

EFRAG  
M. Jean-Paul Gauzès  
President of the EFRAG Board  
35 Square de Meeûs  
1000 Brussels  
Belgique

Paris, 2 septembre 2019

**EFRAG's draft comment letter in response to the IASB's Exposure Draft ED/2019/4 Amendments to IFRS 17**

Dear Jean-Paul Gauzès,

The *Institut des Actuaires* (French Institute of Actuaries) welcomes the EFRAG's invitation for comments on its draft comment letter in response to the IASB's Exposure Draft ED/2019/4 *Amendments to IFRS 17*.

Overall, the Institute of Actuaries welcomes the changes proposed by the IASB. Our comments are included in the first annex.

As you will read, we have some concerns about treatment of reinsurance which could be improved to better reflect economic features of such mechanisms.

Our major concerns if the subject of annual cohorts for contract grouping that has not been amended by the IASB. This is a crucial point, however, especially for the French life insurance contracts.

For contracts with cash-flows that affect or are affected by other contracts, under variable fee approach, the requirement of annual cohorts leads to a burdensome and artificial representation. A representation that is misleading for users, giving an illusion of precision.

On this point, for these contracts, we believe that an exception should be made. We detail proposals of disclosures with the aim of providing financial reporting users with relevant and useful information that is consistent with contractual and economic features of these contracts.

Our comments are detailed in the second annex.

We hope you find these comments useful. Do not hesitate to contact us if you wish to discuss them.

Yours sincerely,

David Dubois  
President

Pierre Théron  
Head of Accounting and Financial  
Reporting Commission

## Appendix 1: Responses to questions raised in the ED

Please find below our detailed comments on some questions raised by EFRAG's invitation to comment.

### **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?

### **Question to Constituents**

18. Insurance contract renewals are not a defined term which may lead to diversity in practice when allocating insurance acquisition cash flows. Do you consider that insurance contract renewals should be defined in order to achieve comparability and, if so, how would you define them?

We agree with the proposed amendments for the following reasons:

- i. They better depict the underlying profitability of the contracts in line with the current practices of commissioning;
- ii. They provide useful information to users of financial statements about the pattern of insurance acquisition cashflows.

We observe that the proposed amendment does not define "insurance contracts renewals". Nevertheless, we do not think the key issue to achieve comparability lies in defining renewals.

### **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?

### Questions to Constituents

35 EFRAG has been informed of possible fact patterns of deferred annuities for which there is no investment component as defined by the ED, nor a right to withdrawal; however, the insurance entity performs asset management activities, revenues of which would not be captured in the CSM release. For example, for particular Deferred Annuities, there is an accumulation phase followed by the annuity phase. The policyholder's beneficiaries receive no return if the policyholder dies during the accumulation phase. During the annuity phase, a surviving policyholder receives a fixed annuity amount based on premiums/technical provisions. In these deferred annuities the policyholder does not have a right to withdraw during either the accumulation phase or the annuity phase. Do you have additional examples of investment activities that are not captured by the proposals in the ED?

36 Entities have to provide quantitative disclosures on the expected recognition in profit or loss of the contractual service margin remaining at the end of the reporting period, in appropriate time bands. Do user constituents agree with this disclosure requirement? Do preparer constituents consider that this information is commercially sensitive? Please explain.

We globally support the EFRAG's answer on these points.

Preparers would have to provide new disclosures in terms of quantitative information on the expected recognition in profit or loss of the contractual service margin remaining at the end of the reporting period, while the disclosure of qualitative information was also possible before amendment.

We understand that this would give more information to users for the analysis of financial statements.

Still, we believe that this would only provide a partial view of the profitability pattern based on the available information as closing date, which also includes namely risk adjustment release and insurance financial result.

Based on that and in view of the significant volatility of IFRS 17 metrics to market

environment, it should not be considered by users as sufficient to monitor the profitability pattern and allow comparisons across entities.

**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 recognise 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?

**Questions to Constituents**

45 For proportionate reinsurance contracts, please provide fact patterns that are not captured by the amendment but for which the solution proposed by the IASB would be relevant.

46 The IASB has not addressed non-proportionate reinsurance contracts. A peculiarity of such contracts is that there is no one-to-one relationship between the direct underlying contract and the reinsurance contract held, for example because there are many underlying contracts that are covered by a single excess loss reinsurance contract held. Addressing non-proportionate reinsurance may therefore require the need to identify a “link” between the reinsured risk and the underlying contracts. EFRAG understands that any accounting mismatch for non-proportionate contracts may, in practice, be reduced due to the impact on the risk adjustment rather than on the CSM.

47 In your view:

(a) Should non-proportionate reinsurance contracts be treated similarly to proportionate reinsurance contracts, i.e. gains in profit or loss when a loss is recognised on underlying contracts? If yes, please provide information about (i) the prevalence of such contracts, including volumes and jurisdictions where the issue arises and (ii) the cash flow pattern of these non-proportionate reinsurance contracts.

(b) How would an accounting solution for non-proportionate reinsurance work?

**We welcome the proposals of the IASB aiming to reduce the accounting mismatches for reinsurance contracts held, but raise concerns about the scope of these proposals.**

We consider that an entity should recognise a gain from reinsurance contracts held when a ‘day one loss’ is initially recognised on underlying business, provided there is a direct link between the losses on the underlying contracts and the net gain on reinsurance contracts held.

This direct link should exist for 'proportionate reinsurance contracts'.

The risk mitigation effect provided by non-proportionate reinsurance contracts is more linked to the occurring of exceptional events (and not to expected losses on the underlying contracts) and should be captured by the risk adjustment of reinsurance contracts held.

We are also concerned that some types of contracts such as surplus reinsurance or loss occurring contracts, that are considered as 'proportionate reinsurance' in the market practice, may be excluded from the scope of this amendment due to the wording in paragraph B119D, BC80 and BC91.

*Surplus reinsurance* is a type of proportionate reinsurance contract where no single 'fixed percentage' exists for a group of underlying contracts. Instead, the proportion of the risk that is ceded to the reinsurer is determined for each underlying policy, based on their sum insured and on the retention of the cedant.

The table below provides an illustration of the mechanism of such contract, in the case of a retention by the ceding company of 100 CU.

Policy	Sum insured total	QS ceded	Retention by ceding company
A	100	0%	100%
B	1000	90%	10%
C	500	80%	20%

Based on the above, we consider that surplus reinsurance contracts should benefit from the amendments to IFRS 17 as there exists a direct link between the reinsurance contract held and the risk borne by underlying contracts, and that the wording of the definition of 'proportionate reinsurance contracts' and of paragraph B119D should be adjusted to take into account effects that apply at the level of each underlying contract. This is also consistent with BC79 and BC80 of the exposure draft amendments to IFRS 17, since the recovery of losses is known at the inception of the underlying contract.

*Loss occurring contracts* are a type of proportionate reinsurance where the 'fixed percentage' applies not to a group of underlying contracts, but to all claims that occur on the underlying portfolio of risks during the coverage period.

There is a direct link with the underlying policies since the loss occurring contracts apply to all policies that are in force during the coverage period of the reinsurance contract held. However, some participants have raised the concern that such contracts might be excluded from the scope of the amendment due to proportionate contracts being linked to the 'right to recover from the issuer a percentage of *all claims incurred on groups of underlying insurance contracts*', and not to the 'right to recover a percentage of *all claims incurred during the coverage period of the reinsurance contract held*'.

When an underlying onerous contract is initially recognised, a net gain should be recognised from reinsurance contracts held, provided there is an overlap between the coverage periods of the underlying contracts and of the loss occurring reinsurance contract held.

The table below provides an example of the economic effect of a 50% quote-share loss occurring contract inception 1/1/N for several underlying contracts, based on their own inception date.

Policy	Inception date	% of coverage period covered by LOD	Effective QS (cession of D1 loss)
A'	Jan, 1 <sup>st</sup>	100%	<b>50%</b>
B'	Apr, 1 <sup>st</sup>	75%	<b>37,5%</b>
C'	Jul, 1 <sup>st</sup>	50%	<b>25%</b>

Some participants consider that a deferred asset could be recognised in anticipation of future renewals of loss occurring contracts, in order to benefit from the full effect of the reinsurance coverage. This asset would be depreciated at year end closing, in case of a change of the reinsurance structure. Taking into consideration the above example, with each underlying policy having an initial day one loss of 100 CU, this asset would function as follows:

Policy	Effective QS	Net gain recognised on reinsurance contract held	Deferred reinsurance asset (to be amortised over the next renewal)
A'	<b>50%</b>	50	0
B'	<b>37,5%</b>	50	12,5
C'	<b>25%</b>	50	25

At closing time, an entity should assess the recoverability of such an asset if facts and circumstances indicate the asset may be impaired. Such facts and circumstances may include a change in the reinsurance structure of the entity.

Based on the above and similarly to the proposal in paragraph 9, we consider that loss occurring contracts should benefit from the amendments to IFRS 17 as there exists a direct link between the reinsurance contract held and the risk borne by underlying contracts, and that the wording of the definition of 'proportionate reinsurance contracts' and of paragraph B119D should be adjusted to take into account effects that apply at the level of each underlying contract. This is also consistent with BC79 and BC80 of the exposure draft amendments to IFRS 17, since the recovery of losses is known at the inception of the underlying contract.

Some participants have raised the concern that the calculation method proposed in paragraph B119D may be oversimplistic and does not consider the entire economy of the reinsurance contracts. This, however, is a practical assumption that is consistent with BC79.

#### **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?

IA agrees with the IASB's amendments to aggregate, for presentation purposes, assets and liabilities at a portfolio level instead of at a group level.

**Question to Constituents who are Users**

54 Do Constituents that are Users agree that separate balance sheet presentation (of insurance contracts that are in an asset position from those that are in a liability position) on a portfolio level rather than at group level will not significantly reduce the information available? Please explain.

**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?

**Questions to Constituents**

64 EFRAG has heard that the extension of the risk mitigation option should be widened, for example, to include non-derivative instruments such as when hedging of interest rate risk is carried out using a combination of swaps, swaptions and fixed interest securities.

65 Please explain the prevalence including volumes and jurisdictions involved, of the risk mitigation strategies identified in paragraph 64 above.

The proposed amendment to paragraph B116 would extend the risk mitigation option to reinsurance contracts held to mitigate financial risk arising from insurance contracts with direct participation features.

We acknowledge that the amendment resolves some accounting mismatches where an entity manages financial risk in a VFA contract by holding a reinsurance contract that transfers some of the risk.

However, we believe that the measurement under the VFA of reinsurance contracts held to cover direct par contracts would much better eliminate the accounting mismatch than the proposed solution of extending the scope of the risk mitigation option. We do not understand the reasons of the current exclusion and note the recognition of the reinsurance as similar to derivatives is an argument in favor of the application of the VFA to reinsurance contracts held that satisfies the conditions specifies in B101.

We are also in favor of the extension of the current amendment to derivatives held to mitigate non-financial risk arising from insurance contracts with direct participation features.

**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?

**Questions to Constituents**

73 Do you consider that the proposed deferral of the effective date to 1 January 2022 is sufficient or would you support an additional year (i.e. 1 January 2023)?

74 Arguments in favour of accepting the proposed effective date of 1 January 2022 include:

- (a) Further delaying the application of IFRS 17 beyond 2022 will be disruptive, as will increase the costs of their implementation processes; and
- (b) A delay beyond 2022 may encourage entities to defer their implementation efforts rather than using the extended period to better implement the Standard.

75 Arguments in favour of further delaying the effective date to 1 January 2023 include:

- (a) Some entities, mainly small and medium sized ones, often rely on third IT systems providers and so far there are no IT solutions for IFRS 17 available on the market, thereby making it difficult to meet the proposed 2022 effective date;
- (b) The IASB expects to finalise the amendments by mid-2020. As a result, there will only be six months before the comparative period for IFRS 17 starts and this may be challenging for some entities; and
- (c) Entities that would like to apply IFRS 17 earlier would be able to do so.

IA agrees with EFRAG welcoming the IASB's decision to defer the effective date of IFRS 17. However, we consider that the IASB should consider the major feedbacks from the public consultation and address all relevant concerns before finalizing the amendments.

The effective date for IFRS 9 should continue to be aligned with the effective date of IFRS 17 (and accordingly the European "Top-up" be extended).

**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?

### Questions to Constituents

94 Do Constituents agree with the approach suggested by EFRAG, i.e. to prefer retrospective application of paragraph B115 instead of supporting the two consequential amendments? Please explain why.

95 If you expect to apply the risk mitigation retrospectively under the approach proposed by EFRAG, how would you find the required evidence in practice? What would be the starting point for collecting the evidence and what process would you use?

We agree with the proposed amendment. The proposal introduces a welcome simplification for contracts acquired in a portfolio transfer or business combination before the transition date. Without this amendment, it might have been impracticable on transition to distinguish between claims liabilities that arose from acquired contracts and those arising from initiated contracts.

Applying the risk mitigation option from the transition date, rather than from the date of initial application of IFRS 17, would eliminate accounting mismatches in the comparative periods presented.

### **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 IASB 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?

### **Question to Constituents**

110 Do Constituents consider that there may be any unintended consequences arising from the proposed change in terminology? Please explain.

IA welcomes improvement on terminology as addressed by IASB.

## Appendix 2: Other comments

### Topic 1 - Annual cohorts

#### Questions to Constituents

140 For contracts with cash flows that affect or are affected by cash flows to policyholders of other contracts:

(a) EFRAG is suggesting to the IASB to provide an exception to the requirement to restrict the grouping of contracts using the annual cohorts. Would Constituents agree with this proposal? Please explain why or why not.

(b) Please provide fact patterns - and their prevalence - for which the application of the annual cohorts requirement results in added complexity that is not justified and, as a consequence, should be captured in such an exception. For example:

(i) Contracts to which the VFA applies compared to other contracts;

(ii) Contracts with full sharing of risks compared to other contracts that only share a substantial or significant part of the risks;

(iii) Contracts that share all risks or only particular risk types; and

(iv) Contracts with sharing of asset returns of underlying pools compared to other contracts.

141 As reported in paragraph 129, the exception should meet the reporting objectives of IFRS 17 (i.e. depicting profit trends over time, recognising profits of contracts over the duration of those contracts and timely recognising losses onerous contracts).

With reference to the pattern of recognition of the CSM, EFRAG in its case study received mixed results as to whether the resulting information would be impacted by the removal of the annual cohorts.

In your opinion, how would you ensure that the CSM release pattern would be in line with the IFRS 17 stated objectives? Do you envisage any loss of information as contemplated by the IASB in paragraph BC177 of the ED? If so, how would you address that loss of information?

142 Are there other types of contracts in the life insurance business, other than the contracts with cash flows that affect or are affected by cash flows to policyholders, that create similar complexity?

143 Some have observed that when a grouping approach broader than annual cohorts is applied, there is a benefit in providing additional information about trends in profitability. Such disclosure could include:

(a) Reconciliations for the CSM of those groups from the opening to the closing balances (according to paragraph 101 of IFRS 17)

(b) Disclosure on profitability trends by presenting the CSM effect of new business joining the groups, extracted from (a), as a series of historical data (for example, the last 3 years);

(c) Disclosure of the actuarial techniques applied for computing the CSM effect of new business joining the group as well as disclosure about the method used for assessing the profitability referred in (b).

Would Constituents consider it appropriate to include these additional disclosures?

We agree with EFRAG's proposal to provide an exception to the requirement to restrict the grouping of contracts using the annual cohort, since this requirement fails to give a making-sense representation of contracts with cash-flows that affect or are affected by cash-flows of other contracts.

This point is of paramount importance for the French life insurance market for which participating investment and insurance contracts represent more than one thousand billion euros.

These contracts share participating mechanisms based on the returns of an underlying pool of items that back all generations. Moreover, asset allocation is determined, under Asset and Liability Management, considering expectations and associated risks of all contracts.

As a consequence, grouping by cohort requires to make a burdensome artificial cash-flows allocation to annual cohorts that do not reflect contractual and economic features of contracts.

**IA's view is that contracts with cash-flows that affect or are affected by cash-flows of other contracts, under the Variable Free Approach, should be exempted from considering annual cohorts for grouping.**

We agree with §129 objectives. We believe and experienced (for example with Market Consistent Embedded Value disclosures) that such objectives could be fulfilled with relevant and systematic disclosures.

On this matter we share ANC's proposal that for contracts that benefit from the exception, the following could be introduced:

- (a) a qualitative disclosure describing the grouping criteria for contracts to which the annual cohort requirement is not applied;
- (b) reconciliations for the CSM of those groups from the opening to the closing balances (according to paragraph 101 of the standard);
- (c) disclosure on profitability trends by presenting the CSM effect of new business joining the groups, extracted from (b), as a series of historical data (in the last 3 years);
- (d) disclosure on the actuarial technique applied for computing the CSM effect of new business joining the group as well as disclosure on method used for assessing the profitability referred to in (c).

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

### **Question to Constituents**

155 Please provide specific prevalent fact patterns where the application of the modified retrospective approach is proving particularly challenging in practice. This would assist EFRAG in understanding better the interpretation difficulties arising in obtaining reasonable and supportable information and in estimating missing information that is required to apply the modified retrospective approach.

### **Topic 3 - Balance sheet presentation: Non-separation of receivables**

#### **Questions to Constituents**

161 Do Constituents support the presentation of separate information about premiums receivable? If so, should information about premiums receivable:

- (a) be mandatory?
- (b) be based on a predefined definition of "premium receivables" and , in this case, how should premiums receivable be defined?
- (c) be provided on the face of the balance sheet or in the notes?
- (d) be separated by insurance portfolio?

IA does not support a separate presentation about premiums receivables, in general cases. Nevertheless, if premiums receivables are of paramount importance to appraise counterpart risk of an entity, it would be logical that the entity provides some information about it, considering materiality of this kind of risks.

### **Topic 4 - Reinsurance contracts: contract boundary**

#### **Questions to Constituents**

172 Do Constituents support the IASB's tentative decision not to amend IFRS 17 for the contract boundary of reinsurance contracts held?

173 Do Constituents that are Users consider that CSM for the reinsurance contracts held which reflects future expected contracts would provide useful information? Please explain.

174 EFRAG understands that there is no material impact on the balance sheet and probably not a significant impact on profit or loss (until certain events occur as explained in paragraph 169 above). Please explain the prevalence of holding reinsurance contracts that relate to underlying contracts that have not yet been issued, including volumes and the jurisdictions where the issue arises.

IA does not support the IASB's tentative decision not to amend IFRS 17 for the contract boundary of reinsurance contracts held. We believe that reflecting future insurance contracts that are not recognized on the liability side does not provide useful information for users.

Therefore, we consider that the boundary of reinsurance contracts held should be amended to be limited to the boundary of recognized underlying insurance contracts.