8-26-2020

PRA statement on Covid-19: IFRS 9 and capital requirements – Guidance as Covid-19 specific payment deferrals come to an end

Bank of England/Central Bank of the United Kingdom: Prudential Regulation Authority (PRA)

PRA statement on Covid-19: IFRS 9 and capital requirements – Guidance as Covid-19 specific payment deferrals come to an end

This statement clarifies the PRA's approach to IFRS 9 and capital requirements in response to updated FCA guidance on retail mortgage payment deferrals.

Published on 26 August 2020

On 26 March and 4 June 2020 the PRA wrote to banks and building societies (firms) on the consistent and robust application of IFRS 9 and the regulatory capital requirements to Covid-19 related payment deferrals and on some other Covid-19 related matters. The PRA's guidance explained that, under the terms of the FCA's guidance then in place, Covid-19 related payment deferrals were being made widely available to borrowers requesting a deferral and were therefore not based on the individual financial circumstances of the borrower. As a result, they were not necessarily good indicators of significant increases in credit risk (SICR), credit impairments, or defaults.

The FCA has today published draft updated guidance for firms in relation to mortgage payment deferrals. That guidance explains that, at the end of the existing, widely available Covid-19 specific payment deferrals, if the borrowers involved are not able to resume payments in full immediately with all deferred sums either paid in full or capitalised, tailored forbearance arrangements provided in accordance with the draft updated guidance should be considered.

Such tailored forbearance arrangements are likely to be as good an indicator of SICR, credit impairments or defaults as forbearance was prior to the pandemic. Prior to Covid-19, loans subject to forbearance would not automatically have been treated as having experienced a SICR or become credit impaired or in default, and that will also be the case with tailored forbearance provided in accordance with the draft updated guidance. While in some cases the position will be clear-cut, in other cases a judgment will need to be made. The guidance in the PRA's June letter on a framework for making holistic assessments of loans subject to payment deferrals for indicators of SICR or credit impairment will be relevant when making that judgment.

The PRA's earlier guidance stating payment deferrals are not necessarily good indicators of SICR, credit impairments or defaults may however continue to be relevant to payment deferrals used outside of the UK, depending on the facts and circumstances involved (including the availability of the deferrals and the circumstances in which they are used). The earlier guidance on holistic assessments of loans also continues to be relevant where firms have limited data to assess the individual financial circumstances of the borrower.

The PRA's March and June letters address other matters and some of that guidance also continues to be relevant. In particular, the guidance in the March letter on the treatment of borrowers that breach covenants due to Covid-19, on IFRS 9 expected credit loss (ECL) model risk, and on the need for post-core ECL model adjustments continues to be relevant.

We consider the guidance in this statement to be consistent with IFRS and the EU Capital Requirements Regulation (CRR). However, it is the responsibility of firms to satisfy themselves that they have prepared their annual and interim financial reports in accordance with the applicable reporting frameworks and for auditors to reach their own audit or review conclusions about those reports. Similarly, it is for firms to ensure they comply with the requirements of CRR.

BANK OF ENGLAND