

EBA/OP/2017/02

06 March 2017

Opinion of the European Banking Authority on transitional arrangements and credit risk adjustments due to the introduction of IFRS 9

Introduction and legal basis

On 22 November 2016, International Financial Reporting Standard 9, *Financial Instruments* (IFRS 9), was adopted in the EU¹ to replace the previous accounting standard International Accounting Standard 39, *Financial Instruments: Recognition and Measurement* (IAS 39). The EBA welcomed this change, which marks a move from an incurred loss model under IAS 39 to an expected credit losses (ECL) model under IFRS 9, as well as the timely adoption of IFRS 9 in the EU.²

On 30 September 2016, the European Parliament issued a resolution for the adoption for IFRS 9,³ calling for an examination of the possibility of introducing a phase-in regime for the impairment requirements of IFRS 9 of either three years or such duration until an adequate international solution is put in place, to avoid any sudden unwarranted impact on institutions' capital ratios and lending. On 23 November 2016, the European Commission, as part of its CRR II/CRD V proposals, made certain suggestions on transitional arrangements to mitigate the effect of the introduction of IFRS 9 on CET1 capital (CET1) resulting from the impairment requirements of IFRS 9.⁴

¹ http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=uriserv:OJ.L_.2016.323.01.0001.01.ENG&toc=OJ:L:2016:323:TOC

² See the EBA's advice to the European Financial Reporting Advisory Group (EFRAG) on the endorsement of this standard: <http://www.eba.europa.eu/documents/10180/943157/Letter+to+EFRAG+Board+on+IFRS+9+endorsement.pdf>. IFRS 9 is, overall, an improvement over IAS 39 in terms of accounting for financial instruments by institutions. The changes in credit loss provisioning should contribute to addressing the G20's concerns about the issue of 'too little, too late' in the recognition of credit losses, as well as improving the accounting recognition of loan loss provisions by incorporating a broader range of credit information. IFRS 9 is, therefore, expected to address some banking prudential concerns and contribute to financial stability in the EU.

³ <http://www.europarl.europa.eu/sides/getDoc.do?pubRef=-//EP//TEXT+MOTION+B8-2016-1060+0+DOC+XML+V0//EN>

⁴ <http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=COM:2016:0850:FIN>

The EBA has performed a first assessment of the potential effects of the introduction of IFRS 9⁵ on institutions' capital, and taking into account the views of the European Parliament and the Commission is now contributing to the ongoing discussion regarding potential transitional arrangements. Further, in response to calls from some stakeholders, this opinion also includes the EBA's views on the interaction of IFRS 9 with Commission Delegated Regulation (EU) No 183/2014 (RTS on Credit Risk Adjustments).⁶

This opinion is addressed to the European Commission, the European Parliament, the Council of the EU and competent authorities in the Union.

The EBA's competence to deliver an opinion is based on Article 34(1) and Article 29(1)(a) of Regulation (EU) No 1093/2010,⁷ as IFRS 9 and its interaction with prudential requirements relates to the EBA's area of competence.

In accordance with Article 14(5) of the Rules of Procedure of the Board of Supervisors,⁸ the Board of Supervisors has adopted this opinion.

Comments/proposals

a. Transitional arrangements

1. The Commission has introduced into the CRR review a proposal for transitional arrangements to lessen the impact of IFRS 9 on capital ratios. In line with the EBA report on IFRS 9, the EBA considered the mechanics of possible transitional arrangements, taking as the basis for the discussion the Commission's proposal, as well as the relevant discussions at international level (e.g. within the Basel Committee of Banking Supervision 'BCBS').⁹
2. The following observations can be made with regard to the Commission's proposal:
 - It provides the option for institutions to apply the transitional arrangements: it is not up to competent authorities to decide whether they should be applied.

⁵ See the first EBA impact assessment of the introduction of IFRS 9: <https://www.eba.europa.eu/-/eba-provides-its-views-on-the-implementation-of-ifs-9-and-its-impact-on-banks-across-the-eu>. The second EBA impact assessment is currently ongoing; the results of that assessment are expected to feed into shaping the EBA's final views on the need for transitional arrangements in this area.

⁶ Commission Delegated Regulation (EU) No 183/2014 of 20 December 2013, supplementing Regulation (EU) No 575/2013 of the European Parliament and of the Council on prudential requirements for credit institutions and investment firms, with regard to regulatory technical standards for specifying the calculation of specific and general credit risk adjustments (OJ L 57, 27.2.2014, p. 3).

⁷ Regulation (EU) No 1093/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Banking Authority) amending Decision No 716/2009/EC and repealing Commission Decision 2009/78/EC (OJ L 331, 15.12.2010, p. 12).

⁸ Decision adopting the Rules of Procedure of the European Banking Authority Board of Supervisors of 27 November 2014 (EBA/DC/2011/01 Rev4).

⁹ <https://www.bis.org/press/p161011.htm>

- It allows institutions to add back to CET1 the amount of loss allowances that are classified in stages 1 and 2 under IFRS 9 during each year (each year a different factor is applied). However, the following observations can be made:
 - i. The factors proposed by the Commission would result in the full neutralisation of any impact on CET1 arising from the application of IFRS 9 (due to impairment) during the first year of the transitional arrangements.
 - ii. The period proposed by the Commission for the transitional arrangements is five years.
 - iii. Under IAS 39, institutions recognise losses for impaired assets (which most likely would be close to stage 3 under IFRS 9) and also set aside provisions for incurred but not reported losses (IBNR). This means that some of the amount of stage 1 and stage 2 provisions is already recognised under IAS 39. Therefore, if the total amount of stage 1 and stage 2 provisions is neutralised, this will result in a positive adjustment in CET1 due to the application of IFRS 9 (as a result of the impairment requirements).
 - iv. The aim of the Commission's proposal is to cover provisions in stages 1 and 2; however, the proposal refers to paragraph 5.5.3 of IFRS 9, which is interpreted as covering exposures classified in stage 3 as well.
 - v. The transitional arrangements would apply only to the impairment requirements of IFRS 9 and would not take into account the full impact of IFRS 9.
 - vi. They would not take into account the actual impact on prudential metrics either.
 - vii. Some debt instruments previously classified in the available for sale category under IAS 39 and then classified in the fair value through other comprehensive income category under IFRS 9 would benefit from transitional arrangements without any new impact on CET1.¹⁰
- It is a 'dynamic', as opposed to a 'static', transitional approach, as the adjustment in CET1 takes into consideration the amount of stage 1 and stage 2 provisions in each reporting period.

¹⁰ For instance, for a bond acquired for EUR 100, whose fair value decreases to EUR 90 at the end of the reporting period, in accordance with IAS 39 the change in fair value will be recognised in other comprehensive income (if not impaired) and the impact on CET1 will be EUR 10. Under IFRS 9, the impact on CET1 would be the same; however, as IFRS 9 requires that part of the change in fair value is recognised as an impairment loss (through profit or loss), transitional adjustments would be applied when in fact there had not been any additional impact on CET1 due to IFRS 9.

- For institutions applying the internal ratings based (IRB) approach to measure credit risk, the proposal does not consider whether there is an excess or shortfall of accounting provisions in comparison with regulatory expected losses.

Reasons for the introduction of transitional arrangements

3. In the EBA's view, transitional arrangements may be introduced for various reasons, which are as follows:

- **One-off impact:** the initial impact of IFRS 9 could be significant for some institutions in some Union Member States, depending on several aspects, as described in the EBA report on its first impact assessment of IFRS 9 and to be further investigated in the ongoing second EBA impact assessment of IFRS 9. Institutions are not yet able to estimate with reasonable certainty the initial impact on 1 January 2018 when IFRS 9 comes into effect, considering also that, all other elements being equal, the economic conditions could be different when IFRS 9 is initially applied.
- **Interaction with the regulatory framework:** there is ongoing work in the regulatory community on understanding the interaction of accounting with regulatory provisions in the context of IFRS 9 and on assessing the need to revise the regulatory framework to ensure that prudential objectives are met without unintended consequences.
- **Level playing field between SA and IRB institutions:** institutions using the standardised approach (SA) to measure credit risk would experience a negative impact on CET1 due to the increased provisions under IFRS 9 and would not be able to recognise any part of their accounting provisions in Tier 2 capital if all provisions were considered specific (see also the relevant section in this opinion on credit risk adjustments), while institutions using the IRB approach to measure credit risk might have regulatory expected losses exceeding accounting provisions under IAS 39, which could reduce the negative impact on CET1 (or even result in no impact) under IFRS 9, and they would be able to recognise in their Tier 2 capital any excess accounting provisions.

4. In addition to helping to address the issues described above, the transitional arrangements should also strike the right balance between prudence, simplicity, comparability and developing an approach that can be implemented by institutions and understood by regulators and other stakeholders.

5. The EBA acknowledges that under IFRS 9 the level of provisions could change over time and in particular during downturns – all other elements being equal – because there will be more exposures from stage 1 (for which 12 months' expected losses are calculated) migrating to stage 2 (for which lifetime expected losses are calculated). This is a result of the forward-looking nature of IFRS 9, which should also help in the early recognition of losses. The EBA

believes that it is not the objective of transitional arrangements to account for potential change in provisions, which may occur also after the end of the transitional period.

6. Taking the above into account, the EBA proposes some elements that, in its view, should be part of the transitional arrangements.

Static or dynamic approach

7. The Commission has proposed a dynamic approach that will lead to institutions adding back to CET1 the amount of ECL in stages 1 and 2 for each year (after multiplying this part of the ECL for each year by a different factor each year).¹¹ This approach does not require the estimation of provisions under IAS 39 after 1 January 2018 and it aims to address the main impact of IFRS 9, which results from the impairment requirements, particularly those relating to stages 1 and 2.
8. This approach considers the evolution of institutions' balance sheets, including changes in the volume of loans and in the amount of provisions after the initial application of IFRS 9. For instance, if there were an increase in provisions due to a deterioration of economic conditions, the dynamic approach would reflect this increase by adjusting the amount within the scope of application of transitional arrangements.
9. However, as currently drafted, the Commission's proposal is not sufficiently prudent, as it may allow provisions that would exist under IAS 39 to be subject to the transitional arrangements and therefore added back to CET1. For example, the following should be considered:
 - ECL in stages 1 and 2 under IFRS 9 will also include the IAS 39 IBNR provisions, which will be added back to CET1 if IBNR provisions are in the scope of application of transitional arrangements.

¹¹ Article 473a of the Introduction of IFRS 9:

'1. Until [date of application of this Article + 5 years] institutions that prepare their accounts in conformity with the international accounting standards adopted in accordance with the procedure laid down in Article 6(2) of Regulation (EC) No 1606/2002 may add to their Common Equity Tier 1 capital the amount calculated in accordance with paragraph 2 of this Article multiplied by the applicable factor laid down in paragraph 3.

2. The amount referred to in paragraph 1 shall be calculated as the twelve month expected credit losses determined in accordance with paragraph 5.5.5 of Commission 262 regulation (EU) No / 2016 (32) and the amount of the loss allowance for financial instruments equal to the lifetime expected losses determined in accordance with paragraph 5.5.3 of Commission Regulation (EU) No / 2016 (1).

3. In calculating the amount referred to in paragraph 1, the following factors apply: (a) 1 in the period from [date of application of this Article] to [date of application of this Article + 1 year – 1 day]; (b) 0,8 in the period from [date of application of this Article + 1 year] to [date of application of this Article + 2 years – 1 day]; (c) 0,6 in the period from [date of application of this Article + 2 years] to [date of application of this Article + 3 years – 1 day]; (d) 0,4 in the period from [date of application of this Article + 3 years] to [date of application of this Article + 4 years – 1 day]; (e) 0,2 in the period from [date of application of this Article + 4 years] to [date of application of this Article + 5 years – 1 day].

Institutions shall include in their own funds disclosures the amount added to their Common Equity Tier 1 capital in accordance with paragraph 1.'

- The references to IFRS 9 in the Commission's proposal as it currently stands could be interpreted as allowing institutions to add back ECL in stage 3 under IFRS 9 (which are deemed similar to the current IAS 39 provisions) and therefore, it would result in the neutralisation of the existing IAS 39 incurred loss provisions.
 - The Commission's proposal does not consider that for institutions using the IRB approach to measure credit risk there may be an excess or shortfall of accounting ECL in comparison with regulatory expected losses. For instance, if an institution were in a shortfall situation under IAS 39 and as a result of IFRS 9 was still in shortfall (despite an increase in provisions under IFRS 9), there would be no impact on CET1 due to the application of the impairment requirements of IFRS 9. However, if an institution decided to apply the transitional arrangements, it would be able to add provisions back to CET1 and therefore have a positive impact due to IFRS 9.
10. Therefore, to address these issues, greater clarity is needed in the Commission's current proposal, as are legal provisions on how to avoid increases in own funds due to adding back the impact of provisions that would otherwise exist under IAS 39, but without requiring institutions to calculate IAS 39 provisions during the transitional period, as this would be operationally burdensome.
11. A static approach would be simpler than a dynamic approach, as under a static approach the initial one-off impact could be clearly identified and could be calculated only once (on the initial application of IFRS 9) and amortised over a number of years, instead of institutions having to recalculate the amount of the adjustment over time and make additional adjustments to avoid unintended adding back of IAS 39 provisions to own funds. This is notwithstanding the fact that any static approach has the drawback of potentially phasing in an impact that might evolve during the transitional period, as the portfolio or the estimation of provisions might change after the application of IFRS 9.

The EBA's views

12. **Overall, a dynamic approach would add more complexity to the already complicated process of explaining the new IFRS 9 concepts and their impact on CET1 to stakeholders. Taking into consideration that both approaches have limitations, the EBA believes that a static approach achieves a better balance between addressing the rationale of the transitional arrangements and at the same time being a prudent (as it avoids adding back IAS 39 provisions) and simple approach that can be applied by institutions and understood by stakeholders.**
13. **If the dynamic approach were to be retained, stringent disclosure requirements would be even more important to ensure a harmonised implementation and a clear understanding of the different impacts of IFRS 9 for all stakeholders, given the increased complexity inherent in this approach.**

Scope: in relation to the impact of the impairment requirements only or of the entire IFRS 9

14. The Commission's proposal refers only to the impact of the impairment requirements of IFRS 9 (as in the BCBS proposals). This is consistent with the indications provided in the first EBA impact assessment of IFRS 9 and through related outreach activities that the main impact of IFRS 9 will result from the impairment requirements. The proposal may also allow the application of a dynamic approach in a cost-efficient and less complex manner.
15. The application of transitional arrangements only in relation to the impairment requirements of IFRS 9 is mainly justified by the fact that the main impact of IFRS 9 is expected to come from the new impairment requirements; these are the most relevant change resulting from IFRS 9 and therefore the transitional arrangements should focus on this area. If a dynamic approach is preferred to a static approach, it could be operational only if the transitional arrangements addressed only the impairment requirements.
16. However, the EBA believes that it should also be considered whether transitional arrangements should apply to IFRS 9 as a whole and not only to the impairment requirements of IFRS 9. IFRS 9 is a new standard and includes changes in areas other than those related to impairment. Therefore, focusing on the impact only of the impairment requirements would not meet the objective of addressing the one-off impacts of the other requirements of IFRS 9 (such as from classification and measurement), which may be significant for some institutions (although they are estimated to be relevant to a limited number of institutions). In addition, some institutions may experience a positive impact on CET1 as a result of the other requirements of IFRS 9. If transitional arrangements were to apply only in relation to the impact of the impairment requirements of IFRS 9, this could lead in some cases to an increase in CET1 due to IFRS 9 (e.g. if the positive impact of classification and measurement were greater than the negative impact of impairment).
17. It should also be mentioned that the application of transitional arrangements in relation to the impact of all IFRS 9 requirements together with the application of a dynamic approach would require the calculation of the IAS 39 figures every year (as the impact of classification and measurement and hedge accounting requirements under IAS 39 and IFRS 9 would also need to be considered every year). As explained above, although it would be a prudent policy, it would be operationally burdensome and difficult for institutions to implement and stakeholders to understand.
18. In addition to IFRS 9, other amendments to international accounting standards become effective on 1 January 2018, for example changes to IFRS 2 and IFRS 15. The effects of these other changes would have to be excluded from the transitional arrangements, possibly increasing the complexity of the approach.

The EBA's views

19. **Having said that, the EBA believes that both approaches, considering either the impact of the impairment requirements only or of all the requirements of IFRS 9, have limitations. Depending on the final transitional arrangements to be agreed, it will be necessary to strike an appropriate balance between prudence and simplicity.**

Neutralisation of IFRS 9 impact

20. Applying the Commission's proposal would result in the full neutralisation of any impact on CET1 arising from the application of IFRS 9 (due to impairment) during the first year of the transitional arrangements. However, it should be reiterated that the supervisory community has welcomed the introduction of IFRS 9 to the EU and expects that institutions will be sufficiently prepared for the initial application of IFRS 9, given that this change has been expected for some time.

The EBA's views

21. **Therefore, the EBA believes that the effects of the application of IFRS 9 should apply from the initial application of IFRS 9 on 1 January 2018 and onwards, and that there should not be full neutralisation of the new standard's impact during the first year or any of the years following that.**

Duration of the transitional arrangements

22. In the Commission's proposal, the proposed period of the transitional arrangements is five years.
23. Various aspects should be considered when setting the period:
- i. the significance of the impact of IFRS 9 on own funds;
 - ii. a transitional period of four years is used in other transitional provisions of the CRR;
 - iii. the effective date of the ECL model in US Generally Accepted Accounting Principles (US GAAP) will be two years after¹² IFRS 9 is effectively applied;
 - iv. the BCBS consultative document¹³ is based on the working assumption that the period allowed for transition would be between three and five years;
 - v. the BCBS has not yet reached a conclusion on what should be the permanent interaction between ECL accounting and the prudential regime, and therefore a

¹² 1 January 2020 for certain institutions that are public companies and 2021 for all other institutions, with early application permitted for all institutions in 2019.

¹³ <https://www.bis.org/bcbs/publ/d386.htm>

longer transitional period in the EU could allow the results of this revision to be taken into account;

- vi. extended transitional arrangements may create some legal uncertainty in the sense that they may be effective in the first few years but, after that, the market (e.g. financial analysts and rating agencies) usually requires the full impact to be recognised for comparability purposes. On the other hand, smaller institutions generally experience lower pressure from the market.

The EBA's views

- 24. Taking into consideration that the EBA's preference would be not to fully neutralise the impact in the first year, as explained above, and bearing in mind the results of the first EBA impact assessment of IFRS 9, the EBA believes that a phased-in transitional period of four years would be appropriate (80% in 2018, 60% in 2019; 40% in 2020; 20% in 2021 and 0% beyond that).**

Mandatory regime or institution's decision

25. The Commission's proposal provides the option for institutions to apply the transitional arrangements. The EBA believes that a decision on the application of the transitional arrangements made by each institution provides institutions with the flexibility to decide depending on the impact that IFRS 9 might have and could also result in their deciding not to apply transitional arrangements if the benefits were less than the costs of applying them (e.g. if the impact of IFRS 9 were small). On the other hand, it would also lead to an inconsistent transition to IFRS 9 in the EU internal market, in addition to the overall delay in the transition to IFRS 9.
26. Mandatory application by all institutions would ensure maximum harmonisation and a consistent transition to IFRS 9 among EU institutions, and it would also address any unintended discrimination against institutions ('the stigma effect'). However, this would mean that all institutions would have to apply the arrangements. It is arguable whether this would be appropriate, as an institution might prefer to apply IFRS 9 in full if it so wishes.

The EBA's views

- 27. Taking into account all of the above, the EBA believes that the application of transitional arrangements should be a baseline regulatory requirement (mandatory application), while allowing the option for institutions to recognise, if they so wish, the full impact of IFRS 9 on own funds on 1 January 2018 (without transitional arrangements). However, it should not be possible for institutions to apply transitional arrangements later if they initially decided not to apply them. In addition, it will be of the utmost importance that institutions provide disclosures on the use of this option.**

Other aspects to be considered in designing transitional arrangements

28. **Date of implementation:** the Commission's proposal refers to first application expected in 2019, whereas IFRS 9 enters into force on 1 January 2018. Although the EBA understands that this is because the Commission's proposal is included in the wider CRR review, it is necessary that the proposal be finalised in a timely manner, before the implementation of IFRS 9, so that it is in place to address the impact of IFRS 9 from its introduction.
29. **National accounting frameworks:** another aspect to consider is that, to ensure a consistent transition to IFRS 9 among EU jurisdictions, the application of transitional arrangements should also be possible in those cases where Member States move from an incurred loss model to an expected loss model under national accounting frameworks. This should be clarified in the legal text of any transitional arrangements.
30. **Disclosures:** according to the Commission's proposal, those institutions that make use of the transitional arrangements must include in their own funds disclosures the amount added to CET1 as a result of the application of the transitional arrangements. In this regard, the EBA will assess how the application of transitional arrangements should be reported in the COREP templates and will collaborate with the Commission on the inclusion of this information in the Pillar 3 reports.
31. **Overall principle:** as there are complex technical issues to be considered in the application of transitional arrangements, as also outlined in the BCBS consultative document on the regulatory treatment of accounting provisions, the EBA believes that a clear principle should be included in the Commission's proposal to require that, where an ECL accounting provision in effect has not been deducted from CET1 because of the application of the transitional arrangements, it should not be considered in other prudential metrics.¹⁴

b. Specific and general provisions

32. For institutions applying the SA to measure capital requirements for credit risk, credit risk adjustments (CRAs)¹⁵ can be considered general (GCRAs) or specific (SCRAs). The criteria used to differentiate between SCRAs and GCRAs under the applicable accounting framework are established in the RTS on Credit Risk Adjustments. While both SCRAs and GCRAs have an impact on CET1, the difference is that GCRAs do not reduce the exposure value and are included in Tier 2 capital up to 1.25% of the institution's credit risk-weighted assets, while SCRAs reduce the exposure value and are not added back to any part of the regulatory capital.

¹⁴ Any deferred tax asset (DTA) arising from a temporary difference associated with such a non-deducted provision amount must be disregarded for regulatory purposes during the transitional period. Such provision amounts should not be included in Tier 2 capital, would not reduce the exposure amounts in the SA and would not reduce the total exposure measure in the leverage ratio.

¹⁵ According to Article 4(1)(95) of the CRR, 'credit risk adjustment' means the amount of specific and general loan loss provision for credit risks that has been recognised in the financial statements of the institution in accordance with the applicable accounting framework.

33. Under IAS 39 or national accounting standards, provisions are generally classified as SCRA^s.
34. However, as a result of the move from the incurred losses of IAS 39 to the expected losses of IFRS 9, which is more forward-looking than IAS 39, there may be different interpretations of whether provisions classified under IFRS 9 in stages 1 and 2 should be considered SCRA^s or GCRA^s according to the RTS.

Criteria for the classification of provisions as SCRA^s or GCRA^s

35. The RTS on Credit Risk Adjustments includes two criteria, both of which need to be fulfilled, for the recognition of GCRA^s,¹⁶ and in particular it requires that provisions are freely and fully available, as regards to timing and amount, to meet credit risk losses that have not yet materialised (paragraph 2(a) of Article 1). Under IFRS 9, provisions need to be allocated to individual exposures or groups of exposures, and therefore are not freely and fully available, as they are ascribed to these exposures. Therefore, the EBA considers that provisions under IFRS 9 should be considered SCRA^s.
36. It should also be noted that all provisions under IFRS 9 need to reflect an unbiased estimate of ECL on the existing portfolio. Therefore, all IFRS 9 provisions are already considered necessary to account for expected losses, and they do not function as a buffer to cover other losses that are currently not expected.
37. In addition, under the current accounting frameworks (IAS 39 or national accounting standards) provisions are generally considered SCRA^s for prudential purposes. The move to an expected loss model, which was welcomed by prudential regulators, should lead to a faithful representation of ECL, which implies that the depiction of those credit losses is neutral and free from bias (IFRS 9, BC5.86).

The EBA's views

38. **Taking into account all of the above, the EBA believes that all IFRS 9 provisions should be considered SCRA^s and that the current RTS on Credit Risk Adjustments should be read accordingly. One of the main reasons is that provisions under IFRS 9 will not be freely and fully available to meet losses that subsequently materialise, as these provisions are ascribed to particular assets, whether individual or grouped.**
39. While a revision of the RTS text could be desirable to make this explicit, the EBA considers that the current RTS text does not prevent this reading. It might be preferable at this point to instead postpone such an amendment of the RTS until there is further clarity on the issue following discussions at international level. Once there have been further regulatory

¹⁶ Paragraph 60 of Basel III defines general provisions as 'Provisions or loan-loss reserves held against future, presently unidentified losses are freely available to meet losses which subsequently materialise and therefore qualify for inclusion within Tier 2'. It states: 'Provisions ascribed to identified deterioration of particular assets or known liabilities, whether individual or grouped, should be excluded.'

developments on the interaction of IFRS 9 with existing prudential requirements, the RTS may be updated as necessary.

40. In addition, once IFRS 9 comes into effect, it is expected that institutions using the IRB approach to measure credit risk will recognise some IFRS 9 provisions in Tier 2 capital (as an increase under IFRS 9 in provisions exceeding regulatory expected losses seems more likely), while institutions using the SA to measure credit risk will not be able to recognise any provisions in Tier 2 capital (as all IFRS 9 provisions are considered SCRA). However, the transitional arrangements discussed above would help to address the initial impact of IFRS 9 on CET1 while the results of the work on the interaction of IFRS 9 with prudential requirements, in particular with regard to the calculation of regulatory own funds, were awaited.
41. The EBA participates in discussions at international level (e.g. with the BCBS) on longer-term considerations with regard to the impact of IFRS 9, and in particular the long-term approaches that could be adopted in relation to the interaction of regulatory expected losses and accounting expected losses and, inter alia, the capital treatment of excess provisions in the IRB approach. The EBA will reflect on similar discussions at EU level as well.

This opinion will be published on the EBA's website.

Done at London, 06 March 2017

[signed]

Andrea Enria

Chairperson
For the Board of Supervisors