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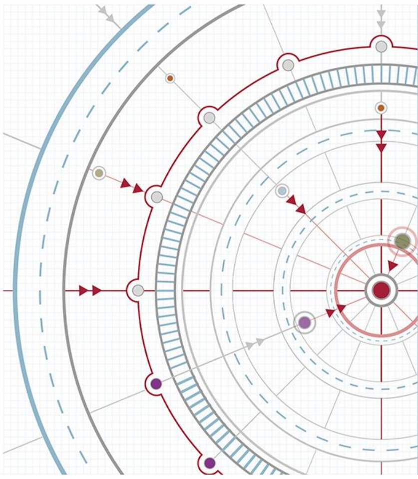

Mind the gap
What do the IFRS 4 amendments on applying IFRS 9 for insurance companies mean for analysts & investors?

Joint Outreach Event
EFRAG ,AIAF, EFFAS, and OIC
Milan
29 November

The views expressed in this presentation are those of the presenter, not necessarily those of the International Accounting Standards Board (the Board) or IFRS Foundation.

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Agenda

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- Background – Mind the gap
- IFRS 4-9 Amendment
- Overview of Overlay Approach
- Overview of Temporary Exemption

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Background – Mind the gap

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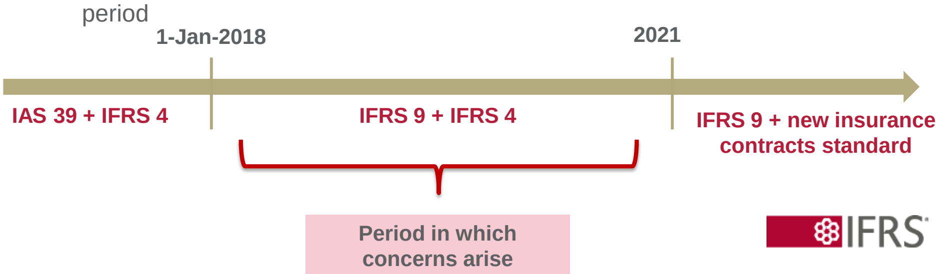
- IFRS 4 *Insurance Contracts* is the current IFRS Standard.
- The Board has decided that the new insurance standard will be effective in 2021
- IFRS 9 *Financial Instruments* is effective from 1 January 2018.
- The gap in effective dates has made insurance companies concerned about:
  1. Implementing two consecutive major accounting changes
  2. Potential accounting volatility in profit or loss (P&L) that could arise in this period



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Why the concern? Accounting mismatch

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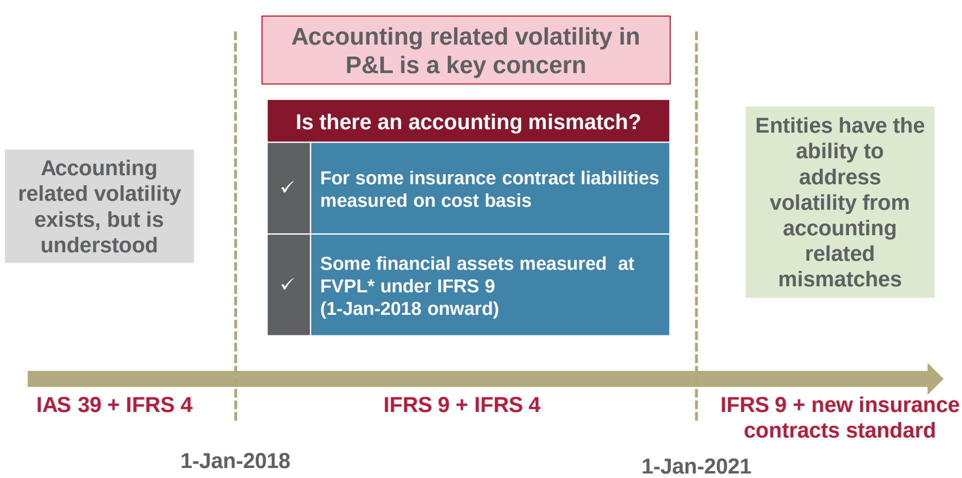

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* FVPL = Fair Value Through Profit or Loss

What is the solution? IFRS 4-9

- 2 optional approaches introduced in the amendments to IFRS 4:

The **overlay approach:**

- Available to all issuers of insurance contracts
- Recognises in Other Comprehensive Income (OCI), rather than in P&L, the volatility that could arise when IFRS 9 is applied before the new insurance contracts Standard
- Available until 2021

The **temporary exemption:**

- Available to companies whose activities are predominantly connected with insurance
- IAS 39 is applied rather than IFRS 9
- Available until 2021

IFRS 4-9: the basics

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- Who does the amendment apply to?
  – Issuers of insurance contracts
- When can it be applied?
  – During annual periods beginning 1.1.2018* up until 2021
- What does the amendment aim to achieve?
  – An outcome where insurance companies can cope with the accounting volatility related concern by presenting some information under IAS-39 instead of IFRS 9

* The Overlay Approach can be applied earlier than 1.1.2018 if an entity early adopts IFRS 9

What does this mean for investors?

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- The period between 1.1.2018 and 2021 may see mix of practices across different companies.

Insurance Company PLCs (IFRS)

IFRS 9 adopted	IFRS 9 adopted & overlay approach	IFRS 9 deferred, IAS 39 applied & disclosures

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Overlay approach – available to all

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Applying the overlay approach

IFRS 9 is applied in full

Information remains comparable with other companies
- balance sheet classification and measurement of financial assets

Option to apply IAS 39 to eligible financial assets

Single line item adjustment to profit or loss so as to reflect profit or loss as under IAS 39
- for assets relating to insurance contracts measured at FVTPL under IFRS 9, but not FVTPL under IAS-39

Objective:
Remove any additional volatility from P&L in a transparent manner while maximising comparability

Illustrative statement of comprehensive income

Statement of Comprehensive Income	
	20XX
Insurance contracts revenue	X
Incurred claims and expenses	(X)
Operating result	X
Investment income 'IFRS 9'	X
Interest on insurance liability	(X)
Overlay approach–adjustment	(X)
Investment result	X
Profit or loss	X
Overlay approach–adjustment	X
Effect of discount rate changes on insurance liability	(X)
Other comprehensive income	X
Total comprehensive income	X

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Overlay Approach: disclosures

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Disclosure Objectives	
The Big Picture	Disclose information that enables investors to understand: • How the "overlay" was calculated • Effect of the reclassification on the financial statements
Key Details	**Information to be provided by disclosures**
Affected Financial Assets	• Carrying amount of financial assets with overlay approach. • Details by class of financial asset • Basis for designating financial assets for overlay
Explanation of P&L/OCI overlay amounts	Enable investor to understand • Amount reported in P&L for designated financial assets applying IFRS 9, and • Amount that would have been reported in P&L if IAS-39 had been applied
Other P&L/OCI effects	Impact on other line items in P&L/OCI (eg Tax)

Temporary exemption approach (*reporting entity)

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Temporary Exemption to apply IAS-39 only

Who can apply it?

Entity's activities must be <u>predominantly connected with insurance</u>.

To qualify, the company must have:
- Not previously applied IFRS 9* and
- Pass the predominance test

- Significant IFRS 4 liabilities compared to total liabilities; and
- Predominance percentage (P^) > 90% or 80% < P^ ≤ 90% and no significant activity unconnected with insurance

$$\hat{P} = \frac{\text{Liabilities from contracts within the scope of IFRS 4} + \text{Investment contracts at FVPL} + \text{Other connected liabilities (e.g. tax)}}{\text{Total liabilities}}$$

Temporary Exemption Approach: Disclosures

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Disclosure Objectives	
The Big Picture	Disclose information that enables investors to: • Understand how the insurer qualified for temporary exemption • Compare insurers applying the temporary exemption with those applying IFRS 9
Key Details	**Information to be provided by disclosures**
Predominance test outcome	• Are insurance contracts >90% of liabilities • Are insurance contracts >80% of liabilities but <90%

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Temporary Exemption Approach: Disclosures

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Disclosure Objectives	
Key Details	**Information to be provided by disclosures**

Group 1
Financial assets with contractual cash flows are SPPI*
• **Excluding held for trading, or managed on fair value basis**
	• Fair value information
	  • period end FV
	  • Change in FV during period
	• Credit risk exposure information, including carrying amounts by credit risk rating grades

Group 2
All other financial assets, such as:
• **Held for trading,**
• **Managed on a fair value basis**
• **Not SPPI**
	• Fair value information
	  • period end FV
	  • Change in FV during period

Similar to population of assets to which ECL requirements would apply**

Similar to population of assets mandatorily applying FVPL under IFRS 9

*Solely Principal and Interest (SPPI)
** Expected Credit Loss (ECL)

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IFRS 4-9 in summary

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- New accounting standards are coming
  - IFRS 9 is effective from 1.1.2018
  - IFRS 17 effective date tentatively agreed as 1.1.2021
- The IFRS 4-9 Amendment addresses concerns during the intervening period.
- IFRS 4-9 requirements aim to:
  - Help avoid unnecessary accounting volatility while waiting for IFRS 17 to be implemented
  - Provide sufficient disclosures to understand how a company has applied the amendment
  - Provide transparency and a basis of comparison during a period of transition.

IFRS 4-9 project page

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- Link to project page
- http://www.ifrs.org/Current-Projects/IASB-Projects/Different-effective-dates-of-IFRS-9-Financial-Instruments-and-the-new-insurance-contracts-Standard/Pages/default.aspx

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Appendix

IFRS 4-9: Eligibility flowchart

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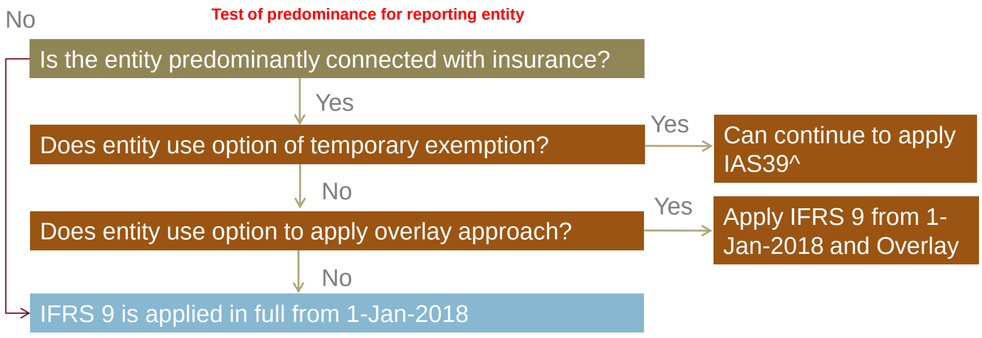
The Board issued final amendments to IFRS 4 in September 2016, introducing two optional approaches for issuers of insurance contracts that have not previously applied IFRS 9*:



*Other than 'own credit requirements' in insolation
^Until 1-Jan-2021 , when IFRS 17 is applied

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Temporary Exemption

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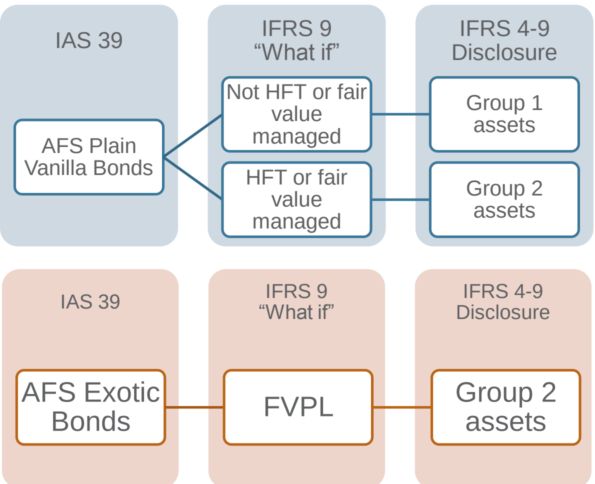

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Temporary Exemption