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IFRS 17 Insurance Contracts – IFRS IC issue Cover Note

Objective

- 1 The objective of this session is for EFRAG TEG to discuss and recommend a draft comment letter ('DCL') to the EFRAG FR Board on the IFRS Interpretations Committee (IFRS IC) issue regarding profit recognition for annuity contracts under IFRS 17 *Insurance Contracts*.

Introduction and Background

- 2 At its meeting on 4 April 2022, the EFRAG FR Board:
 - (a) acknowledged that EFRAG does not, in general, issue comment letters to the IFRS IC because EFRAG does not comment on interpretations of standards. However, the EFRAG FR Board considered that this issue was different because the IFRS IC is deciding on a standard that is not yet effective; and
 - (b) agreed to issue a comment letter to the IASB regarding the IFRS IC tentative agenda decision highlighting the disruption to the implementation process rather than focusing on the conceptual analysis of Methods 1 and 2 (as described below in paragraph 8).
- 3 The following is the planned process to approve the comment letter:

DCL:	
EFRAG IAWG	7 April 2022
EFRAG FR TEG – Recommend DCL	12 April 2022
EFRAG FR Board – Approval of DCL	Written procedure (deadline 20 April)
Public consultation	Limited to 1 week (deadline of 29 April) – TO BE CONFIRMED
FCL:	
EFRAG IAWG	Written input at the same time as written procedure for EFRAG FR TEG (deadline 11 May)
EFRAG FR TEG – Recommend FCL	Written procedure (subject to no substantive changes from EFRAG IAWG) (deadline 11 May)
EFRAG FR Board - Approval of FCL	Written procedure (deadline 19 May)
IASB deadline for submission	23 May 2022

The IFRS IC Issue

- 4 The IFRS IC received a submission about the recognition of profit applying IFRS 17 *Insurance Contracts*. The submission asks how to determine the services provided under a group of immediate annuity contracts in each period and, more specifically,

how to determine the quantity of benefits¹ provided under each contract in the group. The submission refers to UK annuity contracts and the only service is insurance coverage for survival, i.e., the policyholder is entitled to a constant annual benefit starting from inception of the contract for as long as the policyholder survives.

- 5 In February 2022, the IFRS IC received an educational session on an overview of the IFRS 17 requirements.
- 6 In March 2022, the IFRS IC discussed the submission.

What is the issue?

- 7 The submission sets out two methods and asks whether both methods meet the principle in IFRS 17 of reflecting the insurance contract services provided under a group of insurance contracts.
- 8 The following are two methods whereby the quantity of the benefits provided in each period as being reflected by:
 - (a) Method 1 - the constant annual benefit, that is, the contractual service margin ('CSM') allocation is determined based on the periodic benefit payable in each period that services are provided; and
 - (b) Method 2 - the present value of the current and future benefits, that is, the CSM allocation is determined based on the value to the policyholder of surviving to the end of the period which includes both the annuity payment in the period as well as the continued access to receive a continuous stream of payments for as long as the policyholder survives.

IFRS IC's tentative decisions (March 2022)

- 9 The tentative agenda decisions can be found [here](#). The IFRS IC concurred with the IASB Staff's analysis and recommendation.
- 10 The IFRS IC observed that, under the contractual terms of the annuity contracts described in the request, an entity is obliged to pay a periodic from the start of the annuity period for each year of the policyholder's survival (the insured event). Survival in one year does not oblige the entity to pay amounts that compensate the policyholder for surviving in future years; that is, claim amounts payable to the policyholder in future years are contingent on the policyholder surviving in those future years.
- 11 The IFRS IC concluded that, in applying IFRS 17 to determine the quantity of the benefits of insurance coverage for survival provided under each annuity contract, a method based on:
 - (a) the amount of the annuity payment the policyholder is able to validly claim (Method 1) meets the principle in paragraph B119 of IFRS 17 of reflecting the insurance coverage provided in each period by:
 - (i) assigning a quantity of the benefits only to periods for which the entity has an obligation to investigate and pay valid claims for the insured event (survival of the policyholder); and
 - (ii) aligning the quantity of the benefits provided in a period with the amount the policyholder is able to validly claim in each period.
 - (b) the present value of expected future annuity payments (Method 2) does not meet the principle in paragraph B119 of IFRS 17 of reflecting the insurance coverage provided in each period because it would:

¹ The number of coverage units in a group is determined by considering for each contract the quantity of the benefits provided under the contract and its expected coverage period.

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- (i) assign a quantity of the benefits to periods for which the entity has no obligation to investigate and pay valid claims for the insured event (for example, to the deferral period of a deferred annuity contract); and
 - (ii) misrepresent the quantity of the benefits provided in a period by considering amounts the policyholder is able to claim and benefit from only in future periods.
- 12 The IFRS IC concluded that the principles and requirements in IFRS Accounting Standards provide an adequate basis for an issuer of a group of annuity contracts as described in the request to determine the amount of the contractual service margin to recognise in profit or loss in a period because of the transfer of insurance coverage for survival in that period. Consequently, the IFRS IC [decided] not to add a standard-setting project to the work plan.

Agenda Papers

- 13 In addition to this cover note, agenda paper 01-02 – *EFRAG Draft Comment Letter* – has been provided for the session.