Association of British Insurers

IFRS 9 Financial Instruments

The ABI's response to the EFRAG's Assessments

1. The ABI is the voice of insurance, representing the general insurance, protection, investment and long-term savings industry. It was formed in 1985 to represent the whole of the industry and today has over 300 members, accounting for some 90% of premiums in the UK.

ABI comments

2. We welcome the opportunity to comment on the EFRAG's Assessments on IFRS 9 *Financial Instruments*.

3. We agree with the EFRAG's assessments that, on balance, IFRS 9 meets the technical criteria for endorsement and would be conducive to the European public good, but only if its mandatory effective date is temporarily deferred for insurers.

4. The technical assessment balance largely rests on IFRS 9 bringing improved loan loss provisioning for banks and better hedge accounting for other corporates, and we acknowledge the importance of these changes.

5. The impact on UK insurers is different. IFRS 9 brings little to help their accounting. Instead, there is some extra cost and some distortion of performance reporting. Their use of fair value through profit and loss accounting is made more difficult by the classification and measurement changes. The change in impairment approach makes reporting sense much more for banking loan books than for insurers' holdings of investment grade securities, and yet this is operationally relatively onerous. And the hedge accounting changes are currently largely irrelevant.

6. Nevertheless, we particularly welcome the EFRAG's support for deferral of IFRS 9's effective date for insurers that need also to apply the IASB's replacement for IFRS 4 at the same time. The draft adoption advice sets out well the distortions in performance reporting and the increase in operational costs that will arise otherwise from those insurers' implementation of the two IFRSs at different dates. We emphasise here:

   - multinational UK insurers would be affected directly in relation to their overseas operations in which accounting for insurance liabilities is on a cost basis under IFRS 4, and so there would be artificial volatility arising from accounting mismatches where financial assets are reclassified to fair value through profit and loss. Likewise, the extra costs may involve the wasteful temporary implementation of IFRS 9's impairment approach;

- all insurers may be affected by a reduction in confidence in the quality of insurers' reporting arising from accounting mismatches and artificial volatility in insurers' results generally. UK and other insurers are looking to IFRS 4's replacement to improve a market perception of 'black box' accounting by insurers, and yet premature adoption of IFRS 9 would not be a step in that direction but a step backwards.

7. We recognise that operationalising IFRS 9's deferral for insurers is not without challenges. But we emphasise that there is no easy solution to the difficulties that arise from the two IFRSs not having aligned effective dates, and we consider that targeted deferral is the the best approach. Further:

   - scope: We suggest that the relevant entities be identified primarily by reference to regulation – that is, entities authorised to issue insurance contracts. These would catch most insurance contracts issued in the UK and probably in Europe at least;

   - conglomerates: We consider that segmental reporting can be applied by groups that need deferral for their insurance business, to explain to users the effects of using different accounting policies for different business models within a diverse group. This can be supplemented by other disclosures, eg for intra-group transfers of financial instruments (which we think are relatively uncommon in practice). Anti-abuse measures could be included in the transitional measures if necessary. We stress, however, that conglomerates should also have the option not to defer IFRS 9 application, based on their cost/benefit assessment;

   - end-date to deferral: It would not be appropriate to fix a firm date in advance of IFRS 4's replacement being further developed than it is now. We suggest, however, that there should be a clear commitment to review the positon in two or three years' time. Such a review should also consider the need for transitional relief in addition to that provided for in IFRS 9 as it currently stands, in the light of work on other issues by the IASB's transition resource group.

8. We note that some commentators on this proposal have objected that IFRS 4 already has sufficient flexibility to make IFRS 9 deferral unnecessary. We do not agree. Any half-way house, such as adopting a Solvency II basis of accounting for liabilities or use of IFRS 4's 'shadow-accounting', will not reduce volatility in reporting sufficiently and would be difficult to explain to users, and this would probably increase the cost/operation burden still further. Solvency II is European specific, it would not produce insurance liability values

that are consistent with those likely to arise from the IASB's IFRS 4 replacement project, and Solvency II provides nothing to guide accounting for insurers' profit. IFRS 4's 'shadow accounting' is limited and efforts to expand that may not achieve enough in reducing mismatches and may increase rather than reduce complexity both for users and preparers.

9. Lastly, we support the EFRAG's call for the IASB to effect the deferral, with EU specific delay being very much a second-best option because it does not help multinational groups enough, and especially those that also have non-European listings where the deferral would not apply. Further, we note that insurers outside Europe share the same concerns and are also calling for the IASB to defer IFRS 9 for insurers.

10. Our answers to the EFRAG's questions are given in the attachment to this letter.

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