Deloitte.

Fifth Global IFRS Banking Survey
Finding your way

May 2015

Preface

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

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

Our global financial services industry group has collated the views of 59 major banks, to keep you informed of how the industry is responding to accounting and regulatory change. In the next slides you will find a graphic summary of survey participants' responses. A full report will be published in due course.

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

Regards,

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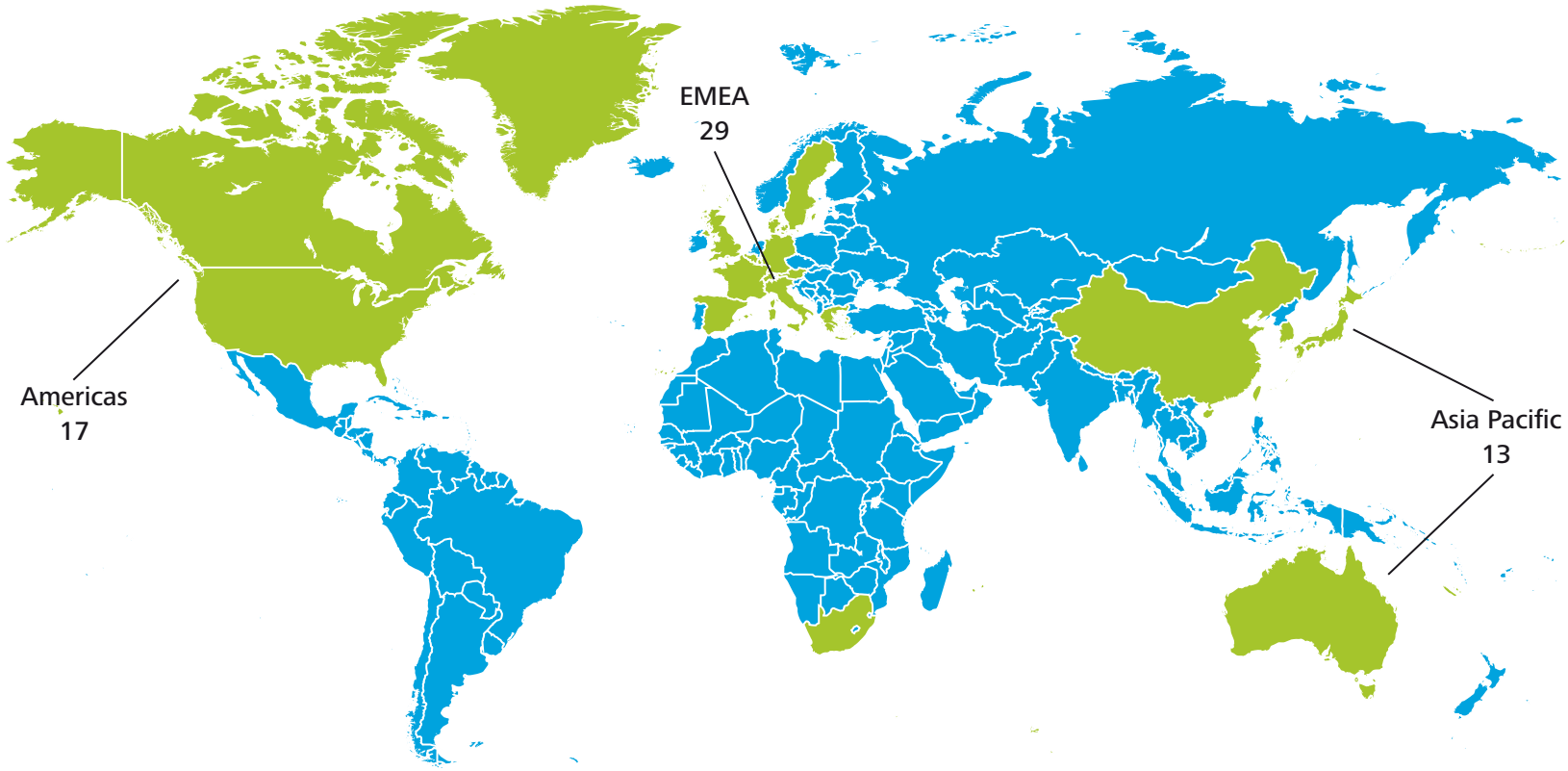
About the Survey – Participants

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

We received responses from 17 of the 30 global systemically important financial institutions (G-SIFIs) determined by the Financial Stability Board (FSB), including 12 of the 18 G-SIFIs who are IFRS reporters.

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



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

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

Key findings

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

Key implementation challenges include:

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

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

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

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

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

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

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

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

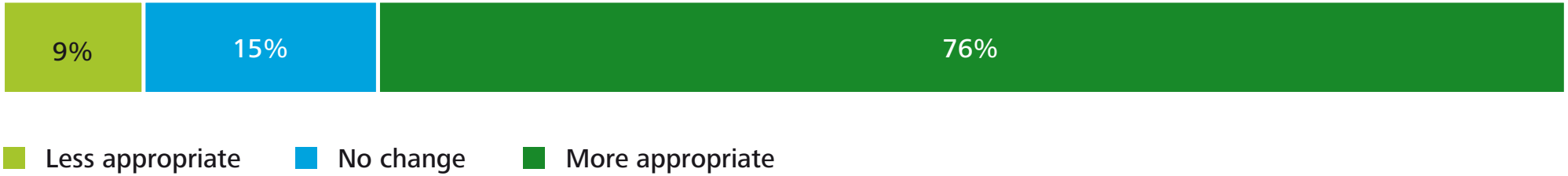
Global and national issues

Q1a: Will financial statement users be better able to compare banks globally under IFRS 9/FASB's CECL model than under IAS 39/US GAAP for the impairment requirements?

Q1b: Do you think regulators will find IFRS 9/FASB's CECL model information more appropriate for supervision purposes than that prepared under IAS 39/US GAAP regarding impairment requirements?

Comparability of financial statements

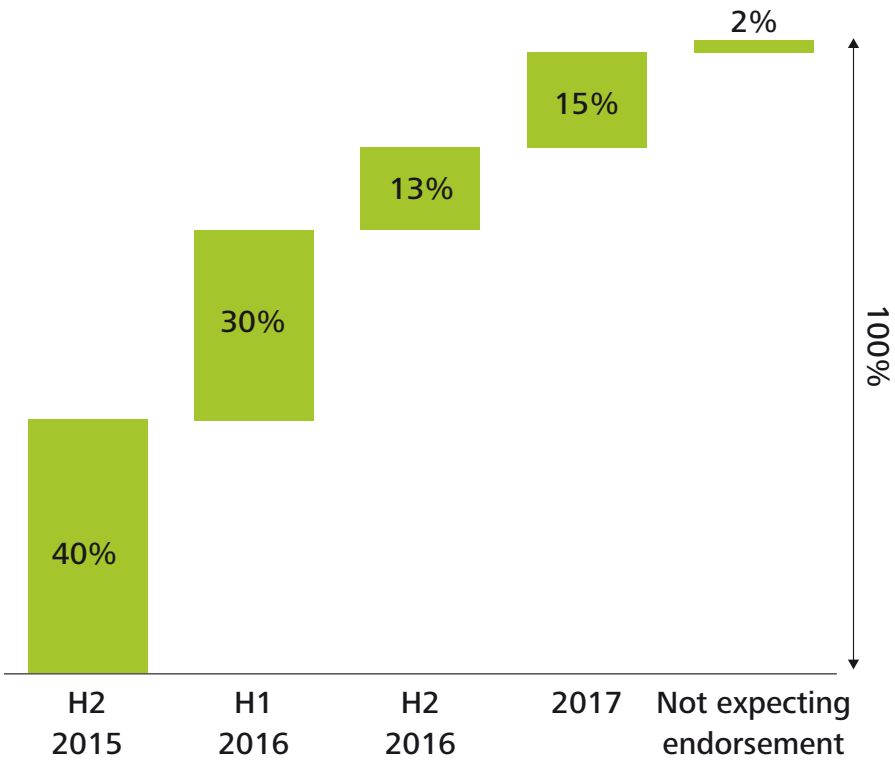
Appropriateness for supervision purposes

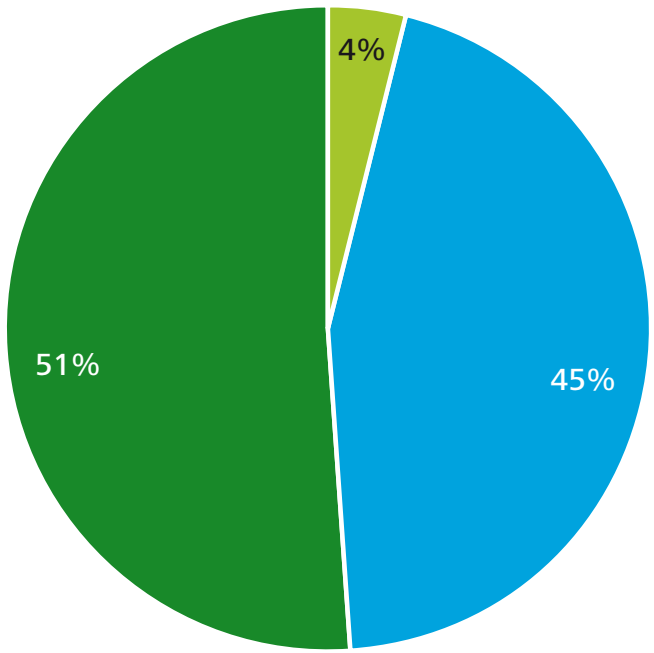


Global and national issues

Q2a: When do you expect IFRS 9 to be endorsed for use in Europe?

Q2b: Will the uncertainty around timing of EU endorsement of IFRS 9 result in the postponement of a significant portion of your IFRS 9 implementation project?

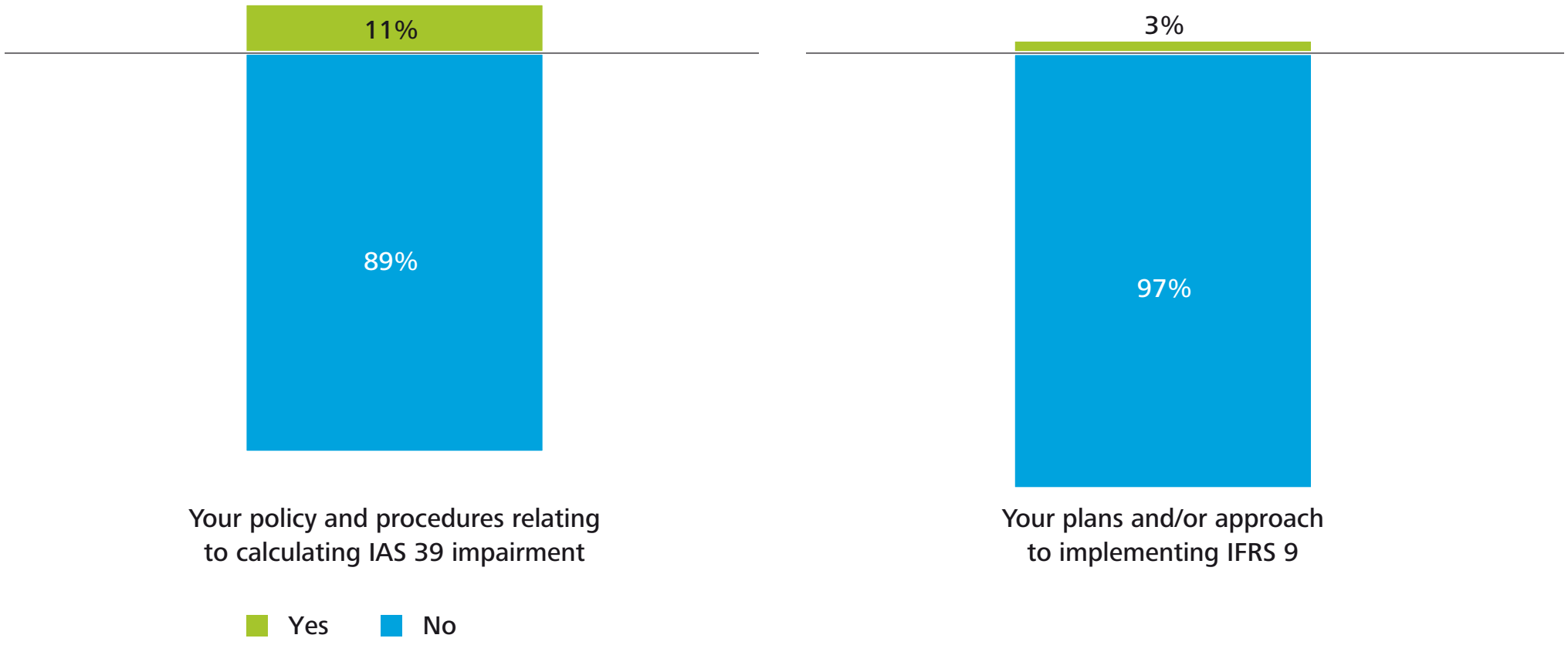




- Yes, as the parent company is based in the EU or the group has major subsidiaries in the EU
- No, as the parent company is not based in the EU or the group does not have major subsidiaries in the EU
- No, even though the parent company is based in the EU or the group has major subsidiaries in the EU

Global and national issues

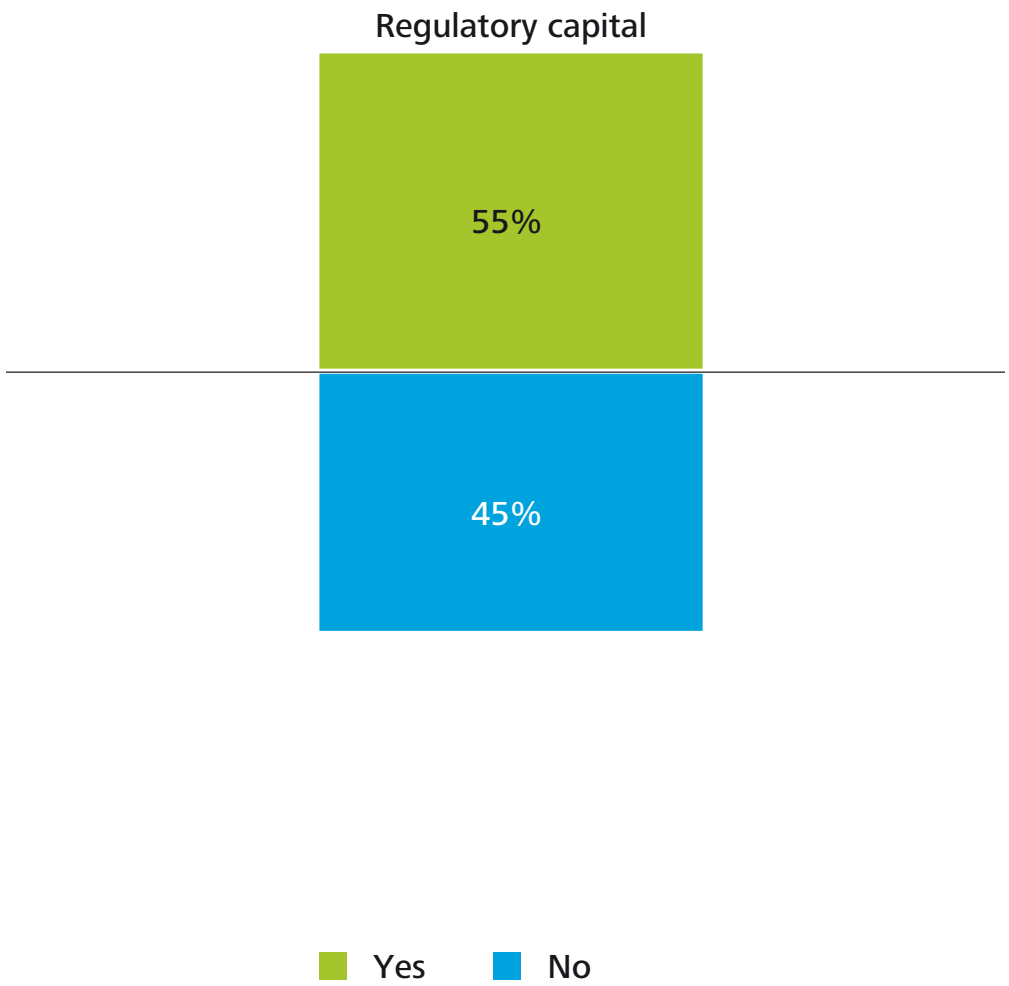
Q3: Following the publication of the European Central Bank findings from the Asset Quality Review (AQR), have you changed:

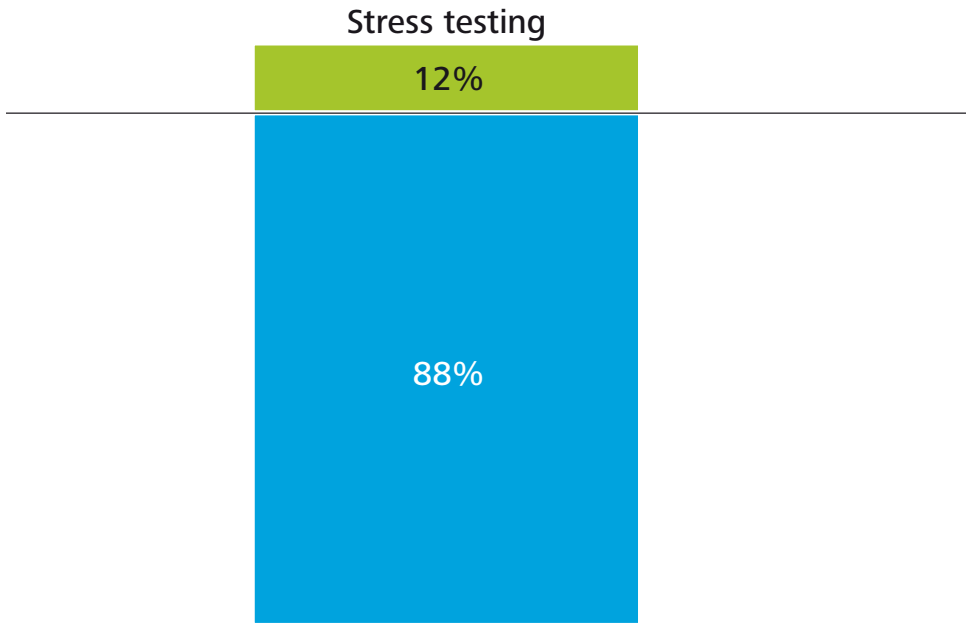


Global and national issues

Q4a: Are you planning to incorporate your IFRS 9 impairment estimates for regulatory capital planning purposes?

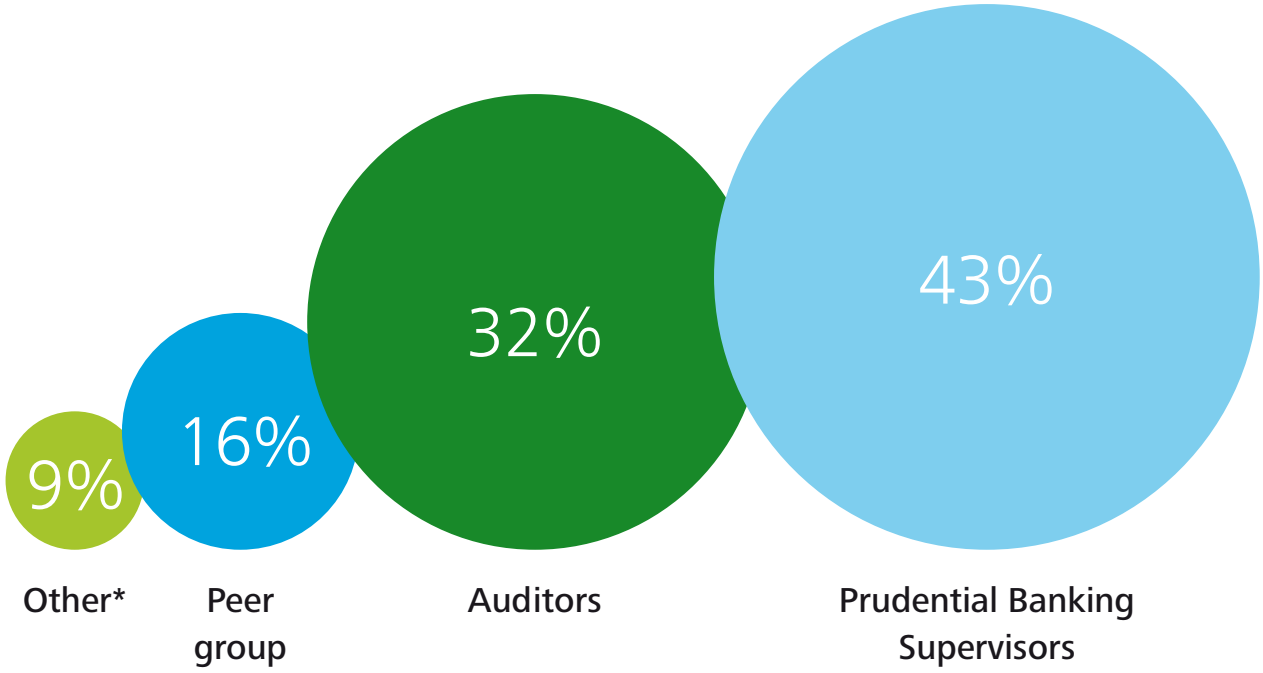
Q4b: Has your regulator requested that you include your IFRS 9 impairment numbers into your stress testing scenarios through 2018?





General considerations

Q5: Which of the following bodies will be most influential when interpreting IFRS 9/FASB's CECL model requirements for your implementation plan? (Rank your top 2)**

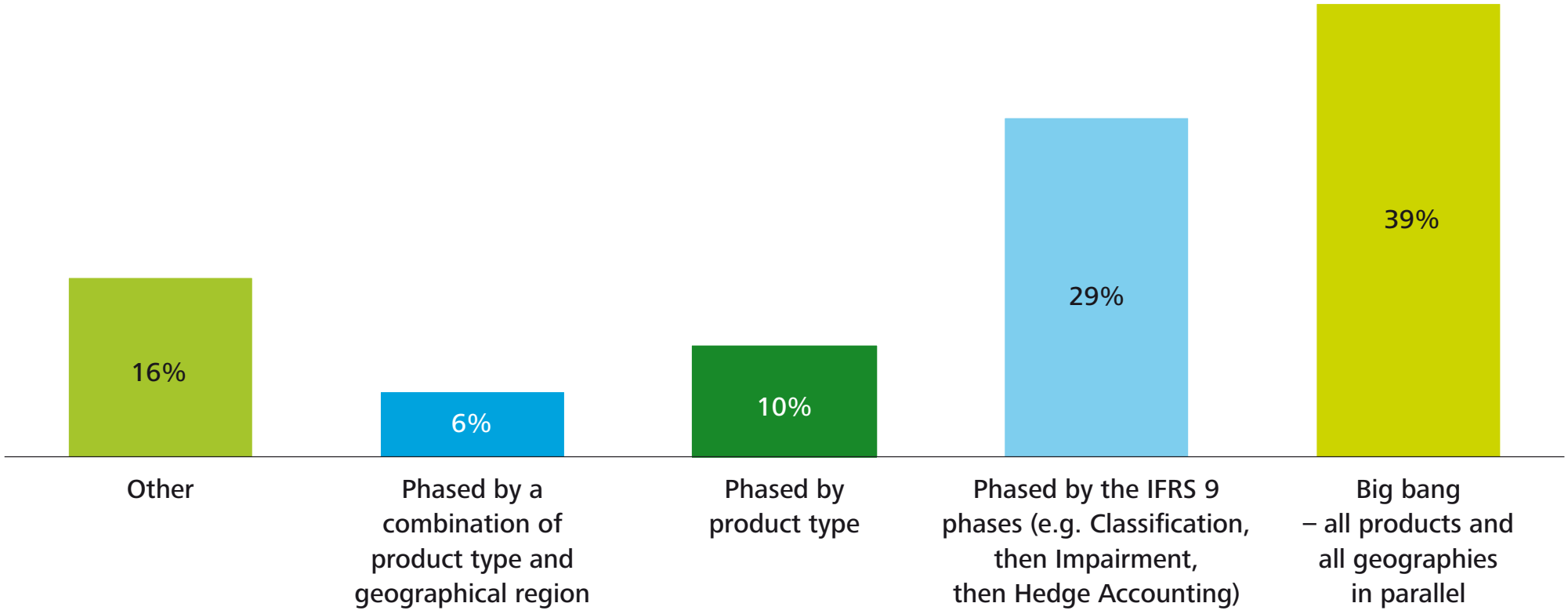


* "Other" includes Industry bodies, Securities regulators and Early adopters of IFRS 9.

** Participants' responses have been weighted, assigning a greater weight to first ranked options over second ranked options. Percentages displayed are based on total weighted responses.

General considerations

Q6: Which approach best describes your IFRS 9/FASB CECL model implementation project plan?



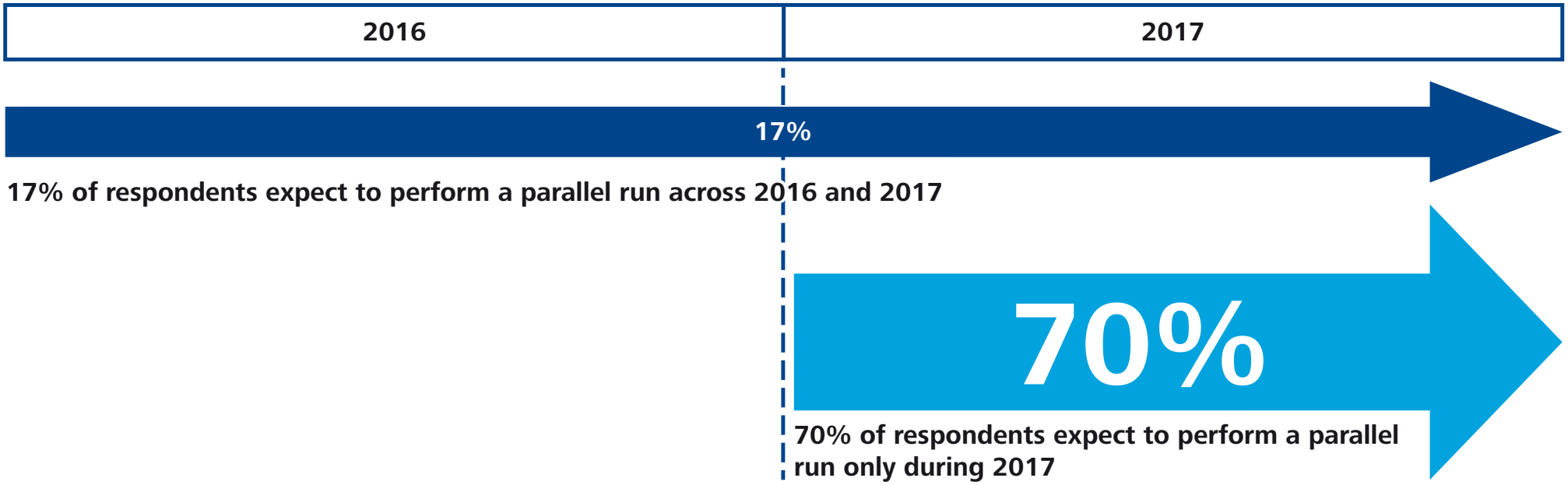
General considerations

Q7: Will you use IFRS 9/FASB's CECL model as a catalyst to align accounting impairment and regulatory capital processes?

- No – Independent stand alone projects
- Partly – Some alignment and integration
- Yes – Full alignment and integration (e.g. common data store, language, systems and governance)

General considerations

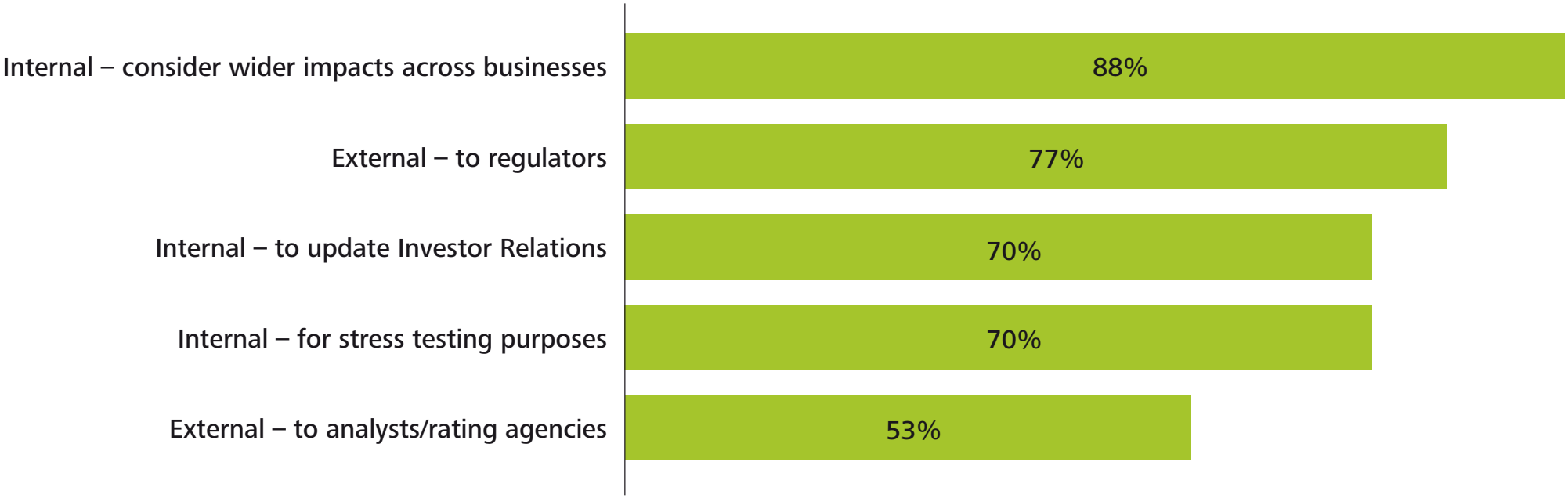
Q8a: To what extent are you considering a parallel run between your IFRS 9/FASB CECL approach and the existing IAS 39/US GAAP approach?



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

General considerations

Q8b: Do you expect to have to estimate your expected loss provisions under IFRS 9/FASB's CECL model before the effective date for communication with:*

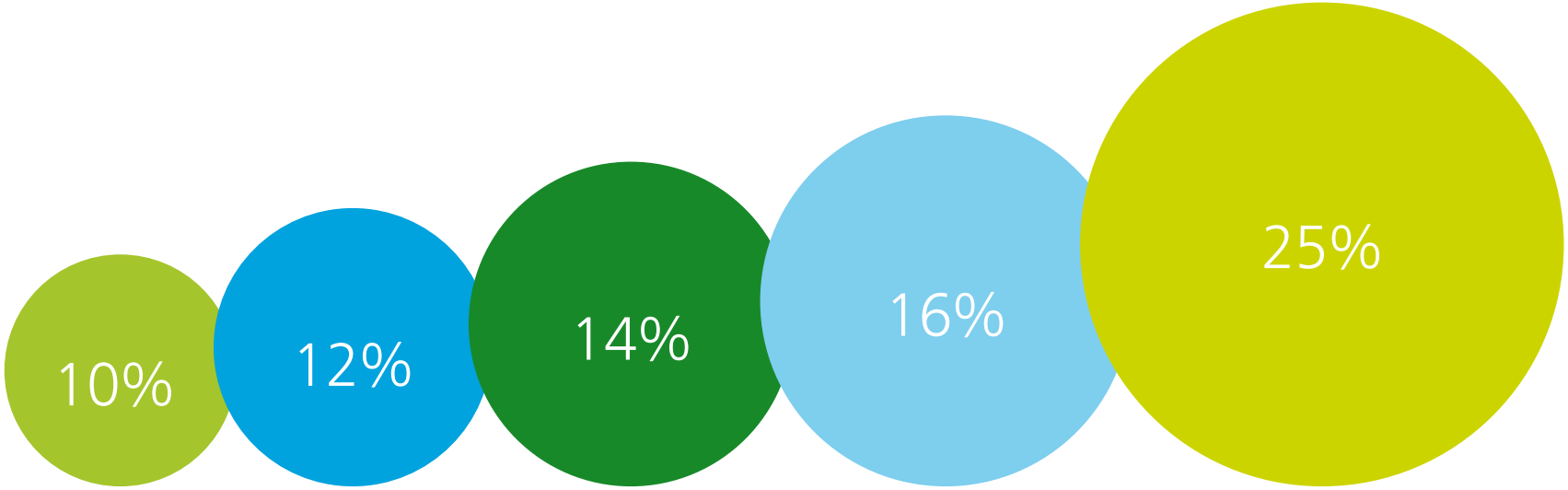


Overall, 96% of respondents anticipate estimating their expected credit loss provisions under IFRS 9/FASB's CECL model before the effective date.

* There was no limit to the number of responses that participants could select. Percentages displayed reflect the proportion of total participant responses to each response option.

General considerations

Q9: What do you see as the three biggest challenges to implementing your IFRS 9/FASB CECL programme? (Rank your top 3)*



Capability to plan and execute a programme of this size in parallel with other current initiatives

Capability to design, build and test new models with limited internal resources

Availability of data

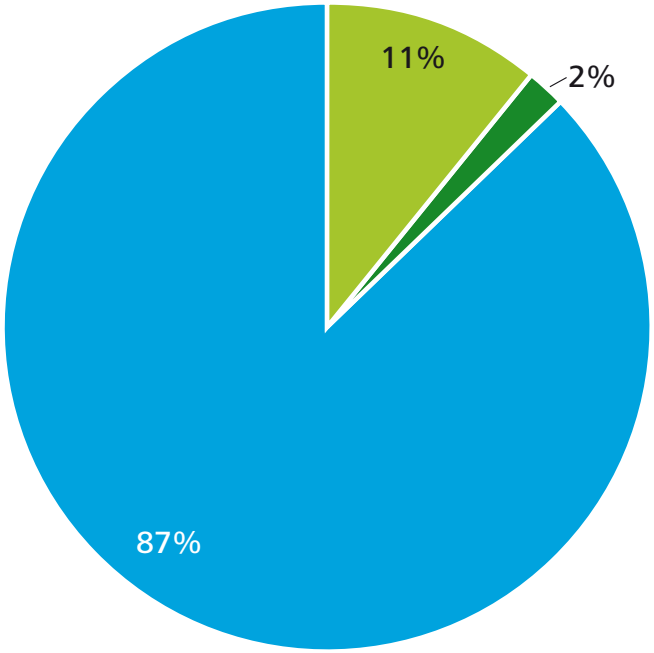
Necessary level of co-ordination between finance, credit, risk, IT and others to deliver plans

Clarity around acceptable interpretation of IFRS 9/FASB's CECL model externally

* Participants' responses have been weighted, assigning a greater weight to higher ranked options than lower ranked options. Percentages displayed are based on total weighted responses.

General considerations

Q10: In addition to recording and measuring credit losses in line with IFRS 9, would you consider disclosing the lifetime expected losses based on the FASB's CECL approach (or vice versa if you report primarily under US GAAP would you consider disclosing the expected credit losses under IFRS 9)?

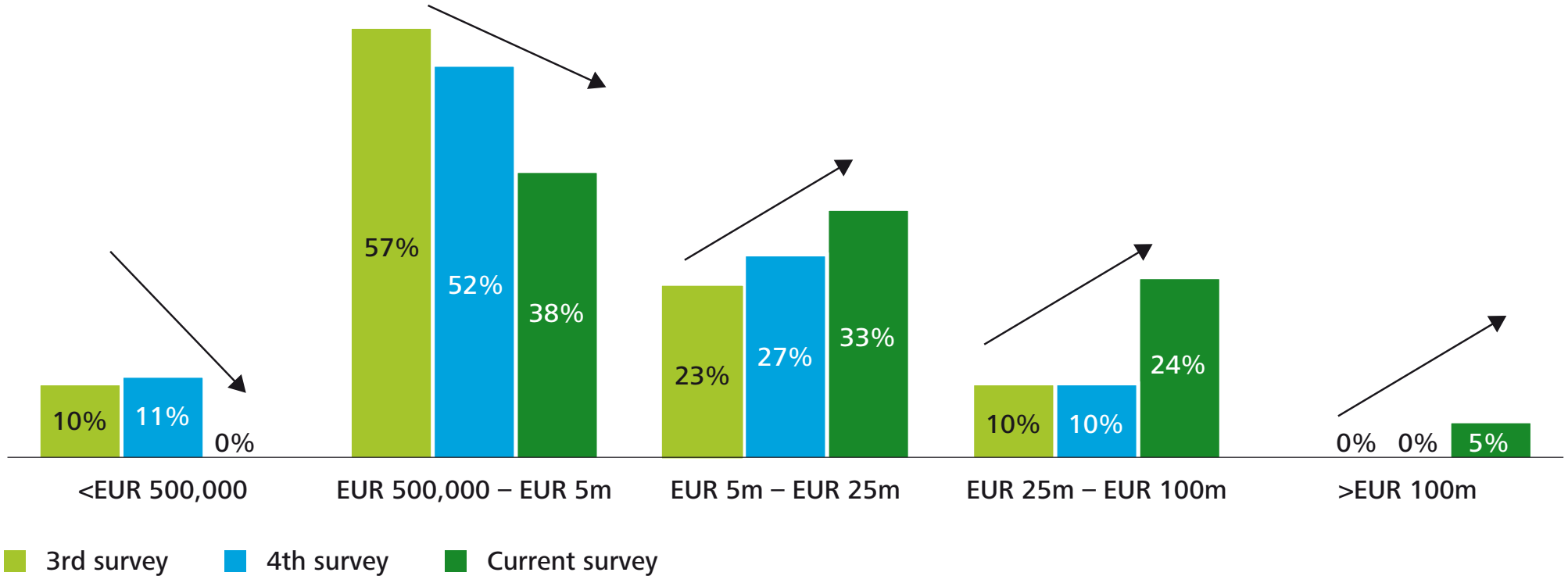


- Yes – because we will be required to produce both sets of data anyway
- Yes – we are not required to but our investors will find it useful
- No – the benefits would not justify the additional effort

Project budgeting and phasing

Q11a: What is your estimated total budget (including all internal and external costs) to change to a fully compliant IFRS 9/FASB CECL program?

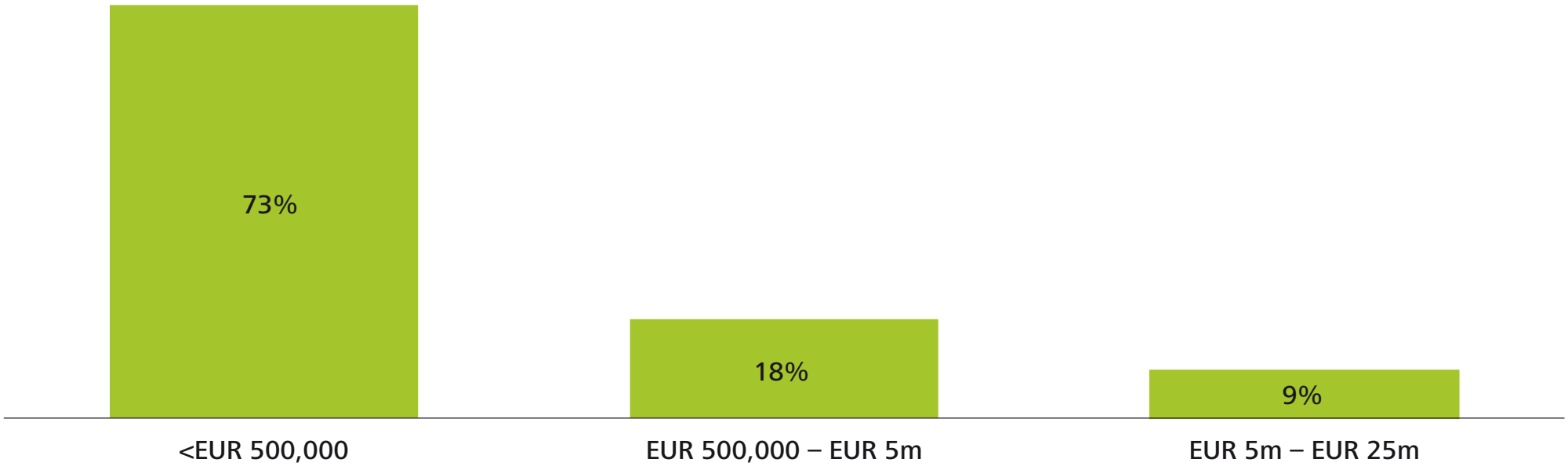
The weighted average implementation budgets have doubled in the year since our previous survey.



Project budgeting and phasing

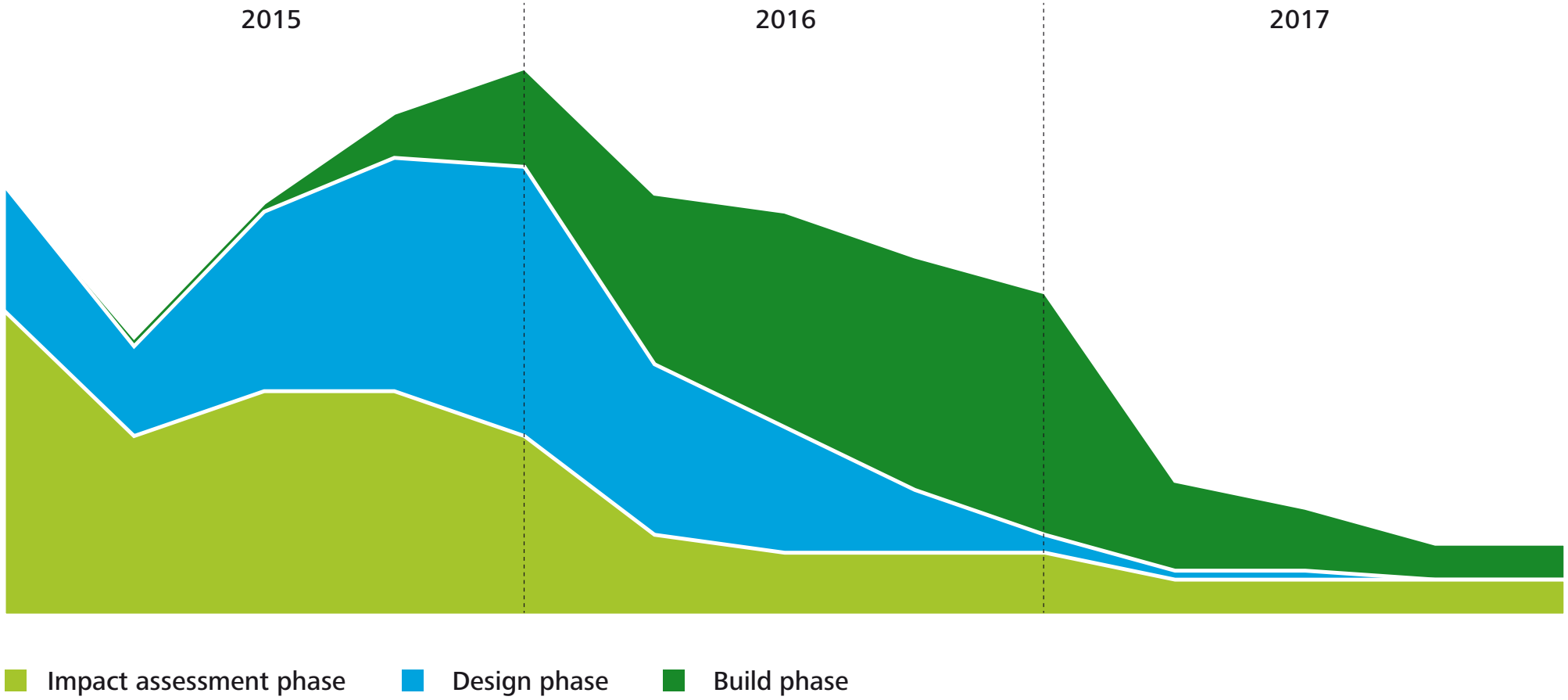
Q11b: What do you anticipate the total annual incremental cost will be of running your IFRS 9/FASB CECL solution (once it is part of your business as usual) when compared to your current incurred loss model?

Only 11 participants answered this question. The majority of them (73%) believes that the total annual incremental cost of running their IFRS 9/FASB CECL solution once it is part of their business as usual will be less than EUR 500,000 when compared to their current impairment model. 18% think that this annual incremental cost will be between EUR 500,000 and EUR 5m, while the remaining 9% think that it will be between EUR 5m and EUR 25m.



Project budgeting and phasing

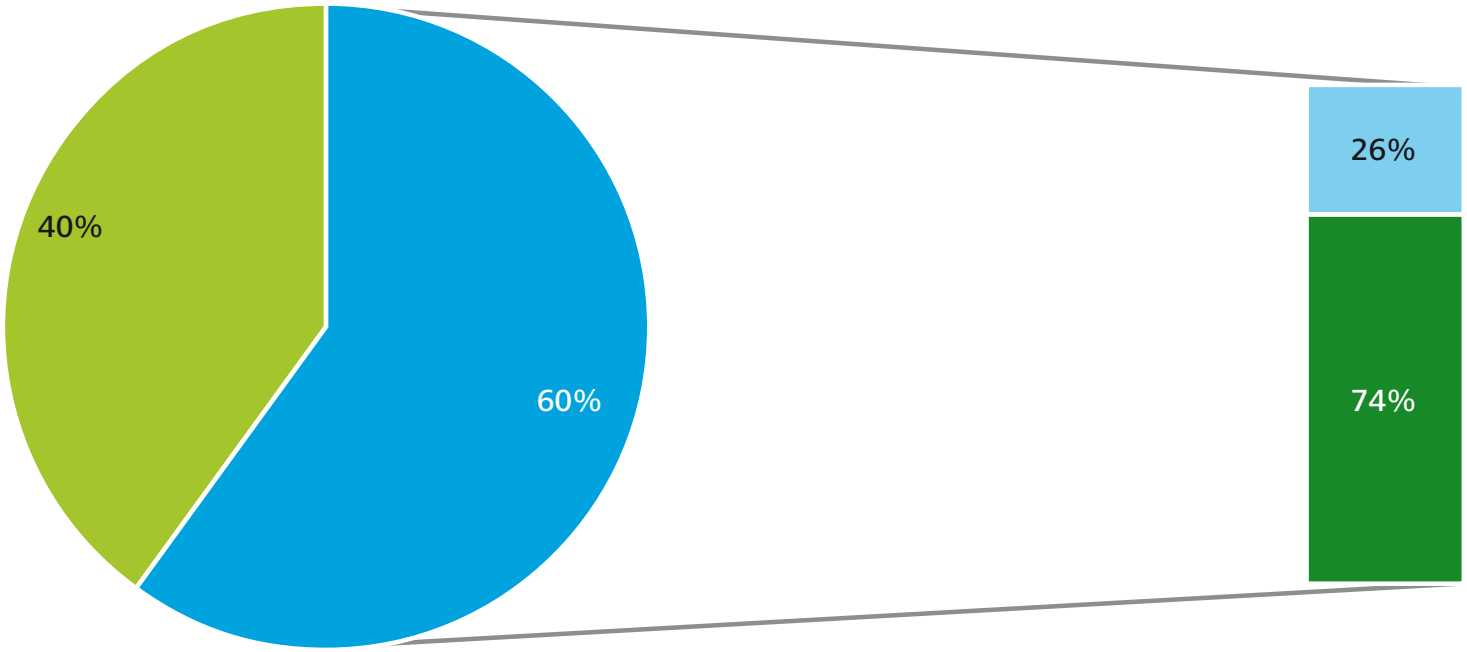
Q12: When do you anticipate starting and finishing (or when have you already started or finished) the following project phases relating to your IFRS 9 impairment/FASB CECL model implementation plan?



Project budgeting and phasing

Q13a: Do you believe there are enough technical resources available in your organisation to deliver your IFRS 9/FASB CECL model project?

Q13b: If 'no', do you think there will be enough technical expertise in the external market to cover any shortfall of internal resources across the industry?



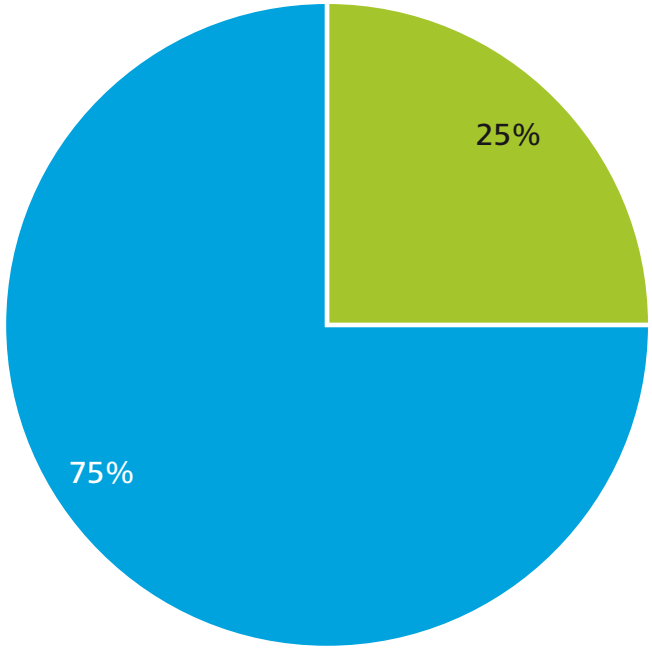
- No, there are not enough technical resources internally
- Yes, there are enough technical resources internally
- No, there will not be enough technical expertise in the external market
- Yes, there will be enough technical expertise in the external market

Project budgeting and phasing

Q14: IFRS 9/FASB's CECL model is likely to require new systems or enhancements to existing systems. Which options best describe the position of IT in your IFRS 9/FASB CECL model delivery plan?

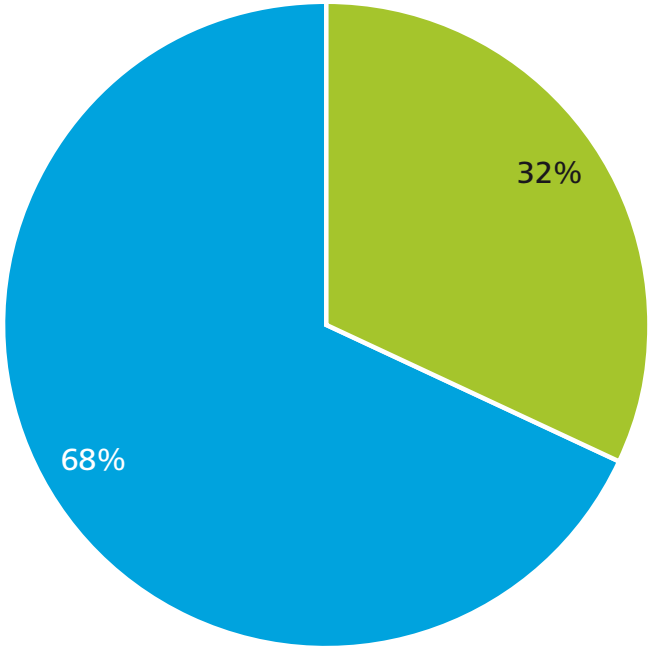
Where internal IT function will be used:

IT budget



- IT budget has been agreed by senior management
- IT budget has not been agreed by senior management

IT commitment



- Commitment from IT agreed and forms part of their 2015-2018 work schedule
- Intend to use internal IT but commitment not agreed and is not currently on their 2015-2018 work schedule

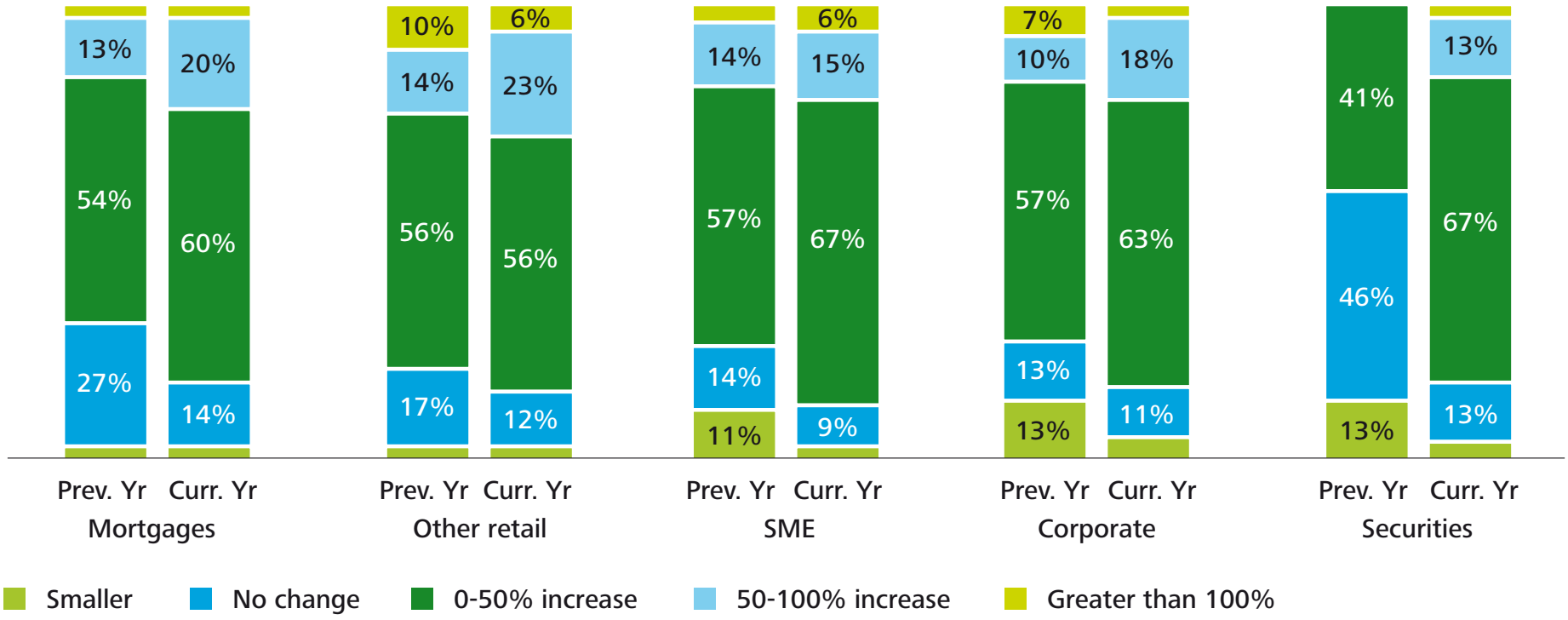
Project budgeting and phasing

Q15: Where system build/enhancements form part of your IFRS 9/FASB CECL model implementation plan, how flexible will this solution be in meeting additional regulatory requirements (e.g. US GAAP (for US respondents, IFRS); EBA Forbearance; BCBS 239; Basel III; CRD IV)?

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

IFRS 9/FASB's CECL model impact analysis

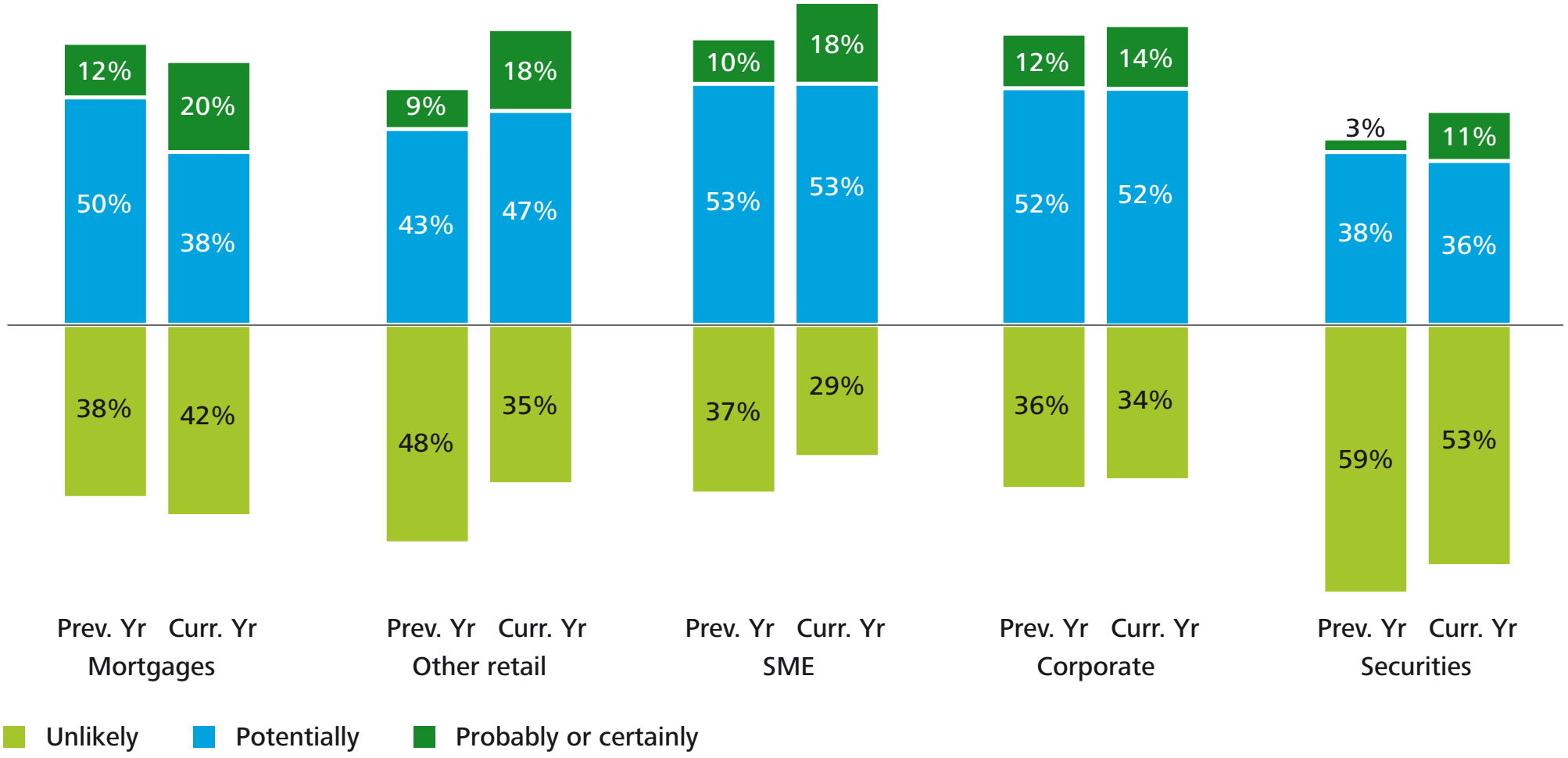
Q16: Assuming today's credit environment were to apply, how is your bank's total impairment provision in the balance sheet likely to change on transition to IFRS 9/FASB's CECL model?*



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

IFRS 9/FASB's CECL model impact analysis

Q17: Do you think moving to an expected loss impairment model will affect the pricing of the following products?



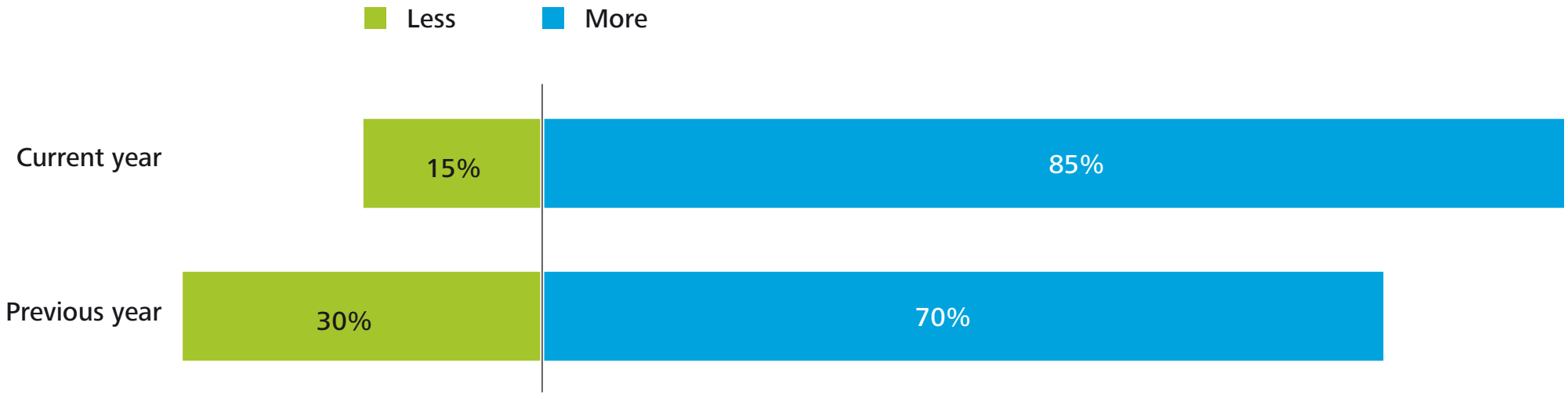
IFRS 9/FASB's CECL model impact analysis

Q18: Do you know how the tax authorities will treat the changes arising from the adoption of IFRS 9/FASB's CECL model?

86% of respondents do not know how the tax authorities will treat changes arising from the adoption of IFRS 9/FASB's CECL model.

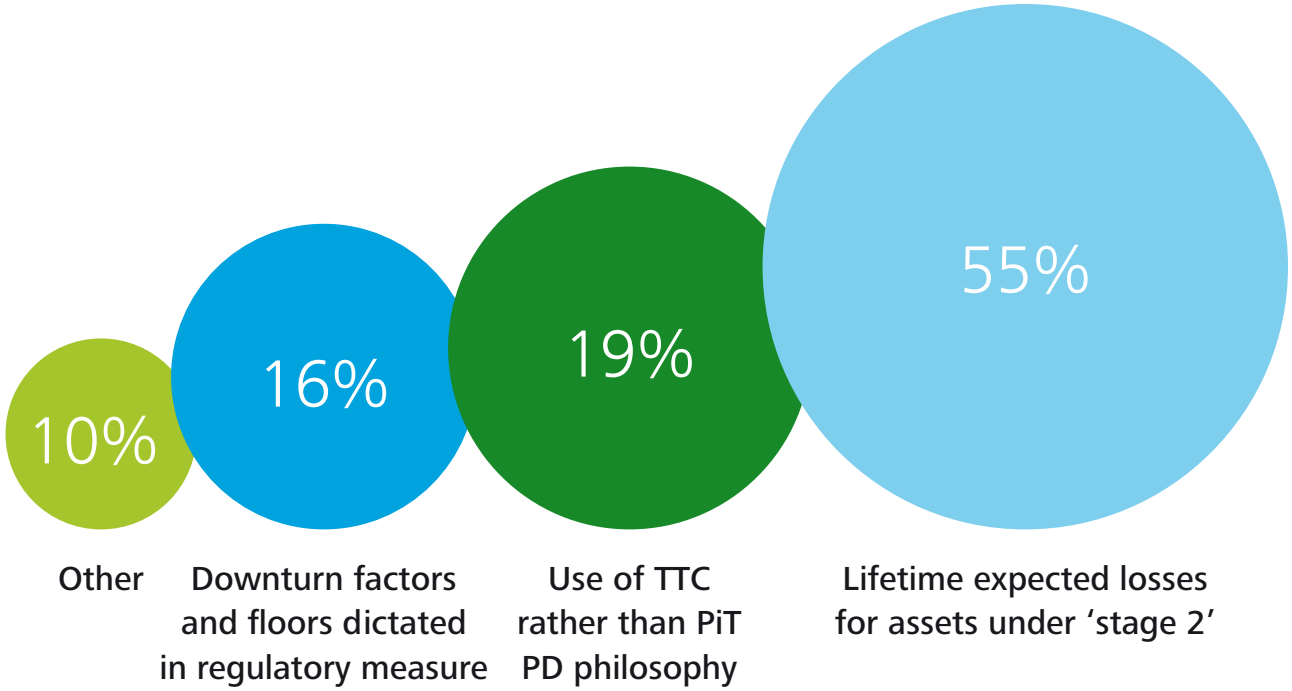
IFRS 9/FASB's CECL model impact analysis

Q19: Do you expect your IFRS 9 expected credit loss/FASB CECL provision to be more or less than your existing expected loss calculation under the Basel Internal Ratings Based regulatory capital approach?



IFRS 9/FASB's CECL model impact analysis

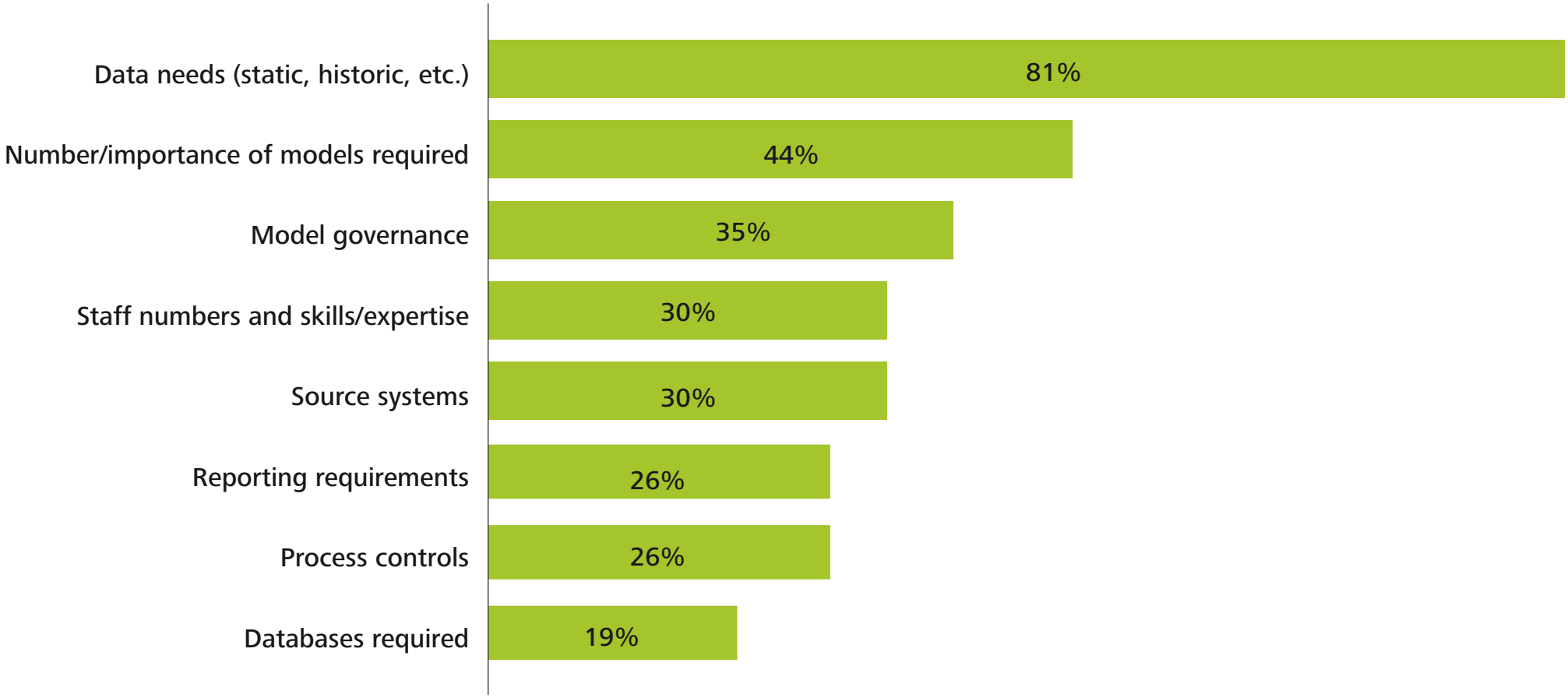
Q20: What do you see as the biggest contributing factors to differences between Internal Rating Based expected loss and IFRS 9/FASB's CECL model? (Rank your top 2)*



* Participants' responses have been weighted, assigning a greater weight to first ranked options over second ranked options. Percentages displayed are based on total weighted responses.

IFRS 9/FASB's CECL governance model

Q21: Which three factors do you see as the biggest model risk challenges under IFRS 9/FASB's CECL model?*



* Participants were asked to select up to three responses. Percentages displayed reflect the proportion of total participant responses to each response option.

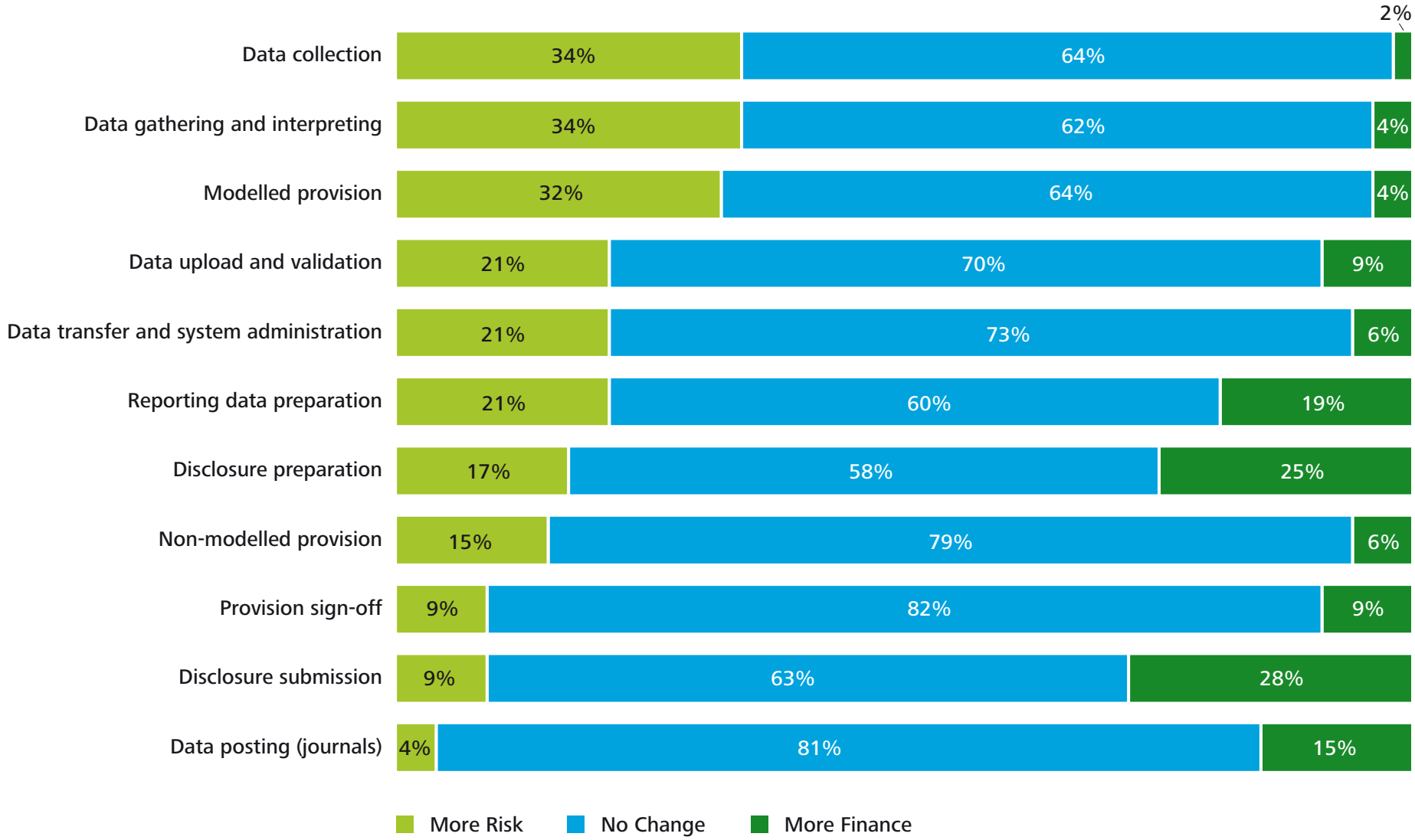
IFRS 9/FASB's CECL governance model

Q22: What are your biggest concerns about using credit risk management systems and data for financial reporting purposes? (Rank from 1 to 3)*

* Participants' responses have been weighted, assigning a greater weight to higher ranked options than lower ranked options. Percentages displayed are based on total weighted responses.

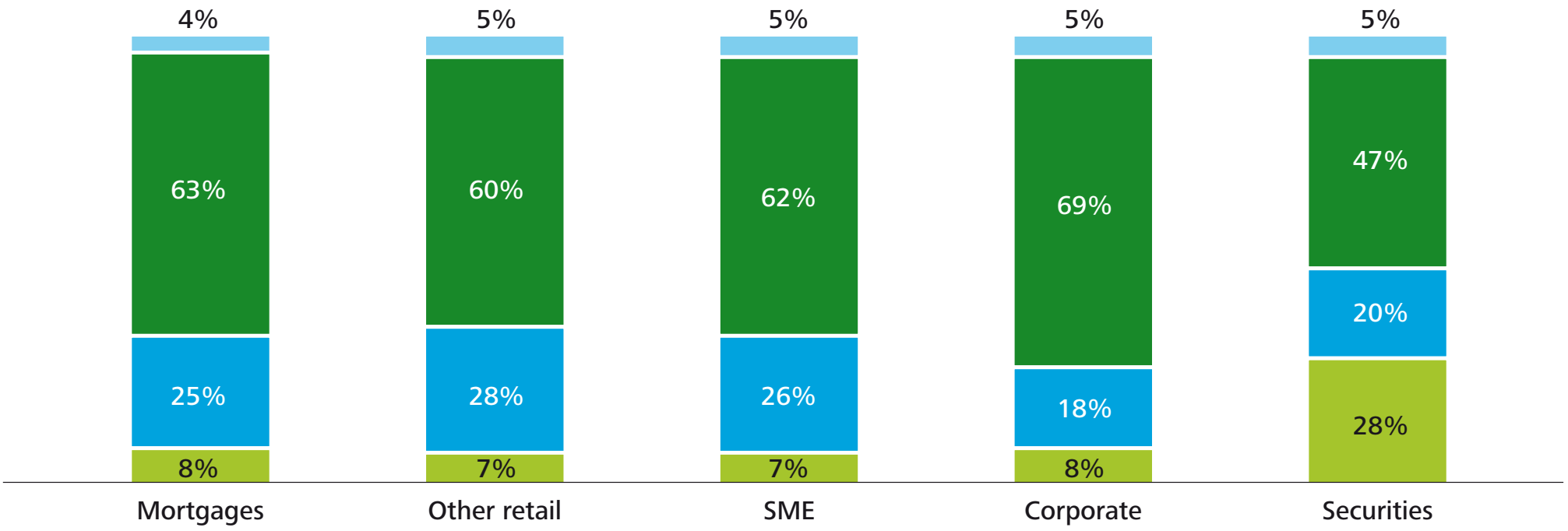
IFRS 9/FASB's CECL governance model

Q23: To what extent do you think the division of labour between Risk and Finance will change under the new IFRS 9 impairment/FASB CECL operating model when compared to the existing incurred loss operating model?



IFRS 9/FASB's CECL model: impairment

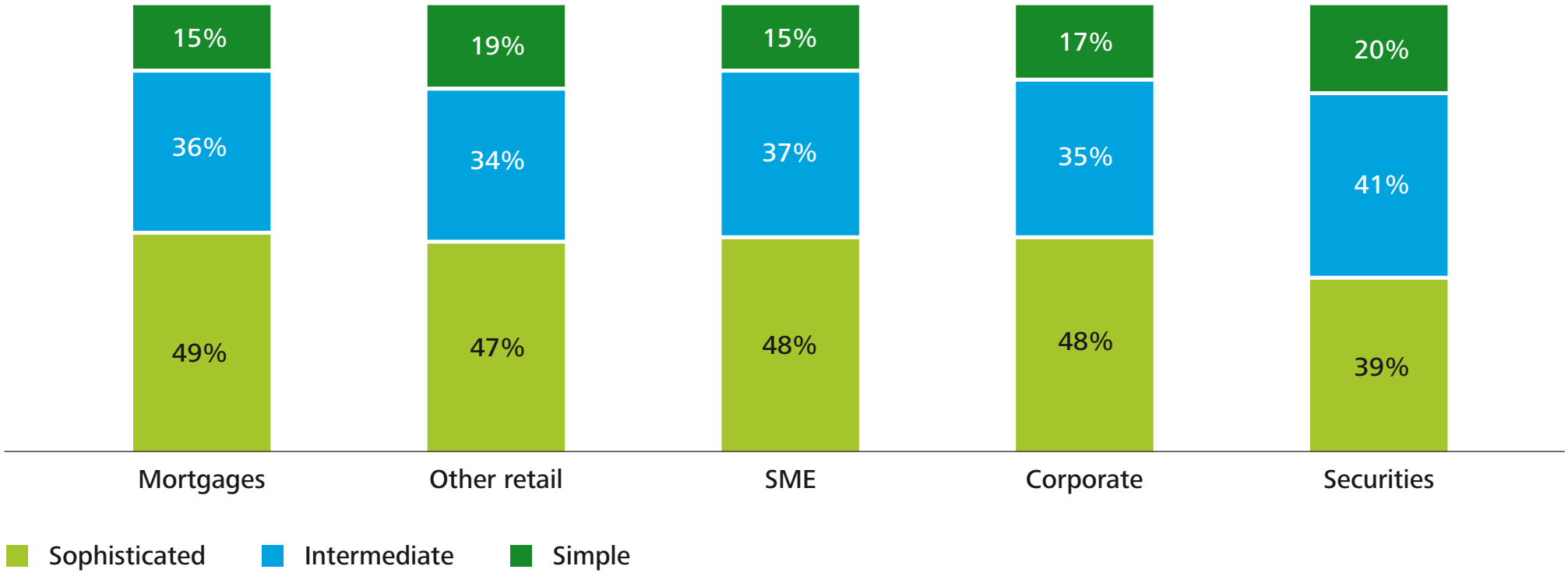
Q24a: What best describes your delivery approach for IFRS 9 impairment/FASB's CECL model development?



- Build new models for IFRS 9/FASB's CECL model purposes only
- Leverage existing models (e.g. IAS 39) used in the existing collective impairment methodology
- Leverage existing models used for Basel purposes
- Other

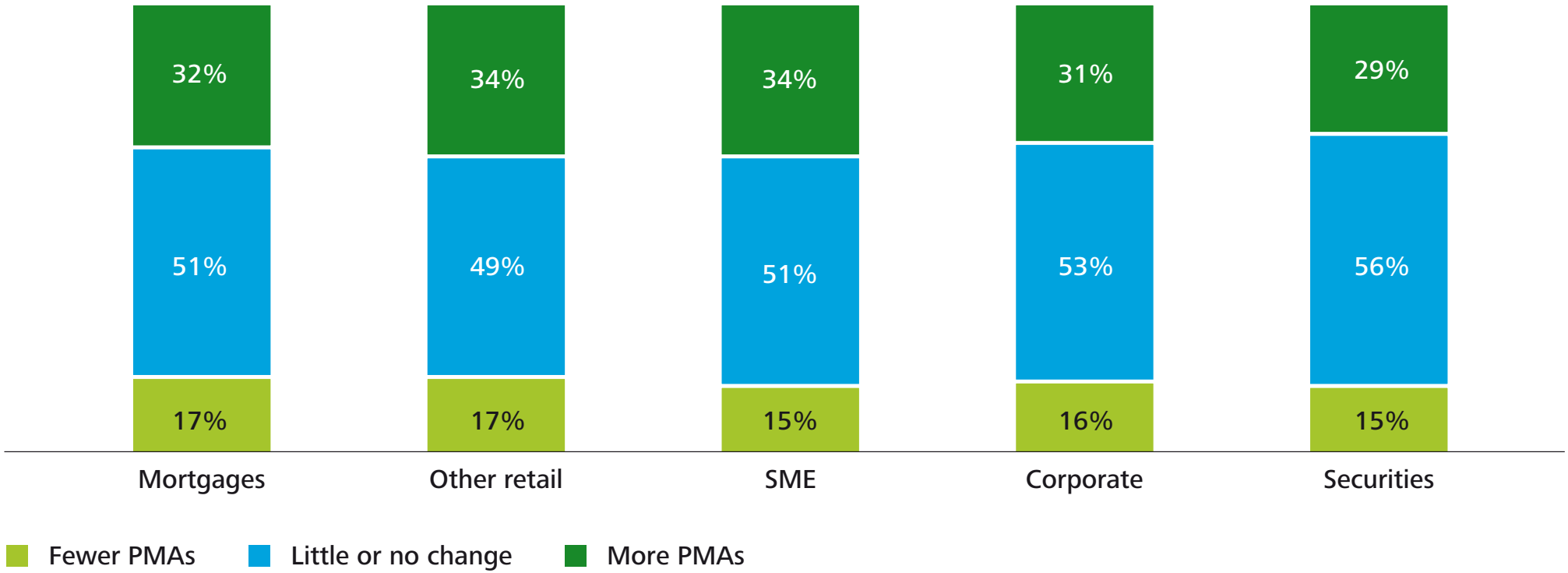
IFRS 9/FASB's CECL model: impairment

Q24b: For your chosen IFRS 9 impairment/FASB CECL model delivery, how would you describe your approach?



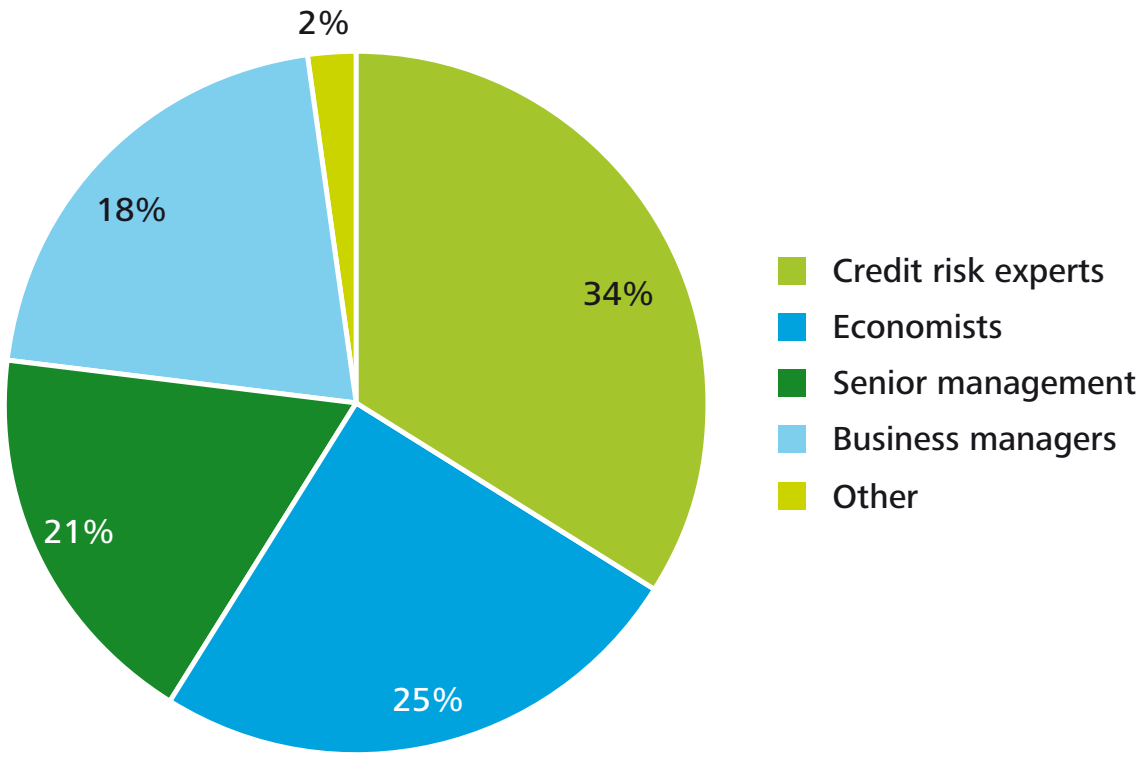
IFRS 9/FASB's CECL model: impairment

Q24c: As IFRS 9/FASB's CECL model increases the complexity of impairment calculations and introduces additional areas for judgement, do you expect this to change the number of post model adjustments (PMAs) held when compared to existing impairment requirements?



IFRS 9/FASB's CECL model: impairment

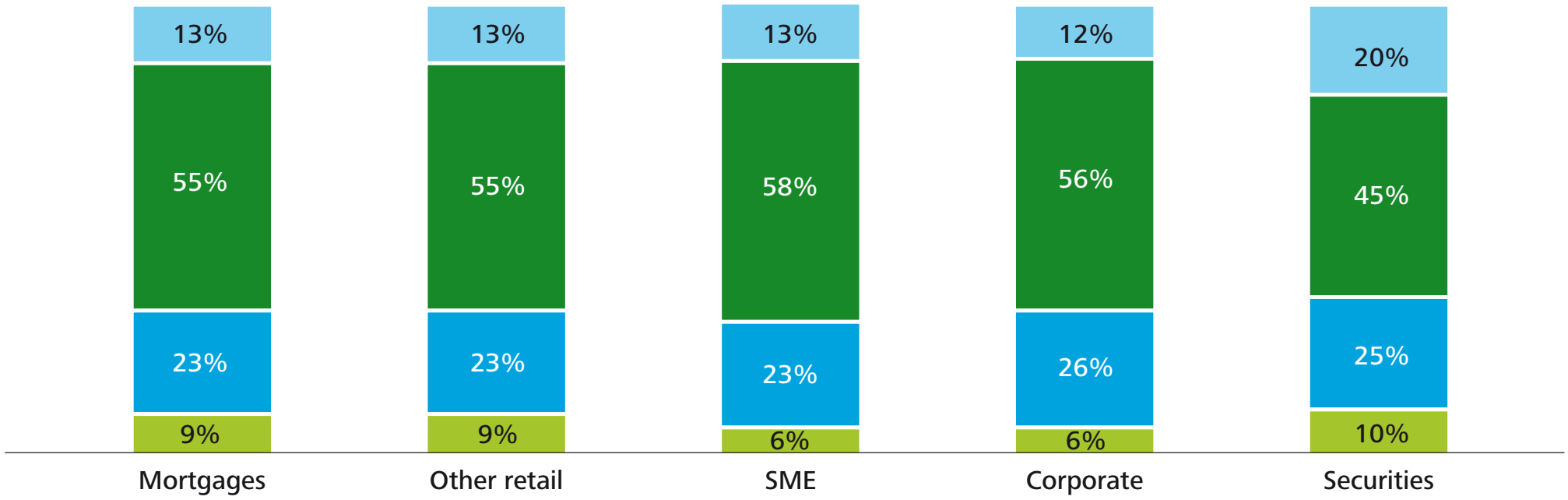
Q25: When selecting forward looking information relevant to the bank's credit risk profile, who will be the key experts involved? (Rank from 1 to 4)*



* Participants' responses have been weighted, assigning a greater weight to higher ranked options than lower ranked options. Percentages displayed are based on total weighted responses.

IFRS 9/FASB's CECL model: impairment

Q26: How do you intend to forecast future economic conditions?



- Create new approach using all available economic data
- Leverage our regulatory capital models and methodology to meet IFRS 9/FASB's CECL model requirements
- Leverage our stress-testing models and methodology to meet IFRS 9/FASB's CECL model requirements
- Other

IFRS 9/FASB's CECL model: impairment

Q27a: How do you expect to define and measure 'significant deterioration' in credit quality? (Rank your top 3)*

	Mortgage	Other retail	SME	Corporate	Securities
Missed payments	39%	41%	15%	14%	14%
Step changes in grading scale	19%	18%	27%	30%	35%
Change in PD exceeds a trigger	17%	16%	21%	18%	19%
PD exceeds a trigger	8%	7%	11%	9%	9%
Enters a watch list/specialist problem credit team	5%	6%	16%	20%	11%
Modification/forbearance	8%	8%	6%	6%	5%
Other	4%	4%	4%	3%	7%

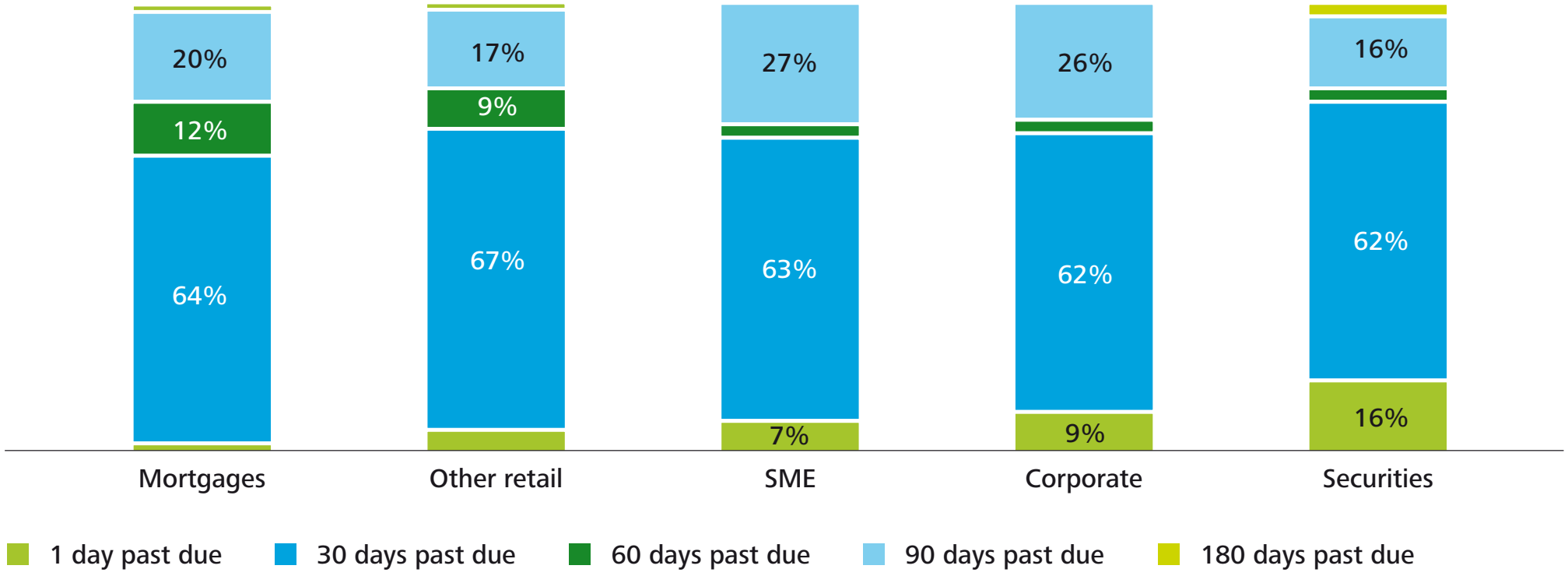
Most important factor

Second most important factor

*Participants' responses have been weighted, assigning a greater weight to higher ranked options than lower ranked options. Percentages displayed are based on total weighted responses by asset category.

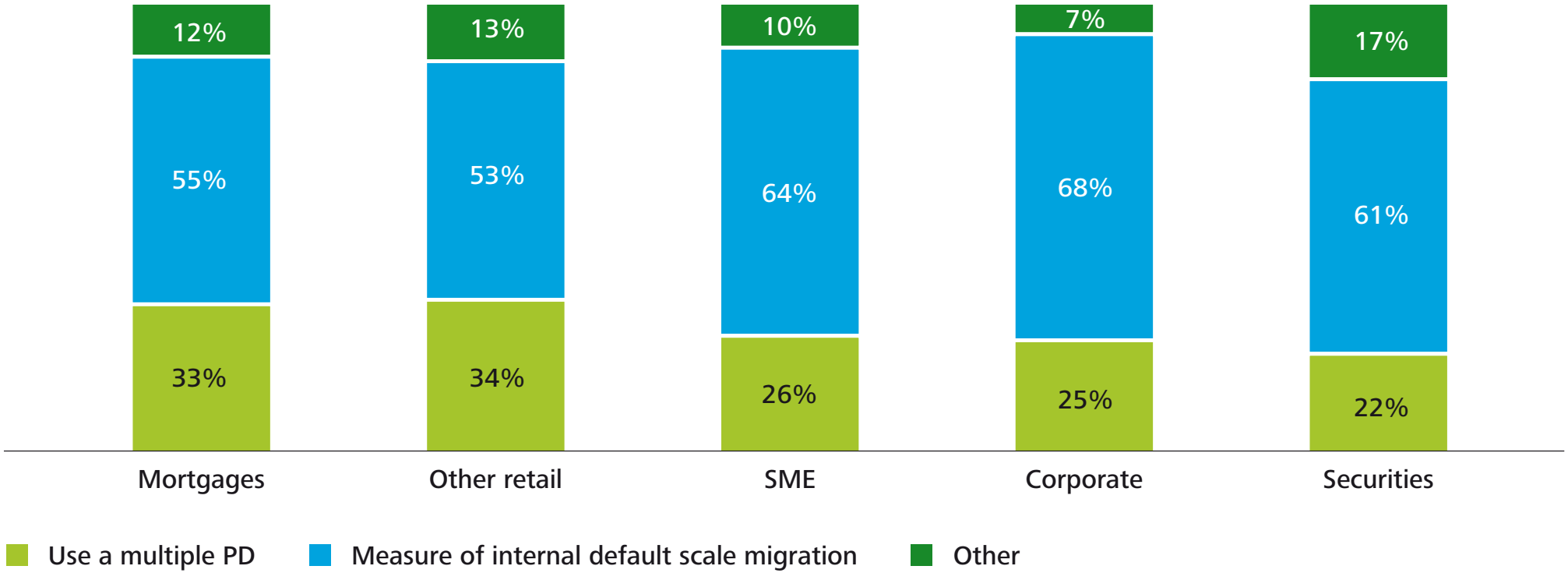
IFRS 9/FASB's CECL model: impairment

Q27b: If missed payments are a key measure of 'significant deterioration' which is the trigger?



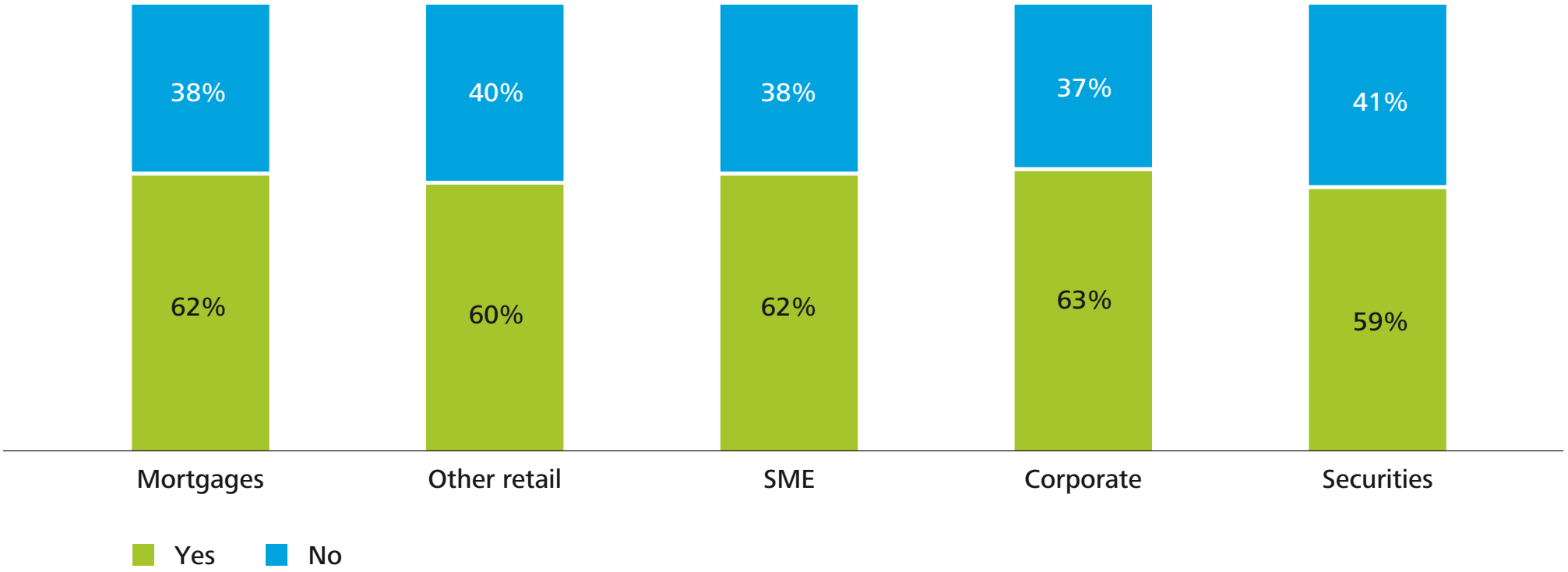
IFRS 9/FASB's CECL model: impairment

Q27c: Where a change in Probability of Default is a key measure of 'significant deterioration', which approach is most likely to be used by asset class?



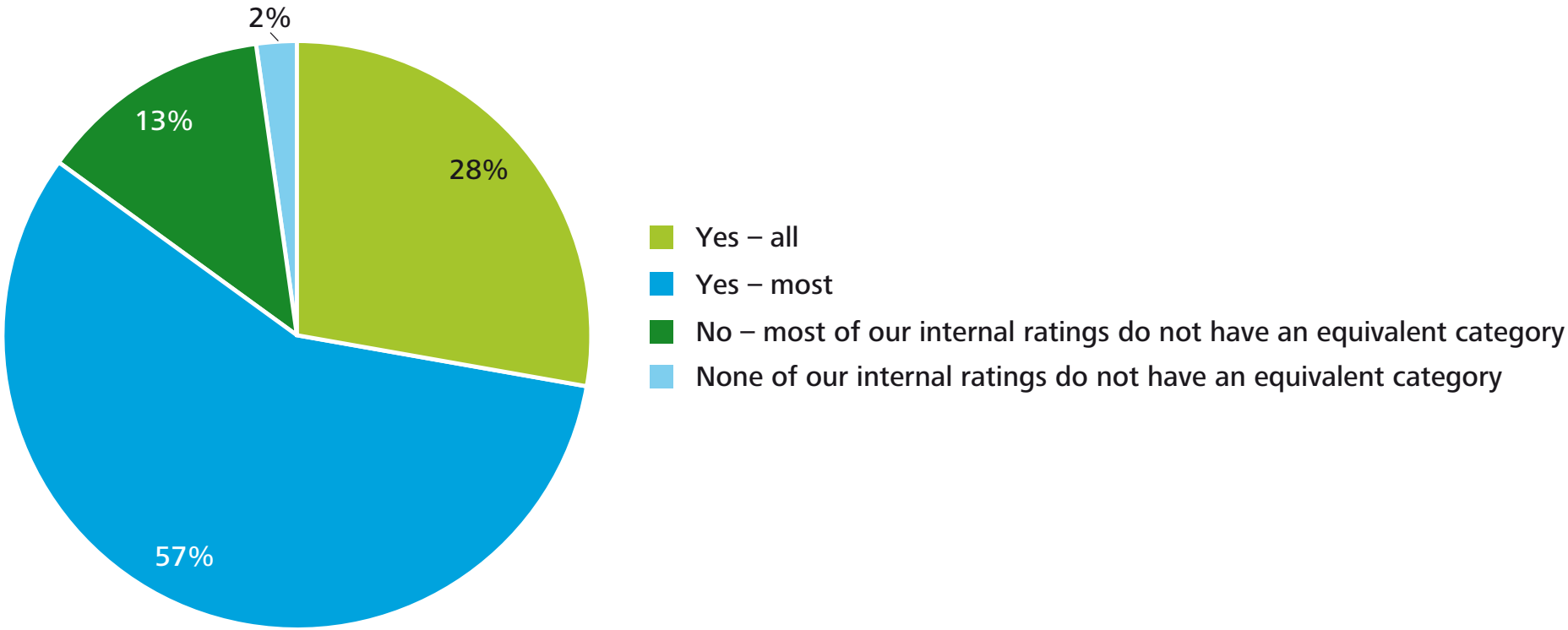
IFRS 9/FASB's CECL model: impairment

Q28: Regardless of credit deterioration status, do you anticipate calculating both a 12 month expected loss and a Lifetime Expected Loss for all exposures?



IFRS 9/FASB's CECL model: impairment

Q29a: Do you have internal ratings that indicate 'investment grade' across your asset classes or products?

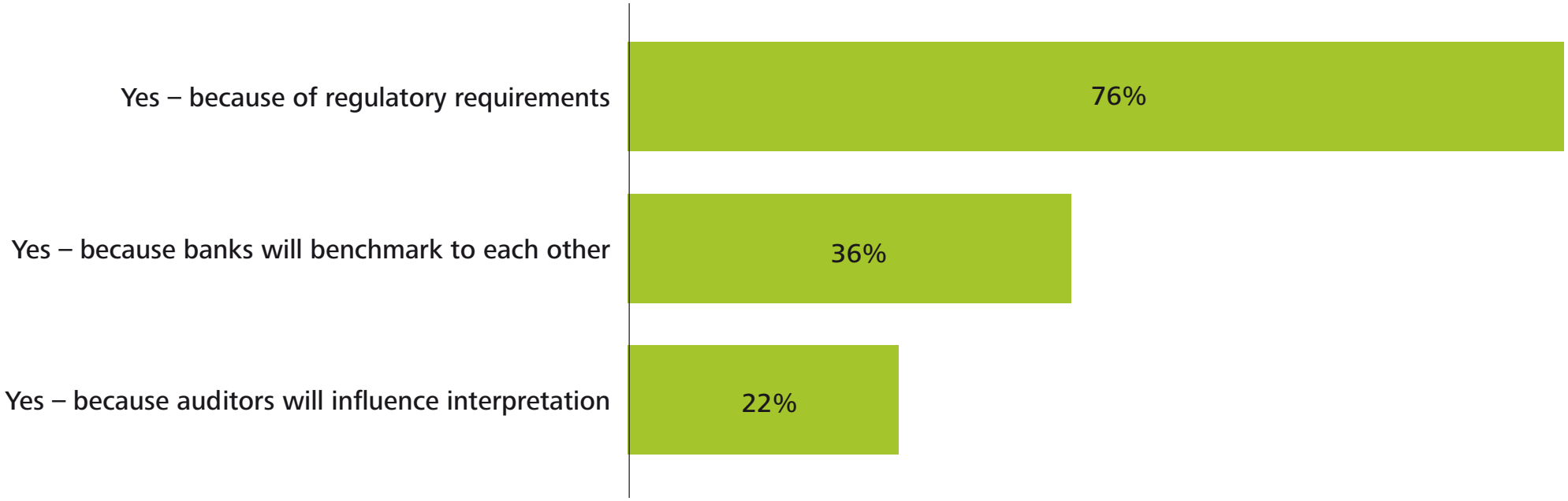


IFRS 9/FASB's CECL model: impairment

Q30a: IFRS 9 states that the default definition should be aligned with an entity's credit risk management practices. Do you think competitor banks will define default in a comparable manner?*

12% of respondents believe that competitor banks will not define default in a comparable manner, while 88% think this definition will be comparable.

The drivers for consistency for the latter respondents are as follows:



* There was no limit to the number of responses that participants could select. Percentages displayed reflect the proportion of total participant responses to each response option.

IFRS 9/FASB's CECL model: impairment

Q30b: By exposure type, how do you intend to define default for IFRS 9/FASB's CECL model purposes?*

	Mortgage	Other retail	SME	Corporate	Securities
90 dpd on any exposure	34%	34%	35%	36%	34%
Basel 'unlikeliness to pay' triggers met	20%	20%	22%	20%	21%
Meets existing accounting impairment triggers under IFRS/US GAAP	17%	17%	17%	19%	20%
Forbearance granted – classed as a default trigger if another default indicator also present	10%	10%	10%	10%	10%
180 dpd on any relevant exposure	8%	9%	4%	3%	4%
Forbearance granted, always classed as a default trigger	3%	3%	3%	3%	2%
Other	8%	7%	9%	9%	9%

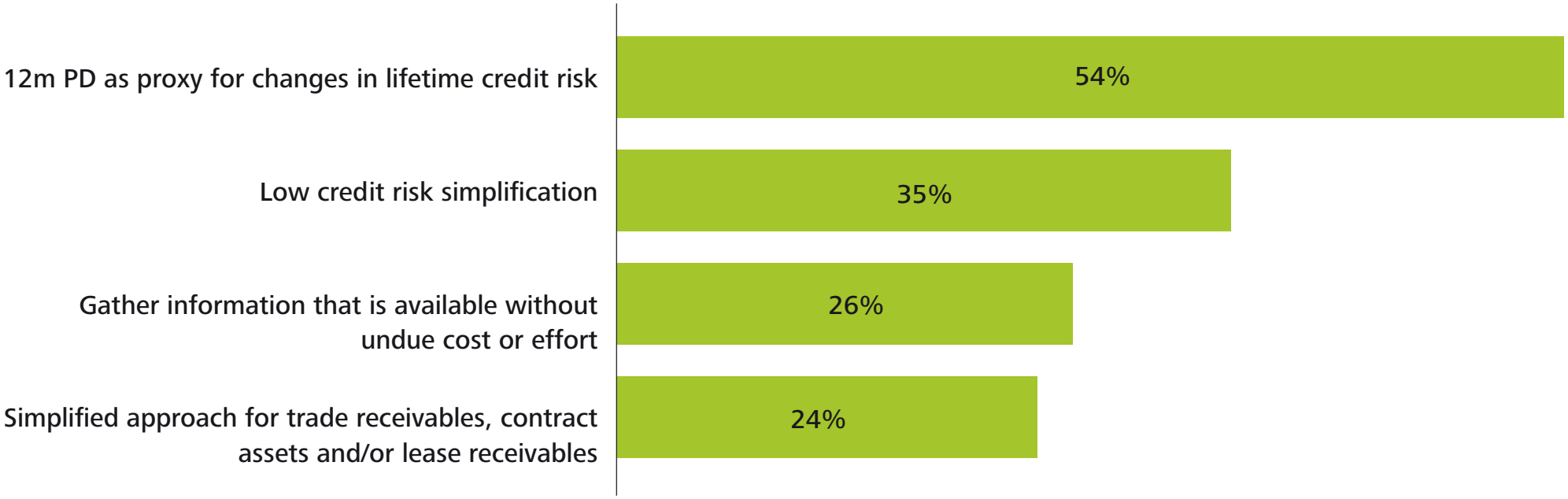
Most important factor

Second most important factor

*There was no limit to the number of responses that participants could select per exposure type. Percentages displayed reflect the proportion of total participant responses to each response option, by exposure type.

IFRS 9/FASB's CECL model: impairment

Q31: Do you expect to make significant use of the operational simplifications available under the IFRS 9 impairment model?*

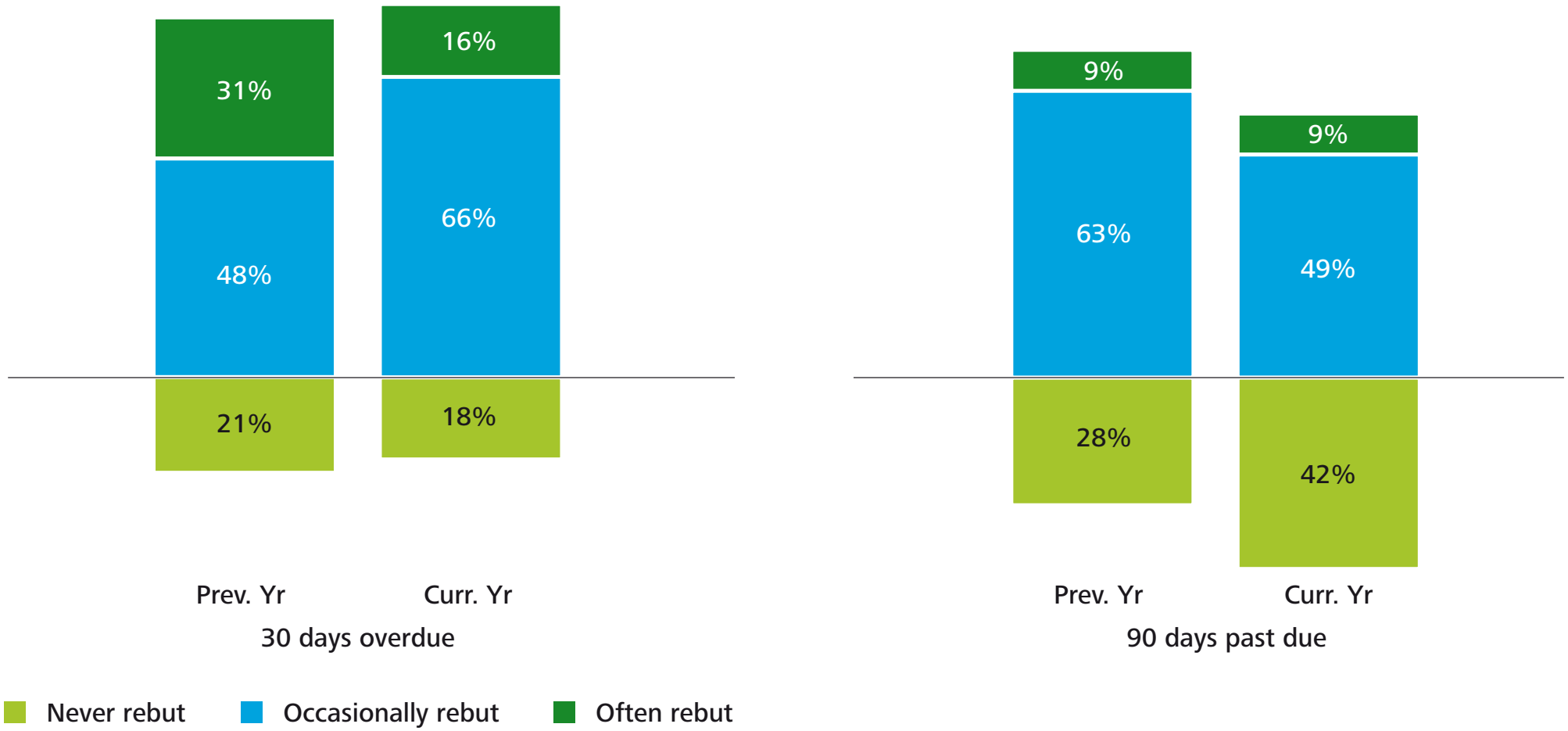


26% of respondents do not expect to make significant use of any of the operational simplifications available under the IFRS 9 impairment model.

* There was no limit to the number of responses that participants could select. Percentages displayed reflect the proportion of total participant responses to each response option.

IFRS 9/FASB's CECL model: impairment

Q32: Do you expect to rebut the presumption that financial instruments (a) have significantly deteriorated if they are overdue by 30 days and (b) default does not occur later than 90 days past due:



IFRS 9/FASB's CECL model: impairment

Q33: What are the key data collection challenges that you expect to face when designing and implementing your IFRS 9/FASB CECL model project plan?

The major challenge cited by our respondents is the availability and tracing of historical data for PD calculation and significant deterioration in credit risk assessment. Other significant challenges are the link of macroeconomic and forward looking information to loan portfolios and bucket change monitoring.

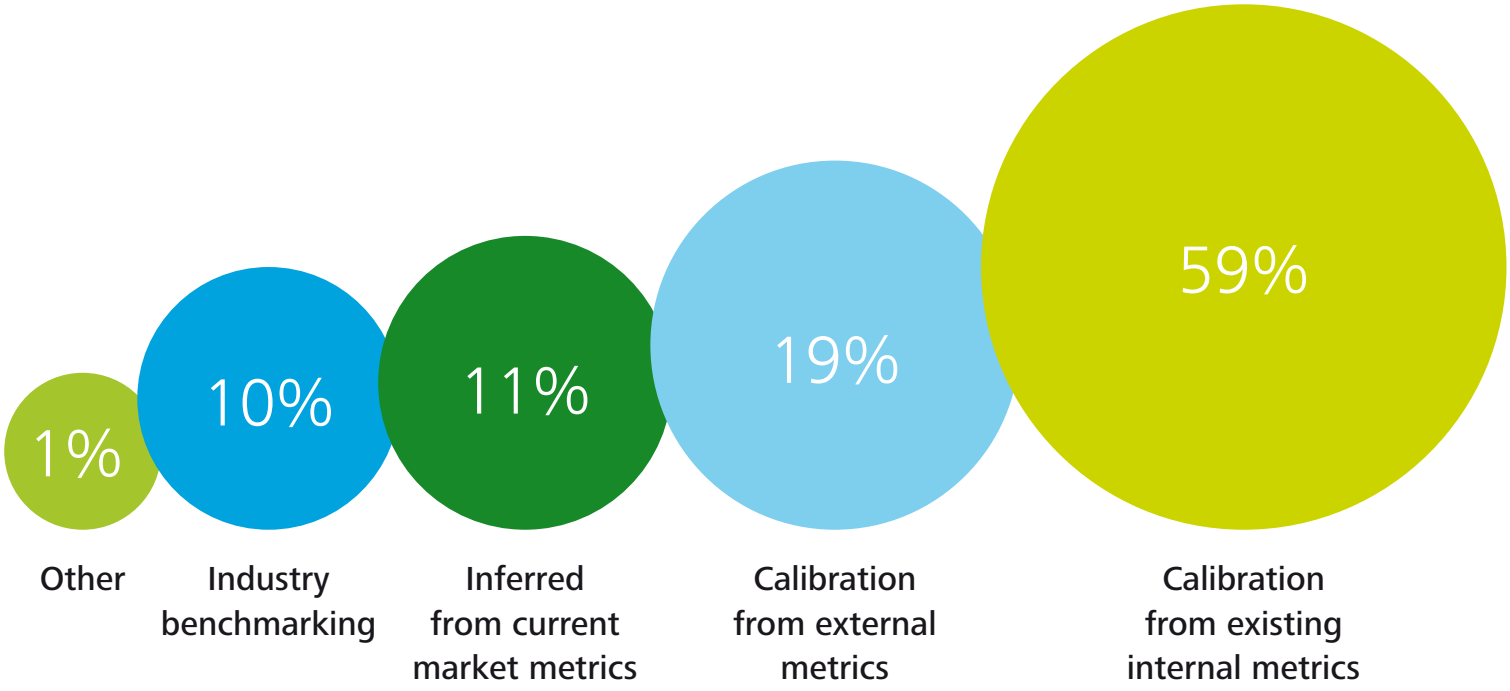
IFRS 9/FASB's CECL model: impairment

Q34: Has the AQR exercise in Europe/CCAR (if applicable) helped to improve data quality?

64% of respondents believe that the AQR exercise carried out in Europe and the capital stress testing "CCAR" exercise have helped or will help in some way to improve data quality.

IFRS 9/FASB's CECL model: impairment

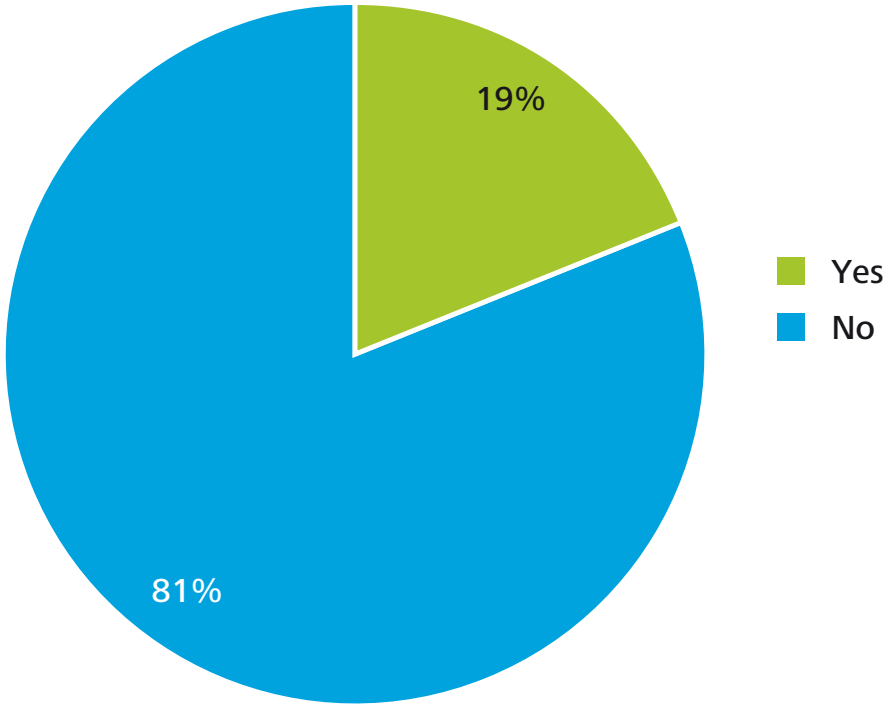
Q35: Where Probability of Default and Loss Given Default are used, how do you expect to approach data gathering? (Rank the following options)*



* Participants' responses have been weighted, assigning a greater weight to higher ranked options than lower ranked options. Percentages displayed are based on total weighted responses.

IFRS 9/FASB's CECL model: impairment

Q36: IFRS 9 and IAS 39 require the use of EIR when discounting expected recoverable cash flows. Do you anticipate changing the way you calculate and use EIR under IFRS 9 when compared to IAS 39?



Acronyms

AQR	Asset Quality Review
BCBS	Basel Committee on Banking Supervision
BCBS 239	Basel Risk Data Aggregation
CCAR	Capital Stress Testing
CECL	Current Expected Credit Loss
CRD IV	Capital Requirements Directive IV
DPD	Days Past Due
EBA	European Banking Authority
EIR	Effective Interest Rate
EMEA	Europe, Middle East and Africa
EU	European Union
EUR	Euro
FASB	Financial Accounting Standards Board
FSB	Financial Stability Board
G-SIFI	Global Systemically Important Financial Institution
IAS	International Accounting Standard
IASB	International Accounting Standards Board
IFRS	International Financial Reporting Standard
PD	Probability of Default
PiT	Point In Time
PMA	Post Model Adjustment
SME	Small and Medium Enterprises
TTC	Through The Cycle
US GAAP	United States Generally Accepted Accounting Principles

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