Yandraduth Googoolye: International Financial Reporting Standards (IFRS 9) - implementation issues

Keynote address by Mr Yandraduth Googoolye, Governor of the Bank of Mauritius, at the Seminar on "International Financial Reporting Standards (IFRS 9) - Implementation Issues", Ebène, 19 August 2019.

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Ladies and gentlemen

Good morning.

I thank Mr Abdoul Aziz Wane, the Director of AFRITAC South and the Africa Training Institute, and Mr Ravi Mohan, Resident Advisor, for inviting me to address you this morning.

The AFRITAC South (AFS) has been instrumental in promoting capacity building in this side of the continent. It has hosted a few seminars on International Financial Reporting Standards (IFRS) for countries in Sub-Saharan Africa to enable them to prepare for the implementation of IFRS9. In case you are not aware, the origin of these seminars was from a suggestion made by the Bank of Mauritius at one of the Steering Committee meetings of the AFS. Let me thank the AFS for its efforts to build capacity in this region.

With the onset of the global financial crisis more than a decade ago, bank supervisors were heavily criticised for having failed to spot the risks building up in the financial system and the inadequacy of provisions made by banks. The incurred loss model of provisioning came under heavy criticism, as it resulted in too little provisions too late. In the midst of public backlash, the International Accounting Standards Board was faced with the need to review the provisioning methodology to make it more forward-looking. This triggered the development of the expected loss model under IFRS9.

IFRS9 is a complex accounting standard. It relates to financial instruments and requires great deal of understanding and application on the part of prudential supervisors and auditors of financial statements. Intricately connected to IFRS9 are two other accounting standards, namely IFRS7 (Financial Instruments: Disclosures) and IFRS13 (Fair value measurement of financial instruments). This seminar, I understand, covers important aspects of these three standards. Rest assured, I will not go into the details but leave it to the experts to delve into the technicalities of IFRS9.

It is essential that supervisors and regulators are well aware of the underlying concepts of IFRS9. They need to be equipped with the right tools and techniques to conduct supervision of banks and financial institutions in the most effective way. It is only then that they will be able to gain adequate insights into the implications of IFRS9 on credit risk models and blend the IFRS9 requirements with existing methods and models used for risk and regulatory purpose.

Given the complexities of IFRS9, many jurisdictions still consider that it can be very beneficial to share country experiences on implementation issues and challenges. Allow me, ladies and gentlemen, to share the experience of Mauritius in the implementation of IFRS9. I will also brush over some of the recent developments in the regulatory and supervisory framework of the jurisdiction.

Experience on implementing IFRS9

As an International Financial Centre, Mauritius is committed to adopting international standards and best practices. IFRS9 became effective since January 2018 in Mauritius. To meet the deadline of January 2018, the preparatory work for the execution of IFRS9 started as early as

2016.

The Bank of Mauritius introduced a programme to closely monitor progress by each bank and non-bank deposit-taking institution in implementing IFRS9. As from March 2016, the Bank of Mauritius held a series of consultations with external auditors and banks to ensure smooth execution of IFRS9. Regular meetings were held with each licensee to discuss their execution plans and the potential impact of the new standards. The central bank started requesting for quarterly progress reports from concerned institutions to monitor progress.

In the light of the complexities involved, these institutions were requested to complete a comprehensive survey, where they were asked details about the impact of IFRS9 on their profitability and capital adequacy as well as the expected completion date. The survey revealed that the increase in provisions would generally range between 2 to 87 per cent, with an average increase of 18 per cent. Eight banks out of a total of 21 reported that there would not be any increase in provisions. The predicted impact on the Capital Adequacy Ratio ranged from 0.1 per cent to negative 2.20 per cent, with an average impact of negative 0.48 per cent.

The survey also revealed that banks used varying models to estimate credit losses given that IFRS9 is a principles-based standard and thus was not prescriptive on the calculation of the expected losses. However, judgement was required in choosing forward-looking parameters for the model used and in identifying significant increase in credit risk. The Bank of Mauritius was aware that banks might lack the required historical data on defaults in order to estimate losses accurately. This might partly explain the varying potential impact of the standard on the provision required by banks.

Conscious of the challenges ahead, the Bank of Mauritius revised its Guideline on Credit Impairment Measurement and Income Recognition, which will come into effect as from 1 January 2020. To ensure consistency and address the concerns on modelling risk, the Guideline sets regulatory floors for provisioning. That is, when a financial institution makes accounting provisions lower than the regulatory floors, the shortfall will be accounted for either through additional provisions or a charge to the equity of the financial institution. The Bank of Mauritius is equally considering the possibility of a phase-in period of one year for provision levels to be met so that financial institutions have ample time to make the necessary adjustments.

In March 2019, the Bank of Mauritius conducted a workshop on IFRS9 in collaboration with the Mauritius Bankers Association and a consultancy firm. The Bank of Mauritius has also hired a Consultant to train supervisors on IFRS9 and to assist in the development of a set of IFRS9 returns to be submitted by the financial institutions. The returns will capture data on the calculation of expected credit losses under IFRS9 and on governance as well as the model's methodology and set of assumptions. The draft returns are expected to be finalized shortly.

Recent developments

Ladies and gentlemen, as we now reach the second part of my remarks, I will provide an overview of some of the recent developments in the regulatory and supervisory landscape in Mauritius.

The Bank of Mauritius is actively working on the modernization and consolidation of its supervisory framework. We have embarked on the implementation of a full-fledged risk-based supervisory framework. Our supervisory approach is evolving from a compliance-based framework to a risk-based framework, which is expected to be completed by end-2020.

A separate module on Money Laundering/Fighting against Terrorism risks is being incorporated in our risk-based supervisory framework. The Supervision Department now has a dedicated unit to monitor Money Laundering/Fighting against Terrorism risks in the banking sector through off-site surveillance as well as on-site examinations.

Many of you might be aware of the Mutual Evaluation Report published by the ESAAMLG in September 2018 on the assessment of the AML/CFT measures of Mauritius. We have since made significant strides in addressing the deficiencies highlighted in the Report. In a follow-up Mutual Evaluation Report published in April 2019, the ESAAMLG concluded that Mauritius has made significant progress in resolving the technical compliance shortcomings. Further, Mauritius submitted an application for Technical Compliance Re-rating of 12 recommendations, of which 11 were successfully upgraded. The Financial Services Commission, the Bank of Mauritius and the Financial Intelligence Unit closely collaborate to fight financial crime. A memorandum of understanding between the three regulatory institutions was signed last year.

The central bank is currently working on the establishment of a Deposit Insurance Scheme. The legislation was approved by Parliament and received Presidential Assent in April 2019. However, it is yet to be proclaimed. The central bank has already started working on the operational aspects of the Scheme, which will guarantee coverage to eligible depositors up to a specific amount. At the same time, we are also working on a crisis resolution framework.

Collaboration with Supervisory Authorities

Many jurisdictions represented here are host to Pan-African banking groups and Mauritius is no exception. Some of our local banks have also extended their footprint on mainland Africa. Home and host authorities are increasingly required to work closely for effective supervision of banks. The Bank of Mauritius has signed Memoranda of Understanding with 17 foreign regulatory authorities, which include banking sector regulators of Kenya, South Africa, Nigeria, to name a few. Consolidated supervision is now part of our supervisory toolkit and is conducted on a regular basis. Home and host regulators are able to share their insights on the risk management framework of banking groups in supervisory college meetings. New areas such as cyber risks are closely monitored.

In March 2019, the Ombudsperson for Financial Services was appointed. Complaints from consumers of financial services against financial institutions licensed by the Bank of Mauritius and the Financial Services Commission are now handled by the Ombudsperson’s Office. This is expected to fast-track complaints resolution. It is also incumbent on the Office of Ombudsperson for Financial Services to inform and educate the general public on investments in financial services offered by financial institutions.

My address will be incomplete if I do not mention the significance of corporate governance in banks. Although a risk-based supervisory framework will ensure the strength and credibility of our financial system, it cannot eliminate the possibility of failure of an institution. I constantly remind my officers to keep a close watch on the governance practices of banks. It is an advice that I extend to all of you.

Concluding note

I am sure that the seminar will provide you with a good insight into the challenges of implementing IFRS9 as well as key takeaways from the experiences of other countries. Learning from others’ experience will undoubtedly assist you all to improve your own supervisory practices.

I am delighted to open this Seminar on “International Financial Reporting Standards: Implementation Issues” and wish you all fruitful deliberations.

Thank you.