

Amendments to IFRS 17 *Insurance Contracts* **Basis for EFRAG TEG discussions**

Introduction

- 1 This paper is to be read in conjunction with agenda paper 09-10 relating to the Issues paper on EFRAG's six topics and provides a basis for the EFRAG TEG discussions on these EFRAG topics.
- 2 This paper provides the following information on the EFRAG topics (where applicable):
 - (a) Concerns raised;
 - (b) IASB staff's reasoning for recommending/not recommending an amendment to IFRS 17;
 - (c) Input from CFO Forum;
 - (d) Input from ANC; and
 - (e) Input from UNESPA (Spanish Association of Insurers and Reinsurers).

Issue 1 - Transition: Modified retrospective approach and fair value approach

Summary of IASB tentative decisions

- 3 The IASB tentatively decided to retain the transition requirements in IFRS 17 relating to the cumulative amounts included in other comprehensive income.
- 4 The IASB tentatively decided to:
 - (a) retain the IFRS 17 transition requirements without making amendments that would reduce the optionality included in those requirements; and
 - (b) retain the IFRS 17 requirement to present restated comparative information for the annual reporting period immediately preceding the date of initial application of IFRS 17.
- 5 The IASB tentatively decided to:
 - (a) retain the transition requirements in the modified retrospective approach set out in IFRS 17 that:
 - (i) prohibit an entity from using a specified modification to the extent that the entity has reasonable and supportable information to apply the related IFRS 17 requirement retrospectively; and
 - (ii) permit an entity to use a specified modification only when the entity has reasonable and supportable information to apply that modification.
 - (b) retain the transition requirements in IFRS 17 for the modified retrospective approach, without an amendment that would permit an entity to develop its own modifications that it regards as consistent with the objective of the modified retrospective approach. However, the IASB Board noted the importance of the clarification in the paper that the existence of specified modifications does not preclude the normal use of estimation techniques.
 - (c) amend the transition requirements in IFRS 17 for liabilities that relate to the settlement of claims incurred before an insurance contract was acquired as follows:
 - (i) to add a specified modification to the modified retrospective approach so that an entity classifies such liabilities as a liability for incurred claims. Consistent with the other specified modifications, an entity would be permitted to use this specified modification only to the extent that it does not have reasonable and supportable information to apply a retrospective approach.
 - (ii) to permit an entity applying the fair value approach to choose to classify such liabilities as a liability for incurred claims.
 - (d) retain without amendment the specified modification in the modified retrospective approach relating to the use of cash flows that are known to have occurred, instead of estimating retrospectively cash flows that were expected to occur.
 - (e) retain the modified retrospective approach for insurance contracts with direct participation features, without an amendment that would permit an entity to apply to such contracts the specified modifications permitted for insurance contracts without direct participation features.
- 6 The IASB tentatively decided to amend the requirements of IFRS 17 to:
 - (a) permit an entity to apply the risk mitigation option prospectively from the IFRS 17 transition date, provided that the entity designates its risk mitigation relationships to apply the risk mitigation option no later than the IFRS 17 transition date; and

- (b) permit an entity that can apply IFRS 17 retrospectively to a group of insurance contracts with direct participating features to use the fair value transition approach for the group, if and only if it:
 - (i) chooses to apply the risk mitigation option to the group prospectively from the transition date; and
 - (ii) has used derivatives or reinsurance contracts held to mitigate financial risk arising from the group before the transition date.
- 7 The IASB tentatively decided to amend paragraph B118 of IFRS 17 to clarify that an entity can discontinue the use of the risk mitigation option to a group of insurance contracts only if the eligibility criteria for the group cease to apply.
- 8 The IASB tentatively decided to amend the transition requirements in IFRS 17 for liabilities that relate to the settlement of claims incurred before an insurance contract was acquired as follows:
 - (a) to add a specified modification to the modified retrospective approach so that an entity classifies such liabilities as a liability for incurred claims. Consistent with the other specified modifications, an entity would be permitted to use this specified modification only to the extent that it does not have reasonable and supportable information to apply a retrospective approach.
 - (b) to permit an entity applying the fair value approach to choose to classify such liabilities as a liability for incurred claims.

Issue 1A: Modified retrospective approach

Concerns raised

- 9 EFRAG IAWG members expressed their concern that the modified retrospective approach is difficult to apply. Members noted the complexities in trying to find reasonable and supportable information in order to utilise the different modifications. Members specifically noted that data gaps forces them to use the fair value approach.
- 10 EFRAG IAWG members assessed that the relief provided for business combinations is useful.

IASB staff's reasoning for not recommending an amendment to IFRS 17

- 11 The IASB staff think that the following possible amendments to IFRS 17 would reduce optionality relating to the transition requirements, could increase comparability between entities and would therefore address the concerns about optionality raised by stakeholders:
 - (a) removing the choice between the modified retrospective approach and the fair value approach when retrospective application is impracticable;
 - (b) requiring the application of the fair value approach when retrospective application is impracticable; or
 - (c) removing the choices available to an entity when applying the fair value approach.
- 12 The IASB staff did not think that amending the transition requirements of IFRS 17 would meet the criteria for amending IFRS 17 set by the IASB at its October 2018 meeting because:
 - (a) limiting the availability of any approach or removing the choices available to an entity applying the fair value approach may unduly disrupt implementation already under way; and

(b) the IASB already exposed a version of the approaches described in paragraphs 11(a) – 11(c) of this paper for comments and developed the transition requirements based on feedback.

- 13 The IASB staff recommended that the IASB retain the IFRS 17 transition requirements, without amendments that would reduce the optionality included in those requirements.

Input from CFO Forum

- 14 Extend relief available to enable widespread capability to use the MRA and remove requirements to allocate contracts between separate profitability groupings.

Input from ANC

- 15 There is no need for detailed guidance on how to apply the principle set in IFRS 17.C8.
- 16 The ANC is very supportive of the suggestion made in February's board meeting (IASB 2019-02.AP 2D §36) to explain that a retrospective approach (either FRA or MRA) does not prohibit from making estimates and further to clarify to which extent an estimates stops and becomes a departure to the retrospective approach. This explanation would be better placed in the standard itself.
- 17 For instance, applying a mixed approach on transition: full retrospective as long as reasonable and supportable information is available (i.e. for the last 10 years) and a FVA as initial value for the period before.
- 18 The ANC consider that there is no need for a detailed guidance on how to apply the principle set in IFRS 17.C8.

IFRS 17.C8: To achieve the objective of the modified retrospective approach, an entity is permitted to use each modification in paragraphs C9–C19 only to the extent that an entity does not have reasonable and supportable information to apply a retrospective approach. In addition, the existence of specified modifications in the modified retrospective approach does not prohibit an entity from:

(a) making estimates that are necessary in retrospectively applying an accounting policy as described in paragraph 51 of IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors; or

(b) similarly, making estimates when applying a specified modification in the modified retrospective approach

- 19 The ANC's suggested amendment for the business combinations issue is as follows.

IFRS C5bis: On transition and regardless of the approach retained, an entity may depart from IFRS 17.B93 in applying the date when the contract was issued instead of the date of the transaction (e.g. business combination or portfolio transfer) to contracts acquired before transition.

Issue 1B: Fair value approach

- 20 Refer to agenda paper 09-12 for this meeting.

Issue 1C: Retrospective application of risk mitigation approach

Concerns raised

- 21 If not addressed:
- (a) Additional income volatility will arise from hedging, both reducing the incentive to mitigate risk and requiring significant effort to analyse results;
 - (b) The absence of retrospective application of risk mitigation could negatively impact willingness and ability of companies to offer certain product types to customers, particularly indirect par contracts.

IASB staff's reasoning

- 22 The IASB acknowledged that a retrospective application that did not use hindsight would provide useful information to users of financial statements about risk mitigation activities that took place in previous periods. However, the Board observed that it is hard to see how the option could be applied retrospectively without the use of hindsight, and without risking 'cherry picking' opportunities. The IASB observed that any approach taken to address stakeholders' concerns that allows retrospective application may have this problem, albeit to different degrees.
- 23 Therefore, the IASB tentatively decided to retain the prohibition in IFRS 17 of retrospective application of the risk mitigation option. The IASB asked the staff to explore alternative proposals that would address stakeholders' concerns about the results of not applying the option retrospectively.
- 24 The IASB staff considered two possible ways, other than retrospective application of the risk mitigation option, to address stakeholders' concerns:
- (a) permitting entities to apply a prospective application of the risk mitigation option from the IFRS 17 transition date; and
 - (b) permitting entities that have used derivatives or reinsurance contracts held to mitigate financial risk arising from insurance contracts with direct participating features before the transition date to apply the fair value approach to transition, even if they are able to apply IFRS 17 retrospectively.

Input from CFO Forum

- 25 The inability to apply the hedging adjustment retrospectively fully may lead to significant impacts on the CSM at transition and distort future results. Our companies' testing results shows that for representative portfolios with such significant hedging programmes there could be material distortions to CSM, impacting shareholder equity and subsequent results.
- 26 Proposed solution: Enable retrospective hedging adjustment as part of transition

Input from ANC

- 27 Suggest removing the prohibition of a retrospective application of the risk mitigation provisions.
- 28 Suggested modifications by the ANC: removing the prohibition in IFRS 17.C3(b) of a retrospective application of the risk mitigation provisions.
- 29 IFRS 17.C3: An entity shall apply IFRS 17 retrospectively unless impracticable, except that:
- (a) an entity is not required to present the quantitative information required by paragraph 28(f) of IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors.; ~~and~~
 - (b) ~~an entity shall not apply the option in paragraph B115 for periods before the date of initial application of IFRS 17.~~

Issue 1D: Setting OCI to nil at transition

Concerns raised

- 30 Setting the cumulative OCI balance on insurance liabilities to nil on transition, while not doing so for the cumulative OCI balance on assets measured at FVOCI, will distort components of equity on transition, and impact financial information post transition.

IASB staff's reasoning for not recommending an amendment to IFRS 17

- 31 Permitting entities to deem the cumulative amount in OCI related to corresponding assets as nil at transition to IFRS 17 would involve an amendment to IFRS 9. The IASB staff thought this makes the transition requirements in IFRS 9 more complicated, and would significantly reduce the comparability of information related to the financial assets held between (a) insurers applying that amendment and (b) entities other than insurers and insurers that do not apply the amendment.
- 32 The IASB staff also observed that a component of the cumulative amount recognised in OCI applying IFRS 9 for FVOCI financial assets relates to expected credit losses. Hence it would not be possible to set that component of the cumulative amount at nil because of the effect on the accounting in future periods for expected credit losses.
- 33 Permitting entities to deem the cumulative amount of insurance finance income or expenses recognised in OCI for insurance contracts at transition at the same amount as the cumulative amount in OCI relating to related assets would affect the insurance finance income or expense that will be recognised in future reporting periods. The insurance finance income or expense recognised in profit or loss in future periods would reflect the historical discount rate for the assets held at transition date that the entity determines to be related to the insurance contracts.¹ The IASB staff think that this suggested approach would reduce the usefulness of information provided on the performance of the insurance contracts because:
- (a) that information will be affected by the assets an entity holds so may significantly reduce comparability between entities issuing similar contracts but holding different assets; and
 - (b) of the potential subjectivity involved in determining which assets relate to which insurance contracts.
- 34 The IASB staff considered that the disclosure requirements are adequate to provide useful information to users of financial statements on the related assets.

Input from ANC

- 35 In ANC's view, from an economic standpoint, there is an issue in considering that changes in discount rate have not yet been recognised on the asset side (measured at amortised cost of FVOCI), whereas the insurance liability would be recognised on transition at a current value, e.g. implicitly considering that past changes in discount rate have been recorded in the retained earnings.
- 36 ANC proposes that the fulfilment cash flows be discounted at the rate the entity is expecting to be committed to against its policyholders.

IFRS 17.C19: ...

¹ This is because the amount recognised in OCI cumulatively over the duration of the groups of contracts is required to total zero.

(b)(ii) for insurance contracts for which an entity will apply the methods of systematic allocation set out in paragraph B132 on the basis of the difference at transition date between the current rate and the rate based on which the entity expects to determine its commitment under the contract (crediting rate); otherwise on the basis that the assumptions that relate to financial risk that applied at the date of initial recognition are those that apply on the transition date, ie as nil;

Input from CFO Forum

- 37 As per the CFO Forum, the option to set OCI to nil under the fair value approach is not available to assets accounted at fair value through OCI.
- 38 The suggested wording changes proposed by the CFO Forum is as follows:

IFRS 17.C18: ...

(b)(i) as nil, unless (ii) applies; and

(ii) ~~for insurance contracts with direct participation features to which paragraph B134 applies~~, as equal to the cumulative amount recognised in other comprehensive income on the underlying ~~items~~ assets.

...

IFRS 17.C19: ...

(b) (ii) for insurance contracts for which an entity will apply the methods of systematic allocation set out in paragraph B132—on the basis that the assumptions that relate to financial risk that applied at the date of initial recognition are those that apply on the transition date, i.e. as nil unless paragraph C19(b)(iv) applies;

...

(b)(iv) ~~for insurance contracts with direct participation features to which paragraph B134 applies~~,—as equal to the cumulative amount recognised in other comprehensive income on the underlying ~~items~~ assets.

IFRS 17.C24: In applying the fair value approach ...

(c) ~~for insurance contracts with direct participation features to which paragraph B134 applies~~, — as equal to the cumulative amount recognised in other comprehensive income from the underlying ~~items~~ assets.

Input from UNESPA

- 39 Under MRA:
- (a) UNESPA proposes that the cumulative OCI at transition date should be consistent with the financial assets associated, for all the portfolios managed by cash flows matching (as per Solvency II), as long as they are classified in the FV-OCI portfolio.
- 40 Under FVA:
- (a) UNESPA proposes that the transition requirements provide a solution to the OCI for contracts under cash flow matching, and not only to the OCI of

contracts with participation features. A modification of IFRS 17, paragraph C24(c) would lead to a locked-in rate established at the date of transition for the fair value methodology equal to the rate of the underlying assets. This proposed approach would avoid the mismatch in the company equity.

- (b) The wording changes proposed for FVA is as follows:

IFRS 17.C24 (c): ~~for insurance contracts with direct participation features to which paragraph B134 applies~~ as equal to the cumulative amount recognised in other comprehensive income from the underlying assets.

- 41 Further simplifications are necessary. In particular:

- (a) It could be permitted to estimate the future cash flows at the date of initial recognition as the amount of the future cash flows at the transition date without adjusting by cash flows known previous to the transition date, and to apply a retrospective calculation only when it is possible (for example, for estimating the IFRS 17 discount rate).
- (b) The cumulative OCI at transition date should be consistent with the financial assets associated, for all the portfolios managed by cash flows matching, as long as they are classified in the FV-OCI portfolio.

Issue 2 – Reinsurance

Issue 2A: Reinsurance contracts – Onerous underlying contracts that are profitable after reinsurance

Summary of IASB tentative decisions

- 42 The IASB tentatively decided to amend IFRS 17 to require an entity to recognise a gain in profit or loss when the entity recognises losses on onerous underlying insurance contracts, to the extent that a reinsurance contract held covers the losses of each contract on a proportionate basis.

Concerns raised

- 43 Prior to the above IASB tentative decisions, onerous contracts issued by the cedant were immediately recognised as a loss in profit or loss, whereas for the reinsurance contract held by the cedant, any net cost or gain was recognised over the coverage period. Preparers have indicated that this IFRS 17 requirement gives rise to accounting mismatches.
- 44 A concern has arisen regarding the application of IFRS 17 to non-proportionate reinsurance.

IASB staff's reasoning for recommending an amendment to IFRS 17

January 2019 IASB staff papers 2B and 2C

- 45 The IASB staff thought the amendment would:
- (a) Avoid significant loss of useful information relative to that which would be provided by IFRS 17 for users of financial statements. The accounting for the underlying insurance contracts issued would be unaffected. The accounting for the reinsurance contracts held would change but IFRS 17 already provides an exception to the general requirements for reinsurance contracts held to avoid some accounting mismatches. This possible amendment would expand the scope of the existing exception.
 - (b) Not be contrary to the general principle in IFRS Standards that gains should not be recognised before service is provided. The IASB staff thought that this possible amendment would not result in an overall gain being recognised in profit or loss because a gain on the reinsurance contract held would only be recognised to the extent that the reinsurance contract held covers a loss that is also recognised in profit or loss at the same time.
- 46 The IASB staff observed that exceptions, by nature, add complexity. However, in this circumstance, expanding the existing exception could reduce complexity in applying the requirements in IFRS 17 because it would introduce consistency between the accounting treatment relating to the initial recognition of underlying onerous contracts and adverse changes in underlying onerous contracts subsequently. By eliminating accounting mismatches, it could also reduce complexity for users in understanding the accounting.
- 47 The IASB staff thought that this possible amendment might disrupt implementation for entities that have already begun to develop their systems. However, the IASB staff thought that the disruption could be justified given stakeholder feedback about the likely significant impact of the accounting mismatch which some stakeholders suggest reduces the usefulness of the information provided by IFRS 17.

Input from ANC

- 48 In ANC's view, proportional and non-proportional reinsurance treaties are conceptually similar. They are both risk mitigation instruments comparable to derivatives, whereas proportional reinsurance could be assimilated to a swap

(exchange of cash-flows) and non-proportional reinsurance could be assimilated to an option (no cash-flows until the strike is reached).

- 49 The ANC suggests a continuous symmetry in the accounting treatment of reinsurance contract held and the underlying insurance contracts issued and no distinction between proportional and non-proportional reinsurance treaties.

IFRS 17.66: Instead of applying paragraph 44, an entity shall measure the contractual service margin at the end of the reporting period for a group of reinsurance contracts held as the carrying amount determined at the start of the reporting period, adjusted for:

(a) the effect of any new contracts added to the group (see paragraph 28). Where newly issued insurance contracts are onerous, the entity shall recognise any net gain on purchasing the group of reinsurance held immediately in profit or loss to the extent the gain relates to losses on the group of underlying insurance contracts that are recognised in profit or loss;

...

Input from CFO Forum

- 50 In the CFO Forum's view, for onerous contracts at inception, recognise a gain on proportionate reinsurance to the extent reinsurance covers the loss.

- 51 The CFO Forum proposes solutions as follows:

Mismatch at initial recognition

- 52 Amend IFRS 17.65 as follows:

IFRS 17.65(c): Only for groups of insurance contracts being reinsured on a proportionate basis, at inception of the reinsurance contract:

- (i) a proportionate share of the loss component for the group of underlying insurance contracts (IFRS 17.47) shall be replaced by a negative contractual service margin representing the reinsurer's share in the underlying contracts. This shall only apply if the reinsurance contract held is recognised prior to or at the same time as the underlying insurance contracts.
- (ii) a proportionate share of the contractual service margin for the group of underlying insurance contracts (IFRS 17.38) shall be released representing the reinsurer's share in the underlying contracts, after deducting net costs (IFRS 17.65b) resulting from these reinsurance contracts held.

- 53 Regarding subsequent measurement of the underlying direct contracts reinsured in accordance with IFRS 17.65(c), IFRS 17.66 needs to be extended as follows:

IFRS 17.66A: For insurance contracts reinsured according to IFRS 17.65(c)(i) the following applies.

- (i) The carrying amount of the negative contractual service margin shall be adjusted for any changes in fulfilment cash flows relating to future service, notwithstanding IFRS 17.66.
- (ii) The amount recognised in profit or loss because of the transfer of services in the period determined by the allocation of the contractual service margin remaining at the end of the reporting period shall be presented in accordance with IFRS 17.84 and shall not change insurance revenue.

- (iii) If the conditions of IFRS 17.65(c) cease to exist as either the reinsurance contracts held or the underlying insurance contracts are derecognised, IFRS 17.76 shall be applied accordingly.

54 Similarly, IFRS 17.69 needs to be extended as follows:

IFRS 17.69A: For insurance contracts under the scope of IFRS 17.65(c), IFRS 17.65(c) and IFRS 17.66A are applied consistently leading to an adjustment of the liability for remaining coverage when the entity expects not to differ materially from a comparable adjustment of the contractual service margin.

Mismatch in projected fulfilment cash flows of underlying contracts and reinsurance held

55 IFRS 17.62(a) should read:

if the reinsurance contracts held provide proportionate coverage—at the beginning of the coverage period of the group of reinsurance contracts held or at the initial recognition of ~~any underlying contract~~ the underlying contracts, whichever is the later; and

56 Furthermore, IFRS 17.BC305(a) should read:

when the group of reinsurance contracts held covers the loss of a group of insurance contracts on a proportionate basis, the group of reinsurance contracts held is recognised at the later of the beginning of the coverage period of the group of reinsurance contracts held or the initial recognition of ~~any the~~ underlying contracts.

This means that the entity will ~~not recognise the group of reinsurance contracts until it has recognised at least one of the underlying contracts~~ only recognise the group of reinsurance contracts held to the extent that the underlying direct contracts are already recognised.

Retroactive reinsurance

57 IFRS 17.BC312 should be amended as follows:

The Board also decided that the net expense of purchasing reinsurance should be recognised over the coverage period as services are received unless the reinsurance covers events that have already occurred. For such reinsurance contracts held, the Board concluded that entities should recognise the whole of the net expense at initial recognition, to be consistent with the treatment of the net expense of purchasing reinsurance before an insured event has occurred. ~~If, and only if, the insured event that triggers future cash outflows has already occurred, the corresponding net costs shall be recognised at initial recognition.~~ The Board acknowledged that this approach does not treat the coverage period of the reinsurance contract consistently with the view that for some insurance contracts the insured event is the discovery of a loss during the term of the contract, if that loss arises from an event that had occurred before the inception of the contract. However, the Board concluded that consistency of the treatment of the net expense across all reinsurance contracts held would result in more relevant information.

Issue 2B: Reinsurance contracts - contract boundary

Summary of IASB tentative decisions

- 58 An entity applies the contract boundary requirements in paragraph 34 of IFRS 17 to the insurance contracts it issues and the reinsurance contracts it holds. That is:
- (a) the cash flows within the boundary of an insurance contract issued arise from the entity's substantive rights and substantive obligations as the issuer of that contract. These include the substantive right to receive amounts from the policyholder and the substantive obligation to provide services to the policyholder.
 - (b) the cash flows within the boundary of a reinsurance contract held arise from the entity's substantive rights and substantive obligations as the holder of that contract. These include the substantive right to receive services from the reinsurer and the substantive obligation to pay amounts to the reinsurer.
- 59 Therefore, if an entity has a substantive right to receive services from the reinsurer relating to underlying contracts that are expected to be issued in the future, cash flows within the boundary of the reinsurance contract held will include cash flows relating to those future underlying contracts. However, cash flows within the boundary of the underlying contract issued do not include these contracts expected to be issued in the future.
- 60 The IASB tentatively decided not to amend this IFRS 17 requirement.

Concerns raised

- 61 Some stakeholders are concerned that the requirement is unduly complex, will create a gross up for reinsurance coverage when the direct contracts have not yet been recognised, creating a mismatch, and they think the CSM will be recognised in an inconsistent manner as compared to the direct contract CSM.

IASB staff's reasoning for not recommending an amendment to IFRS 17

December 2018 IASB staff paper 2E

- 62 The IASB staff thought that modifying the contract boundary requirements in IFRS 17 for reinsurance contracts held was not justified. In particular, the IASB staff thought that modifying the IFRS 17 contract boundary requirements for reinsurance contracts held as proposed by stakeholders would result in a significant loss of useful information relative to that which would otherwise be provided by IFRS 17 for users of financial statements, for the following reasons:
- (a) The measurement of reinsurance contracts held would not fully reflect the entity's substantive right to receive services from the reinsurer. This would reduce the relevance and faithful representation of information in the financial statements.
 - (b) The proposed amendment would go against the fundamental principle in IFRS 17 that all future cash flows within the contract boundary are reflected in the measurement of an insurance contract.
 - (c) The proposed amendment would add complexity to the contract boundary requirements.

Input from ANC

- 63 In the ANC's view, recognising reinsurance contracts cash flows relating to insurance contracts not yet written provides information of little relevance whereas it raises significant costs due to the operational complexity to deal with such temporary estimates in the IT systems and their possible discounting effect and subsequent changes.

- 64 In addition, there is no reason for differentiating proportional from non-proportional reinsurance held even if the measurement of the latter may prove more complex.
- 65 The ANC suggest aligning the boundaries of insurance contracts held with those of recognised underlying contracts.

IFRS 17.63: ~~In applying *t*~~The measurement requirements of paragraphs 32–36 to reinsurance contracts held apply; to the extent that the underlying contracts are recognised. ~~also—measured applying those paragraphs, *t*~~The entity shall use consistent assumptions to measure the estimates of the present value of the future cash flows for the group of reinsurance contracts held and the estimates of the present value of the future cash flows for the group(s) of underlying insurance contracts. In addition, the entity shall include in the estimates of the present value of the future cash flows for the group of reinsurance contracts held the effect of any risk of non-performance by the issuer of the reinsurance contract, including the effects of collateral and losses from disputes.

Input from CFO Forum

- 66 In the CFO Forum's view, proportional reinsurance to include cash flows in respect of recognised underlying contracts.
- 67 The CFO Forum proposes to amend IFRS 17 as follows.
- 68 IFRS 17.62(a) should read:

if the reinsurance contracts held provide proportionate coverage—at the beginning of the coverage period of the group of reinsurance contracts held or at the initial recognition of ~~any underlying contract~~ the underlying contracts, whichever is the later; and

- 69 Furthermore, IFRS 17.BC305(a) should read:

when the group of reinsurance contracts held covers the loss of a group of insurance contracts on a proportionate basis, the group of reinsurance contracts held is recognised at the later of the beginning of the coverage period of the group of reinsurance contracts held or the initial recognition of ~~any~~ the underlying contracts. This means that the entity will ~~not recognise the group of reinsurance contracts until it has recognised at least one of the underlying contracts~~ only recognise the group of reinsurance contracts held to the extent that the underlying direct contracts are already recognised.

Issue 3 – Contractual service margin amortisation under the general model

Summary of IASB tentative decisions

- 70 The IASB tentatively decided to amend IFRS 17 so that in the general model the contractual service margin is recognised in profit or loss based on both insurance coverage and investment return service, if any. An investment return service exists only when an insurance contract includes an investment component.
- 71 An assessment of the relative weighting of the benefits provided by insurance coverage and investment return services is required and their pattern of delivery to be made on a systematic and rational basis.
- 72 The one-year eligibility criterion for the PAA should be assessed by considering insurance coverage and an investment return service, if any.

Concerns raised

- 73 Preparers have indicated that IFRS 17 requirements are only appropriate for certain types of contracts. CSM cannot be amortised over the period in which investment services are provided.

IASB staff's reasoning for recommending an amendment to IFRS 17

January 2019 IASB staff paper 2E

- 74 The IASB staff thought that there was a balance on whether including an investment return service when determining coverage units results in useful information because:
- (a) doing so could provide relevant information about the services the entity regards itself as providing to the policyholder; but
 - (b) doing so also introduces greater subjectivity and potentially less comparability between entities.
- 75 The IASB staff were persuaded by feedback that the benefits of paragraph 74(a) above outweigh the costs of paragraph 74(b) above because of the extensive disclosures required around the CSM. Including an investment return service in the determination of coverage units also could reduce the differences between the General Model and the Variable Fee Approach because it would reduce differences in the pattern of recognition of the CSM in profit or loss.
- 76 The IASB staff acknowledged that any change to the requirements on the recognition of the CSM in profit or loss have the potential to disrupt implementation and a large number of insurance contracts have investment components, so this change could have a widespread effect.
- 77 On the other hand, some entities may judge that investment return services should not be considered in the determination of coverage units. On balance, the IASB staff thought that the potential disruption could be justified given the stakeholder feedback about the lack of useful information given by the existing requirements in IFRS 17.

May 2019 IASB staff paper 2C on Sweep issues (Agenda paper 08-05)

- 78 The IASB staff paper proposed to further amend the standard to specify that an investment-return service exists in specified circumstances, sometimes without an investment component.
- 79 The IASB staff proposes that an investment-return service exists if, and only if:
- (a) there is an investment component, or the policyholder has a right to withdraw an amount;

- (b) the investment component or amount the policyholder has a right to withdraw is expected to include a positive investment return; and
- (c) the entity expects to perform investment activity to generate that positive investment return.

Input from ANC

- 80 In ANC's view, the allocation period of the CSM should be extended to the longest period including the investment phase. The latter may be prior (i.e. annuities) or after (life insurance with accumulated benefits) the insurance phase.
- 81 A suggestion has been made by the ANC to define investment return services and extend the definition of the coverage period as follows. They have indicated that if there is no definition of investment return service, there could be a risk of limiting that feature to certain types of contracts.

*IFRS 17.App A: **coverage period:** The period during which the entity provides coverage for insured events and/or investment-return services. This period includes the coverage that relates to all premiums within the boundary of the insurance contract.*

IFRS 17.App A: Investment-return service: is the service providing the policyholder with access to an investment return that would not otherwise be available to the policyholder because of the amounts invested, liquidity, complexity and expertise.

IFRS 17.B119: An amount of the contractual service margin for a group of insurance contracts is recognised in profit or loss in each period to reflect the services provided under the group of insurance contracts in that period (see paragraphs 44(e), 45(e) and 66(e)).

The amount is determined by:

(a) identifying the coverage units in the group. The number of coverage units in a group is the quantity of coverage for insured events and/or of investment-return services provided by the contracts in the group, determined by considering for each contract the quantity of the benefits provided under a contract and its expected coverage period duration.

Input from CFO Forum

- 82 In the CFO Forum's view, CSM amortisation should reflect insurance and investment activity, including related activities performed to deliver the insurance benefits.
- 83 The CFO Forum's proposed solution is to expand the 'coverage units' to include more than only insurance benefits. This is achieved by adding the proposed wording which would permit coverage units to include "related activities performed to deliver those benefits". This is intended to cover key non-insurance benefits such as investment activities. In order to narrow the scope of "related activities" two criteria were added:
- (a) that are required to be performed by law or regulation; or
 - (b) that were assumed in the pricing of the contract, and performance or non-performance of those activities would have had a significant impact on either the premium charged or benefits offered under the contract.
- 84 The suggested wording changes made by the CFO Forum are as follows:

“B119 An amount of the contractual service margin for a group of insurance contracts is recognised in profit or loss in each period to reflect the services provided under the group of insurance contracts in that period (see paragraphs 44(e), 45(e) and 66(e)).

The amount is determined by:

- (a) identifying the coverage units in the group. The number of coverage units in a group is the quantity of coverage provided by the contracts in the group, determined by considering for each contract both the quantity of the benefits provided and the related activities performed to deliver those benefits under a contract and its expected coverage duration. Related activities performed to deliver benefits are those:
 - (i) that are required to be performed by law or regulation; or
 - (ii) that were assumed in the pricing of the contract, and performance or non-performance of those activities would have had a significant impact on either the premium charged or benefits offered under the contract.

Appendix A

coverage period The period during which the entity provides coverage for insured events or investment related services. This period includes the coverage that relates to all premiums within the boundary of the insurance contract.

Basis of conclusions

BC 279 As discussed in paragraph BC21, the Board views the contractual service margin as depicting the unearned profit for coverage and other services provided over the coverage period. Insurance coverage is often the defining service provided by insurance contracts but may not be the sole driver in all cases, for example where there are significant activities performed by the entity to deliver those services or where the contract includes an investment related service. The Board noted that an entity provides this service over the whole of the coverage period, and not just when it incurs a claim. Consequently, IFRS 17 requires the contractual service margin to be recognised over the coverage period in a pattern that reflects the provision of services, including both the contractual benefits coverage and the activities performed to deliver those benefits as required by the contract. To achieve this, the contractual service margin for a group of insurance contracts remaining (before any allocation) at the end of the reporting period is allocated over the coverage provided in the current period and expected remaining future coverage, on the basis of coverage units, reflecting the expected duration, and quantity of benefits provided and the activities performed to deliver the benefits by of the contracts in the group. The Board considered whether:

- (a) the contractual service margin should be allocated based on the pattern of expected cash flows or on the change in the risk adjustment for non-financial risk caused by the release of risk. However, the Board decided the pattern of expected cash flows and the release of the risk adjustment for non-financial risk are not relevant factors in determining the satisfaction of the performance obligation of the entity. They are already included in the measurement of the fulfilment cash flows and do not need to be considered in the allocation of the contractual service margin. Hence, the Board concluded that coverage units better reflect the provision of insurance coverage.”

Issue 4 – Balance Sheet presentation

Issue 4A: Balance sheet presentation – asset/liability

Summary of the IASB tentative decisions

- 85 The IASB tentatively decided to amend the requirements in IFRS 17 so that the presentation of insurance contract assets and liabilities in the statement of financial position is determined using portfolios of insurance contracts rather than groups of insurance contracts.

Concerns raised

- 86 Some stakeholders stated that a significant implementation challenge arises because IFRS 17 requires entities to present groups of contracts that are in an asset position separately from groups of contracts in a liability position in the statement of financial position. This requirement results in the need for an entity to allocate premium cash flows and the liability for incurred claims to each group of insurance contracts to determine if that group of insurance contracts is in an asset or a liability position.
- 87 However, under many existing insurance accounting practices, insurance line items on the statement of financial position reflect a high level of aggregation (for example, at an entity level). For example, entities typically manage separately and at a high level of aggregation the information about premiums receivable and claims payable, and, therefore entities maintain information about cash receipts and payments only at this aggregated level. Similarly, entities typically record the liability for incurred claims only at an aggregated level.

IASB staff's reasoning for recommending an amendment to IFRS 17

- 88 The IASB staff thought that there was merit in providing a practical relief for entities by requiring entities to present insurance contracts at a higher level of aggregation than the group level.
- 89 The IASB staff recommended that entities are required to offset groups at the portfolio level for presentation purposes. This means that an entity would present separately assets and liabilities for insurance contracts subject to similar risks that are managed together. The IASB staff thought that offsetting at an entity level risks a greater loss of useful information.
- 90 Although it will be more costly to implement the requirements at a portfolio level when compared to an entity level, the IASB staff thought that any practical relief should limit the loss of information for users of financial statements.
- 91 The IASB staff considered the criteria set by the IASB at its October 2018 meeting and observed that:
- (a) although offsetting groups in the statement of financial position would result in a loss of useful information for users of financial statements, preliminary discussions with users of financial statements suggested that the loss of information could be regarded as acceptable when balanced against the significant cost relief for preparers of financial statements; and
 - (b) amending IFRS 17 in this way would not unduly disrupt implementation processes that are already under way — the IASB staff had been told that such an amendment might significantly reduce implementation costs and simplify implementation for many entities.
- 92 With respect to the suggestion to change the measurement requirements of the premium allocation approach, the IASB staff observed that the premium allocation approach does not result in revenue being determined on a cash flow basis because insurance revenue is recognised as services are provided and the receipt of

premiums does not affect the timing of revenue recognition. Also, to change the measurement requirements for the premium allocation approach (which is a simplification of the general model) would result in the premium allocation approach being a different measurement model.

Input from ANC

- 93 The ANC supports the proposed IASB amendment if the remaining operational issues are acceptable and refers to the example of commissions due to distribution agents that may relate to several portfolios.

Input from CFO Forum

- 94 The proposed solutions would also remove the requirement to separately report components of groups of contracts that are entirely in an asset position from those in a liability position.

- 95 IFRS 17.78 should be amended as follows: An entity shall present separately in the statement of financial position the carrying amount of **groups of:**

(a) the liability for remaining coverage and the liability for incurred claims for insurance contracts issued

(b) the expected recovery for remaining coverage and the recovery for incurred claims for reinsurance contracts held.

~~insurance contracts issued that are assets;~~

~~insurance contracts issued that are liabilities;~~

~~reinsurance contracts held that are assets; and~~

~~reinsurance contracts held that are liabilities~~

Issue 4B: Balance sheet presentation – receivables/payables

Summary of IASB tentative decisions

- 96 IFRS 17 requires presentation and disclosures of insurance contracts based on the net amounts of all the expected cash flows related to that portfolio of contracts. This means that several components that currently would be presented separately in the statement of financial position such as claims liabilities to be settled, unearned premiums, receivables/payables and policyholder loans would form part of the total insurance asset or liability. The same is true for reinsurance held or issued. As a result, these components are not separately presented in the statement of financial position under IFRS 17.
- 97 The IASB tentatively decided not to amend this IFRS 17 requirement.

Concerns raised

- 98 Insurers are concerned about the loss of information as the IFRS 17 requirements will remove items currently commonly presented on the face of the balance sheet such as premium receivables, policy loans and reinsurance collateral (funds withheld) as well as claims payable.
- 99 Others indicate that there would be significant costs required to their systems in order to meet the presentation requirements of IFRS 17.

IASB staff's reasoning for not recommending an amendment to IFRS 17

- 100 The IASB staff also thought that amending IFRS 17 to require the separate presentation of premiums receivable and claims payable from the insurance contract asset or liability could:
- (a) reduce comparability between entities — the IASB staff understood that systems currently used by entities recognise premiums receivable over different periods for different contracts. For example, one entity may only recognise premiums due in the current month that were not yet received, while another entity may reflect premiums due in the next 12 months in premiums receivable.
 - (b) unduly disrupt implementation already under way and risk undue delays in the effective date of IFRS 17 if the IASB were to develop a consistent definition of premiums receivable and claims payable.

- 101 The IASB staff noted that paragraph 55 of IAS 1 Presentation of Financial Statements permits the presentation of additional line items including by disaggregation of required line items, headings and subtotals in the statement of financial position when such presentation is relevant to an understanding of the entity's financial position.
- 102 The IASB agreed with the staff analysis and declined to amend IFRS 17.

Input from CFO Forum

- 103 The CFO Forum considers that these requirements, that impact only presentation, would require major system changes compared to the current approach, which is a well-established industry practice.
- 104 These changes will also lead to insurance receivables no longer being separately visible in the balance sheet, which is a deterioration in relevance of the financial statements for both life and general insurance insurers.
- 105 Companies have considered the implications for implementation and maintenance of systems for these requirements and found that the complexity and costs will very significant.
- 106 The CFO Forum indicated that IFRS 17.33 should be amended as follows:

An entity shall include in the measurement of a group of insurance contracts all the future cash flows *that are not due* within the boundary of each contract in the group [...]

107 For clarification, IFRS 17.B66 should be amended as follows:

[...] cash flows that are already due to be paid or received. Any rights or obligations to receive or to pay cash flows that are unconditional and due shall be accounted for in accordance with IFRS 9.

Input from ANC

108 The ANC considers it would be a loss of important information and therefore suggests the following amendments to IFRS 17:

IFRS 17.78: An entity shall present separately in the statement of financial position the carrying amount of ~~groups of~~:

- (a) ~~insurance contracts issued that are assets~~ premium receivables related to insurance contracts,
- (b) liabilities for remaining coverage (including contractual service margin) related to insurance contracts,
- (c) liabilities for incurred claims related to insurance contracts,
- (d) premium receivables (reinsurer) and payables (insurer) related to reinsurance contracts,
- (e) liabilities for remaining coverage (reinsurer) and asset for reinsurance contracts held (insurer) for reinsurance contracts,
- (f) liabilities for incurred claims (reinsurer) and assets for reinsurance contracts held (insurer) for reinsurance contracts,
- (g) liabilities for deposits received (insurer) and assets for deposits made (reinsurer) related to reinsurance contracts.
- ~~(b) insurance contracts issued that are;~~
- ~~(c) reinsurance contracts held that are assets;~~
- ~~(d) reinsurance contracts held that are liabilities.~~

70 Appendix A: Premium receivable: represents the unconditional right of the entity to consideration for the coverage to be provided. It takes into account the effective, not the theoretical, period before policyholder's rights to coverage actually lapse.

Issue 5 – Acquisition costs

Summary of IASB tentative decisions

- 109 The IASB tentatively decided to amend IFRS 17 in order to require an entity to
- (a) allocate to any expected contract renewals the part of the insurance acquisition cash flows that is directly attributable to newly issued contracts.
 - (b) recognise the insurance acquisition cash flows allocated to expected contract renewals as assets until the renewed contracts are recognised and to perform an impairment test on the assets.

Concerns raised

- 110 Acquisition cash flows on new business that is expected to renew cannot be allocated to future periods under IFRS 17 as issued. This results in incorrect matching of income and expenses over time and contracts being onerous in accounting (but not in economic reality).

IASB staff's reasoning for recommending an amendment to IFRS 17

- 111 In the light of the concerns expressed by stakeholders relating to the treatment of insurance acquisition cash flows, the IASB staff recommended that IFRS 17 should be amended as follows:
- (a) allocate to any anticipated contract renewals part of the insurance acquisition cash flows that are directly attributable to newly issued contracts. This would result in the entity recognising that part of the insurance acquisition cash flows as an asset applying paragraph 27 of IFRS 17 until the renewed contracts are recognised.
 - (b) assess the recoverability of that asset, based on the fulfilment cash flows of the related contracts, each period before the related contracts are recognised. Consistent with the unit of account in IFRS 17, the staff recommend this assessment is performed on a group of insurance contracts basis – i.e. an entity will assess whether the fulfilment cash flows of the related group of contracts, comprising of anticipated contract renewals, is sufficient to recover the asset.
 - (c) recognise a loss in profit or loss for any unrecoverable carrying amounts of the asset recognised by applying paragraph 27 of IFRS 17.
 - (d) recognise in profit or loss the reversal of some or all of such loss previously recognised when the impairment conditions no longer exist or have improved.

- 112 The IASB staff thinks that by amending IFRS 17 it could provide useful information for users of financial statements, without unacceptably reducing understandability of financial statements. The IASB staff also thinks that it might not unduly disrupt implementation processes that are already under way given it is based on the existing requirements of IFRS 17. The definition of insurance acquisition cash flows, the contract boundary requirements and the unit of account of IFRS 17 will not be affected by the amendment.

Input from CFO Forum

- 113 In the presentation to EFRAG TEG in March 2019 the issue was considered entirely solved without residual concerns.