GROUPEMENT FRANÇAIS DES BANCASSUREURS

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Paris, 2 September 2019

EFRAG's Draft Comment Letter on the IASB's ED/2019/4 Amendments to IFRS 17

Dear Mr Gauzès,

We respond to the EFRAG's Draft comment letter on IASB Exposure Draft Amendment to IFRS 17 (ED) on behalf of the Groupement français des Bancassureurs / French Bankinsurance Group, the professional association of bankinsurance (one of the three components of the French Insurance Federation) which represents 65% of life insurance gross written premiums in France and 61% of technical reserves, as well as a market share of nearly 20% on individual P&C insurance in 2017.

We thank the EFRAG for giving us the opportunity to respond to this draft comment letter and we would like to express our appreciation for the work performed by EFRAG on the concerns we (as most of the preparers) raised on IFRS 17.

In this respect, we welcome the decision of the IASB to reopen IFRS 17 to capture the concerns expressed by its stakeholders. However, if some proposed amendments are positive, others are too limited. Moreover, similarly to the French Insurance Federation (the FFA), we believe that some issues still remain to be solved, specifically the following topics.

Level of Aggregation

We consider that the annual cohort requirement for contracts eligible to the Variable Fee Approach will not appropriately model the legal and contractual terms and economics of French life insurance contracts with direct participation, as they share a significant part of returns on underlying items across generations, independently from their underwriting year. These types of contracts represent a large part of the bankinsurers' activities in France. With the concern to achieve a high-quality standard for insurance contracts, we believe that this requirement should be suppressed for these contracts. Otherwise, the allocation of the Contractual Service Margin by annual cohort to comply with IFRS 17 requirement will be costly, may not correctly reflect their economics and the way they are managed for legal and contractual purposes, and thus will be of little value for the users.

Transition

The modified retrospective approach remains unduly complex and rules based. It should be modified to become more principles based. Otherwise, entities will be forced to use the fair value approach, which may result in reduced comparability of information provided to users, as there is a widespread opinion that the Fair Value approach would result in a lower level of CSM at transition compared to the retrospective approaches.

We consider that the Fair Value approach should provide a level of opening CSM closer to the retrospective approaches and that the choice of transition methodology should not impact the future results and the financial communication in a so significant manner.

We also believe that transitional relief should be provided for risk mitigation (especially for reinsurance), and for past business combinations (due to the Fair Value issue mentioned above).

Finally, a solution to link OCI on assets and liabilities at transition should be found for contracts not eligible to the VFA, to avoid creating a mismatch in OCI and not to distort future performance.

Presentation

The exception to IAS 34 that exists in IFRS 17 should be removed. Recalculating the carrying amount of the contractual service margin on a year to date basis will result in entities treating accounting estimates made in previous interim financial statements similarly and ensure comparability among entities whatever the frequency in the reporting.

We consider that entities should be permitted to not present adjusted comparative information on initial application of IFRS 17, as it was authorized for the first application of IFRS 9. In addition to the specific issues raised by presented a comparative under IFRS 9, we consider that such an amendment will give stakeholders applying IFRS 17 for the first time the same relief that has been provided within IFRS 9. It will significantly facilitate the implementation efforts for many entities. At the same time, as it is an option, entities willing to present adjusted comparatives would be allowed to do it.

Other matter of attention

Whilst we agree with the objective of the VFA model to consider the interaction between assets and liabilities, we consider that under specific economic conditions, a current and prospective measurement model may not appropriately portray the mechanism of some long-term contracts. For valuation purposes, IFRS 17 requires using stochastic methods that capture a large number of scenarios, in order to measure the associated time value of financial options and guarantees (TVOG). Because the changes in the TVOG are recorded against the contractual service margin (CSM), it can represent a significant part of the variation of the CSM, all the more because the sensitivity of the TVOG is closely linked to the exposure to investments in equities.

Following the simulations reported to your attention in our response to the simplified case study in May 2018, we have performed some additional sensitivity analysis on equity exposure in central and stressed scenarios on an aggregated portfolio of 6 bankinsurance companies for which equity share represent around 12% of the underlying financial assets portfolio.

In stressed market conditions (for instance, durable low interest rates), the VFA model may not correctly reflect in the IFRS financial statements the annual performance of these contracts because the change in the value of the options and guarantees may drastically reduce (and even offset) the CSM although it is very unlikely that these options and guarantees may be paid to the policyholders, due to these stressed market conditions. As a result, companies may consider changing their investment policy to reduce their equities exposures, in order to limit the induced volatility and thus secure their IFRS financial performance to the detriment of their statutory results, which nevertheless remain the basis of policyholder's participation benefits and dividends payable to the shareholders.

Implementation date

Regarding the implementation date of IFRS 17, we welcome the proposed deferral of the effective date of IFRS 17 and IFRS 9 by one year. It recognises the importance of the linkage between these two standards on the insurance activities and the necessity to have a comprehensive approach.

However, there is still some uncertainty on the finalisation of the proposed IASB amendments due to the significance of the issues that have not yet been addressed (annual cohorts, transition and presentation).

As such, we consider that a one-year additional delay in the application of IFRS 17 (e.g 1st January 2023), together with that of IFRS 9 (and accordingly the European "Top-up" be extended), **is needed with a possible early application.**

Our detailed responses to the IASB on the Exposure Draft and our comments on EFRAG's draft comment letter to the IASB are contained in the attached appendix and are aligned with the response made by the French Insurance Federation.

If you have any questions regarding this submission, we would be pleased to discuss any of these points further with you. Please do not hesitate to contact us.

Yours sincerely,

Jean Vecchierini de Matra

General Delegate – Groupement Français des Bancassureurs

Appendix 1

Question 1—Scope exclusions—credit card contracts and loan contracts that meet the definition of an insurance contract (paragraphs 7(h), 8A, Appendix D and BC9–BC30)

(a) Paragraph 7(h) proposes that an entity would be required to exclude from the scope of IFRS 17 credit card contracts that meet the definition of an insurance contract if, and only if, the entity does not reflect an assessment of the insurance risk associated with an individual customer in setting the price of the contract with that customer.

Do you agree with the proposed amendment? Why or why not?

An entity shall not apply IFRS 17 to:

(h) *credit card contracts that meet the definition of an insurance contract if, and only if, the entity does not reflect an assessment of the insurance risk associated with an individual customer in setting the price of the contract with that customer (see IFRS 9 Financial Instruments).*

(b) If not excluded from the scope of IFRS 17 by paragraphs 7(a)–(h), paragraph 8A proposes that an entity would choose to apply IFRS 17 or IFRS 9 to contracts that meet the definition of an insurance contract but limit the compensation for insured events to the amount required to settle the policyholder's obligation created by the contract (for example, loans with death waivers). The entity would be required to make that choice for each portfolio of insurance contracts, and the choice for each portfolio would be irrevocable.

Do you agree with the proposed amendment? Why or why not?

Some contracts meet the definition of an insurance contract but limit the compensation for insured events to the amount required to settle the policyholder's obligation created by the contract (for example, loans with death waivers). If such contracts are not excluded from the scope of IFRS 17 by paragraphs 7(a)–(h), an entity shall choose to apply IFRS 17 or IFRS 9 to such contracts that it issues. The entity shall make that choice for each portfolio of insurance contracts, and the choice for each portfolio is irrevocable

Q1 (a) – Specific credit card contracts that meet the definition of an insurance contract

We agree with EFRAG's view on the proposed amendment.

As mentioned by the IASB staff, credit cards combine payment services with the provision of credit (AP 2D March 2019). Indeed, as credit cards, some payment card contracts also include insurance coverage with the same characteristics as those of the credit cards covered by the proposed amendment. As such, the rationale for changing the requirement of IFRS 17 applies also to such payment cards.

Therefore, we agree with EFRAG that payment card contracts that meet the definition of an insurance contract should also be excluded from IFRS 9, if, and only if, the entity does not reflect an assessment of the insurance risk associated with an individual customer in setting the price of the contract with that customer.

Q1 (b) – Loan contracts that meet the definition of an insurance contract

Not applicable to GFBA

Question 2—Expected recovery of insurance acquisition cash flows (paragraphs 28A–28D, 105A–105C, B35A–B35C and BC31–BC49)

Paragraphs 28A–28D and B35A–B35C propose that an entity:

(a) allocate, on a systematic and rational basis, insurance acquisition cash flows that are

directly attributable to a group of insurance contracts to that group and to any groups that include contracts that are expected to arise from renewals of the contracts in that group;

(b) recognise as an asset insurance acquisition cash flows paid before the group of insurance contracts to which they are allocated is recognised; and

(c) assess the recoverability of an asset for insurance acquisition cash flows if facts and circumstances indicate the asset may be impaired.

Paragraphs 105A–105C propose disclosures about such assets.

Do you agree with the proposed amendments? Why or why not?

We agree with EFRAG's view on the proposed amendment.

Regarding the question of the EFRAG about the definition of insurance contracts renewals, we note that contract renewals have not been defined in IFRS 15 (for example regarding the pattern of amortization of contract costs assets). Therefore, consistently with IFRS 15, we believe that IFRS 17 should remain principles based.

We believe there should not be significant divergent practices in this respect.

Question 3—Contractual service margin attributable to investment-return service and investment-related service (paragraphs 44–45, 109 and 117(c)(v), Appendix A, paragraphs B119–B119B and BC50–BC66)

(a) Paragraphs 44, B119–B119A and the definitions in Appendix A propose that an entity identify coverage units for insurance contracts without direct participation features considering the quantity of benefits and expected period of investment-return service, if any, in addition to insurance coverage.

Paragraph B119B specifies criteria for when contracts may provide an investment-return service.

Do you agree with the proposed amendment? Why or why not?

(b) Paragraphs 45, B119–B119A and the definitions in Appendix A clarify that an entity is required to identify coverage units for insurance contracts with direct participation features considering the quantity of benefits and expected period of both insurance coverage and investment-related service.

Do you agree with the proposed amendment? Why or why not?

(c) Paragraph 109 proposes that an entity disclose quantitative information about when the entity expects to recognise in profit or loss the contractual service margin remaining at the end of a reporting period. Paragraph 117(c)(v) proposes an entity disclose the approach used to determine the relative weighting of the benefits provided by insurance coverage and investment-return service or investment-related service.

Do you agree with the proposed disclosure requirements? Why or why not?

We agree with EFRAG's view on the proposed amendment.

Regarding EFRAG's question in §35, we share the view that the criteria chosen in the amendment may not cover all the types of contracts which provide in substance an investment-return service, because the qualification of investment-return service is linked to the existence of an investment component, or the right to withdraw an amount, or to transfer the contract to another insurer. However, this qualification may be too limitative for some French saving products related to retirement, as the right to withdraw an amount or to transfer can be in practice very limited. Considering the diversity in the legal or contractual frameworks across countries, we believe that a definition based on the

economical substance rather than on the legal form would eventually permit measuring and accounting in the same way all products that provide the same kind of service.

Regarding EFRAG's question to constituents (§36), we are not opposed to the quantitative disclosure on the expected recognition in profit or loss of the contractual service margin, unless this information is considered as highly sensitive.

Question 4—Reinsurance contracts held—recovery of losses on underlying insurance contracts (paragraphs 62, 66A–66B, B119C–B119F and BC67–BC90)

Paragraph 66A proposes that an entity adjust the contractual service margin of a group of reinsurance contracts held that provides proportionate coverage, and as a result recognize income, when the entity recognises a loss on initial recognition of an onerous group of underlying insurance contracts, or on addition of onerous contracts to that group. The amount of the adjustment and resulting income is determined by multiplying:

(a) the loss recognised on the group of underlying insurance contracts; and

(b) the fixed percentage of claims on the group of underlying contracts the entity has a right to recover from the group of reinsurance contracts held.

Do you agree with the proposed amendment? Why or why not ?

Reinsurance contracts held – recovery of losses on underlying contracts at initial recognition

We agree with EFRAG's view the proposed amendment.

However, we believe this amendment should be extended to "proportionate" contracts as defined by the IASB. "Other than proportionate" reinsurance contracts held (by opposition to proportionate reinsurance as defined by the IASB) are key elements in the risk management policies of insurers as they permit for example entities to transfer significant part of their risks to reinsurers. Therefore, in order to reflect appropriately the risk mitigation policies of insurance companies and avoid accounting mismatches, we believe that this amendment should be extended to surplus reinsurance treaties and "stop loss" or "excess loss" reinsurance treaties/programs based on the analysis of the contractual term of the reinsurance contract.

Also, as mentioned in ED BC213, the IASB Board "has already acknowledged that in some specific circumstances a reinsurance contract might meet the criteria in paragraph B101 of IFRS 17". We believe that the eligibility to VFA of reinsurance contracts held and issued should have been considered when the underlying insurance contracts are eligible to the VFA, and, more generally, where, under the terms of the treaty, the return of underlying items is shared between the direct insurer and the reinsurer. Such amendment would have permitted to better reflect the economics of the contract and avoid accounting mismatches.

Question 5—Presentation in the statement of financial position (paragraphs 78–79, 99, 132 and BC91–BC100)

The proposed amendment to paragraph 78 would require an entity to present separately in the statement of financial position the carrying amount of portfolios of insurance contracts issued that are assets and those that are liabilities. Applying the existing requirements, an entity would present the carrying amount of groups of insurance contracts issued that are assets and those that are liabilities. The amendment would also apply to portfolios of reinsurance contracts held that are assets and those that are liabilities.

Do you agree with the proposed amendment? Why or why not?

We agree with EFRAG's view on the proposed amendment.

> **Question 6—Applicability of the risk mitigation option (paragraphs B116 and BC101–BC109)**
>
> The proposed amendment to paragraph B116 would extend the risk mitigation option available when an entity uses derivatives to mitigate financial risk arising from insurance contracts with direct participation features. That option would apply in circumstances when an entity uses reinsurance contracts held to mitigate financial risk arising from insurance contracts with direct participation features.
>
> Do you agree with the proposed amendment? Why or why not?

We agree with EFRAG's view on the proposed amendment.

Regarding EFRAG's question, we are aware that non derivative instruments may be used by insurers in a hedging strategy clearly documented, and we believe it may be useful to extend the risk mitigation option to such instruments.

> **Question 7—Effective date of IFRS 17 and the IFRS 9 temporary exemption in IFRS 4 (paragraphs C1, [Draft] Amendments to IFRS 4 and BC110–BC118)**
>
> IFRS 17 is effective for annual reporting periods beginning on or after 1 January 2021. The amendments proposed in this Exposure Draft are such that they should not unduly disrupt implementation already under way or risk undue delays in the effective date.
>
> (a) The proposed amendment to paragraph C1 would defer the effective date of IFRS 17 by one year from annual reporting periods beginning on or after 1 January 2021 to annual reporting periods beginning on or after 1 January 2022.
>
> Do you agree with the proposed amendment? Why or why not?
>
> (b) The proposed amendment to paragraph 20A of IFRS 4 would extend the temporary exemption from IFRS 9 by one year so that an entity applying the exemption would be required to apply IFRS 9 for annual reporting periods beginning on or after 1 January 2022.
>
> Do you agree with the proposed amendment? Why or why not?

We agree with EFRAG's view on the proposed amendment.

There are still some uncertainties on the finalisation of the proposed IASB amendments due to the significance of the issues we have reported in our cover letter and that have not yet been addressed (annual cohorts, transition and presentation).

As such, we consider that a one-year additional delay in the application of IFRS 17, (e.g. 1st January 2023) together with that of IFRS 9, is needed with a possible early application for those entities that are furthest advanced in the implementation of IFRS 17.

> **Question 8—Transition modifications and reliefs (paragraphs C3(b), C5A, C9A, C22A and BC119–BC146)**
>
> (a) Paragraph C9A proposes an additional modification in the modified retrospective approach. The modification would require an entity, to the extent permitted by paragraph C8, to classify as a liability for incurred claims a liability for settlement of claims incurred before an insurance contract was acquired.

Paragraph C22A proposes that an entity applying the fair value approach could choose to classify such a liability as a liability for incurred claims.

Do you agree with the proposed amendments? Why or why not?

(b) The proposed amendment to paragraph C3(b) would permit an entity to apply the option in paragraph B115 prospectively from the transition date, rather than the date of initial application. The amendment proposes that to apply the option in paragraph B115 prospectively on or after the transition date, an entity would be required to designate risk mitigation relationships at or before the date it applies the option.

Do you agree with the proposed amendment? Why or why not?

(c) Paragraph C5A proposes that an entity that can apply IFRS 17 retrospectively to a group of insurance contracts be permitted to instead apply the fair value approach to that group if it meets specified criteria relating to risk mitigation.

Do you agree with the proposed amendment? Why or why not?

We agree with EFRAG's view on the proposed amendment.

Regarding EFRAG's question in §94, we would prefer a retrospective application of paragraph B115 instead of supporting the two consequential amendments induced by this non retrospective application. Indeed, this non retrospective application may lead to accounting mismatches in CSM and shareholder's equities.

Question 9—Minor amendments (BC147–BC163)

This Exposure Draft also proposes minor amendments (see paragraphs BC147–BC163 of the Basis for Conclusions).

Do you agree with the Board's proposals for each of the minor amendments described in this Exposure Draft? Why or why not?

We agree with the comments of EFRAG in its draft comment letter.

Furthermore, we support the topics raised by the EFRAG's questions in §99 to 105, but we have not assessed at this stage the potential consequences in term of costs or consistency.

Question 10—Terminology

This Exposure Draft proposes to add to Appendix A of IFRS 17 the definition 'insurance contract services' to be consistent with other proposed amendments in this Exposure Draft.

In the light of the proposed amendments in this Exposure Draft, the Board is considering whether to make a consequential change in terminology by amending the terms in IFRS 17 to replace 'coverage' with 'service' in the terms 'coverage units', 'coverage period' and 'liability for remaining coverage'. If that change is made, those terms would become 'service units', 'service period' and 'liability for remaining service', respectively,throughout IFRS 17.

Would you find this change in terminology helpful? Why or why not?

Regarding EFRAG's question in §110, we understand the rationale of that change in terminology. However, this change will imply for each constituent undue time to update their internal documentation.

Appendix 2 – Other comments on topics in EFRAG's September 2018 letter to the IASB that have not been addressed by the ED

Topic 1 - Annual cohorts

We agree with EFRAG's view on the annual cohorts topic.

We consider that the annual cohort requirement for contracts eligible to the Variable Fee Approach will not appropriately model the legal and contractual terms and economics of French life insurance contracts with direct participation, as they share a significant part of returns on underlying items across generations, independently from their underwriting year. These types of contracts represent a large part of the bankinsurers' activities in France. With the concern to achieve a high-quality standard for insurance contracts, we believe that this requirement should be suppressed for these contracts. Otherwise, the allocation of the Contractual Service Margin by annual cohort to comply with IFRS 17 requirement will be costly, may not correctly reflect their economics and the way they are managed for legal and contractual purposes, and thus will be of little value for the users.

Topic 2 - Transition: Modified retrospective approach and fair value approach

We agree with EFRAG's view on the transition topic.

The modified retrospective approach remains unduly complex and rules based. It should be modified to become more principles based. Otherwise, entities will be forced to use the fair value approach, which may result in reduced comparability of information provided to users, as there is a widespread opinion that the Fair Value approach would result in a lower level of CSM at transition compared to the retrospective approaches.

We consider that the Fair Value approach should better ensure the comparability of CSM at transition date with retrospective approaches, and should provide a level of opening CSM closer to the retrospective approaches, so that the choice of transition methodology should not impact the future results and the financial communication in a so significant manner.

We also believe that transitional relief should be provided for risk mitigation (especially for reinsurance), and for past business combinations (due to the Fair Value issue mentioned above).

Finally, a solution to link OCI on assets and liabilities at transition should be find for contracts not eligible to the VFA, to avoid creating a mismatch in OCI and not to distort future performance.

Topic 3 – Presentation

The exception to IAS 34 that exists in IFRS 17 should be removed. Recalculating the carrying amount of the contractual service margin on a year to date basis will result in entities treating accounting estimates made in previous interim financial statements similarly and ensure comparability among entities whatever the frequency in the reporting.

We consider that entities should be permitted to not present adjusted comparative information on initial application of IFRS 17, as it was authorized for the first application of IFRS 9. In addition to the specific issues raised by presented a comparative under IFRS 9, we consider that such an amendment will give stakeholders applying IFRS 17 for the first time the same relief that has been provided within IFRS 9. It will significantly facilitate the implementation efforts for many entities. At the same time, as it is an option, entities willing to present adjusted comparatives would be allowed to do it.

Topic 4 – Other matter of attention

Whilst we agree with the objective of the VFA model to consider the interaction between assets and liabilities, we consider that under specific economic conditions, a current and prospective

measurement model may not appropriately portray the mechanism of some long-term contracts. For valuation purposes, IFRS 17 requires using stochastic methods that capture a large number of scenarios, in order to measure the associated time value of financial options and guarantees (TVOG). Because the changes in the TVOG are recorded against the contractual service margin (CSM), it can represent a significant part of the variation of the CSM, all the more because the sensitivity of the TVOG is closely linked to the exposure to investments in equities.

Following the simulations reported to your attention in our response to the simplified case study in May 2018, we have performed some additional sensitivity analysis on equity exposure in central and stressed scenarios on an aggregated portfolio of 6 bankinsurance companies for which equity share represent around 12% of the underlying financial assets portfolio.

In stressed market conditions (for instance, durable low interest rates), the VFA model may not correctly reflect in the IFRS financial statements the annual performance of these contracts because the change in the value of the options and guarantees may drastically reduce (and even offset) the CSM although it is very unlikely that these options and guarantees may be paid to the policyholders, due to these stressed markets conditions. As a result, companies may consider changing their investment policy to reduce their equities exposures, in order to limit the induce volatility and thus secure their IFRS financial performance to the detriment of their statutory results, which nevertheless remain the basis of policyholder's participation benefits and dividends payable to the shareholders.