, among others (a) challenging the staging process (typically, the SICR triggers); (b) testing the days past due and, for a sample of loans, recalculating them; (c) examining the completeness, accuracy, and reliability of historical information; (d) gauging banks’ policies and governance over ECL models’ design, build, and validation (for example, number, selection and probability weighting of forward-looking economic scenarios); and (e) evaluating the appropriateness of model adjustments and overlays, and the standards for sensitivity analysis, back testing, and validation.

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17. The Global Public Policy Committee (GPPC) brings together senior partners from the six large international accounting networks (BDO, Deloitte, EY, Grant Thornton, KPMG and PwC). The GPPC’s primary objectives are to participate constructively in matters concerning global public policy to advance the public interest and to enhance public confidence in the profession.
In the wake of the IFRS 9 implementation, the Prudential Authority (PA) within the South African Reserve Bank (SARB) met with all the auditing firms that performed the audits of banks. The objective was for the PA to communicate its expectations, understand the challenges the firms faced, ascertain their readiness to audit banks and their application of IFRS 9, and encourage them to develop a “firm view” on the macroeconomic scenarios that banks would use in their ECL models. Firm view refers to the audit firms’ internally developed, independent determination of the macroeconomic and other related forward-looking factors used in the computation of ECL. It was envisaged that this be a firm-wide view, across its South African operations, to facilitate consistent application of the macroeconomic outlook across the firm’s audit engagements. The PA also engaged with the Independent Regulatory Board for Auditors (IRBA), facilitating the drafting and issuance of a staff audit practice alert on the audit implications of the ECL.

To address staff capacity concerns, the PA relies to a great extent on the work of external auditors. In accordance with Regulation 46 (4), the external auditor shall within 120 days of the financial year-end of the reporting bank, report to the PA on any significant weaknesses in the system of internal controls that came to the auditors’ attention while performing the necessary auditing procedures as regards to the policies, practices, and procedures of the bank relating to (a) the granting of loans; (b) the making of investments; (c) the ongoing management of the loan and investment portfolios; and (d) the relevant credit impairments or loan loss provisions and reserves. Regulation 46 (b) requires the external auditor to report whether the information contained in the regulatory returns that were submitted to it was prepared in accordance with the directives and instructions in the Banks Act and Regulations. This would include whether asset classification has been properly reported.

The PA therefore relies on the annual Regulation 46 reports. During the annual trilateral meetings between the PA and the banks’ audit committee (including internal audit) and external auditors, Regulation 46 reports are also discussed, including the appropriate corrective actions implemented or to be implemented to address the internal control weaknesses identified by the external auditors.

There is regular and active engagement between the PA and external bank auditors during meetings, but no comprehensive and deep assessment of audit quality is performed by the PA. The relationship has been described by both parties as open and constructive. The auditors hold preliminary bilateral meetings with the PA prior to the commencement of the final audit. After completion of the audit, the PA meets with the auditors as well as the bank during a trilateral meeting to discuss the outcomes of the audit. Moreover, the PA requires two audit firms to act as joint auditors for large banks, each auditor taking equal responsibility for the audit. Feedback from auditors and banks confirmed this practice has contributed to audit quality.

The PA also required external auditors to provide it with an audit verification of the day one impact within five months of adopting IFRS 9 for the first time. In October 2017, the PA conducted an IFRS 9 quantitative impact study (QIS) during which all banks were requested to submit an estimate of the impact of IFRS 9 on their credit impairments, capital and Capital Adequacy Ratios. The main aim of the QIS was for the PA to obtain information on the day one impact of IFRS 9 and to inform it of any required regulatory interventions. In 2018, after the implementation of IFRS 9, banks were required to prepare a set of special purpose financial information showing the actual impact of IFRS 9 on opening retained earnings.

Audit quality has come under pressure in South Africa, particularly following the failure of two smaller banks and other corporate scandals. The IRBA was established under the Auditing Profession Act of 2005 and now has around 40 projects ongoing to support confidence in the audit profession. Moreover, the IRBA has developed a suite of audit qual-

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18. A deep and compressive assessment would include a review of audit working papers.
ity indicators to empower stakeholders to play a role in audit quality. The inspections performed by the IRBA resulted in between 50 and 60 percent of the inspected audits having one or more findings, well above the international rate of 33 percent. (IFIAR 2020). It is important to note that the IRBA only oversees statutory audits, and its reach does not extend to the regulatory audit the PA requires the external auditors of banks to perform. While there are overlaps and synergies between the statutory and regulatory audit work, some aspects of the regulatory audit work have more stand-alone.

**Ongoing investigations by the IBRA of one audit firm, following allegations** of complicity of an audit engagement partner in a bank failure, underscore the importance of establishing adequate oversight of bank audit quality. Indeed, following the VBS Mutual Bank corruption scandal, several banks decided to migrate to a different audit firm or sought enhancements of the audit team at their own initiative (such as addition of nonlocal staff and external review partners).

**Mandatory audit firm and partner rotation has been introduced in South Africa.** The Companies Act states that the same individual may not serve as the auditor or designated auditor of a company for more than five consecutive years. Furthermore, the IRBA has issued a rule on mandatory audit firm rotation of 10 years, which will apply to all banks for financial years commencing on or after April 1, 2023. These rotation requirements are intended to enhance auditor independence although not without putting strain in an oligopolistic market with joint audits and strict independence requirements.

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20. The audit firm concealed the bank’s financial position as an unqualified audit opinion was issued even though it was known to the audit firm that the financial statements were materially misstated. The regulatory audit opinion was also materially misstated. The external audit firm partner who signed the opinions also received very substantial loans from the bank, which were not declared, thus compromising his independence.
Conclusion

Effective January 2018, IFRS 9 introduced the ECL framework, different from the incurred loss methodology used in IAS 39. ECL’s effect both on the timing of the provisioning, which is compulsory when credits are originated (stage 1), and on the amount of allowances, particularly for underperforming loans (stage 2), since the SICR requires banks to move from a 12-month to a lifetime ECL model, incorporates forward-looking information.

We investigated IFRS 9 implementation in EMDEs and advanced economies through a survey and a series of bilateral meetings with selected prudential supervisors. Based on the survey results, the overwhelming majority of respondents (78 out of 91) implemented IFRS 9 for all (53 countries) or certain (25 countries) financial institutions (in the latter case, IFRS 9 applicability depends on the size of the financial institution, whether it is listed on a stock exchange or not, and whether reporting is on a consolidated or individual basis). In addition, there are 13 countries that have not yet implemented IFRS 9.

The survey revealed major challenges faced by prudential supervisors and banks during IFRS 9 implementation. Data availability and low data quality make it difficult to estimate ECLs. To deal with the modeling risk, there is an overreliance on managerial judgment, which supervisors found challenging to constrain. Limited staff capacity by authorities in EMDEs prevents the adequate review of banks’ model validation and data inputs. Most supervisors undertook measures to mitigate the impact of IFRS 9 on banks (for example, transitional arrangements).

The bilateral meetings allowed us to achieve an in-depth understanding of IFRS 9 implementation challenges faced by certain jurisdictions. Among them, it is worth mentioning the excessive reliance on ECL models provided by external vendors, without a thorough understanding, by many banks, of the key parameters of the models. Another recurring issue was how
to ensure consistency between prudential credit classification criteria and the IFRS staging process. Yet the most important debate arose around the procyclical effect of IFRS 9, also due to the timing of the paper, prepared during the COVID-19 pandemic.

The COVID-19 outbreak is an incentive to further postpone IFRS 9 implementation for some jurisdictions. Some countries argued that the pandemic is not the right moment to move to IFRS 9 as it could exacerbate the additional credit losses, which might in turn weaken the banks’ capital position and their ability to support the economy. Notwithstanding IFRS 9 procyclical effects, in our opinion, a decision about the timing should be based on a broader assessment of the preconditions that should be in place for an effective IFRS 9 implementation: quality of the audit profession, robust governance arrangements in banks, and familiarity with credit risk modeling in both banks and supervisory staff.

If these preconditions are not in place, EMDEs should not rush IFRS 9 implementation. EMDEs should improve their supervisory capacity before dedicating resources to IFRS 9 adoption.

For those EMDEs that have already implemented IFRS 9 or plan to do it soon, both the survey and the bilateral meetings suggested the following recommendations. Prudential supervisors, whether they have powers to regulate and issue accounting rules or not, should carefully prepare the transition, taking stock of BCBS international guidance. They could set up a task force responsible for the IFRS 9 implementation, reporting to a board member or the highest level of seniority to strengthen the link between seniority and accountability through a clear allocation of responsibilities. The working group should be equipped with an adequate mix of skills, ideally both accounting and quantitative skills, and should oversee the project management (planning, implementing, reporting, and following up), including the determination of the transition date.

An important choice is to define the perimeter of application of IFRS 9. We observed different policy options as to whether IFRS 9 requirements are being applied to all or a subsection of the wider population of banks. Each policy option has its own advantages and disadvantages, but it important to ensure a level playing field, avoiding potential regulatory arbitraging effects.

Considering that 69 percent of the respondents indicated modeling risk as the major challenge of IFRS 9 implementation, we strongly recommend that prudential supervisors in EMDEs invest in developing quantitative skills. Being cognizant of compelling budget constraints, we suggest relatively cheap solutions. First, a large part of technical assistance can now be performed by means of IT solutions. Second, rotation of staff between financial stability and supervision departments allows for a diversification of experience and avoids silo approaches. Third, SupTech applications can enhance data collection and quality controls. SupTech can also be applied to the central credit registry to derive historical default rates and disseminate PD information, including how the same borrower is classified by different lenders, helping banks build up ECL models.

Supervisors will essentially not be able to challenge banks if they do not have the proper in-depth knowledge of ECL models. Implementing IFRS 9 does not mean that EMDEs should move to IRB approach. In environments where banking supervisors lack the ability to assess internal models, it is relatively easy for banks to achieve capital relief, particularly for subsidiaries of internationally active banks.

Banks might need guidance on IFRS 9 implementation to be able to understand and meet supervisory expectations. In some cases, we noted delays, with guidance issued only several months after IFRS 9 became effective. Obviously, it is better late than never, considering that not all survey respondents issued implementation guidelines.

Prudential supervisory guidance should clarify how to ensure consistency between credit classification criteria and the IFRS 9 staging process. Experience from the field showed that a full alignment is not necessarily needed, but each prudential bucket should find a univocal correspondence into one of the three IFRS 9 stages.

Prudential backstops preserve the coverage ratio against undue discretion and model choices, but they must be set based on statistical evidence of recovery rates. Timely write-offs of uncollectable loans strengthen banks’ balance sheets and allow banks to refocus on their business, that is, lending to the economy.

Entry and exit movements to and from stages 2 and 3 financial instruments must be overseen. Especially during the current pandemic crisis, banks and borrowers are more likely to restructure the terms and conditions of loans. Renegotiation or modification of the contractual cash flows do not necessarily entail a deterioration of asset quality but require banks to assess whether there has been a SICR. Regressions from stage 2 to stage 1 should be based on a history of up-to-date and timely payment performance against the modified...
contractual terms. Prudential supervisors should ensure that neither banks nor borrowers abuse these measures, both under the pressure of related parties.

Capital buffers and transitional arrangements are the main tools to counteract the IFRS 9 procyclical effect. Where a bank’s opening balance sheet on the day that it first applies IFRS 9 reflects a decrease in CET1 capital as a result of increased ECL, compared to the closing balance sheet the previous day, the bank should be allowed to include a portion of the increased ECL in its CET1 capital for a transitional period. For 2020 and 2021, jurisdictions may allow banks to add-back up to 100 percent of the transitional adjustment amount to CET1.
APPENDIX: The Questionnaire
1) Contact information
Jurisdiction:
Institution:
Contact person at the institution, to whom the World Bank can reach out if further clarification on the answers is needed:

2) Contact person
Name:
Email Address:
Phone Number:

BACKGROUND INFORMATION
3) Which accounting standards do banks apply in your jurisdiction?

- [ ] IFRS
- [ ] National accounting standards (in close compliance with IFRS 9)
- [ ] National accounting standards (not compliant with IFRS 9). Please, describe the most important differences related to the calculation of loan loss provisioning:
- [ ] Other. Please, specify:

4) Does the banking regulator have powers to regulate and issue accounting rules (including rules on valuation of assets and public disclosure requirements)?

- [ ] Yes
- [ ] No

5) If the above powers belong to another agency, please, indicate its name. How is coordination between your agencies taking place?

6) Is IFRS 9 effective in your jurisdiction?

- [ ] Yes
- [ ] Applies only to certain financial institutions. Please, specify:
- [ ] No

If you answer Yes or Applies only to certain financial institutions, please, proceed with questions 7–12. If you answer No, please, proceed with questions 13–14.

IMPLEMENTATION AND USE OF IFRS 9
7) From which date is IFRS 9 effective in your jurisdiction?

8) What are the main challenges with implementation and use of IFRS 9 that banks in your jurisdiction experience up to date? Please, select all that apply.

- [ ] Burden due to the involvement of several business areas (budget, IT, risk, finance, governance and processes)
- [ ] Lack of appropriate analytical tools
- [ ] Modeling risk and overreliance on managerial judgement and discretion
- [ ] Limited staff capacity
- [ ] Data availability and low data quality
- [ ] Material effect on banks’ profit and loss account
- [ ] Inability to meet key supervisory metrics (asset quality, capital ratios, etc.)
- [ ] Overreliance on external vendors
- [ ] Need to meet extensive disclosure requirements
- [ ] Other. Please, specify:

9) What are the main challenges that the Supervisor in your jurisdiction faces with implementation and use of IFRS 9? Please, select all that apply.

- [ ] Data availability and low data quality
- [ ] Lack of appropriate analytical tools
- [ ] Modeling risk (for example, measurement of expected credit loss, lifetime probability of default)
- [ ] Limited staff capacity
- [ ] Difficulties with constraining managerial judgement and discretion
- [ ] Regulatory treatment of accounting provisioning
- [ ] Lack of enforcement from a supervisor
- [ ] Other. Please, specify:

10) Do you observe any material effect of IFRS 9 on banks’ profit and loss account as well as on key performance indicators (asset quality, loans losses provisioning, capital ratios, etc.)?

- [ ] Yes, the effect is positive. Please, specify:
- [ ] Yes, the effect is negative. Please, specify:
- [ ] No
11) Did regulator in your jurisdiction provide any support to banks during the transition period (for example, capacity building, official guidance, etc.)?

☐ Yes. Please, specify:

☐ No

12) Does regulator in your jurisdiction apply any tools or policies to mitigate possible negative impact of IFRS 9 on banks’ balance sheets (for example, transitional arrangements, prudential backstops, etc.)?

☐ Yes. Please, specify:

☐ No

13) Does your jurisdiction plan to implement IFRS 9?

☐ Yes. Please, specify when:

☐ No

14) What are the reasons for postponing implementation of the IFRS 9 in your jurisdiction? Please, select all that apply.

☐ Potential negative impact on banks’ profitability

☐ Potential impact on the capital adequacy of the financial system

☐ Lack of appropriate models and analytical tools

☐ Data gaps

☐ Too high costs of transition

☐ Other. Please, specify:
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