IFRS 17 *Insurance Contracts*

Objective

1 The objectives of this session are:

(a) To consider recent developments at the IASB; and

(b) To consider whether, and if so how, EFRAG should be proactive in preparing for a possible future exposure draft (ED) of proposed changes to IFRS 17 while the scope of any such ED remains uncertain.

Recent developments at the IASB

Background

2 At its meeting in October 2018, the IASB identified 25 topics that had been raised by constituents. The IASB decided to consider at future meetings whether any concerns and implementation challenges identified by constituents indicate a need to amend the requirements of IFRS 17 beyond the annual improvements the IASB has already decided to propose.

3 The IASB also decided that, when proposing any amendment to IFRS 17, in addition to demonstrating a need for the amendment the proposal should meet the following criteria:

(a) the amendments would not result in significant loss of useful information relative to that which would otherwise be provided by IFRS 17 for users of financial statements—any amendments would avoid:

(i) reducing the relevance and faithful representation of information in the financial statements of entities applying IFRS 17;

(ii) causing reduced comparability or introducing internal inconsistency in IFRS Standards, including within IFRS 17; or

(iii) increasing complexity for users of financial statements, thus reducing understandability.

(b) the amendments would not unduly disrupt implementation already under way or risk undue delays in the effective date of IFRS 17.

Discussions at the ASAF meeting 6 December 2018

4 ASAF members were asked for views on how the IASB could address the following topics while meeting the conditions in paragraph 3 above. The topics discussed were:

(a) Scope of IFRS 17: loans and other forms of credit risk;

(b) Acquisition cash flows for renewals outside the contract boundary;

(c) Contractual service margin: coverage units in the general model;

(d) Reinsurance contracts held: initial recognition when underlying insurance contracts are onerous;

(e) Separate presentation of groups of assets and groups of liabilities (see paragraph 7 below); and

(f) Transition – modified retrospective approach: further modifications.

5 As ASAF is an advisor to the IASB, the range of views and suggestions provided will be considered as the IASB determines what action to take.

Issues to be discussed at the IASB meeting in December

6 The IASB Staff have identified the first group of issues for discussion by the IASB at the December meeting. Other issues will be brought to the IASB in future meetings. A summary of the IASB Staff proposals for the first group of issues is in the following sections. The outcomes of the IASB meeting will be reported to the EFRAG Board at the December meeting.

Presentation of insurance contracts on the statement of financial position

7 The IASB Staff are recommending that the requirement to separately present groups of insurance/reinsurance contracts that are assets and that are liabilities be at a more aggregated level than at the group level as presently required by IFRS 17.

8 The IASB Staff are not recommending changes to IFRS 17 to permit separate presentation and measurement of premiums receivable and claims payable on the face of the statement of financial position.

Discount rates, risk adjustment and OCI option

9 The IASB Staff are not recommending changes to IFRS 17 for:

(a) the use of locked-in discount rates to adjust the contractual service margin under the general model.

(b) the risk adjustment in a group of entities, so that the risk adjustment is determined as part of the pricing of the insurance contract.

(c) the subjectivity in the determination of discount rates and risk adjustment, which means that preparers will need to apply judgement in determining the discount rate and will not be limited to specified risk adjustment techniques.

(d) the OCI option for insurance finance income or expenses, which means that preparers will continue to have the option to present the effect of some changes in financial assumptions in OCI.

Variable fee approach

10 The IASB Staff are not recommending changes to IFRS 17 for:

(a) the definition of an insurance contract with direct participation features. That is, the IASB Staff are not recommending that the variable fee approach should apply to a wider range of contracts with indirect participation features. At a later meeting, the IASB will be asked to consider the periods over which the contractual service margin is recognised in profit or loss under the general model.

(b) the limited applicability of the risk mitigation exception, including the limitation of risk mitigation to contracts under the variable fee approach and the prohibition on carrying forward at transition any previous hedge accounting.

Business combinations

11 The IASB Staff are not recommending changes to IFRS 17 or to IFRS 3 *Business Combinations* for:

(a) classification at the date of the business combination of acquired contracts as insurance contracts. Some preparers proposed that the classification of an insurance contract at the inception of that contract should be carried forward in a business combination. This requirement will only apply to business combinations that occur when or after IFRS 17 is effective.

(b) identification of the insured event for acquired insurance contracts. As a result, an entity treats insurance contracts acquired in a business combination that cover events that have already happened as providing coverage for the adverse development of claims.

Future cash flows in the measurement of reinsurance contracts held

12 The IASB Staff are not recommending changes to IFRS 17 for the contract boundary of a reinsurance contract. As a result, IFRS 17 will continue to require that reinsurance contracts held are measured on the basis of the contractual terms of the reinsurance contract, which may not align with the already issued primary insurance contracts that are subject to reinsurance. That is, IFRS 17 will continue to require "grossing up" of reinsurance contracts held, but with no impact on the income statement until the primary insurance contracts covered by reinsurance are effected.

The treatment of accounting estimates in interim financial statements.

13 The IASB Staff are not recommending that the IASB amends IFRS 17 as the current requirements are designed to relieve operational complexity. As a result, preparers will not change the treatment of accounting estimates made in previous interim financial statements when applying IFRS 17 in subsequent interim financial statements or in the annual financial statements.

Discussions at future meetings

14 The IASB will be asked to consider the following ten issues at a future meeting:

(a) Scope of IFRS 17 – Loans and other forms of credit that transfer insurance risk;

(b) Level of aggregation of insurance contracts;

(c) Measurement – Acquisition cash flows for renewals outside the contract boundary;

(d) Measurement – Contractual service margin: coverage units in the general model;

(e) Measurement – Reinsurance contracts held: initial recognition when underlying insurance contracts are onerous;

(f) Measurement – Reinsurance contracts held: ineligibility for the variable fee approach;

(g) Effective date – Comparative information;

(h) Transition – Optionality;

(i) Transition – Modified retrospective approach: further modifications; and

(j) Transition – Fair value approach: OCI on related financial assets.

Question for the EFRAG Board

15 Does the EFRAG Board have any comments on the developments at the IASB?

EFRAG's activities in the pre-ED phase of IASB discussions

Active monitoring

16 The EFRAG Board had previously decided that EFRAG would revert to its influencing role (i.e. contributing to the IASB's due process) if more than insignificant changes to IFRS 17 are anticipated. In broad terms this would involve:

(a) Keeping the EFRAG IAWG, EFRAG TEG and EFRAG Board informed of the IASB's ongoing scoping discussions;

(b) Consideration of the IASB's ongoing development of potential solutions to the issues selected in its scoping discussions (prior to any ED). During the pre-ED phase the IASB would be made aware of EFRAG's reactions to potential solutions via IASB observers and other channels such as ASAF. The EFRAG IAWG and EFRAG TEG would normally carry out this 'active monitoring' with the EFRAG Board being kept informed, although the EFRAG Board might prefer a more active role.

(c) Developing a draft then a final comment letter on the IASB's ED. This would be decided by the EFRAG Board, having considered the advice of EFRAG TEG, which in turn would consider advice of EFRAG IAWG.

Questions for the EFRAG Board

17 Does the EFRAG Board agree that EFRAG's influencing role should be executed as described above?

18 Does the EFRAG Board wish to be more actively involved in the pre-ED phase and, if so, how?

Other proactive activities

19 Some members of the EFRAG Board suggested that EFRAG should engage in additional proactive activities. Such activities could include:

(a) Seeking information additional to that collected from the case studies and outreaches on the specific issues under consideration. Preparers and users may have more information on the potential impact of IFRS 17, including implementation projects, and costs and benefits. However, preparers and users may be reluctant to provide updated information before the changes likely to be proposed by the IASB are relatively clear;

(b) Developing EFRAG potential solutions to certain issues;

(c) Discussing potential solutions proposed by other parties.

20 The EFRAG Secretariat suggests that any activity centred on 'non-IASB solutions' gives rise to a number of questions and challenges:

(a) What is EFRAG's objective in working on non-IASB solutions? For example, is it simply to be better prepared to respond to an ED or should there be an alternative objective? If the former, is this an efficient and effective approach?

(b) Which issues should EFRAG focus on (e.g. only those selected on the IASB's scoping discussions; those in EFRAG's letter; some other set)?

(c) What level of due process should EFRAG undertake to adequately evaluate and test any non-IASB solutions?

(d) How can EFRAG ensure that any such activity avoids prejudicing EFRAG's evaluation of IFRS 17 (or IFRS 17 revised)?

Questions for the EFRAG Board

21 Does the EFRAG Board consider that EFRAG should undertake additional proactive activities in the pre-ED phase? If so, what proactive activities does the EFRAG Board propose to be undertaken?

22 If the EFRAG Board wishes to work on non-IASB solutions, what are the EFRAG Board’s views on the questions in paragraph 20?