International Accounting Standards Board
7 Westferry Circus, Canary Wharf
London E14 4HD
United Kingdom

XX October 2021

Dear Mr. Barckow,

Re: Initial application of IFRS 17 and IFRS 9 – Comparative Information

On behalf of the European Financial Reporting Advisory Group (EFRAG), I am writing to comment on the Exposure Draft *Initial Application of IFRS 17 and IFRS 9 – Comparative Information (Proposed amendment to IFRS 17)*, issued by the IASB on 28 July 2021 (the 'ED').

This letter is intended to contribute to the IASB's due process and does not necessarily indicate the conclusions that would be reached by EFRAG in its capacity as advisor to the European Commission on endorsement of definitive IFRS Standards in the European Union and European Economic Area.

EFRAG would like to express its appreciation for the IASB's swift response and delivery of the ED as this is an urgent issue. EFRAG welcomes and supports the IASB proposal as it will allow insurance entities to provide more useful information about their activities during the comparative period. The narrow-scope amendment addresses an important issue related to accounting mismatches between insurance contract liabilities and financial assets arising in the comparative information presented on initial application of IFRS 17 and IFRS 9. EFRAG commends the IASB for addressing most of the comments raised by European constituents in this area.

EFRAG agrees with the IASB proposals in the ED because this would:

- ease the operational challenges for those insurance entities who want to restate the comparative information under IFRS 9;
- alleviate accounting mismatches between financial assets and insurance contract liabilities in the comparative period for those insurance entities who do not intend to provide IFRS 9 comparatives; and
- address the impact of classification differences between financial assets derecognised in the comparative period (where IAS 39 will be applied) and other financial assets (where IFRS 9 will be applied)~~; and~~).
- ~~ease the operational challenges for those insurance entities who want to restate the comparative information under IFRS 9.~~

In addressing the above, the comparative information in the financial statements of insurance entities would be more comparable, thereby providing relevant information for users.

EFRAG notes that most insurance entities will first apply IFRS 17 together with IFRS 9 on 1 January 2023, and the IASB proposals will enable these insurance entities to improve the usefulness of the comparative information presented on initial application of IFRS 17 and IFRS 9.

However, there ~~is a~~are some remaining sources of concern that we would like the IASB to address when finalising the amendment.

Based on ~~preliminary~~ feedback, the difference in scope between the classification overlay and the temporary exemption from applying IFRS 9 may lead to operational complexity (using two general ledgers relating to IAS 39 and IFRS 9) and presentation inconsistencies in the consolidated financial statements ~~and unnecessary operational complexity.~~thereby putting in question the usefulness of a mixed approach within one reporting entity. In finalising the proposals, EFRAG recommends the IASB to align the scope of these two ~~scopes.~~ approaches.

Furthermore, EFRAG suggests that the IASB states explicitly that the classification overlay may be applied from a date pre-dating the publication of the ED or the final amendment.

EFRAG appreciates that the expected credit loss approach of IFRS 9 is not required to be applied when using the overlay approach. Nevertheless, we suggest clarifying the wording to make this clearer by stating that the expected credit loss requirements in IFRS 9 are permitted but not required to be applied.

EFRAG's detailed comments and responses to the questions in the ED are set out in the Appendix.

If you would like to discuss our comments further, please do not hesitate to contact Didier Andries or me.

Yours sincerely,

Jean-Paul Gauzès

President of the EFRAG Board

Appendix – EFRAG's response to the ED Initial Application of IFRS 17 and IFRS 9 – Comparative Information

~~***Notes to Constituents***~~

~~*Description of the issue*~~

~~1 Many insurance entities will first apply IFRS 9 and IFRS 17 at the same time on or after 1 January 2023. The transition requirements in the two Standards apply at different dates:~~

~~(a) The IFRS 9 transition requirements apply on the date of initial application (i.e., 1 January 2023 for many insurance entities); and~~

~~(b) The IFRS 17 transition requirements apply on the transition date, being the beginning of the previous annual reporting period (i.e., 1 January 2022 for many insurance entities), or earlier if the entity voluntarily - or as imposed by regulatory filing requirements (such as the SEC requirements) - restates more than one year of comparative information.~~

~~2 This difference in the transition requirements will result in the following one-time classification differences in the comparative information presented[1] on initial application of IFRS 17 and IFRS 9 by some insurance entities:~~

~~(a) Significant accounting mismatches between insurance contract liabilities measured at current value and some related financial assets measured at amortised cost.~~

~~(b) If the entity chooses to restate comparative information for IFRS 9, classification differences between financial assets derecognised in 2022 and 2021 (to which IAS 39 will apply) and other financial assets (to which IFRS°9 will apply).~~

~~3 In addition to these classification differences, some insurance entities also highlighted operational challenges if the entity chooses to restate comparative information for IFRS 9. Those challenges will arise because the entity will not know to which financial assets IFRS 9 does and does not apply to in the comparative information until the end of 2022 (i.e., once the entity knows which assets have been derecognised in 2022 and 2021).~~

~~*Previous approach by the IASB*~~

~~4 During the *Amendments to IFRS 17* project (2019-2020) some stakeholders asked the IASB to amend IFRS 9 so that insurance entities could apply IFRS 9 from the transition date of IFRS 17 (i.e., 1 January 2022) rather than from the date of initial application (i.e., 1 January 2023).~~

~~5 The IASB acknowledged, both when it developed IFRS 17 and again in the *Amendments to IFRS 17* project, that the transition requirements of IFRS 9 and IFRS 17 differ as a result of the different circumstances that applied[2]. The IASB concluded that amending the date at which insurance entities apply the transition requirements in IFRS 9 would have been a significant change. In the IASB's view, it had not received evidence that suggested that such an amendment was necessary. As such, the IASB did not amend IFRS 9 nor IFRS 17 in response to the previous feedback.~~

~~[1] For those companies that present more than one period of comparative information under IFRS 17, the comparative periods may include 2021.~~

~~[2] The IFRS 9 transition requirements were determined as a simplification to the first-time adoption for the banking industry, as the preparers in that industry indicated that they would not be able to restate comparatives.~~

~~*Previous EFRAG response to transition related issues*~~

~~6 EFRAG acknowledged in its Final Endorsement Advice, dated 31 March 2021, the operational burden that can be caused by applying in the comparative period both IFRS 9 and IAS 39 (the latter to be applied to assets that have already been derecognised) together.~~

~~*Summary of the ED*~~

~~7 The proposed amendment to IFRS 17 would permit an entity to apply the classification overlay when it first applies IFRS 17 and IFRS 9 at the same time. The classification overlay relates only to presentation of comparative information.~~

~~8 An entity:~~

~~(a) shall not apply the classification overlay to financial assets that are held in respect of an activity that is unconnected with contracts within the scope of IFRS 17 (e.g., financial assets that are not eligible for the classification overlay are those held for banking activities) (paragraphs C28E(a) and BC19 of the ED);~~

~~(b) shall use reasonable and supportable information available at transition date to determine how the entity expects that financial asset to be classified on initial application of IFRS 9 (paragraph C28B and BC12-BC16 of the ED);~~

~~(c) is not required to apply the impairment requirements in Section 5.5 of IFRS 9 (paragraph C28C and BC15 of the ED);~~

~~(d) would not apply comparative information for reporting periods prior to transition date of IFRS 17 (paragraph C28E(b) and BC20-BC21 of the ED);~~

~~(e) would apply the classification overlay optionally on an instrument-by-instrument basis (paragraphs C28A and BC17-BC18 of the ED).~~

~~9 The classification overlay would be available to both:~~

~~(a) entities that restate comparative information applying IFRS 9 for financial assets derecognised in the comparative period; and~~

~~(b) entities that do not restate comparative information applying IFRS 9.~~

~~In both cases, the classification overlay is applicable to financial assets held in respect of an activity that is connected with contracts within the scope of IFRS 17 (BC11 of the ED).~~

Question 1

Do you agree with the proposed amendment in this Exposure Draft? Why or why not? If not, what alternative do you propose and why?

EFRAG's response

EFRAG welcomes the rapid response by the IASB to an important and urgent issue identified by the insurance industry.

EFRAG welcomes and supports the IASB proposal as it will allow insurance entities to provide more useful information about their activities during the comparative period. EFRAG commends the IASB for addressing most of the comments raised by European constituents in this area. In particular, EFRAG notes that entities that apply the classification overlay can, but are not required to, apply the ~~impairment requirements~~ECL approach of IFRS 9. EFRAG also notes that the clarification not to apply the classification overlay to comparative information for reporting periods before the transition date of IFRS 17, is very helpful to address the uncertainties raised in this regard.

Based on ~~preliminary~~ feedback, the difference in scope between the classification overlay and the temporary exemption from applying IFRS 9 may lead to ~~inconsistencies in the consolidated financial statements and unnecessary~~ operational complexity (using two general ledgers relating to IAS 39 and IFRS 9~~).~~) and presentation inconsistencies in the consolidated financial statements thereby putting in question the usefulness of a mixed approach within one reporting entity. In finalising the proposals, EFRAG recommends to the IASB to align the scope of these two ~~scopes~~approaches.

Furthermore, EFRAG suggests that the IASB states explicitly that the classification overlay may be applied from a date pre-dating the publication of the ED or the final amendment.

~~10~~1 EFRAG welcomes the IASB's quick response to the issue as identified by the insurance industry. EFRAG notes that the proposals are intended to:

(a) alleviate the burden with respect to restating comparatives under IFRS 9;

~~(a)~~(b) reduce accounting mismatches for those insurance entities who do not intend to restate the comparative information under IFRS 9; and

~~(b)~~(c) reduce accounting mismatches relating to financial assets derecognised in the comparative period for those who do intend to restate comparative information under IFRS 9~~; and~~.

~~(c) alleviate the burden with respect to restating comparatives under IFRS 9.~~

~~11~~2 For these reasons, EFRAG supports the IASB proposal in the ED. EFRAG also compliments the IASB for addressing most of the issues raised by European constituents regarding this IASB proposal. In particular, the issues relating to the application of expected credit loss to derecognised assets and two-year comparatives (further details are provided below).

Use of IAS 39 for financial assets derecognised in comparative period

~~12~~3 EFRAG notes that the requirement to use IAS 39 to account for items derecognised during the comparative period affects all aspects of the financial statements. EFRAG also understands that at least some insurance entities consider that they would need to provide extensive supplementary information to assist users of financial statements to understand the 'actual' comparative information.

~~13~~4 Therefore, EFRAG supports the proposals and notes that the proposed amendments would improve comparability of the information provided both year on year but also between the assets and the insurance liabilities they relate to. This would enable users to understand better the statement of financial position. Therefore, this proposed amendment would result in more relevant information and would reduce the need for supplementary information in this regard.

IFRS 9 transition rules being operationally burdensome

~~14~~5 ~~Some~~The European insurance ~~entities~~industry associations have ~~indicated~~informed EFRAG that the existing IFRS~~-~~ 9 transition requirements are operationally burdensome and may constitute a significant part of the IFRS 9 implementation costs. EFRAG understands that the operational burden may become an obstacle to the voluntary presentation of comparative information under IFRS 9.

~~15~~6 Furthermore, some indicated that the current transitional requirements in IFRS 9 necessitates entities to use data that come from two different accounting ledgers and pointed out that running two different ledgers in parallel is costly and technically challenging. This would disincentivise for example, companies from restating comparative information, with a negative impact on comparability.

~~16~~7 EFRAG acknowledges the operational burden related to the current transition requirements and also notes the increase in usefulness of the information resulting from the proposed amendments. Hence, EFRAG welcomes the IASB's suggestion to address accounting mismatches and implementation challenges through a classification overlay.

Application of expected credit loss

~~17~~8 ~~Some~~The European insurance ~~entities~~industry associations have ~~noted~~informed EFRAG that the transitional requirements of IFRS 9 mean that the requirements regarding expected credit loss cannot be applied to the financial assets derecognised during the comparative period. This would not impact the net profit or loss but the split between the profit on disposal and the amounts recognised in profit or loss relating to provision for impairment. This may not be material, but the effort involved to prove that it is not material is of concern. Furthermore, the efforts involved with applying IAS 39 to these items would mean the same difficulties as previously indicated.

~~18~~9 Therefore, EFRAG welcomes the proposal that in applying the classification overlay, entities can, but are not required to, apply the impairment requirements in Section 5.5. of IFRS 9. This will allow insurance entities that are sufficiently advanced in their implementation to apply the impairment requirements while those that are not sufficiently advanced are not obliged to do so but can still benefit from applying the classification overlay. ~~EFRAG is unclear whether the application of the impairment requirements is an accounting policy which is to be applied consistently or is eligible on an instrument-by-instrument basis and would welcome a clarification on this.~~We suggest clarifying the wording by stating that the application of the ECL approach in Section 5.5 of IFRS 9 is permitted but not required to apply.

~~*Comparative period opening balance sheet concerns*~~

~~19 Some insurance entities have noted that even with the classification overlay, they would be unable to finalise their opening balance sheet as at 1 January 2022 until 31 December 2022 (as only at the end of the year, the assets derecognised in the period would be known). This would mean that, in practice, they would not be able to provide provisional IFRS 17 and IFRS 9 information during 2022 nor to restate the IFRS 9 information which may be negatively perceived by investors.~~

~~20 In EFRAG's view, applying the IFRS 9 expected credit loss requirement as said above would also help address this concern.~~

10 Also, EFRAG understands that the optional application of the ECL would be consistent with the classification overlay, i.e. available on an instrument-by-instrument basis. We also suggest clarifying that the choice is on an instrument-by-instrument basis.

11 EFRAG also considers that the IAS 39 impairment requirements would apply in the absence of the IFRS 9 requirements, but such a clarification may be useful.

Scope of the classification overlay versus the temporary exemption from applying IFRS 9

~~21~~12 ~~Some~~Most insurance entities have noted the scope of the classification overlay is different to that of the temporary exemption from applying IFRS 9 currently in IFRS 4 paragraphs 20A and 20B.

~~22~~13 EFRAG notes the scope of the classification overlay and the temporary exemption from applying IFRS 9 are as follows:

IASB Scope classification overlay	**IASB scope temporary exemption from applying IFRS 9**
Instrument by instrument basis	Reporting entity level

Financial assets that are held in respect of an activity that is not unconnected with contracts within the scope of IFRS 17	All financial assets and financial liabilities, subject to an insurance entity's activities being predominantly connected to insurance (> 80% and no significant activity unconnected to insurance)

14 ~~On the basis of cost/benefit considerations, ~~EFRAG ~~recommends~~is of the ~~IASB in finalising the proposals, to align~~view that the scope of the classification overlay and the temporary exemption from applying IFRS~~-~~ 9~~, in order to avoid operational complexity (~~ should be aligned for the following reasons:

(a) Cost-benefit reasons because the existing IFRS 9 transition requirements would be applied to assets that meet the IFRS 9 temporary exemption criteria but not the classification criteria. Also, it would require using two general ledgers relating to IAS 39 and IFRS 9~~). As a result, EFRAG also recommends the deletion of the example in paragraph BC19 of ~~, resulting in operational complexity.

~~23~~ The proposed ~~amendment prohibition.~~

(b) ~~EFRAG understands that the difference in scope leads to operational complexity and~~approach results in inconsistencies in presentation for those financial assets that relate to the insignificant banking or asset management activities of a predominant insurance entity~~.~~ (where IAS 39 is applied) compared to financial assets under the classification overlay (where IFRS 9 is applied). Therefore, EFRAG questions the usefulness of the resulting mixed approach (same instruments measured according to IAS 39 or IFRS 9 in different segments within one reporting entity).

(c) In addition, EFRAG is of the view that~~ for predominant insurance entities,~~ it is important for users of financial statements to be able to have comparable information within the population of those predominantly insurance entities.

(d) The IASB, in BC19 of the ED, explains that entities will be familiar with this concept because it is also required by paragraph C29(a) of IFRS 17. EFRAG notes, however, that that concept applies in very different circumstances, i.e., when IFRS 9 has been applied before IFRS 17.

15 On the basis of the reasons as described above, EFRAG recommends to the IASB in finalising the proposals, to align the scope of the classification overlay and the temporary exemption from applying IFRS 9, in order to avoid operational complexity, for cost-benefit reasons and also in order to provide more useful information. As a result, EFRAG also recommends the deletion of paragraph BC19 of the proposed amendment prohibition.

~~24~~16 EFRAG also suggests that the IASB deletes paragraph C28E(a) to ensure that the overlay could be applied to all financial assets by entities applying the temporary exemption as implied by the words in C28A ("that first applies IFRS 17 and IFRS 9 at the same time is permitted to apply the classification overlay").

~~25~~17 For financial liabilities within the scope of IAS 39/IFRS 9 (i.e., not relating to insurance contracts), the issue is not expected to be practically significant as it would result in the same classification and measurement under either standard.

~~**Note to constituents: Temporary exemption from applying IFRS 9: situation of financial conglomerates in Europe**~~

~~26 EFRAG notes the specific situation of financial conglomerates who, as part of the European top-up, benefit from an extension of the temporary exemption for their insurance activities. While we understand that this situation creates its own uncertainties [how to separate assets that relate to insurance liabilities from those relating to banking activities and transfers between those, timing needed for the~~

~~endorsement process for an additional top-up], EFRAG considers these are not part of its comment letter which is to be addressed to the IASB.~~

~~Note to constituents: Two years of comparatives~~

~~27 EFRAG notes that when presenting audited financial statements, foreign private SEC registrants[3] are required to present two-years of balance sheets and three years of the statement of comprehensive income[4] (first-time adopters of IFRS may file two years of information).~~

~~28 EFRAG welcomes and agrees with the IASB's decision to include more than one comparative period in the amendment as long as IFRS 17 is also restated but notes that the risk of using hindsight may exist for these periods. EFRAG notes, that the IASB considered the risk of hindsight and indicated that an entity would need to begin collecting relevant information from the transition date of IFRS 17 to apply the classification overlay without the use of hindsight (paragraph BC21 of the ED).~~

~~29 Other than SEC registrants, some preparers currently present two years of comparative information and the question arises if an entity needs to restate two years of comparative information of IFRS 9, or whether restating only one year is sufficient if the entity presents one year of comparative information for IFRS 17. Restating two years of IFRS 17 information may be impracticable because the implementation of IFRS 17 is currently (during 2021) not yet finished and may thus lead to the use of hindsight later on.~~

~~2023~~	~~IFRS 9 applied~~	~~IFRS 17 applied~~
~~2022~~	~~IFRS 9 – restated comparatives~~	~~IFRS 17 – transition date~~
~~2021~~	~~IAS 39 – no restated comparatives~~	~~IFRS 4~~

~~30 The ED indicates that the classification overlay would be available only for comparative periods where information has been restated applying IFRS 17 (paragraphs C28E(b) and BC20 of the ED). Therefore, EFRAG notes that the classification overlay is not to be applied to comparative information for reporting periods before the transition date of IFRS17 if an entity does not restate IFRS 17 for those reporting periods. This resolves the uncertainty that was raised by some as described in paragraph 30 above.~~

~~Note to constituents: IFRS 4 Overlay vs IFRS 17 Classification overlay~~

~~31 As a recollection, IFRS 4, paragraph 35B notes that an insurance entity is permitted, but not required, to apply the overlay approach to designated financial assets. When doing so, the insurance entity shall reclassify between profit or loss and other comprehensive income an amount that results in the profit or loss at the end of the reporting period for the designated financial assets being the same as if the insurance entity had applied IAS°39 to the designated financial assets.~~

[3] ~~Note to constituents: this is a subset of the insurance entities in Europe that have to apply IFRS including IFRS 17.~~

[4] ~~https://www.sec.gov/corpfin/cf-manual/topic-6~~

~~32 Paragraph 35E states that a financial asset is eligible for designation for the overlay approach if, and only if, the following criteria are met:~~

~~(a) it is measured at fair value through profit or loss applying IFRS 9 but would not have been measured at fair value through profit or loss in its entirety applying IAS 39; and~~

~~(b) it is not held in respect of an activity that is unconnected with contracts within the scope of this IFRS. Examples of financial assets that would not be eligible for the overlay approach are those assets held in respect of banking activities or financial assets held in funds relating to investment contracts that are outside the scope of this IFRS.~~

~~*Comparison IFRS 4 overlay approach vs IFRS 17 classification overlay*~~

	~~**IFRS 4 Overlay approach**~~	~~**IFRS 17 Classification overlay**~~
~~IFRS 9 applied or not?~~	~~When applying the overlay approach, the insurance entity applies IFRS 9 but not IFRS 17~~	~~Insurance entity applies IFRS 17 but IFRS 9 is not applicable to the comparatives for specific items~~
~~Which financial assets applied?~~	~~Designated financial assets, i.e., assets must be measured at FVPL[5] under IFRS 9 when they would not have been so measured entirely under IAS 39. Also, qualifying assets must not be held in respect of an activity that is unconnected with contracts within the scope of IFRS 4.~~	~~Financial assets that are held in respect of an activity that is not unconnected with contracts within the scope of IFRS 17~~
~~Approach applies to recognised or derecognised financial assets?~~	~~Recognised financial assets~~	~~Derecognised (during comparative period) financial assets~~ ~~Recognised assets but comparative information is not restated for IFRS 9.~~

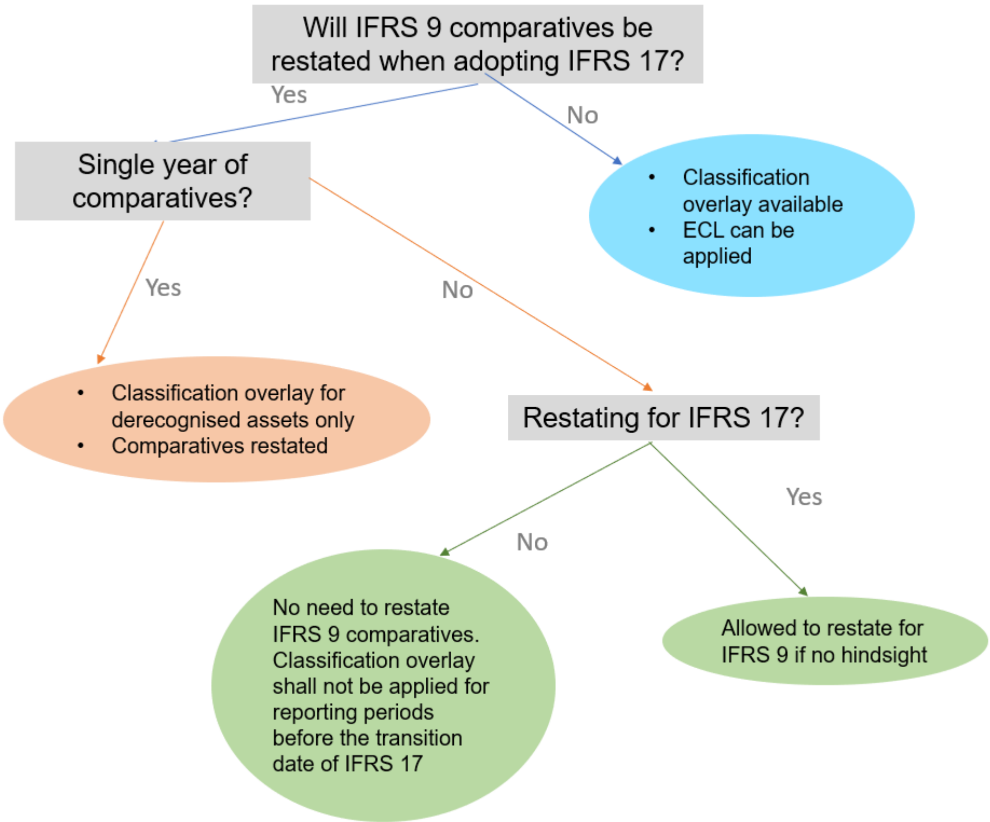
~~33 In analysing the IASB proposals, EFRAG has considered the interaction of the classification overlay with the overlay approach, if any, in IFRS 4 *Insurance Contracts*.~~

~~34 EFRAG understands that these approaches do not overlap as the IFRS 4 overlay approach is applied by those insurance entities that apply IFRS 9 before 2023 and the IFRS 17 classification overlay by those insurance entities that do not apply IFRS 9 before 2023. In addition, by accounting for the difference in financial asset carrying amounts, between the transition date to IFRS 17 and the previous carrying amount at that date, in opening retained earnings or other component of equity, the classification is aligned with insurance entities who apply the overlay approach.~~

[5] ~~Fair value through profit or loss~~

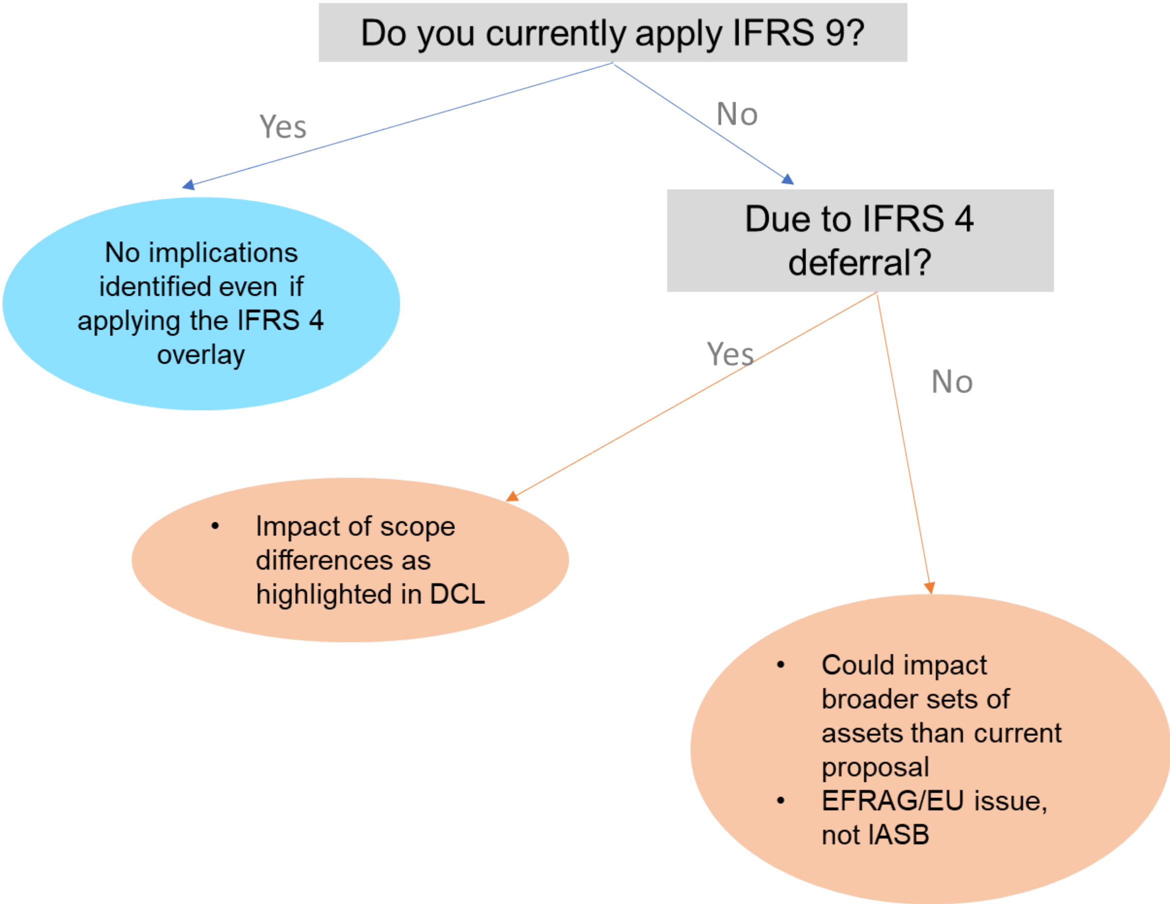
~~Annex 1: Decision tree re proposed classification overlay and related aspects – for those applying IAS 39 currently~~

~~1. This annex is intended to help constituents understand the possible scenarios and outcomes of the ED. Should there be any inconsistency between this annex and the ED, the latter takes precedence.~~



~~Annex 2: Decision tree re proposed classification overlay and related aspects – for those applying IFRS 9 currently~~

~~1. This annex is intended to help constituents understand the possible scenarios and outcomes of the ED. Should there be any inconsistency between this annex and the ED, the latter takes precedence.~~



Applicability of the classification overlay pre-dating the ED publication

18 EFRAG notes that the ED only addresses the use of hindsight in the Basis for Conclusions (BC21 and BC26), even though entities may elect to show 2 years of comparatives (i.e., 2021 and 2022) and the amendment will not be finalised until late 2021. In the absence of guidance, there may be questions as to the applicability of the classification overlay when the ED was only published at the end of July. One way to limit the use of hindsight is to require contemporaneous documentation at the date of transition but this may prove difficult here.

19 Therefore, EFRAG considers that the final amendment should state explicitly that the classification overlay may be applied from a date that pre-dates the publication of the ED or the final amendment.

Disclosures

20 EFRAG agrees with and welcomes the IASB proposal not to add detailed disclosures about applying the classification overlay approach. We support that disclosing the fact of using the classification overlay will also avoid operational burden for the entities.

21 While not putting into question the disclosure requirements under IFRS 9 at this stage, we note that our constituents consider that when applying the classification overlay, providing IFRS 9 transitional disclosures - which are required only as of 1

January 2023 as per paragraphs 42I, 42L and 42M - as from 1 January 2022 would provide useful and relevant information to users. However, the current requirement would mean providing IFRS 9 transition disclosures at 1January 2023 and this would create an additional burden, given the timing constraints in the context of the transition.

22 EFRAG suggests that the IASB considers the need of users to understand potential material differences between the application of the classification overlay as at 31 December 2022 and first time application of IFRS 9 on 1 January 2023.