IFRS™

STAFF PAPER

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IASB Meeting

Project	**Insurance Contracts**		
Paper topic	Responding to the external editorial review		

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This paper has been prepared for discussion at a public meeting of the International Accounting Standards Board (the Board) and does not represent the views of the Board or any individual member of the Board. Comments on the application of IFRS® Standards do not purport to set out acceptable or unacceptable application of IFRS Standards. Technical decisions are made in public and reported in IASB® Update.

At the 22 February 2017 Board meeting, staff noted editorial errors to items B6, B9 and B14 in the original staff paper posted on 13 February 2017. The editorial corrections are highlighted in mark-up.

Purpose of this paper

1. In February 2016, the International Accounting Standards Board (the Board) confirmed that it had completed all the necessary due process steps on the Insurance Contracts project and instructed the staff to commence the drafting process for IFRS 17 *Insurance Contracts*. The staff is now nearing the end of the drafting process, and has recently completed an external editorial review of a draft of IFRS 17. This paper summarises the findings of that review and identifies issues that the staff proposes to address.

2. The staff plans to discuss the issues in this paper with the Board on an exceptions basis, ie the staff will ask only a general question as to whether the Board agrees with the staff's proposals. We will discuss an issue only if requested to do so by a Board member. The staff asks for advance notification from Board members if they intend to discuss any issues to assist in meeting planning.

Question for Board members: Drafting improvements and minor issues
Does the Board agree with the staff proposals for resolving the issues arising from the external editorial review?

3. Appendix A describes issues in which external reviewers have indicated their disagreement with Board decisions. The staff does not propose to revisit those items.

External editorial review: process, objectives and participant selection

4. In December 2016, the Board asked a selected group of reviewers to perform an external editorial review of a draft of IFRS 17. The objective of the external editorial review is to assess whether the draft clearly describes and explains the decisions made by the Board and to confirm that there are no internal inconsistencies or inconsistencies with other Standards. Reviewers were not asked whether they agreed or disagreed with the Board's decisions.

5. The Due Process Handbook states in paragraph 3.31 that 'the nature of the external review, such as who is asked to review the draft and whether the draft is also made publicly available, is at the discretion of the IASB'. Consistent with our general practices, we invited national standard setters, regulators and audit firms with specialist abilities in reviewing technical accounting requirements to participate in this detailed editorial review. In addition, we expanded on the range of usual reviewers by asking some that reviewed the draft for topic-based testing to review again. These additional reviewers were selected based on geographic coverage. We received comments from 25 individuals responding to the external editorial review.

6. The external editorial review supplemented the commentators review conducted during July-September 2016 and the Board's first review of the draft Standard. These two external reviews ensured that we obtained external input to supplement our internal finalisation processes and exceeded the minimum requirements of the *Due Process Handbook*.

7. The Board performed its second review of the draft Standard concurrently with the external editorial review.

Main findings

8. As expected, the comments received on the external editorial review were very specific. There were some comments that were consistently raised by reviewers. However, in general, there was little overlap in the comments. There were significantly fewer comments received than in the previous review and those reviewing for the second time commented on the improvements made in the revised draft.

9. The following tables list (in the order of occurrence in draft IFRS 17):

    (a) Table A: Issues raised by both the Board members and the external reviewers that have resulted in the staff proposing a change to the Standard; and

    (b) Table B: Clarifications to the Standard that the staff propose in the light of comments received on the draft.

10. This paper includes extracts from the staff's working draft. This drafting has been provided to aid in the Board's consideration of the issue. The drafting has yet to be reviewed by the Board and is subject to further editorial changes.

11. The tables do not list all the comments received or all the drafting improvements that were made in response to the comments. Instead it highlights those that are more significant. The full list of comments received is available to Board members on the internal website.

Changes to the Standard

12. The following table lists issues raised by Board members and the external reviewers that have resulted in the staff proposing a change to the Standard, together with the staff's recommendations for action.

Issue #	Topic	Issue	Proposed action
A1	Contractual service margin	This issue is discussed in Agenda Paper 2A *Changes to the contractual service margin.*	
A2	Level of aggregation: Regulatory-affected pricing	This issue is discussed in Agenda Paper 2B *Narrow exemption for the grouping of regulatory-affected pricing of insurance contracts*.	
A3	Mutualisation	Some reviewers asked for further guidance on how mutualisation affects: (a) the level of aggregation. In particular, they asked how the "no more than one year apart" grouping	The staff proposes that IFRS 17 include guidance on how to account for insurance contracts with payments made to or received from other insurance contracts as a result of specific contractual requirements, and the Basis for Conclusions will clarify how these requirements

Issue #	Topic	Issue	Proposed action
		requirement applies where there is a mutualisation of benefits, including on an intergenerational basis; (b) the measurement of insurance contracts, including the measurement model to be applied. Some reviewers asked that the Standard define mutualisation.	interact with the requirement that only contracts issued within one year may be grouped. Appendix B sets out wording to be included in the Standard (see B67-B71 and B103). The staff note that the term mutualisation is used to describe divergent existing accounting practices, some of which in substance result in economic losses arising from some insurance contracts being offset by economic gains arising from other contracts, even in the absence of any contractual link between those contracts. The staff thinks that using the term 'mutualisation' in the Standard would be unhelpful because of the different ways in which the term is understood.
A4	Premium allocation approach: Investment	Some reviewers disagreed with the requirement that an entity may not apply the premium allocation approach to groups of contracts with an investment component, noting that the existence of an investment component	The staff proposes to delete the requirement that an entity may not apply the premium allocation approach to contracts with an investment component. Instead the Standard will require revenue arising under the premium

Issue #	Topic	Issue	Proposed action
	components	that is closely related to the insurance contract would not affect the measurement of the insurance contract.	allocation approach to exclude any investment component.
A5	Variable fee approach: Loss component	Some reviewers noted that changes in the entity's share of underlying items can make contracts with direct participation features onerous, and asked for guidance on how to account for such changes.	The staff propose to clarify that the adjustment to the contractual service margin arising from the entity's share of the change in the fair value of the underlying items should exclude: (a) the entity's share of a decrease in the fair value of the underlying items that exceeds the carrying amount of the contractual service margin, giving rise to a loss; and (b) the entity's share of an increase in the fair value of the underlying items that reverses the amount in (a). Any loss (or reversal of the loss) will be recognised as part of the insurance services result, not as insurance finance income or expenses.

Issue #	Topic	Issue	Proposed action
A6	Contract boundary: Removing inconsistencies	Some reviewers questioned why the contract boundary requirements had been amended from the 2013 Exposure Draft. Draft IFRS 17 now requires that a substantive obligation to provide coverage or other services ends when the entity can set a price or level of benefits that fully reflects the risks of the particular policyholder and the pricing of the premiums for coverage up to the date when the risks are reassessed does not take into account the risks that relate to future periods. This is now consistent for the requirement for evaluating when there is a substantive obligation to provide coverage or other services at a portfolio level. In the 2013 Exposure Draft, for individual contracts, there was no requirement that the pricing of the premiums for coverage up to the date when the risks are reassessed should not take into account the risks that	The reason for this change was to make consistent the requirement for assessing when there is a substantive obligation to provide coverage or other services to a particular policyholder or to a portfolio of insurance contracts. The staff thinks the effect of pricing that takes into account risks that relate to future periods apply equally when the entity assesses if it can set a price that fully reflects risks of a particular policyholder as to when the entity assesses if it can set a price that fully reflects the risk of a portfolio of insurance contracts.

Issue #	Topic	Issue	Proposed action
		relate to future periods.	
A7	Contract boundary: Frequency of assessing the boundary	Some reviewers asked for clarification on whether entities should reassess the contract boundary at each reporting period.	The staff propose to clarify that an entity should reassess the boundary of an insurance contract in each reporting period in the coverage period of the contract, to include the effect of changes in circumstances on the entity's substantive rights and obligations.
A8	Contract combination and separation	The 2013 ED included a paragraph on contract combination that some reviewers were concerned would require entities to combine contracts inappropriately. The staff had proposed replacing that paragraph with the more principles-based statement from the Conceptual Framework ED that addresses both contract combination and separation. However, some reviewers were concerned that the on contract combination and separation would: (a) require entities to combine contracts	The staff propose that IFRS 17 remains silent on contract separation and to retain only the principles-level paragraph on contract combination that is consistent with the principles in the Conceptual Framework, as follows: 10. A set or series of insurance contracts may achieve, or be designed to achieve, an overall commercial effect. In order to report the substance of such contracts, it may be necessary to treat the set or series of contracts as a whole. For example, if the rights or obligations in one contract entirely negate the rights or obligations in another contract entered into at the same time with the same counterparty, the combined effect is that no rights or obligations exist.

Issue #	Topic	Issue	Proposed action
		inappropriately; and (b) require entities to separate contracts that covered different insurance risks into different contracts.	
A9	Interim financial reporting	Some reviewers asked for guidance on how the requirements of IAS 34 *Interim Financial Reporting* would apply to the measurement of contracts within the scope of draft IFRS 17.	The staff propose to add guidance to IFRS 17 that an entity should not recalculate amounts recognised in previous interim financial statements when applying IFRS 17 in subsequent interim financial statements or in the annual reporting period.
A10	Exclusion of VAT from revenue	Some reviewers asked whether VAT (that is included in the fulfilment cash flows) is to be included or excluded from revenue.	The staff propose to clarify that amounts that relate to transaction based taxes, including value added tax, should be excluded from revenue.
A11	Consequential amendments: IFRS 1 *First-time Adoption of International Financial Reporting*	A reviewer questioned whether the transition relief to require the restatement of only one year of comparatives available for existing preparers should also be applicable to first-time adopters.	The staff recommend that first-time adopters should be required to restate all comparative periods presented as required by IFRS 1 (including that they should present three balance sheets applying IFRS 17). Thus, the staff recommend that first-time adopters should not be

Issue #	Topic	Issue	Proposed action
	Standards Exemption for comparatives for a first-time adopter		allowed the exemption for earlier comparative periods presented provided as a transition relief in IFRS 17 for existing preparers. The staff note that in developing IFRS 1, the Board concluded that the requirements for comparative information for a first-time adopter should be different from the requirements for comparative information for an existing preparer.
A12	Consequential amendments: IFRS 3 *Business Combinations* Classification of insurance contracts on a business combination	IFRS 3 paragraph 14 generally requires an acquirer to classify assets and liabilities based on facts and circumstances that exist at the acquisition date. The existing IFRS 3 has an exception to that principle for insurance contracts. It requires an acquirer to classify a contract as an insurance or non-insurance contract based on facts and circumstances existing at the inception date (or modification date).	The staff recommend that the classification of insurance contracts should be based on the facts and circumstances that exist at the acquisition date because this is consistent with the subsequent measurement requirements at the acquisition date for insurance contracts acquired in a business combinations applying IFRS 17. The staff note that this consequential amendment to IFRS 3 applies to business combinations that occur

Issue #	Topic	Issue	Proposed action
		Different reviewers: (a) thought this exception should continue to apply. Of those, some thought this exception should be extended to apply to contracts acquired in a portfolio transfer and the classification of a contract as having, or not having, direct participation features. (b) noted that this exception was inconsistent with the requirements of IFRS 17 that contracts acquired in a business combination are measured using the estimates at the acquisition date.	when or after IFRS 17 is effective.
A13	Consequential amendments: IAS 32 and IFRS 9: Exemption for own debt and treasury shares	The consequential amendments include an exemption for own debt and treasury shares when specified entities repurchased those instruments. When those instruments are repurchased by the entity, an entity could choose to not apply the requirements in IFRS 9 or IAS 32 and instead recognise that instrument as if it is a financial asset and measured at fair value through profit or loss. Some commentators:	The staff proposes: (a) to clarify that the scope of the exemption applies only when the investment fund provides investors with benefits determined by units in the fund and recognises financial liabilities for the amounts to be paid to those investors, (b) to clarify that the election to measure the financial asset at fair value through profit or loss must be

Issue #	Topic	Issue	Proposed action
		(a) requested clarification on the scope and nature of the election to measure the resulting financial asset at fair value at profit or loss; and (b) noted that there were no disclosures to provide information that this exemption was used.	made at initial recognition of each instrument and that election is irrevocable. The staff note that the resulting financial asset would be treated as if it were a financial asset measured at fair value through profit or loss in accordance with IFRS 9. (c) to require separate disclosure of the fair value of the financial assets applying the exemption for own debt and treasury shares by amending IFRS 7 paragraph 8(a).
A14	Consequential amendments: IFRS 7 Disclosure of the fair values of investment contracts with discretionary participation features	IFRS 7 paragraphs 29(c) and 30 provide an exception so that the issuer would not need to disclose the fair value of investment contracts with discretionary participation features when the fair value of the discretionary participation feature cannot be measured.	The staff propose to delete the disclosure requirement in IFRS 7 paragraphs 29(c) and 30 as they are no longer necessary in the light of IFRS 13 *Fair Value Measurement*.

Clarifications

13. The following table lists clarifications to the Standard that the staff propose in the light of comments received on the draft.

Issue #	**Topic**	**Issue**	**Proposed action**
B1	Level of aggregation: Example of contracts in different portfolios	Some reviewers were concerned that including specific product types (annuities, whole-life, term-life) as examples of contracts that should be in different portfolios might result in contracts with similar risks inappropriately being separated into different portfolios. For example, a very long term-life contract could have similar risks to a whole-life contract. They suggested that many insurers define their product lines in different ways and that examples are not needed in a principles-based Standard.	The provision of examples was intended to provide direction on how an entity should interpret similar risks. The staff propose to revise the examples to refer to products that clearly have different risks, ie single-premium fixed annuities compared to regular term life assurance.

Issue #	Topic	Issue	Proposed action
B2	Level of aggregation: Determining groups at initial recognition	Some reviewers requested further guidance and clarification on how to determine when contracts are onerous at initial recognition, or when contracts that are not onerous at initial recognition have no significant possibility of becoming onerous. The following comments were raised: (a) some reviewers stated that the proposed requirement for identifying onerous contracts at inception may need to be performed at a contract level because of the reference to individual contracts. (b) some reviewers stated it was unclear what the term ‘a set of contracts’ represents and noted that there are inconsistencies on the unit of account to be applied in assessing whether contracts are onerous on initial recognition (individual or aggregated) and for subsequent measurement	The staff propose that the guidance should be clarified to make the Board’s intent clearer, in particular: (a) to reflect that the Board expects that many entities will be able to use reasonable and supportable information to determine whether a set of contracts will either all be onerous or will contain no onerous contracts. However, should it not be possible, that the assessment should be performed at an individual contract level, as the prohibition of the offsetting of gains and losses at initial recognition is one of the key aspects of IFRS 17. (b) The staff propose not to define a set of contracts, as a set typically would be the most appropriate level of aggregation to achieve the objective. (c) The staff did not intend significant to be interpreted in the same was as significant insurance risk and have amended the drafting to clarify this.

Issue #	Topic	Issue	Proposed action
		purposes (performed at a group level). (c) some reviewers questioned whether the term "significant risk of becoming onerous" should be interpreted in a consistent way with the term "significant insurance risk".	Appendix B sets out wording to be included in the Standard (paragraphs 18 and 19).

Issue #	Topic	Issue	Proposed action
B3	Level of aggregation: Recognition	Some reviewers asked for clarification as to how an entity should determine appropriate estimates for discount rates where the issue dates of contracts within group of contracts extend over two or more reporting periods.	The staff propose to add guidance clarifying that an entity will need to make estimates at the end of the reporting period based on the contracts issued by that date, and to update its estimates of the discount rates for the group on each period in which newly issued contracts are added to the group.
B4	Level of aggregation: Modification and derecognition	Some reviewers asked how the requirements for grouping contracts would apply when a contract modification results in an entity derecognising the original contract and recognising a new contract. They requested guidance on how the contractual service margin of the new contract should be accounted for.	When a contract is derecognised from a group, the contractual service margin for the group is adjusted to reflect the coverage units that are derecognised. The staff have amended the draft to ensure that entities do not double count the contractual service margin of the newly recognised contract.

Issue #	Topic	Issue	Proposed action
B5	Level of aggregation: Recycling on derecognition	Some reviewers thought that it was unclear whether, when a group of contracts is derecognised, an entity should recognise in profit or loss amounts previously recognised in other comprehensive income.	The staff propose to clarify that an entity should: (a) reclassify to profit or loss any remaining amounts for the group that were previously recognised in other comprehensive income because the entity applied an effective yield or crediting rate approach; and (b) not reclassify to profit or loss any remaining amounts for the group that were previously recognised in other comprehensive income because the entity applied a current period book yield approach.
B6	Level of aggregation: Premium allocation approach	Some reviewers asked for clarification on the effect of level of aggregation on the premium allocation approach, as follows: (a) determining when contracts eligible for the premium allocation approach are onerous, and	The staff propose to clarify the requirements for determining onerous contracts in the premium allocation approach and to add guidance that an entity assesses whether a group of contracts is onerous if at any time during the coverage period facts and circumstances indicate that a group of contracts is onerous. See

Issue #	Topic	Issue	Proposed action
		when a loss should be recognised; (b) whether the assessment as to whether the premium allocation approach is a reasonable approximation of the general model is to be performed at group level or at an individual contract level; and (c) whether a group of insurance contracts can qualify for applying the premium allocation approach when the coverage period of contracts within the group is 12 months or less, but coverage for the contract within the group starts on different dates.	Appendix B, paragraph 20. The staff also propose to clarify that a group of insurance contracts is eligible for the premium allocation approach: (a) if applying the premium allocation approach at a group level results in a reasonable approximation of the general model; or (b) if the coverage period of each contract in the group is one year or less.
B7	Variable fee approach: Scope - General	Some reviewers thought the scope criteria for the variable fee approach was not clear, in particular what the difference was between the requirement that the entity expects to pay to the policyholder an amount equal to a substantial share of the returns	The staff propose to address these concerns by amending the drafting as set out in Appendix B, see paragraphs B102, B105, B108 and B109.

Issue #	Topic	Issue	Proposed action
		from the underlying items, and that a substantial proportion of the cash flows that the entity expects to pay to the policyholder should be expected to vary with the cash flows from the underlying items. In addition, some reviewers asked how to interpret the requirement that the amounts the entity expects to pay to the policyholder should be expected to vary with the cash flows from the underlying items.	
B8	Variable fee approach: Scope - Meaning of constructive obligations	Some asked for further guidance on the meaning of “contractual terms” in the scope of the variable fee approach, in particular whether such terms needed to be specifically included in the wording of the contract with the policyholder.	The Board intended that “contractual terms” in IFRS 17 should include terms included in the contract by law or regulation. The staff propose that the following guidance, already present in draft IFRS 17 in the context of assessing whether there is a link between insurance contracts and underlying items, be moved to apply throughout the Standard: 3. An entity shall consider its substantive rights and obligations, whether they arise from a contract, law or regulation, when applying IFRS 17. A contract is an agreement between two or more parties that creates enforceable rights and obligations. An

Issue #	Topic	Issue	Proposed action
			entity shall disregard terms that have no commercial substance (ie no discernible effect on the economics of the contract). Enforceability of the rights and obligations in a contract is a matter of law. Contracts can be written, oral or implied by an entity's customary business practices. The practices and processes for establishing contracts with customers vary across legal jurisdictions, industries and entities. In addition, they may vary within an entity (for example, they may depend on the class of customer or the nature of the promised goods or services). The paragraphs in IFRS 17 on the scope of the variable fee approach included a cross reference to the above paragraph. The guidance is consistent with similar guidance in IFRS 15 *Revenue from Contracts with Customers.*

Issue #	Topic	Issue	Proposed action
B9	Variable fee approach: Transition	Some reviewers asked for clarification on the requirements for the variable fee approach when an entity applies the Standard for the first time using a modified retrospective approach.	The staff propose to clarify the adjustments to the fair value of the underlying items at the transition date that need to be made in the modified retrospective approach, as follows. C16. To the extent permitted by paragraph C8 for contracts with direct participation features, an entity shall determine the contractual service margin at the transition date as: (a) the total fair value of the underlying items at that date; minus (b) the fulfilment cash flows at that date; plus or minus (c) an adjustment for: (i) amounts charged by the entity to the policyholders (including amount deducted from the underlying items) before that date; (ii) cash outflows that occurred before that date that did not reduce the underlying items; (iii) the release of the risk adjustment for non-financial risk before that date. The entity shall estimate this amount by reference to release of risk for similar insurance contracts that the entity issues at the transition date; and (iv) the amount of contractual service margin that relates to service provided before that date. The entity shall estimate this amount by comparing the remaining coverage units to the total coverage units of the group of insurance contracts.

Issue #	Topic	Issue	Proposed action
B10	Fair value of contracts *or* fair value of fulfilment cash flows?	Draft IFRS 17 requires fair value measurement in some cases, for example as part of transition; business combinations and the transfer of a group of insurance contracts. Some reviewers asked for guidance on whether the item being measured at fair value is the individual contract, or the group of contracts; or the fulfilment cash flows.	As the item being measured in each case is the group of insurance contracts, the fair value refers to the fair value of the group of contracts. The staff will ensure that this is clear.
B11	Coverage units	Some reviewers asked for more guidance or a definition to explain 'coverage units'.	The staff propose to add guidance that the number of 'coverage units' in a group is the amount of coverage provided by the contracts in the group, determined by considering for each contract the quantity of the benefits provided under the contract and its expected duration.
B12	Valuation of options and guarantees	A reviewer asked the Board to clarify whether options and guarantees should be measured on a market-consistent basis.	The staff propose to add the following guidance (change underlined): B48. Techniques other than a replicating portfolio technique, such as stochastic modelling techniques, may be more robust or easier

Issue #	Topic	Issue	Proposed action
	embedded in insurance contracts		to implement if there are significant interdependencies between cash flows that vary based on returns on assets and other cash flows. Judgement is required to determine the technique that best meets the objective of consistency with observable market variables in specific circumstances. In particular, the technique used must result in the measurement of any options and guarantees included in the insurance contracts being consistent with observable market prices for such options and guarantees.
B13	Inflation	Some reviewers asked for clarification of whether inflation should be treated as a financial assumption.	The staff propose to add guidance that, for the purposes of IFRS 17: (a) assumptions about inflation based on an index of prices or rates or on prices of assets with inflation-linked returns are financial assumptions; and (b) assumptions about inflation based on an entity's expectation of specific prices changes are non-financial assumptions.
B14	Disclosure: investment contracts with	Some questioned the benefits of requiring separate disclosures for investment contracts with	The staff propose that separate disclosures need not be specifically required for investment contracts with discretionary participation features. The staff notes that

Issue #	Topic	Issue	Proposed action
	discretionary participation features	discretionary participation features.	the general principles on aggregation for disclosure purposes may result in separate disclosure for such contracts in some cases.
B15	Disclosure: transition relief	Draft FRS 17 requires disclosure of amounts relating to the measurement of insurance contracts in each period for which there are contracts that were measured at transition using the fair value or modified retrospective transition approaches. Some reviewers questioned whether entities would need to disclose only amounts relating to the contractual service margin or all amounts relating to both the contractual service margin and the fulfilment cash flows.	The staff propose to clarify that the disclosure requirements identifying the effects of contracts measured using the modified retrospective approach or fair value approach at the transition date apply only to the contractual service margin and revenue.

Appendix A: Items the staff does not propose be reconsidered

The following table lists comments received on items that the Board has already considered, ie items where commentators disagree with the Board's decisions rather than drafting comments.

Issue #	Topic	Issue	Reasons not to reconsider
C1	Accounting mismatches: general	Some commentators observe that IFRS 17 will not fully eliminate accounting mismatches between insurance contracts and related assets. In particular, they note that accounting mismatches arise due to: (a) the approach to accounting for hedging activities. (b) the accounting for reinsurance contracts. (c) the requirement to measure contracts with direct participation features on the basis of the fair value of underlying items.	The staff notes that the development of an accounting model for insurance contracts inevitably results in possible accounting mismatches because of the different basis of accounting in other Standards. In the mixed measurement model that exists in IFRS Standards, accounting mismatches are inevitable. Nonetheless the Board has minimised the extent of accounting mismatch, where possible, while recognising this limitation. Issues C2-C4 below discuss specific issues relating to perceived accounting mismatches.

Issue #	Topic	Issue	Reasons not to reconsider
C2	Hedging activities	Some commentators note that the approach to accounting for hedging activities does not fully eliminate accounting mismatches. In particular: (a) some requested that the Board create a hedge accounting solution for insurance contracts without direct participation features. (b) some noted that the Board is developing a macro hedge accounting model for dynamic portfolio hedging, and suggested aligning the projects. (c) some noted that the application of the risk mitigation requirements on a prospective basis would not eliminate accounting mismatches for relationships that started before the date of transition.	The Board noted that entities could choose to avoid some accounting mismatches using the general hedge accounting requirements by applying IFRS 9 (or IAS 39 *Financial Instruments: Recognition and Measurement*) or by deciding whether, and for which group of contracts, to present in OCI some changes in insurance finance income or expense. The Board's tentative decisions reduce the accounting mismatches that were introduced by the introduction of the variable fee approach by providing an option to align the overall effect of the variable fee approach more closely to the general model. However, the Board concluded that it would not be appropriate to develop a bespoke solution for all hedging activities for insurance contracts, noting that such a solution should form part of a broader project

Issue #	Topic	Issue	Reasons not to reconsider
			for all industries. See November 2016 Agenda Paper 2F *Mitigating financial risks reflected in insurance contracts* for more details.

Issue #	Topic	Issue	Reasons not to reconsider
C3	Reinsurance contracts	Some commentators disagree with the requirements for the recognition of the contractual service margin of reinsurance contracts held. They believe that these requirements result in accounting mismatches with the insurance contracts that are being reinsured.	The Board's decision results from the conclusion that the reinsurance contract is accounted for separately from the underlying insurance contracts, and that the allocation of profit from the reinsurance contract is therefore independent from the allocation of profit from the underlying insurance contract.
C4	Fair value: underlying items	Some commentators noted that the liability for a group of insurance contracts with direct participation features is measured on the basis of changes in the fair value of the underlying items, irrespective of the carrying value for the underlying items. These respondents suggest that: (a) the costs of measuring underlying items at fair value when the carrying amount is not at fair value may not be commensurate with the benefits.	The staff note that: (a) measuring underlying items at fair value is consistent with the premise that the variable fee approach reflects the view of the contracts as providing investment-related services. (c) although the Standard has eliminated some sources of accounting mismatch between changes in the carrying value of underlying items and changes in the contract with direct

Issue #	Topic	Issue	Reasons not to reconsider
		(b) when the underlying items are not measured at fair value, accounting mismatches will arise. (c) there is a need for more guidance on how to measure the fair value of the underlying items.	participation features, it would be possible to fully eliminate mismatches only by measuring all underlying items at fair value. (d) guidance on fair value measurement is provided in IFRS 13 *Fair Value Measurement*.
C5	Use of a locked-in discount rate in the measurement of the contractual service margin for contracts without direct participation features	Some commentators disagree with requiring the use of a locked-in discount rate to measure adjustments to the contractual service margin for contracts without direct participation features, and for the accretion of interest on the contractual service margin.	The Board decided it would not apply an updated discount rate to measure adjustments to the contractual service margin because: (a) the adjustments represent a change to amounts previously determined in contractual service margin at initial recognition, and those amounts are not updated for changes in discount rates; and (b) the balance of the contractual service margin is not a future cash flow.

Issue #	Topic	Issue	Reasons not to reconsider
C6	Unit of account – interaction between mutualisation and the requirement that groups comprise contracts issued not more than a year apart	Some commentators disagree with the requirement for grouping contracts issued not more than a year apart. They believe that this requirement would prevent them reflecting mutualisation between contracts, including on an open-portfolio, and an intergenerational basis.	The Board decided to introduce the requirement that contracts that are issued more than a year apart should not be combined in the same group to achieve two outcomes: (a) to ensure that the contractual service margin for the group reflects the contracts within the group that still have coverage to provide (ie have not lapsed or expired); and (b) to ensure that the allocation of the contractual service margin to profit or loss faithfully depicts changes in profitability of contracts over time. The Board considered how this requirement would apply when there is cross-generational mutualisation. The Board noted that, for ***fully*** mutualised contracts, the annual groups will give the same results as the single combined mutualised portfolio. Therefore, the

Issue #	Topic	Issue	Reasons not to reconsider
			Board concluded that it did not need to give an exception to the requirement to restrict groups to those issued within one year. Such an exception would introduce further complexity to the Standard, and create the risk that the boundary of the exception would not be robust or appropriate in all circumstances, eg if the contracts are not fully mutualised.
C7	Differences between variable fee approach and general model	Some commentators note that there will be differences between a contract accounted for using the variable fee approach and contracts accounted for using the general model. They believe that the extent of the differences in outcome may not be justified because they believe that the economic differences do not reflect the economic differences between contracts with or without direct participation features.	Some insurance contracts provide investment-related services in addition to insurance coverage. The Board previously proposed a single accounting model for all insurance contracts, based on expected cash flows without distinguishing the insurance cash flows from the investment related cash flows. However, when the contract is primarily investment-related, some think that the accounting outcome should be more consistent with that of asset

Issue #	Topic	Issue	Reasons not to reconsider
			management contracts. Consequently, the Board was persuaded to develop a separate approach for contracts that are, substantially, investment management service contracts and set the scope for this approach accordingly.
C8	Allocation of contractual service margin	Some commentators disagree that the allocation of the contractual service margin should be on the basis of the passage of time. The concern is that this may result in profit that is front-end loaded.	The insurance model is an expected cash flow model, requiring an entity to assess expected future cash flows over the life of a contract, based on unbiased future expectations. The contractual service margin represents the profit the entity expects to earn for the services it provides. The objective for the allocation of the contractual service is that the entity recognises the contractual service margin according to the service to be provided. The Board explored requiring entities to define the various services provided under the contract, and then allocate contractual service margin according to

Issue #	Topic	Issue	Reasons not to reconsider
			the delivery of those services. However, the Board concluded that this approach would be operationally difficult. Consequently, the Board decided to require that the allocation of the contractual service margin be on the basis of the defining service provided by an insurance contract, which is insurance coverage. Insurance coverage is delivered on the basis of coverage units. Therefore, the contractual service margin is allocated on the basis of coverage units. The Board concluded that the least complex and subjective approach would be to require entities to recognise the contractual service margin for all insurance contracts on the same basis.
C9	Mutual companies	Some commentators stated that draft IFRS 17 lacks guidance regarding application of the requirements to mutual companies. It was stated that although a mutual company can apply the requirements of draft	The Board aims to set principles-based standards that can be applied to all entities issuing insurance contracts irrespective the legal form or company structure. In that context, the staff believes that

Issue #	Topic	Issue	Reasons not to reconsider
		IFRS 17 as they are currently set out, applying IFRS 17 without any guidance can lead to significant divergence in application and interpretation issues.	developing guidance within the Standard for a specific form of entity is not justified. The staff notes that the need for educational or implementation guidance will be evaluated after the Standard is issued, and material could be developed if needed.

Appendix B: Revised wording in draft of IFRS 17

This Appendix shows extracts from the latest staff working draft of IFRS 17. This drafting has been provided to aid in the Board's consideration of the issues in this paper. It has yet to be reviewed by the Board and is subject to further editorial changes.

Extract on Level of aggregation

15 An entity shall identify *portfolios of insurance contracts*. A portfolio comprises contracts that are subject to similar risks and managed together. Contracts within a product line would be expected to have similar risks, and hence be in the same portfolio if they are managed together. Contracts in different product lines (for example single premium fixed annuities compared to regular term life assurance) would not be expected to have similar risks and hence would be expected to be in different portfolios.

16 Paragraphs 17–25 apply to insurance contracts issued. The requirements for the level of aggregation of reinsurance contracts held are set out in paragraph 60.

17 An entity shall divide a portfolio of insurance contracts issued into a minimum of:

(a) a group of contracts that are onerous at initial recognition (see paragraph 46), if any;

(b) a group of contracts that at initial recognition have no significant possibility of becoming onerous subsequently (see paragraph 47), if any; and

(c) a group of the remaining contracts in the portfolio, if any.

18 For contracts issued to which an entity does not apply the premium allocation approach (see paragraphs 52—58), an entity shall determine which contracts are onerous at initial recognition, by measuring:

(a) any sets of contracts, if using reasonable and supportable information the entity can determine that the contracts in the sets are either all onerous or all not onerous; or

(b) individual contracts.

19 For contracts issued to which an entity does not apply the premium allocation approach (see paragraphs 52—58), an entity shall assess whether contracts that are not onerous at initial recognition have no significant possibility of becoming onerous:

(a) based on the likelihood of changes in assumptions which, if they occurred, would result in the contracts becoming onerous.

(b) using information about estimates provided by the entity's internal reporting. Hence;

(i) an entity shall not disregard information provided by the its internal reporting about the effect of changes in assumptions on different contracts on the possibility of their becoming onerous; but

(ii) an entity need not gather additional information beyond that provided by the entity's internal reporting about the effect of changes in assumptions on different contracts.

20 For contracts issued to which an entity applies the premium allocation approach (see paragraphs 52—58), an entity shall assume that no contracts in the portfolio are onerous at initial recognition, unless facts and circumstances indicate otherwise. An entity shall assess whether contracts that are not onerous at initial recognition have no significant possibility of becoming onerous subsequently by assessing the likelihood of changes in applicable facts and circumstances.

21 If, applying paragraphs 15–20 contracts within a portfolio would fall into different groups only because law or regulation constrains the entity's practical ability to set a different price or level of benefits for policyholders with different characteristics, the entity may include those contracts in the same group. The entity shall not apply this paragraph by analogy to other items.

22 An entity is permitted to sub-divide the groups described in paragraph 17. For example, an entity may choose to divide the portfolios into:

(a) more groups that are not onerous at initial recognition if the entity's internal reporting provides information that distinguishes:

(i) more detailed levels of possibilities of contracts becoming onerous subsequent to initial recognition; or

(ii) different levels of profitability in addition to whether there is a significant possibility of becoming onerous; and

(b) more than one group of contracts that are onerous at inception, if the entity's internal reporting provides information at a more detailed level about the extent to which the contracts are onerous.

23 An entity shall not include contracts issued more than one year apart in the same group. To achieve this, if necessary, the entity shall further divide the groups described in paragraphs17 and 21.

24 A group shall comprise a single contract if that is the result of applying paragraphs 15–22.

25 An entity shall apply the recognition and measurement requirements of IFRS 17 to the groups of contracts issued determined by applying paragraphs 15–24. An entity shall establish the groups at the inception of the contracts, and shall not reassess the composition of the groups subsequently. To measure a group of contracts, an entity may estimate the fulfilment cash flows at a higher level of aggregation than the group or portfolio, provided the entity is able to include the appropriate fulfilment cash flows in the measurement of the group applying paragraphs 33 and 41(a) by allocating such estimates to groups of contracts.

Extract on Mutualisation

Contracts with cash flows that affect or are affected by cash flows to policyholders of other contracts

B67. Some insurance contracts affect the cash flows to policyholders of other contracts by requiring:

(a) the policyholder to share with policyholders of other contracts the returns of the same specified pool of underlying items; and

(b) either:

(i) the policyholder to bear a reduction in their share of the returns of the underlying items as a consequence of payments to policyholders of other contracts that share in that pool, including payments arising under guarantees made to policyholders of those other contracts; or

(ii) policyholders of other contracts to bear a reduction in their share of returns of the underlying items as a consequence of required payments to the policyholder, including guarantees made to the policyholder.

B68. Sometimes, such contracts will affect the cash flows to policyholders of contracts in other groups. The fulfilment cash flows of each group reflect the extent to which the contracts in the group cause the entity to be affected by expected cash flows, whether to policyholders in that group or in another group. Hence the fulfilment cash flows for a group:

(a) include payments arising from the terms of existing contracts to policyholders of contracts in other groups, regardless of whether those payments are expected to be made to current or future policyholders; and

(b) exclude payments to policyholders in the group that, applying (a), have been included in the fulfilment cash flows of another group.

B69. For example, to the extent that payments to policyholders in one group are reduced from a share in the returns on underlying items of CU350 to CU250 because of payments of a guaranteed amount to policyholders in another group, the fulfilment cash flows of the first group would include the payments of CU100 (ie would be CU350) and the fulfilment cash flows of the second group would exclude CU100 of the guaranteed amount.

B70. Different practical approaches can be used to determine the fulfilment cash flows of groups of contracts that affect or are affected by cash flows to policyholders of other contracts. In some cases, an entity might be able to identify the change in the underlying items and resulting change in the cash flows only at a higher level of aggregation than the groups. In such cases, the entity shall allocate the effect of the change in the underlying items to each group on a systematic and rational basis.

B71. After all the coverage has been provided to the contracts in a group, the fulfilment cash flows may still include payments expected to be made to current policyholders in other groups or future policyholders.

An entity is not required to continue to allocate such fulfilment cash flows to specific groups but can instead recognise and measure a liability for such fulfilment cash arising from all groups.

B103. To the extent that insurance contracts in a group affect the cash flows to policyholders of contracts in other groups (see paragraphs B67–B68), an entity shall assess whether the conditions in paragraph B102 are met by considering the cash flows that the entity expects to pay the policyholder determined applying paragraphs B68–B70.

Extract on Scope of variable fee approach

B102 Insurance contracts with direct participation features are defined as insurance contracts for which:

(a) the contractual terms specify that the policyholder participates in a share of a clearly identified pool of underlying items (see paragraphs B106-B107);

(b) the entity expects to pay to the policyholder an amount equal to a substantial share of the fair value returns from the underlying items (see paragraph B108); and

(c) the entity expects a substantial proportion of any change in the amounts to be paid to the policyholder to vary with the change in fair value of the underlying items (see paragraph B108).

B105. The conditions in paragraph B102 ensure that insurance contracts with direct participation features are contracts that are, substantially, investment management service contracts, under which the entity's obligation to the policyholder is the net of:

(a) the obligation to pay the policyholder an amount equal to the fair value of the underlying items; and

(b) a variable fee (see paragraphs B108–B114) that the entity will deduct from (a) in exchange for the future services provided by the insurance contract, comprising

(i) the entity's share of the fair value of the underlying items; less

(ii) amounts payable to the policyholder that do not vary based on the underlying items.

B108. Paragraph B102(b) requires that a substantial share of the returns on the underlying items are paid to the policyholder and paragraph B102(c) requires that a substantial proportion of any change in the amounts to be paid to the policyholder should vary with the change in the fair value of the underlying items. An entity shall:

(a) interpret the term 'substantial' in both paragraphs in the context of the objective of insurance contracts with direct participation features being contracts under which the entity provides investment management services and is compensated by for the services by a fee that is determined by reference to the underlying items; and

(b) assess the variability in the amounts in paragraphs B102(b) and B102(c):

(i) over the duration of the group of contracts; and

(ii) on a present value probability-weighted average basis, not a best or worst outcome basis (see paragraph B39).

B109. Hence, for example, if the entity expects to pay a substantial share of the fair value returns from underlying items, subject to a guarantee of a minimum return, and estimates that the fair value returns will exceed the minimum return in almost all possible scenarios, the entity's assessment of the variability in paragraph B102(c) will reflect the estimate that in almost all of scenarios, the cash flows that the entity expects to pay to the policyholder vary with the changes in fair value of the underlying items.