

This paper has been prepared by the EFRAG Secretariat for discussion at a public meeting of the EFRAG Board. The paper does not represent the official views of EFRAG or any individual member of the EFRAG Board or EFRAG TEG. The paper is made available to enable the public to follow the discussions in the meeting. Tentative decisions are made in public and reported in the EFRAG Update. EFRAG positions, as approved by the EFRAG Board, are published as comment letters, discussion or position papers, or in any other form considered appropriate in the circumstances.

## **IFRS 17 *Insurance Contracts* Project Update**

### **Objective**

- 1 The objective of this session is to:
  - (a) provide the EFRAG Board with an update on the discussions at the recent meeting of EFRAG TEG and seek the views of the EFRAG Board as to whether they have any questions to raise with EFRAG TEG;
  - (b) ask the EFRAG Board for its views on the strategic direction of the draft comment letter on the forthcoming Exposure Draft on IFRS 17 *Insurance Contracts* and
  - (c) seek comments from the EFRAG Board on the project plan for the next six months.

### **A FEEDBACK FROM EFRAG TEG**

- 2 The IFRS 17 topics discussed at the March 2019 EFRAG TEG meeting comprised:
  - (a) A presentation from the CFO Forum on its views of the current status of the IASB's re-deliberations;
  - (b) ASAF paper in preparation for the forthcoming meeting;
  - (c) Feedback on questions raised to EFRAG IAWG; and
  - (d) Preliminary views of EFRAG TEG on issues/tentative decisions considered by the IASB at its January 2019 meeting, having noted the views of EFRAG IAWG on these issues.

### **CFO Forum presentation**

- 3 Members of the CFO Forum provided EFRAG TEG with their views on the current status of the issues raised by EFRAG and the CFO Forum based on the IASB's tentative decisions. The discussion focussed on:
  - (a) CSM amortisation under the general model for UK deferred annuity contracts;
  - (b) Presentation issues relating to current separate actuarial and accounting systems with interaction only on a significantly aggregated level; and
  - (c) Transition and the difficulty of applying the modified retrospective approach.
- 4 The CFO Forum considered that the first and third issues relate to financial reporting impact (for example accounting mismatch, misstated equity/income statement, inconsistent approach applied between in force business on adoption of the standard and subsequent new business) whilst the first issue also has a potential impact on comparability between reporting entities. The second and third issues relate (also) to operational complexity and costs.

- 5 The CFO Forum confirmed that the issues in the presentation correspond to the ones previously communicated to EFRAG and the IASB and that the impact of these issues differ in the severity of the impact on their members. EFRAG TEG members asked various questions including whether and how the use of Alternative Performance Measurements would change with the adoption of IFRS 17.

### **ASAF preparation**

- 6 The April Accounting Standards Advisory Forum (ASAF) meeting aims to obtain views from members about the IASB's tentative decisions on IFRS 17.
- 7 EFRAG TEG members expressed different views on whether it would be appropriate to comment on the IASB's tentative decisions individually at this time, given that EFRAG's due process on its comment letter is at an early stage, or to make only general comments. It was concluded that any comments made should be accompanied by a clear statement on the status of EFRAG's work.

### **Feedback from EFRAG IAWG**

#### *Presentation of insurance contracts in the statement of financial position*

- 8 EFRAG TEG requested further information from EFRAG IAWG on the concern around separate presentation of premiums receivable and claims payable. Members of the EFRAG IAWG provided differing definitions of premiums receivable and noted that there is very little credit risk in the receivables taken as a whole. This was confirmed by background research of the EFRAG Secretariat.
- 9 EFRAG TEG members expressed mixed views as to whether they needed further clarification from EFRAG IAWG.

#### *Discount rates*

- 10 EFRAG TEG requested input from the EFRAG IAWG about its assessment of comparability in the context of discount rates or estimation of the risk adjustment in the context of EIOPA's concerns<sup>1</sup>. In general, the EFRAG IAWG members did not share EIOPA's concerns.
- 11 EFRAG TEG considered that insurance liabilities are to be measured in line with their characteristics, however it was important to apply the same methodology in determining the different discount rates.

#### *Future cash flows in the measurement of reinsurance contracts held*

- 12 EFRAG TEG asked EFRAG IAWG to provide further information on a possible risk adjustment mismatch between underlying contracts and reinsurance contracts held.
- 13 EFRAG IAWG responses identified that different risks (or only some of the risks in an insurance contract) may be reinsured, resulting in differing diversification benefits; different contract boundaries as well as current uncertainty as to whether the risk adjustment includes the risk of non-performance of the reinsurer or not.
- 14 EFRAG TEG members had no comments on the answers from EFRAG IAWG members.

---

<sup>1</sup> EIOPA's report on IFRS 17 states: "IFRS 17's requirements on determining the applicable discount rate and risk adjustment may have exceeded the appropriate level of entity-specific inputs and consequently may give rise to significantly different and potentially incomparable results." The full report is available at: [https://eiopa.europa.eu/Publications/Reports/EIOPA-18-717\\_EIOPA\\_Analysis\\_IFRS\\_17\\_18%2010%202018.pdf](https://eiopa.europa.eu/Publications/Reports/EIOPA-18-717_EIOPA_Analysis_IFRS_17_18%2010%202018.pdf)

*Variable fee approach - risk mitigation approach*

- 15 EFRAG TEG asked EFRAG IAWG to provide further information on hedging strategies and related mismatches as well as why IFRS 9 *Financial Instruments* hedging cannot be used, if that is the case.
- 16 On hedging strategies, one EFRAG IAWG member referred to responses to the 2014 EFRAG hedging survey and results. EFRAG IAWG members indicated that they would investigate further the impact or not of IFRS 9 and provide feedback where relevant.
- 17 Some EFRAG TEG members noted that the economic hedging applied by insurers was similar to macro-hedging for which there was no current accounting solution in IFRS 17.
- 18 EFRAG TEG members agreed to further investigate the reasons for limited use of IFRS 9 hedge accounting. The EFRAG Secretariat will prepare a hedging questionnaire in order to seek information from EFRAG IAWG.

**IASB January 2019 meeting**

- 19 In its March meeting EFRAG TEG considered the January 2019 tentative decisions of the IASB. In doing so, EFRAG TEG considered the views of the EFRAG IAWG which were discussed at the EFRAG IAWG meeting in February.
- 20 EFRAG TEG and EFRAG IAWG were asked to provide views on:
  - (a) Where the IASB tentatively decided to change IFRS 17, whether that change was supported, including the impact on the draft comment letter on the forthcoming Exposure Draft.
  - (b) Where the IASB tentatively decided not to change IFRS 17, how the underlying issue should be reflected in the forthcoming draft endorsement advice.

*IASB tentative decisions to amend IFRS 17*

*Acquisition cash flows for renewals outside the contract boundary  
(issue raised by EFRAG)*

- 21 The IASB tentatively decided to amend IFRS 17 to require allocation of those insurance acquisition cash flows directly attributable to expected renewals of those contracts outside the contract boundary. Therefore, these insurance acquisition cash flows would be recognised as an asset until the expected contract renewals are recognised. Recoverability of the asset would have to be considered during each period and impaired if relevant.
- 22 EFRAG TEG members supported the IASB tentative decision and EFRAG IAWG members had also supported this proposal.
- 23 Overall, the preliminary view of EFRAG TEG is that this proposal from the IASB should be supported in the draft comment letter on the forthcoming Exposure Draft.

*Contractual service margin: coverage units in the general model  
(issue raised by EFRAG)*

- 24 The IASB has tentatively decided that the contractual service margin ('CSM') under the general model should be amended to require allocation of CSM based on coverage units that considers both insurance coverage and investment return services. An investment component is necessary for an investment return service but is not enough on its own to demonstrate such a service and so judgement would be required.
- 25 EFRAG TEG members generally supported this proposal.

- 26 EFRAG IAWG members generally supported the IASB tentative decision. However, some members indicated that an investment return service could be present in the absence of an investment component and vice versa. Others questioned what service is being provided to the policyholder if the policyholder does not always benefit from the investment-related services.
- 27 Overall, the preliminary view of EFRAG TEG is that this proposal from the IASB should be supported in the draft comment letter on the forthcoming Exposure Draft. The remaining concerns raised by EFRAG IAWG members should be addressed in preparing the draft endorsement advice.

*Variable fee approach: limited applicability of the risk mitigation approach (issue not raised by EFRAG)*

- 28 The IASB agreed to expand the risk mitigation exception under the variable fee approach ('VFA') to include reinsurance contracts held where these are used to mitigate financial risks along with derivatives currently allowed by the standard.
- 29 EFRAG TEG members generally expressed initial support for the IASB's tentative decision, but one EFRAG TEG member argued that cash instruments should also be allowed as hedging instruments and for risk mitigation to be applicable retrospectively. Another TEG member pointed out the complexities that would arise from allowing cash instruments to be used in the risk mitigation approach.
- 30 Further information was requested from EFRAG IAWG members on the use of cash instruments as hedging instruments.
- 31 EFRAG IAWG members thought the proposal was an improvement but was insufficient as a CSM mismatch may remain (e.g. due to differing contract boundaries) as well as the impact of differing discount rates used for the two types of insurance contracts. Furthermore, concerns about cash instruments used and retrospective application were also voiced. Some also noted that whilst this could help the insurer in an intra-group situation, it would not help the reinsurer.
- 32 Overall, the preliminary view of EFRAG TEG is that this proposal from the IASB should be supported in the draft comment letter on the forthcoming Exposure Draft. The remaining concerns raised by one EFRAG TEG member should be addressed in preparing the draft endorsement advice.

*Reinsurance contracts held: initial recognition when underlying insurance contracts are onerous (issue raised by EFRAG)*

- 33 The IASB has tentatively decided to amend IFRS 17 to require an insurer that recognises losses for onerous contracts at initial recognition, to also recognise a gain at the same time in profit or loss on reinsurance contracts held, to the extent that the reinsurance contracts cover the losses of the underlying contracts on a proportionate basis. Such a gain would apply only to reinsurance contracts entered into before – or at the same time as – the onerous underlying contracts are issued. The amendments would apply to contracts measured under the premium allocation approach and the general model.
- 34 The majority of EFRAG TEG members expressed initial support for the IASB tentative decision, but some EFRAG TEG members wanted further information on the use of non-proportional reinsurance.
- 35 EFRAG IAWG members generally supported the decision. However, members noted that a definition for proportional reinsurance would be required and where both proportional and non-proportional reinsurance are used, would need to be analysed. Members expressed concern that no similar solution is available for non-proportional reinsurance.

- 36 Overall, the preliminary view of EFRAG TEG is that this proposal from the IASB should be supported in the draft comment letter on the forthcoming Exposure Draft. The remaining concerns should be addressed in preparing the draft endorsement advice.

**Question for the EFRAG Board**

- 37 Based on the information currently available, does the EFRAG Board agree that:
- (a) the proposals to amend IFRS 17 should be supported in the draft comment letter that will be brought to the EFRAG Board for approval at a public meeting?
  - (b) the remaining concerns should be addressed in preparing the draft endorsement advice?

*IASB tentative decision to retain the requirements in IFRS 17*

*Reinsurance contracts: ineligibility for the variable fee approach (issue not raised by EFRAG)*

- 38 The IASB has tentatively decided to retain the current requirements in IFRS 17 and not to allow reinsurance contracts to be accounted for under the variable fee approach.
- 39 EFRAG TEG members generally expressed initial support for the IASB tentative decision but a TEG member mentioned that some co-insurance contracts in France may be in the form of reinsurance contracts and therefore this could be an issue outside group situations.
- 40 EFRAG IAWG members were concerned that this does not reflect the economics, specifically in an intra-group situation where risks are consolidated in one reinsurance entity.
- 41 The issue should be further addressed in preparing the draft endorsement advice.

**Questions for the EFRAG Board**

- 42 Does EFRAG Board agree that this issue should be addressed in preparing the draft endorsement advice?
- 43 Does EFRAG Board have any additional comments on this issue?

**B IASB EXPOSURE DRAFT ON IFRS 17 AMENDMENTS**

- 44 The IASB has indicated that it will issue the Exposure Draft of its proposed amendments to IFRS 17 towards the end of June 2019 for a three month comment period. If the Exposure Draft is issued before the end of June, it should be possible for EFRAG TEG to consider a draft letter at its meeting on 4 July and for the EFRAG Board to consider the draft comment letter at its meeting on 9 July.
- 45 In its deliberations, the IASB considered 25 issues raised by constituents, including those referred to in the EFRAG letter of September 2018. The current status of the EFRAG issues is as follows:

Issues identified by EFRAG	IASB tentative decision
Acquisition costs (for costs incurred in expectation of contract renewals)	Part of the acquisition cash flows can be allocated to expected contract renewals

Issues identified by EFRAG	IASB tentative decision
CSM amortisation (impact on contracts that include investment services)	For insurance contracts under the general model, an entity would recognise the CSM in profit or loss by considering both insurance coverage and any investment return service
Reinsurance (onerous underlying contracts that are profitable after reinsurance, contract boundary for reinsurance contracts where underlying contracts are not yet issued)	<p>Losses on contracts that are onerous at initial recognition would be offset by a gain on reinsurance contracts held to the extent that the onerous contracts cover the loss on a proportionate bases and are entered into before the onerous contracts are issued</p> <p>No change to boundary for reinsurance contracts</p>
Transition (extent of relief offered by modified retrospective approach and challenges in applying fair value approach)	Reliefs including for liabilities for claims settlement acquired in a business combination; risk mitigation option may be applied from the transition date
Annual cohorts (cost-benefit trade-off, including for VFA contracts)	No change proposed
Balance sheet presentation (cost-benefit trade-off of separate disclosure of groups in an asset position and groups in a liability position and nonseparation of receivables and/or payables)	<p>Insurance contract assets and insurance contract liabilities are presented in the balance sheet based on portfolios rather than groups</p> <p>No change to the non-mandatory separation of receivables and/or payables</p>

- 46 The forthcoming Exposure Draft will include proposals on topics additional to those identified by EFRAG. These topics include:
- (a) Deferring the effective date of IFRS 17 to 1 January 2022;
  - (b) For VFA contracts, an entity is permitted to use the risk mitigation exception when the entity uses reinsurance contracts held to mitigate financial risks; and
  - (c) Loans that transfer insurance risk may be recognised under either IFRS 9 or IFRS 17.
- 47 Given the short timeline for the preparation of a draft comment letter, the EFRAG Board is asked for its preliminary recommendation to EFRAG TEG on the scope of the draft comment letter. The approach could:
- (a) Be limited to the proposals in the Exposure Draft; or
  - (b) Include the six topics identified by EFRAG as meriting further consideration by the IASB.
- 48 All the issues raised by the European Commission, the European Parliament and the insurance industry will be considered in preparing the draft endorsement advice,

unless they are resolved through the changes arising from the forthcoming Exposure Draft.

- 49 The EFRAG Secretariat is not aware of significant new issues being raised by constituents since the EFRAG Board identified the six issues on which it wrote to the IASB. This was confirmed by the CFO Forum in its presentation to EFRAG TEG.

**Question for the EFRAG Board**

- 50 Based on the information currently available, what is the EFRAG Board's preferred approach to the forthcoming IFRS 17 Exposure Draft?

**C PROJECT PLAN**

- 51 As previously agreed, during the next few months the work on the IFRS 17 project will focus on:

- (a) preparation for the forthcoming IASB Exposure Draft; and
- (b) continuing to analyse IFRS 17 from a technical perspective with a particular focus on the six matters EFRAG identified as meriting further consideration by the IASB.

- 52 At its January 2019 meeting, the EFRAG Board agreed to a workplan where input from the EFRAG IAWG on the IASB's tentative decisions have been requested for purposes of both a draft comment letter and ultimately, a draft endorsement advice. EFRAG TEG considers the input received and requests further information as required. The outcome of the discussions is then reported to the EFRAG Board at its next meeting.

- 53 So far, the project has generally worked as planned:

Topic	EFRAG IAWG	EFRAG TEG	EFRAG Board
Issues discussed at the IASB meeting December 2018	January 2019	February 2019	Update February 2019
Presentation by EIOPA		February 2019	Planned: April Deferred to May
Questions from EFRAG TEG to EFRAG IAWG (new action)	February 2019	March 2019	
Issues discussed at the IASB meeting January and February 2019	February 2019	March 2019	Update April 2019

- 54 The EFRAG IAWG discussions on the IASB tentative decisions will continue in May as scheduled and where possible, other topics relevant to the draft endorsement advice will be included in the agendas of the EFRAG IAWG and EFRAG TEG.

- 55 The remainder of the topics for discussion per the work plan is as follows:

Topic	EFRAG IAWG	EFRAG TEG	EFRAG Board
CFO Forum explanation of issues		March 2019	Update April 2019

*IFRS 17 Insurance Contracts Project Update*

<b>Topic</b>	<b>EFRAG IAWG</b>	<b>EFRAG TEG</b>	<b>EFRAG Board</b>
Issues discussed at the IASB meeting March 2019	March 2019	April 2019	May 2019
Issues to be discussed at the IASB TRG meeting April 2019	March 2019	April 2019	May 2019
Detailed analysis of EFRAG matters	May 2019	May 2019	June 2019 joint meeting
IASB ED – preliminary discussion			June 2019 joint meeting
IASB ED draft comment letter	Consideration June 2019	Recommendation July 2019	Approval July 2019
IASB ED final comment letter	Consideration September 2019	Recommendation September 2019	Approval October 2019

**Question for the EFRAG Board**

56 Does EFRAG Board have comments on the project plan?