STAFF PAPER

18 – 22 November 2013

REG IASB Meeting

Project	**Financial Instruments: Impairment**		
Paper topic	Mandatory effective date of IFRS 9		
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Introduction

1. As part of the Exposure Draft *Financial Instruments: Expected Credit Losses* ('the Impairment ED'), the IASB noted that all phases of IFRS 9 *Financial Instruments* have the same effective date and asked for feedback on what lead time was required to implement the proposals on expected credit losses and also asked for views on what the resulting mandatory effective date for IFRS 9 should be.

2. At the July 2013 meeting, the IASB noted that it will only be able to determine the mandatory effective date after the redeliberations on the impairment and classification and measurement requirements have been completed, and the issue date of the final version of IFRS 9 is known. The IASB therefore agreed to defer the mandatory effective date of IFRS 9 without specifying a new mandatory effective date, pending the finalisation of both the impairment and classification and measurement requirements.[1]

3. The deliberations for both the impairment and classification and measurement requirements are still ongoing and the target date (based on the current work plan)

[1] Refer to Agenda Paper 6A *'Own credit' and IFRS 9 effective date* and the July 2013 IASB Update available at http://www.ifrs.org/Updates/IASB-Updates/Pages/IASB-Updates.aspx

for the completion of the impairment and classification and measurement phases of IFRS 9 is the first half of 2014[2].

4. Since the July 2013 meeting, the IASB has received requests from various constituents seeking clarification on a potential effective date of the completed IFRS 9. We have been told that prior to setting a date, it would be helpful for entities' planning purposes if the IASB were to provide a signal on the earliest mandatory effective date.

5. This Agenda Paper follows from the decision to defer the mandatory effective date and considers the minimum time period that would be appropriate for the implementation of the proposed impairment requirements in order to determine *the earliest* date for the mandatory effective date of IFRS 9.

6. This paper does **not** propose a mandatory effective date. This paper also does not consider the transition requirements that should be applied on the initial date of implementing IFRS 9. These matters will be discussed at a future meeting.

Detailed feedback received

7. The Impairment ED, published in March 2013 asked for responses to the following question:

> Question 12
>
> (a) What lead time would you require to implement the proposed requirements? Please explain the assumptions that you have used in making this assessment. As a consequence, what do you believe is an appropriate mandatory effective date for IFRS 9? Please explain.

Feedback on the Impairment ED

8. In the comment letter analysis presented at the July 2013 joint board meeting, we reported that respondents generally commented that a 2-3-year lead time from the date of issuing the final version of IFRS 9 is necessary to implement the proposed

[2] Refer to the Work plan on our website http://www.ifrs.org/Current-Projects/IASB-Projects/Pages/IASB-Work-Plan.aspx

requirements. Many respondents noted that even sophisticated entities would need to make significant system changes in order to implement the model and that specialist resources would need to be sourced. Respondents indicated that such a lead time would enable them to apply the model in parallel with an annual reporting period to ensure operability and information quality. In contrast, some respondents thought two years would be sufficient, while a few indicated that 4-5 years would be needed. A few respondents also requested that the mandatory effective date of IFRS 4 *Insurance Contracts* and IFRS 9 should be aligned.

9. Respondents acknowledged the importance of finalising and implementing the new impairment requirements as soon as possible, and also acknowledged the pressure on the IASB to deliver this, because of the time that has elapsed since the project started. However, they commented that it is essential that enough time be provided for the final Standard to be implemented in a robust and consistent manner.

Subsequent submissions

10. Subsequently, participants at various outreach events have provided more detail about the reasons why a three-year implementation period is needed. Some of the reasons provided for this period included:

    (a) the size and complexity of the necessary changes to credit risk management systems and processes and the volume of data required to apply the proposed model;

    (b) the interaction between the proposed impairment model and regulatory capital requirements;

    (c) the desire to run this system in parallel with IAS 39 *Financial Instruments: Recognition and Measurement* for a period prior to the date of application; and

    (d) the need to inform users of financial statements and other stakeholders of the accounting, regulatory capital and business impacts before IFRS 9 becomes effective.

11. In addition, more letters have recently been submitted to the IASB to further support why financial institutions will require three years from the date of issuing to implement IFRS 9.

12. The reasons provided can be summarised as follows:

    (a) ***Model changes***: the proposed impairment model will involve the construction or significant adaptation of risk models for numerous portfolios within the scope of the requirements. It will also require the development and introduction of entirely new processes, such as systematically capturing significant increases in credit risk, and the application of the appropriate forward-looking data to the measurement of the resulting lifetime expected losses, as well as significant system changes.

    (b) ***Availability of information***: the availability of historical data and trend information is critical for assessing increases in credit risk over time and estimating expected credit losses. For many portfolios, this information will need to be collected or estimated for the first time. The incorporation of forward-looking information was emphasised as a particular area in which current systems will need to be upgraded. It is therefore vital that sufficient time is allowed for data to be collected and trend information to be developed in order to implement the approach to the required standard.

    (c) ***Parallel reporting***: because of the scale of the credit risk management system and model changes, a one year parallel run period is required to perform systems and process dry runs to verify the reliability of the new models and the reporting systems. This time is also needed to provide management with sufficient time to understand the assumptions, judgements and sensitivities involved in determining impairment allowances under the new requirements.

    (d) ***Interaction with regulatory capital requirements*****:** constituents said that the interaction of IFRS 9 with the regulatory requirements is likely to be complex and that managing the impact on regulatory capital will be a key element of the implementation of IFRS 9 for all banks. Lead time would assist regulators in understanding the accounting requirements and associated impact and to foresee any resulting changes needed to regulatory requirements.

(e) ***Interaction with other major regulatory reforms***: financial institutions are currently in the process of implementing a number of significant regulatory projects that involve demands on similar resources across Risk and Finance functions. All these projects are running concurrently and put a strain on the availability of resources to ensure effective implementation of IFRS 9.

(f) ***Interaction between IFRS 9 other IFRS Projects***: entities are not able to finalise the scope of the new impairment proposals until the classification and measurement elements of IFRS 9 are completed. In addition it was noted that the timing of other IFRS projects affects the appropriate effective date for IFRS 9. In this context, the interaction with the Insurance Contacts project was particularly noted.

13. Until we finalise the redeliberations, entities' ability to prepare is limited. For example, we are yet to redeliberate transition and the disclosure requirements, the details of which can have significant effects on data requirements and systems design. Entities have indicated that even when deliberations are complete, until the final wording is available it is difficult to undertake full implementation, because of the risk of change (for example the wording of rebuttable presumptions and disclosure requirements can cause changes in scope and/or date requirements).

14. In the light of these arguments, respondents indicated that they believe a mandatory effective date earlier than 1 January 2017 would compromise the effective implementation and quality of information provided by IFRS 9.

Staff analysis and recommendation

15. We acknowledge the feedback and arguments put forth by respondents during the comment period and subsequently during our outreach and fieldwork activities.

16. As noted in Agenda Paper 6A discussed at the July 2013 IASB meeting, the *IASB and IFRS Interpretations Committee Due Process Handbook*, as issued in February 2013, describes how the IASB determines effective dates:

> *A Standard, or an amendment to a Standard, has an effective date and transition provisions. The mandatory effective date is set so that jurisdictions have sufficient time to incorporate the new requirements into their legal systems and those applying IFRS have sufficient time to prepare for the new requirements*.

17. The IASB usually tries to allow at least 18 months between the issuance of a final Standard and the mandatory effective date.

18. If the final version of IFRS 9 is issued before the end of June 2014, as per the current work plan, an 18-month implementation period would result in an effective date of 1 January 2016. However, in the light of the arguments discussed in paragraphs 8-14, we believe that an implementation period of only 18 months may put undue pressure on entities to implement IFRS 9. Indeed, we question whether robust implementation of the requirements within such a short time frame would even be feasible. We note that in other cases in which there have been potential material system changes, such as in the case of Revenue Recognition, the IASB has agreed a longer implementation period.

Staff recommendation

19. While deliberations are continuing and the outcome of the final IFRS 9 is being deliberated, we are not recommending that the IASB should yet determine the mandatory effective date of IFRS 9. However, because of the required lead time and the size of the implementation projects that will result, we believe it would be helpful for preparers' planning purposes to provide some guidance about the earliest mandatory effective date for IFRS 9.

20. On the basis of the feedback and information received, we recommend that the final IFRS 9 should have a mandatory effective date **no earlier than** annual periods beginning on or after 1 January 2017.

21. Once the redeliberations on classification and measurement are complete, we shall provide the IASB with a separate paper to consider the appropriate mandatory effective date of IFRS 9.

Question to the IASB
Does the IASB agree with our recommendation that IFRS 9 *Financial Instruments* should have a mandatory effective date no earlier than annual periods beginning on or after 1 January 2017? If not, what would the IASB prefer?