

# Beyond the IFRS 9 Governance and Controls

## Preface

This document starts with a discussion of the purpose and principles of designing and implementing an IFRS 9 governance and control framework (“the Framework”). It then provides examples of new controls associated with the IFRS 9 impairment assessment to illustrate how to implement those principles. Finally, it provides some suggestions regarding how to leverage available information to ensure the completeness of the Framework.

This document goes beyond the scope of the IFRS 9 program for the following reasons:

- IFRS 9 represents a merger of risk management and financial accounting, which has wide and deep impact on an organization’s business operation; therefore, the IFRS 9 program should not be viewed in isolation, rather, should be viewed in the context of the whole organization’s business management, financial management and risk management.
- Any significant regulatory initiative or business initiative would require that new processes and controls be identified and established so as to avoid material control failures.

## Purpose

A key component of the IFRS 9 program is designing and implementing effective governance and controls in order to:

- 1) achieve the compliance with the IFRS 9 Standard; and
- 2) mitigate related risks, including but not limited to reputational risk, regulatory compliance risk, operational risk, credit risk and financial reporting risk.

## Principles

An effective IFRS 9 governance and control framework can be established based on the following principles:

- I. The Framework should be put in place before, during and after the IFRS 9 transition;
- II. The Framework should take account of views from across the three lines of defense to achieve the goals;

- III. The Framework should cover the end-to-end IFRS 9 processes, from selection of methodologies, data input and assumptions, processing and modelling, output review, regular monitoring, to approval and reporting;
- IV. The Framework should cover the governance of the enterprise-wide program as well as of individual components;
- V. The Framework should enable regular maintenance and update of the IFRS 9 program.

### An Example of New Control Chart

The chart below contains example new controls that are related to the IFRS 9 impairment assessment. It was developed to illustrate how the principles stated above can be carried out, and it is by no means exhaustive.

Control Name	Control Description	Control Frequency
<b>Overall Governance</b>		
<b>Allowance Policy</b>	The Allowance Policy is subject to annual approval by the Audit Committee and the Board of Directors, or more frequently if required. The IFRS 9 Committee is responsible for recommending any material changes to this policy to the Board as needed.	Annual
<b>Review of Credit Risk Management</b>	Periodically, independent reviews of the credit risk management processes as they relate to the ECL are conducted to ensure that weaknesses and inefficiencies are identified and addressed on a timely basis.	Periodic

**Design and Input**

<b>Probabilities of Macro Scenarios</b>	On a quarterly basis, the Economics group reviews, updates and documents the macroeconomic factors used in determining the probabilities of macroeconomic scenarios to ensure their validity.	Quarterly
<b>Segmentation Monitoring</b>	On a quarterly basis, the Risk Management group reviews in-scope portfolio segmentation for appropriateness. If borrower credit characteristics change such that segments are no longer established on the basis of shared credit risk characteristics, the Risk Management group will evaluate if segmentation should be re-conducted and if credit risk parameter models should be re-calibrated to revised segments.	Quarterly
<b>Macroeconomic Factors Monitoring</b>	For quarterly IFRS 9 reporting, the Economics group updates and documents macroeconomic factors, and the Risk Management group analyzes the impact of change on ECL on a quarterly basis to ensure that accurate macroeconomic factor input is used in ECL estimation.	Quarterly
<b>Beacon Score Refresh</b>	Retail Credit business unit obtains Beacon score refresh and conduct score analysis (e.g., comparison of past and current scores, impact analysis on risk ratings) on a quarterly basis. The analysis results are communicated to Risk Management and saved on line to ensure that borrower's creditworthiness as reflected in Beacon score is captured on a timely basis.	Quarterly
<b>Beacon Score Monitoring</b>	Risk Management reviews Beacon Score Analysis results from Retail Credit business units, and performs additional analysis for ECL measurement purposes to ensure that appropriate staging analysis is performed on a timely basis.	Quarterly
<b>Risk Rating Update</b>	When a change in risk rating is supported by change in credit risk characteristics, business units will recommend a change of risk rating. The change will be reviewed by VP of business units and submitted to the Credit Risk Committee for review and approval.	Ad hoc
<b>Risk Rating Review</b>	On a periodic basis, lending business units performs a formal review of lending exposures to which credit risk ratings are assigned to reasonably assure that those risk ratings are accurate and up to date.	Periodic
<b>Risk Rating Monitoring</b>	Risk Management reviews risk rating status from business units, and performs additional analysis for ECL measurement purposes to ensure that appropriate staging analysis is performed on a timely basis.	Quarterly
<b>Inclusion of Historical Data</b>	On an annual basis, Risk Management reviews an additional year of historical data, including but not limited to internal credit data and loss data as well as external economic data and benchmarking data, and incorporates relevant data into the ECL models. Such review and inclusion of available historical data is to ensure that all relevant and available information is considered in the ECL estimate.	Annual
<b>Review of Overlay</b>	On a quarterly basis, Risk Management and Finance work together to review management overlays (including both temporary and long-term overlays) and associated amount, to account for weaknesses/limitations in the ECL models. The results will be presented to the Executive Committee and the Board for review and approval.	Quarterly

### Operation and Monitoring

<b>Automation of ECL Calculation</b>	IT, Risk Management and Finance work together to automate quarterly ECL calculation processes as much as possible to avoid undue cost and effort and ensure accuracy.	Ad hoc
<b>IT General Admin</b>	The ECL models are password-protected and only authorized personnel have access to them.	Ad hoc
<b>Criteria of Material Change</b>	In the Allowance Policy, the process/criteria used to determine the materiality of changes to the ECL methodology and level are clearly described to ensure that material changes are communicated to all stakeholders in a timely manner.	Ad hoc
<b>Change Management</b>	Any material changes to IFRS 9 methodologies and/or models are documented and submitted to the IFRS 9 Committee and the Board for review and approval. If approved, the effect of changes is effectively disclosed by Finance.	Ad hoc
<b>Independent Model Review</b>	An independent review of the ECL models/methodologies is conducted on a periodic basis by qualified personnel to ensure that the ECL models perform as intended. This may involve Internal Audit or third-party consultant.	Annual

### Output Review

<b>Review of ECL Results</b>	On a quarterly basis, ECL results are prepared by Risk Management and reviewed by the Executive Committee for reasonableness to ensure that at minimum, the following changes in the Company's strategy or approach are reflected in the ECL results: - relaxation in the underwriting standards; - increasing sales of higher risk products or products with less collateral or less robust risk mitigation; - new distribution methods, or increased distribution through channels that result in higher losses.	Quarterly
<b>Backtesting</b>	Risk Management back-tests ECL results on a periodic basis to assess the reasonability of the ECL models.	Periodic

### Leveraging Available Information

To ensure completeness, a draft of the Framework could be benchmarked to the following information:

- Regulator's IFRS 9 self-assessment templates;
- Consulting firm's survey on IFRS 9; and
- Internal/external auditor's expectation of governance and controls.