

International Accounting Standards Board
(IASB)
7 Westferry Circus
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United Kingdom

12 September 2019

Exposure Draft ED/2019/4 ‘Amendments to IFRS 17’ (“Exposure Draft”)

This letter has been drafted by the European Insurance CFO Forum (“CFO Forum”), a body representing the views of 23 of Europe’s largest insurance companies and Insurance Europe, representing 95% of the premium income of the European insurance market. Accordingly, it represents the consensus view of the European insurance industry.

Our members continue to support a high quality standard for insurance contract accounting and have contributed significant efforts in the earlier EFRAG testing of IFRS 17 ‘Insurance Contracts’. In July 2018, the CFO Forum summarised the significant issues identified by its members during the EFRAG field test and in October 2018 proposed solutions to those issues through proposed track change edits to the standard.

We appreciate the efforts by the IASB in considering the concerns raised by the insurance industry and others about IFRS 17 ‘Insurance Contracts’, which resulted in the changes proposed in the Exposure Draft. The proposals in the Exposure Draft represent welcome improvements in a number of areas, such as the scope exclusion for certain credit-based contracts, recognition of acquisition expenses on renewals and the presentation of insurance contracts as assets or liabilities at the portfolio level. However, the IASB has chosen not to propose amendments for several other important issues and for other issues has proposed less effective amendments. As a result, we believe that further changes to IFRS 17 are needed to obtain a high quality standard that can be implemented at a reasonable cost.

In this context, we welcome the opportunity to comment on the Exposure Draft 2019/4 ‘Amendments to IFRS 17’.

The appendices to this letter include our responses to the IASB on the Exposure Draft, our comments on EFRAG’s draft comment letter to the IASB and our responses to the questions raised by EFRAG to its constituents. The comments in the appendices cover the three issues with the largest impact that we communicated earlier, changes that are proposed in the Exposure Draft but do not fully resolve the issues identified in the EFRAG testing, other issues for which no changes are proposed in the Exposure Draft and certain other proposed changes that have unintended consequences. Furthermore, the comments in the appendices also cover the proposed effective date.

Issues with the largest impact

In our efforts to continue to work towards a high quality accounting standard, whilst recognising the limitation for fundamental changes in this phase of the project, we have already highlighted the three issues that are most widespread amongst our members and that have the largest impact on the operational complexity and costs of implementing the standard. We have summarised these three issues below as they have not been resolved through the proposals in the Exposure Draft:

- **Level of Aggregation** – Whilst we continue to believe that the requirement for annual cohorts in general is not aligned to the fundamentals of insurance business, we believe that **at a minimum** annual cohorts should not be used for contracts in the variable fee approach with significant mutualisation and for all contracts at transition. This will significantly reduce operational complexities without significantly affecting

the outcome. See our responses in Question 3 for more information.

- **Transition** – We believe that the current limitations in the modified retrospective approach unduly limit the ability to utilise this transition method and will result in too much default to the fair value approach, even where this is less appropriate. We believe that the criteria for the modified retrospective approach should be more principles based. In addition, we believe that transitional relief is required for the risk mitigation approach (to be applied retrospectively), for OCI at transition (to be aligned for assets and liabilities in the general measurement model) and for historical business combinations. See our responses in Question 8 for more information.
- **Presentation** – We believe that changes should be made to remove the inconsistency between group and solo reporting that is solely due to differences in reporting frequency as this results in unnecessary costs of dual accounting. Furthermore, we believe that the requirement to present comparatives at transition should be removed to align with IFRS 9 and to allow further relief in implementation time and costs. See our responses in Question 5 for more information.

Our detailed comments on these three issues are included in the appendices.

Proposed changes in the Exposure Draft that do not fully resolve the issues identified

In the appendices, we have also commented on proposed changes in the Exposure Draft that do not resolve the identified issues. In this respect we would like to highlight the following:

- Risk mitigation is a critical element of insurance business. As such, our comments in the appendices propose an extension of the risk mitigation option to include non-derivative financial instruments and to be applicable to all insurance contracts – not only contracts accounted for under the variable fee approach. See our responses in Question 6 for more information.
- Whilst we welcome the objective of the proposed changes to accounting for proportional reinsurance in the Exposure Draft, we are concerned that the proposed definition of proportionate provides little relief in practice and still would create significant accounting mismatches. See our responses in Question 4 for more information.
- We are concerned that the proposed amendments on investment-return services do not capture economically similar products that include an insurance and investment return service but do not meet the criteria, as the contract cannot be surrendered nor transferred. In our view the proposed criteria for recognition of investment-return services need further consideration. See our responses in Question 3 for more information.

Other issues for which no changes are proposed in the Exposure Draft

In addition, we have commented in the appendices on other important issues identified in the EFRAG field testing that are not addressed by the proposals in the Exposure Draft. These comments are included in our responses to the relevant questions under the section “Other issues”.

Other proposed changes that have unintended consequences

Furthermore, we have identified amendments proposed in the Exposure Draft that introduce unintended consequences. These include for example the amendment to the guidance on the level at which eligibility for the variable fee approach should be assessed. This is a significant change which could result in disruption to implementation programmes. See our responses in Question 9 for more information.

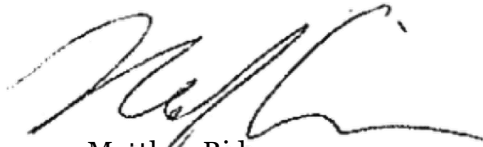
Proposed effective date

European insurers are working hard to implement IFRS 17 in accordance with the currently proposed effective date (1 January 2022). However, there are significant concerns on the tight deadlines, both in relation to the time needed to make the necessary improvements to the standard and the time needed for a high quality implementation. The European endorsement process will likely not result in an endorsed standard until late in 2021, which creates a great deal of uncertainty. We do not see this as purely a European endorsement issue, as we strongly believe that there should be one consistent global effective date of an endorsed standard. Taking into

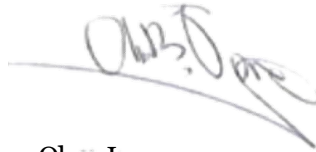
account the above, many in the industry see a need for a delay to the global effective date of IFRS 17 and IFRS 9 for insurers until 1 January 2023, while others see the need to retain a 2022 effective date.

In summary, we welcome the changes proposed in the Exposure Draft as these represent a significant improvement, but we believe that additional changes (as set out above and in the appendices) are still required. We appreciate the opportunity to provide input for resolving these remaining issues and would be pleased to discuss these further with you.

Yours faithfully,



Matthew Rider
Chair
European Insurance CFO Forum



Olav Jones
Deputy Director General
Director Economics & Finance, Insurance Europe

APPENDICES: DETAILED RESPONSES

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?

(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?

Response to the IASB:

We welcome the proposed amendments. For contracts issued by insurance companies, we believe that the proposed amended requirements better reflect the economics of the relevant products. The proposed amendments are a significant improvement to the scope of the standard and resolve the issues with certain products that we have highlighted earlier.

Other issues related to scope: contracts that change in nature over time

In July 2018, we highlighted the issue relating to products that change significantly in nature during their life due to the execution of an option by the policyholder. For example, a product with a savings phase with profit sharing may become an annuity in payment or remain paid-up without any participation if elected by the policyholder. As the classification between general model and variable fee approach occurs at inception and is irrevocable, certain products may have to be accounted for under the variable fee approach, whereas, after the execution of the option, the variable fee approach is not suitable and not comparable to similar products with a different 'history'.

Our proposed solutions included an amendment to treat a significant change in the nature of a contract due to the execution of an option by the policyholder as a contract modification. The 'new' contract post execution of the option by the policyholder could be reassessed and treated under the appropriate measurement model.

Further analysis of the facts and circumstances of the product features and terms of the option indicate that, as an alternative solution, a contract boundary may be established when the option is exercised and a transfer out of the with profits fund to the general fund occurs. This alternative solution does not require any change to the contract boundary criteria, however paragraph B24 and the relevant basis of conclusions would need to be worded as follows:

“In circumstances where the exercise of the option results in a cash flow that settles a liability between different components of the reporting entity such as policyholder and shareholder funds, this may result in a contract boundary being established (provided the criteria in paragraphs 34 and B61- B71 are met) such that the cash flows subsequent to the settlement of the option are measured as a new contract.”

EFRAG Additional questions to constituents:

- 10 *Paragraph B.4.1.9.E of IFRS 9 allows a regulated interest rate as a proxy for the time value of the money in doing the SPPI test, under certain conditions. EFRAG understands that in some countries the insurance element is not required by the regulation and, as a consequence, the financial instrument could fail the SPPI test and would have to be measured at fair value through profit or loss. How prevalent are these concerns within your jurisdiction?*

Response to EFRAG:

We support the comments made by EFRAG in its draft comment letter. We have no specific comments on the scope of this amendment in the context of payment cards and/or the impact on the SPPI test, as these are not specifically relevant to our members' insurance operations.

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 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?

Response to the IASB:

We welcome the proposed amendments that would require the allocation of insurance acquisition cash flows 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 contracts in that group. The amendment better reflects economic reality and increases the consistency between the requirements of IFRS 17 and the treatment of non-insurance acquisition cash flows in IFRS 15. The proposed amendments are an improvement and resolve the issues with directly attributable acquisition expenses related to renewals that we have highlighted earlier.

EFRAG Additional questions 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?*

Response to EFRAG:

We support the comments made by EFRAG in its draft comment letter. We do not consider it necessary for IFRS 17 to define insurance contract renewals as we believe that the requirements in IFRS 17 should be principles-based and consistent with IFRS 15, which does also not include a definition of contract renewals. We do not believe that there is significant diversity in practice 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?

Response to the IASB:

In response to question 3a: We welcome the amendment to require investment return services to be considered when allocating the contractual service margin (“CSM”) using coverage units. This amendment also recognises that many insurance contracts that qualify for measurement under the general measurement model have significant elements of both insurance coverage and investment return services. The CSM established at inception for these types of contracts includes expected profit from both insurance and investment related activities. We agree that the profit from these services should be recognised in line with the service provision over the life of the contract. In our view the proposed amendments significantly improve the relevance of the income statement for these contracts.

However, we believe that further changes are needed. We are concerned that the proposed amendments on investment-return services do not capture economically similar products that clearly include both insurance and investment return service but do not meet the criteria, as the contract cannot be surrendered nor transferred. In our view the proposed criteria for recognition of investment-return services need further consideration, since as currently drafted they would result in economically similar contracts having different accounting results.

For example, a deferred annuity contract in Country A offers the policyholder an option to transfer to a new annuity provider on retirement. In practice, even if this option is never utilised, the contract would meet the criteria for an investment-return service in paragraph B119B of the Exposure Draft. A nearly identical deferred annuity contract in Country B, which is managed in the same way during both the accumulation and annuity payout periods, but does not offer a policyholder the option to transfer out, cannot include investment-return services during the deferral period because it fails the requirement proposed in paragraph B119B(a) for “the policyholder [to have] a right to withdraw an amount.” We believe both contracts provide insurance and investment return services throughout their duration.

The current proposed definition of investment return services would also result in issues with the recognition of investment expenses in the best estimate insurance liability in the balance sheet. We understand from the IASB Staff papers that were prepared for the discussions in the IASB's IFRS 17 Transition Resource Group ("TRG") that the requirements on investment return services equally determine whether investment management expenses are to be included in the expected cash flows in the insurance liability. As such, a requirement that was intended to apply to the presentation of insurance revenue and the recognition of the CSM has resulted in different measurements of insurance contracts in the balance sheet.

We support the inclusion of investment management expenses in the fulfilment cash flows for all contracts to which investment return services are provided. However, as currently drafted, the criteria do not enable all contracts which provide investment return services in practice to be included, hence increasing the inconsistency in measurement between economically similar contracts. For example, where the criteria in B119 (a) (right to withdraw or existence of an investment component) are not met, an investment return service is deemed to not apply and investment management expenses are not reflected in the liability in the balance sheet. Similarly, where the investment return service only applies to part of the coverage period, investment management expenses will either not be included in the expected cash flows or only be included for part of the coverage period. For insurance contracts with an investment return service, investment management expenses are reflected in the expected cash flows in full. This results in a lack of consistency in the measurement of insurance liabilities in the balance sheet for economically similar contracts. This lack of consistency will reduce comparability in financial results between economically similar contracts as well as increase the cost and effort required to implement and run IFRS 17.

Our earlier proposed solution was to permit entities to determine coverage units based on insurance benefits and related non-insurance activities (including investment services) performed to deliver those benefits.

However, given the proposed amendments in the Exposure Draft, we believe a further amendment to the definition of an investment return service could resolve this issue.

We believe that an investment return service is present where the contract provides the policyholder with a positive expected investment return. This distinguishes contracts which provide investment return and insurance services from contracts which provide only insurance services.

We therefore propose that paragraph B119B is reworded as follows:

"Insurance contracts without direct participation features may provide an investment-return service if, and only if

- a) the contract provides (on an expected basis at group level) a positive investment return (which could be below zero, for example in a negative interest rate environment); and
- b) the entity expects to perform investment activity to generate that positive investment return."

We believe that under this definition an investment return service would either be absent, or present throughout the lifetime of the contract. As such, the operational difficulties associated with coverage units changing once investment return services are deemed to have ceased would be avoided. Equally, the issue of investment management expenses being only partly included in the fulfilment cash flows would be resolved.

In response to Question 3b: We support the requirement to identify coverage units for insurance contracts with direct participation features (variable fee approach contracts) which considers the quantity of benefits and the expected period of both insurance coverage and investment-related service.

In response to Question 3c: We do not object to the proposed amendment to require an entity to disclose quantitative information about when it expects to recognise in profit or loss the remaining CSM at the end of a reporting period.

Other issues related to the CSM: Level of aggregation

As noted in our cover letter, we continue to believe that the level of aggregation caused by the annual cohorts requirement is too prescriptive as it is not in line with the economics of insurance businesses and adds undue operational complexity. This remains one of the industry's top concerns with the implementation of the new standard. On this ground, we have earlier proposed that, **at a minimum**, relief from the use of annual cohorts is provided for:

- contracts measured using the variable fee approach with significant mutualisation; and
- in force business at transition, under all three transition approaches.

Grouping mutualised business measured using the variable fee approach into annual cohorts is inconsistent with the way such business is managed and regulated, as returns on underlying items are shared between contracts written more than one year apart. The removal of annual cohorts from the measurement of mutualised business will therefore produce financial results that are more representative of the economic performance of the portfolio.

Once issued, a new contract in a mutualised portfolio is part of the mutualisation and the individual CSM ceases to be pertinent; there is only one mutualised CSM for the total portfolio comprised of existing and newly added contracts. Once a policyholder has joined a mutualised population, the margin contributed by this contract is linked to the mutualised portfolio and not to the sole contract. When policyholders accept sharing of significant risks, a contract does not become onerous (for the insurer) unless the mutualisation among policyholders is insufficient to cover the risks. There is no onerous contract within a part of a mutualised population unless the whole population becomes onerous.

In an intergenerational mutualised portfolio, the mandatory allocation of the CSM to annual cohorts under IFRS 17 requires discretion from the insurer and consequently does not necessarily better reflect the performance or the profitability of each cohort. In practice, profitability would be assessed at a mutualised level and then allocated to cohorts, making the provision of information at cohort level purely artificial.

The impact of new business on the mutualised portfolio would be already disclosed in the rollforward note disclosures for the CSM which would provide any trend information without the artificial and costly allocations caused by annual cohorts. Therefore, our view is that removing the annual cohort requirement would not lead to any loss of useful information and would actually result in a better representation of how the business is managed.

The use of coverage units for the release of the CSM would already ensure that the CSM is fully recognised over the life of the underlying contracts.

Furthermore, removing the requirement for annual cohorts on transition under all approaches would provide significant operational relief for all entities implementing IFRS 17. Significant operational issues result from retroactively trying to gather the necessary cohort information as this information has never been tracked in the past and therefore would require costly system changes and significant data collection efforts. Removing this requirement would also make the three transition approaches more consistent.

While the above highlights what we believe to be the minimum changes needed, we still would prefer a more comprehensive solution which we have highlighted in the past. This comprehensive solution would be to remove the requirement to group contracts by annual cohort in general (including for contracts not qualifying for the variable fee approach), under the condition that contracts issued in different years would be in the same profitability group. This comprehensive solution is preferred because many insurers issue long term insurance contracts and thus do not manage their business on an annual cohort basis. Measuring insurance contracts using annual groups that are inconsistent with the way the contracts are managed and regulated may not generate useful information. As the CSM is calculated retrospectively, outputs will need to be stored, referenced and updated in each subsequent reporting period. In order to achieve this, projected cash flows and the risk adjustment will need to be segmented and stored at an annual cohort level, despite the fact that no information will be presented externally on this basis. The changes to systems and processes that are required in order to achieve this functionality will require significant effort and cost.

Other issues related to the CSM: Locked-in discount rates for the CSM

We continue to disagree with the use of a locked-in discount rate for measuring the CSM under the general model where the impact of changes in discount rates are recognised directly in profit or loss. This is inconsistent with the measurement of expected cash flows, which are discounted using a current discount rate. The requirement to recalculate the impacts of changes in fulfilment cash flows using the locked-in discount rate for CSM recalibration, and record the differences between the current and locked-in rate in profit or loss, increases the operational complexity of IFRS 17 and may significantly distort the financial results in a given period.

Furthermore, inconsistencies arise due to the different discount rates for BEL (current rate) and CSM (locked-in rate). The income statement is distorted by the use of different discount rates for different components of the insurance liability.

As stated in our letter to EFRAG and the IASB dated 17 October 2018, we propose an amendment for portfolios where the impact of changes in discount rates is recognised directly in profit or loss, such that the current discount rate should be utilised for all CSM measurements, re-measurements and movements. As such, the impact of changes in non-financial assumptions, calculated at the current discount rate, would be recognised in the CSM and not be split between the CSM and the income statement. All components of the liability would be measured consistently at the current interest rate in this scenario.

EFRAG Additional 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.*

Response to EFRAG:

We support the comments made by EFRAG in its draft comment letter. However, while we believe that the principle of the proposed amendments to require an investment return service to be considered when allocating the contractual service margin using coverage units is an improvement to the current requirements in IFRS 17, we believe that further changes are needed. The current proposals would produce differing results for economically similar contracts, depending on whether they include an option to surrender/transfer or not. We refer to the deferred annuity example in our response to the IASB on how the IASB's current proposed definition would result in differences in measuring economically similar contracts, which would adversely affect comparability. In the example, we believe both contracts provide insurance and investment return services throughout the duration of the contract and the presence or otherwise of a transfer option does not affect the services provided to the policyholder. In our response to the IASB we propose a solution that addresses this and the impact of the inconsistency in investment return services between similar products on the measurement of the best estimate liability in the balance sheet through the recognition of investment management expenses.

We do not object to the requirement for entities to disclose the expected recognition of the CSM by appropriate time bands.

We have included in our response to the IASB a number of other issues in relation to the CSM.

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?

Response to the IASB:

We support the direction of change that is proposed in the Exposure Draft, which is based on the principle that a gain on proportionate reinsurance should be recorded in profit or loss to the extent that it (partially) offsets a loss on onerous underlying insurance contracts.

However, we believe that the proposed wording is insufficient to address the issue in many situations. While in certain cases the amendment reduces differences between the initial and subsequent measurement of reinsurance contracts and underlying insurance contracts, and helps to ensure that the income statement better reflects the economic mitigation provided by the reinsurance contract, we are concerned about the extent to which the amendment can be applied in practice. This is mainly a result of the proposed definition of a “reinsurance contract held that provides proportionate coverage” in Appendix A of the Exposure Draft:

“A reinsurance contract that provides an entity with the right to recover from the issuer a percentage of all claims incurred on a group of underlying insurance contracts. The percentage the entity has a right to recover is fixed for all contracts in a single group of underlying insurance contracts, but can vary between groups of underlying insurance contracts.” (emphasis added)

In many cases, proportionate reinsurance contracts cannot be aligned on a fixed percentage basis to all underlying insurance contracts in a group. Examples of proportionate reinsurance that are not captured by the proposed definition are:

- where multiple proportionate reinsurance contracts cover different contracts in a group of underlying insurance contracts in different proportions;
- where a proportionate reinsurance contract only reinsures some, but not all, underlying contracts in a group;
- where a proportionate reinsurance contract only reinsures some, but not all, risks in a group of underlying contracts;
- where a proportionate reinsurance contract sets minimum and/or maximum limits on the reinsurance cover, for example contracts that provide proportionate reinsurance above and below a fixed level.

If the proposed definition is retained, then the risk mitigation efforts of insurers using reinsurance would not be appropriately reflected in the financial statements. As a principle, we do not see a need for IFRS 17 to include a definition of proportionate reinsurance. However, if a definition is included, we propose that a reinsurance contract held that provides proportionate coverage is defined as follows:

“A reinsurance contract held that provides an entity with the right to recover from the issuer a contractually defined portion of each claim incurred on individual underlying insurance contracts within a group of contracts.”

Amendments should be made to B119D and B119(c) as necessary to uphold the principle that there must be the ability to objectively measure the impact on individual insurance contracts within a group. The proposed new footnote to paragraph BC304 in the Exposure Draft should not be added.

The updated definition of a reinsurance contract held that provides proportionate coverage ensures that, to meet the definition, the reinsurance contract must cover a specified, proportionate share of each underlying insurance contract that is reinsured but there is no requirement for it to cover all contracts in a single underlying unit of account in the same proportion.

Other issues related to reinsurance: contract boundary

We do not support the IASB's tentative decision not to amend IFRS 17 for the contract boundary of reinsurance contracts. We believe that reflecting potential future insurance contracts in the reinsurance asset, when these are not yet reflected in the underlying insurance liability, does not provide useful information. For example, the unit of account for the reinsurance contract (net gain or net cost) is dependent on a forecast of future new underlying business, which adds significant complexity. As such, including the impact on reinsurance of expected future underlying contracts in the CSM for reinsurance contracts held would not provide useful information for investors. We believe that this issue is important, both because of its conceptual nature and the impact on operational complexity.

Other issues related to reinsurance: Use of the variable fee approach for reinsurance contracts

A mismatch arises where reinsurance contracts issued are used to reinsure contracts accounted for under the variable fee approach, where the reinsurance includes the link to underlying items and the reinsurer holds the underlying items. In this case the reinsurance contract issued can meet the eligibility requirements for the variable fee approach, but paragraph B109 of IFRS 17 disallows this approach. Paragraph BC213 of the Basis for Conclusions on the Exposure Draft states the "reinsurance contracts provide insurance coverage and do not provide substantially investment-related services" but this example, which is common across Europe, particularly between different entities within the same group, shows the reinsurance can provide substantial investment-related services.

We believe reinsurance contracts issued that meet the eligibility criteria should be required to use the variable fee approach. This should be restricted to reinsurance contracts that meet the eligibility requirements, share the underlying items and cover contracts with direct participation features.

EFRAG Additional 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 reinsurance excess loss 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?*

Response to EFRAG:

We support the comments made by EFRAG in its draft comment letter. In our response to the IASB we note that, whilst we support the objective of the proposed amendments, we believe that the proposed wording is insufficient to address the issue in many situations. We refer to our response to the IASB on this topic.

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?

Response to the IASB:

We welcome the proposed amendments to require each portfolio, rather than group, of insurance contracts to be presented as an asset or liability. We believe that this proposed amendment is a significant improvement that will reduce the operational burden to preparers, with no material loss of information to users. This proposed amendment will also remove the requirement which would otherwise have been imposed on preparers to analyse incurred claims by underwriting year.

Other issues related to presentation: measurement differences solely due to frequency of reporting

The requirement in paragraph B1 37 of IFRS 17 that the CSM must be “locked-in” at interim reporting means that any differences in external reporting frequency between group and subsidiary entities would result in different CSMs at different levels of consolidation. This adds significant operational complexity in the production of financial statements in a group, with little impact on the financial information reported at group and subsidiary level. As such, we would support an amendment to IFRS 17 to require an annual “year to date” approach to be taken in the calculation of the CSM and other estimates, irrespective of the frequency of reporting. Such an amendment would prevent the need to calculate different CSMs and other estimates at different levels in the group consolidation only because of the different reporting frequency.

The issue related to interim financial statements raised by the discrete approach required by B1 37 of IFRS 17 goes beyond the difference in treatment between group and subsidiary financial statements. Indeed, under the current IFRS 17 requirement, two identical insurers with identical estimates of fulfilment cash flows and the same economic and non-economic factors will measure the CSM differently depending the frequency of their external financial reporting. As such, the IFRS 17 does not currently ensure comparability between industry competitors.

For example: Company X produces quarterly financial statements in compliance with IAS 34 while Company Y only produces annual financial statements. If all actual and expected fulfilment cash flows and other financial effects are identical for Company X and Company Y, users of the financial statements will see differences in the reported profit for Company X and Company Y purely due to the timing effect created by B137.

This is an important issue in terms of operational complexity, also in the context of transition as set out in our response to Question 8.

Other issues related to presentation: relief from presentation of comparatives on transition

We proposed earlier that IFRS 17 is amended to make the presentation of comparative financial information under IFRS 17 in the first published financial statements optional, similar to the requirements IFRS 9. Whilst key comparative information would still be presented to the market, the relief from providing comparatives with disclosure in the (audited) quarterly, semi-annual and/or annual accounts would provide further relief in implementation time and costs.

Other issues related to presentation: premiums, claims and other associated cash flows on a cash basis

The proposed amendments do not address the concerns previously raised by the CFO Forum regarding the inclusion of premiums, claims and other associated cash flows in insurance liabilities on a cash basis. At present, accounting and reserving for insurance companies is typically done on an accrual basis, meaning that cash flows are included on their due date, rather than the date they are actually paid or received. Premiums receivable, claims payable and the related cash flows are currently managed in separate systems from the actuarial cash flow systems. The impact of the IFRS 17 requirement to measure premiums, claims and other associated cash flows on a cash basis would require significant investment in actuarial and finance systems to ensure financial information is prepared on the theoretical cash basis.

In addition, the removal of insurance receivables from the balance sheet reduces the value of information presented by insurers. For general insurers, basing liabilities on premium received rather than premium receivable will have a significant impact on financial statement presentation.

We believe that IFRS 17 should be amended to include premiums, claims and other associated cash flows on an accrual basis in the measurement of insurance liabilities, with premiums receivable and claims payable balances included separately on the balance sheet. Benefits of this change include reduced implementation efforts and improvements in the quality of financial information presented.

Other issues related to presentation: non-distinct investment components

We consider the current prevalence of non-distinct investment components (with often small non-distinct investment components being identified in everything from funeral plans to reinsurance treaties) is operationally extremely onerous for preparers. We consider that in certain cases (funeral plans being a good example), the measurement of non-distinct investment components is arbitrary and likely to lead to a lack of comparability between entities, and consequently non-useful information for users.

We consider increasing the comparability of the income statement to other industries such as banking and fund management where products have deposit features, can be achieved by revising the definition of an investment component to include only contracts where the policyholder has the right to make withdrawals. We consider the defining features of a deposit is the right of the policyholder to withdraw their deposit (adjusted as appropriate by investment return added and fees deducted from the deposited amount), and in the absence of this right to withdraw a deposit does not exist. We believe such a change would better meet the needs of users.

We believe the original intention of the IASB was that non-distinct investment components only need to be identified and measured when a claim occurs. We note changes to the definition of an investment component, have created uncertainty around when a non-distinct investment component is identified and measured. We ask the IASB to resolve the uncertainty around identification by clarifying that non-distinct investment components are identified based on facts and circumstances at initial recognition of the contract.

EFRAG Additional questions to constituents:

54 *Do Constituents that are Users agree with 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.*

Response to EFRAG:

We support the comments made by EFRAG in its draft comment letter.

In our response to the IASB, we have also highlighted a number of other presentation issues. Please see our comments in our response to the IASB.

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?

Response to the IASB:

We welcome the proposed amendment to extend the risk mitigation option that is currently available only when an entity uses derivatives to mitigate financial risk to circumstances when an entity uses reinsurance contracts held to mitigate financial risk. However, we believe that further changes are needed to the risk mitigation provisions as IFRS 17 could still create significant accounting volatility in profit or loss when risk mitigation is applied. These further changes needed relate to the following:

Expansion of the risk mitigation option to non-derivative financial instruments

We believe that the risk mitigation option in IFRS 17 should be extended further to financial instruments other than derivatives and reinsurance contracts. Insurance company hedging strategies generally employ a combination of derivatives and other financial instruments. Strategies involving non-derivatives are particularly prevalent in the hedging of minimum return guarantees and long duration cash flows, which are widespread in modern insurance products. Financial instruments other than derivatives are useful to avoid exacerbating potential derivative-related collateral and liquidity demands and to address regulatory accounting and capital framework limitations. As such, derivatives and non-derivative financial instruments are frequently used in combination to hedge risks. For hedging arrangements that include non-derivative instruments, existing IFRS 17 requirements create an accounting mismatch as the effect of the change in the insurance liability adjusts the CSM, while the corresponding movement in the hedging instrument is recorded in profit or loss or in OCI. The resulting volatility creates a disincentive for insurers to hedge using non-derivative financial instruments, potentially leading to hedging solutions that are either less effective or more costly.

Expansion of the risk mitigation option to all insurance contracts

The risk mitigation option should be available to all insurance contracts, rather than being limited to contracts accounted for under the variable fee approach. The inability to use the risk mitigation option outside the variable fee approach results in accounting mismatches, as the effects of changes on hedging instruments is not recognised in the same location as the changes on the hedged items. This significantly distorts the net result and creates misalignments between accounting results and risk management. Furthermore, insurance company risk management is typically organised at a macro level, covering both contracts accounted for under the variable fee approach and the general measurement model.

For example, for products accounted for under the IFRS 17 general measurement model, using the OCI option for changes in interest rates results in volatility in profit or loss caused by accounting mismatches. The effect of the derivatives used for economic hedging will be recognised in profit or loss, while the entire effect of interest rate changes will be recognised in OCI. Therefore, if OCI is elected, additional volatility in profit or loss from hedging will create a disincentive for companies to mitigate risk. Similar accounting mismatches occur in situations where an insurer applies the OCI option to a portfolio but only hedges a subset of contracts within the portfolio.

It is sometimes suggested that the ‘through profit or loss’ approach in the IFRS 17 general measurement model, together with using the fair value option for the financial assets, would be sufficient to address this problem. However, if those options are elected profit or loss could still show short-term volatility from mismatches that otherwise could have been reported in OCI. Some of these mismatches are fundamental, as credit spread changes on assets are not necessarily reflected equally in the IFRS 17 liability. Other mismatches could result from a company decision, based on ALM objectives, not to hedge financial risks in full.

Retrospective application of the risk mitigation option

We refer to our comments in Question 8 where we set out that the risk mitigation option should be applied retrospectively on transition. Without such a change, the economics of existing hedging arrangements cannot be accurately reflected on transition. Such a restriction could affect the measurement of the CSM on transition and distort future results. Our proposed amendment would permit entities to apply the hedging adjustment retrospectively on transition if they can do so without the use of hindsight, for example where documentation exists that describes the hedging strategy and the hedge objective targets prior to the date of initial application of IFRS 17 and where the entity can compute the cumulative risk mitigation impact in the CSM using reasonable methods.

Other issues related to risk mitigation: Observations on *Hedge accounting in IFRS 9*

We are aware of the viewpoint that either current IFRS 9 hedge accounting or the IASB's dynamic risk management project should address the above issues. However, there are a number of issues that complicate the ability of insurers to use hedge accounting in IFRS 9, in particular:

- Hedge accounting requires the hedged item to be separately identifiable and reliably measurable, which is not possible where investment and insurance components of an insurance contract are highly interrelated.
- Insurers generally hedge open portfolios and, even in case of closed portfolios, hedging is regularly carried out dynamically. Consequently, both hedged items and hedging instruments constantly change over the hedge term.
- Policyholder behaviour and other future expectations (e.g. lapses, surrenders, new business sales, and mortality) are intertwined with the impact of financial market variables. It is not evident how these items could be excluded from the hedging relationship. The hedge effectiveness requirements to qualify for hedge accounting are operationally onerous to comply with.

IFRS 9 hedge accounting is not well suited for the more macro approach that is common within the insurance industry, and the dynamic risk management project has, to date, not contemplated many of the issues of concern. Moreover, the dynamic risk management project will not be finalised for at least a few more years. Therefore we believe that additional changes to IFRS 17 are necessary. Since the mismatches described above result from the requirements of IFRS 17 (e.g. the variable fee approach and liability OCI accounting), it is appropriate that these are resolved within the IFRS 17 standard. The current IFRS 4 includes several mechanisms to reduce the accounting volatility in profit or loss (e.g. shadow accounting, accounting for the impact of guarantees at fair value through profit or loss, etc.) which are not available within IFRS 17.

EFRAG Additional 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.*

Response to EFRAG:

We support the comments made by EFRAG in its draft comment letter. As indicated in our response to the IASB, whilst we welcome extending the risk mitigation option to reinsurance held for financial risk, the extension of the risk mitigation option should be extended to cover other methods than just the sole use of derivatives, or reinsurance held for financial risk and contracts other than just contracts accounted for under the variable fee approach.

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 underway 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?

Response to the IASB:

We welcome the deferral of the effective date of IFRS 17 and IFRS 9.

Taking into account the changes that are still being proposed to IFRS 17, the time needed to get clarity on the endorsement of IFRS 17 in Europe and the significant operational challenges that insurers face in implementing the complex requirements, we believe that deferral of the effective date is absolutely needed as the current effective date of 1 January 2021 for IFRS 17 is unrealistic. We also support extension of the temporary exemption from applying IFRS 9. For insurers, it is vital to apply IFRS 17 and IFRS 9 at the same time. Any change to the effective date of IFRS 17 should result in an equal change to the temporary exemption from applying IFRS 9.

European insurers are working hard to implement IFRS 17 in accordance with the currently proposed effective date (1 January 2022). However, there are significant concerns on the tight deadlines, both in relation to the time needed to make the necessary improvements to the standard and the time needed for a high quality implementation.

In any case, these current timelines for a finalised IFRS 17 standard from the IASB and the resulting European endorsement process would likely not result in an endorsed standard until late in 2021, which is after the IFRS 17 proposed transition date of 1 January 2021 and very close to its effective date of 1 January 2022. Once IFRS 17 is endorsed in the European Union, time will be required for entities to prepare communications (including educating users of the financial impact of IFRS 17 and providing them with time to understand these significant changes). This creates a great deal of uncertainty. We do not see this as purely a European endorsement issue, as we strongly believe that there should be one consistent global effective date of an endorsed standard, which would avoid a number of operational issues for multinationals operating in various jurisdictions with, potentially, different effective dates.

Taking into account the above, many in the industry see a need for a delay to the global effective date of IFRS 17 and IFRS 9 for insurers until 1 January 2023, while others see the need to retain a 2022 effective date.

EFRAG Additional 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 the 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 of 1 January 2023 include:*
- (a) Some entities, mainly small and medium sized ones, often rely on third party 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.*

Response to EFRAG:

We support the comments made by EFRAG in its draft comment letter. We refer to our response to the IASB for our comments on the currently proposed timelines. We specifically note that the timeline for endorsement of IFRS 17 in Europe, following the anticipated publication of the revised IFRS 17 standard in the first half of 2020, is very tight. Assuming the European Union's endorsement of IFRS 17 takes approximately 12-18 months, the EU endorsement date would fall in late 2021, which is after the IFRS 17 transition date of 1 January 2021 and very close to its effective date of 1 January 2022. We do not see this as purely a European endorsement issue, as we strongly believe that there should be one consistent global effective date of an endorsed standard. A single global effective date would avoid a number of operational issues for multinationals operating in various jurisdictions with, potentially, different effective dates.

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 the 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 amendment? 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?

Response to the IASB:

In response to Question 8a: We welcome the proposed amendments regarding business combinations prior to transition, which allows claims in payment at the acquisition date to be treated as incurred claims. However, we believe that this should be permitted even if it is practicably possible to apply the standard without the relief as, even if the required data is available, it will represent a considerable workload whilst it would not result in more useful information.

In addition, we believe that a corresponding change should be made for business combinations occurring post transition. Including incurred claims in the liability for remaining coverage after the business combination date is likely to reduce transparency and impair comparability with other portfolios and other entities. Insurance revenue would be generated on claims that have already been incurred, when there is no further insurance service provided to the policyholders. Complexity would be introduced in calculating the CSM and insurance revenue on incurred claims, which are calculated and stored using separate systems and processes from insurance contracts in their coverage period. We believe that claims incurred before the business combination date should be treated as a liability for incurred claims by the acquiring company post acquisition, independent whether the acquisition is made before or after the transition date. The inclusion of such an amendment in IFRS 17 would increase comparability between acquired portfolios and those that have not been subject to a business combination.

Also, a business combination would require the acquiring group to re-assess the classification of the acquired contracts as insurance or not. The existing IFRS 17 requirement for the acquiring group to assess the classification of the acquired contracts on the business combination date presents operational challenges. If the acquired contracts change in nature during their life, the differing requirements of IFRS 17 will result in significantly different accounting treatments between the group and subsidiary financial statements. A similar issue exists for the classification of contracts as having ‘direct participating features’ or not, as contracts that would be eligible for the variable fee approach at inception but no longer at the date of the business combination because of changes in financial market conditions. This adds significant unnecessary complexity and costs and may require the capability to measure insurance contracts using the general model only if a future business combination takes place.

Our proposed solution would be, to not require the acquiring group to reassess the classification of acquired contracts at business combination date, and would instead permit the classification at inception to be retained. If this change cannot be made, we request, at a minimum, that relief from this requirement, for the classification of the contract as 'direct participating features', or not, to be reassessed at the business combination date is granted to business combinations occurring before the initial application date. We note that the Exposure Draft does propose a change to IFRS 3, to grant relief from the requirement to classify contracts as insurance or not at the business combination date, for business combinations occurring before the initial application date of IFRS 17.

We also note an inconsistency in the proposed amendments in the Exposure Draft between the classification of a liability for settlement of claims under the modified retrospective and fair value approaches. We believe that the classification of a liability for the settlement of claims under the modified retrospective approach should be optional in order to be consistent with the option under the fair value approach.

Other issues related to modified retrospective approach: principles-based approach

In addition to the proposed amendments in the context of business combinations, we believe that the modifications currently permitted under the modified retrospective approach, as set out in paragraphs C9 to C19 of IFRS 17, are too restrictive and do not provide the simplifications that make retrospective application possible in practice. If the modified retrospective approach is not improved, insurers will be forced to use the fair value approach for many portfolios, potentially reducing the level of comparability between the basis of reporting for in force business at the date of transition and new business written thereafter. Examples of the limitations of the current modified retrospective approach include the following:

- Full information on acquisition cash flows broken down by the cohorts under IFRS 17 is unlikely to be available retrospectively. Under the current modified retrospective approach requirements, insurers would not be permitted to estimate the allocation of these acquisition costs by cohorts and thus would be forced into the fair value approach.
- In order to estimate cash flows and risk adjustment entities need to know all adjustments made between the initial recognition and transition dates. Such information is unlikely to be available for older portfolios of long term life insurance contracts.
- It is often impracticable to estimate the amortisation of the CSM based on coverage units between the initial recognition and transition dates given that for older life insurance policies such information is unlikely to be available and cannot be estimated reasonably.
- The proposed amendment made in paragraph 62 of the Exposure Draft only allows part of the initial gain on reinsurance to be recognised immediately in profit or loss if the reinsurance contract is entered into either before, or at the same time as, the onerous underlying insurance contracts are issued. This may cause problems for insurers who re-tender reinsurance arrangements on a regular basis, for example annually. Whilst it would be possible to apply the requirements prospectively we believe that applying it pre-transition would add significant additional complexity to the transition process.
- The requirements of paragraph B1 37 of IFRS 17, which require separate measurement of interim and annual reporting periods, increase the cost and complexity of all retrospective transition approaches. This is even more difficult for entities that have changed their frequency of external reporting over time. Our proposed solution in our response to Question 5 would address this issue.

We believe a principles-based solution to the modified retrospective approach should be developed, by replacing specific prescribed modifications with a more general principle to allow reasonable approximations to be made. This change would retain the principles of modified retrospective approach but allow greater flexibility for insurers to apply it based on the extent of retrospective data they hold. Our proposed solutions would allow insurers to increase the use of retrospective transition approaches and would also reduce the operational effort associated with applying retrospective transition approaches. We note specifically that more flexibility in applying the modified retrospective approach would result in more comparability amongst insurers than the current default to the fair value approach.

In response to Questions 8b and 8c: We welcome the proposed amendments to apply the risk mitigation option prospectively from the transition date instead of the effective date, thereby allowing comparative financial

information to be prepared on the same basis in the first IFRS 17 financial statements. We also support the proposed amendment to permit an entity to apply the fair value approach to transition when it uses derivatives or reinsurance to mitigate financial risk before the transition date.

However, while these amendments resolve some of our concerns, these still do not permit retrospective application of the risk mitigation option for entities that do not use the fair value transition approach, resulting in distortion in the measurement of the CSM on transition and subsequent results. Therefore, we believe that the risk-mitigation option should be applied retrospectively on transition, subject to the following conditions:

- an entity can apply the risk mitigation option without the use of hindsight;
- documentation exists that describes the hedging strategy and objective targets prior to the date of initial application of IFRS 17; and
- the cumulative risk mitigation impact on the CSM can be computed using reasonable methods.

Without such a change, the economics of existing hedging arrangements cannot be accurately reflected on transition. Such a restriction could affect the measurement of the CSM on transition and distort future results. As an additional benefit, if the risk mitigation option were to be applied retrospectively, the amendments referred to in Question 8b and 8c would no longer be relevant.

Other issues related to transition: difference in OCI between assets and liabilities on transition

While the fair value and modified retrospective approaches allow the accumulated OCI balance on insurance liabilities to be set to nil on transition, as stated in paragraph C24(b) of IFRS 17, no such relief is available to assets measured at fair value through OCI. Setting OCI on the liabilities to nil at transition, whilst maintaining the historical OCI on related assets may significantly distort equity at transition and future results. Assets will generate a yield based on the historical effective interest rate, whilst liabilities will unwind at the market rate at transition date. For contracts accounted for under the variable fee approach, such mismatch does not occur as it is allowed to set the OCI on the related liabilities at transition equal to the accumulated OCI on the related assets.

We propose an amendment that extends the matching of accumulated OCI on assets and liabilities that already exists for the variable fee approach to the general model under both fair value and modified retrospective transition approaches. For the general model, the accumulated OCI balance on liabilities should be set equal to the accumulated OCI on a reference portfolio of assets at transition. This proposal would avoid the distortion of financial information that is created when the existing option is taken to set accumulated OCI on liabilities at transition to nil, while leaving accumulated OCI on assets unchanged.

Other issues related to transition: proposed changes for operational benefits

The following proposed changes would provide significant operational benefits when implementing IFRS 17 without significantly impacting the resulting balances:

- Historical data may only be available at product level, and not at the contract level which would practically be needed to recognise separate groups for onerous and non-onerous contracts. Therefore, we request a modification which would not require contracts at transition to have to be split between those which would have been onerous or non-onerous on initial recognition.
- For contracts with direct participating features the 'roll forward and roll back' method set out in C17, would in principle often give very little difference in CSM, to the current value of the underlying items less fulfilment cash flows. (This is the case for products where the insurer takes their variable fee from the underlying items relatively evenly over the contract life, such as for most unit-linked contracts). We therefore request a modification to be added permitting preparers to set the CSM for contracts with direct participating features equal to the fair value of the underlying items, less the fulfilment cash flows at the transition date, subject to this being a reasonable approximation to a 'roll forward and roll back'.

EFRAG Additional 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?*

Response to EFRAG:

We strongly support the comments in the draft comment letter of EFRAG on the risk mitigation option. We believe that IFRS 17 must be amended to allow retrospective application of the risk mitigation option. We agree with EFRAG that such an amendment would imply that the two amendments proposed by the IASB would no longer be required.

Risk mitigation is an integral part of normal business operations in the insurance industry and is routinely planned and documented. There should be no significant difficulty in providing the evidence in practice to support the retrospective application of the risk mitigation option, as all risk mitigation documentation should be readily available.

Whilst we support the proposed amendment on business combinations, we have highlighted in our response to the IASB that we believe that further amendments are required.

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?

Response to the IASB:

We support the proposed amendments set out in paragraphs BC147-BC163, with the exception of the points noted below:

Treatment of changes in underlying items (paragraph B128 of IFRS 17)

The amendment to paragraph B128(c) includes the term “underlying items” but does not relate solely to contracts accounted for under the variable fee approach. It is unclear whether the amendment introduces the concept of underlying items to contracts measured using the general model or whether it should be amended to specify that references to underlying items refer to contracts accounted for under the variable fee approach only. We are also concerned about the potential accounting mismatch if the underlying items are non-financial. Changes in financial risk would be presented in the insurance finance result, while the changes in the underlying item would be presented in the insurance service result, distorting both sections of the income statement. To avoid an accounting mismatch, it is imperative that the change in financial risk and associated movement in underlying items are reported together in insurance finance result.

Furthermore, we do not agree with the amendment to paragraph B128, which is only effective when all underlying items are assets. If underlying items include a mixture of assets and other items, this change is not effective. As such, we propose that the amendment is modified to fit different combinations of underlying items.

Change to the level at which the variable fee approach eligibility criteria are assessed

In the Exposure Draft, paragraph B107 b (ii) is proposed to be changed to “over the duration of the insurance contract,” whereas previously it was “over the duration of the group of insurance contracts.” Neither the revised Basis for Conclusions, nor any other document explains why this change has been made. We are concerned that this could be a major change, which is inconsistent with the rest of IFRS 17 (that uses groups of contract as the unit of account, not individual contracts) and could seriously disrupt the implementation of IFRS 17 and significantly increase costs. Such a fundamental change would not appear to be in line with the IASB's principles for considering and approving potential changes to IFRS 17.

We currently assume that the eligibility test for the variable fee approach can be performed at the level of the group based on paragraph 24 of IFRS 17, which states that recognition and measurement should be performed at this level. However, the change in paragraph B107 could be interpreted as requiring the VFA test to be carried out at the contract level rather than the group. This would require the allocation of all cash flows to individual contracts before the test can be performed. Mutualisation effects would also need to be allocated to contract level in all scenarios. Such a change would require significant additional effort and additional cost for all entities and would be inconsistent with the principles of IFRS 17.

Investment contracts with discretionary participation features (paragraph 11 (b) of IFRS 17)

Paragraph 11(b) of the Exposure Draft states that a distinct investment component should be separated from the insurance component and measured under IFRS 9 unless it is an investment component with discretionary participation features. We believe it would be helpful if it would be clarified that an investment contract with discretionary participation features may contain a distinct investment component that could be separated and measured under IFRS 9; for example, a unit linked contract with a unitised with profit component attached.

Mutual entities issuing insurance contracts (paragraphs BC264-269 of IFRS 17)

We agree that clarification is needed that not all mutual entities have a feature that the most residual interest of the entity is due to a policyholder. However, it would be much clearer to amend BC264-269. In our view, it is very unsatisfactory to add a footnote to explain that, although this section reads as if it applies to all mutual entities, when in fact it does not. The IASB's separately published educational material, *Insurance contracts issued by mutual entities*, wrongly makes the same assumption as BC264-269 with the result that it is misleading as a whole and should be withdrawn.

Recognition of contracts within a group (paragraph 28 of IFRS 17)

We believe it is unhelpful to amend paragraphs 24 and 28 to replace the term “issued” with references to the recognition date, while continuing to refer to “contracts issued more than one year apart” in paragraph 22. IFRS 17 should be consistent in referring to either the recognition date or the date of issue throughout.

EFRA G Additional questions to constituents:

99 *Do Constituents consider that there are any unintended consequences arising from the minor amendments? Please explain.*

100 *EFRA G has heard two concerns which are described in the following paragraphs.*

B128 of the amended IFRS 17

101 *Paragraph B128 of the amendments to IFRS 17 clarifies that changes in the measurement of a group of insurance contracts caused by changes in the fair value of underlying items should be treated as changes in investments and hence as changes in the time value of money and financial risk. The concern is that there would be a misclassification between insurance service result and finance result requiring the presentation of non-financial items in the financial result.*

Paragraph 28 of the amendments to IFRS 17 and paragraph 22 of IFRS 17

102 *Paragraph 28 of the amendments to IFRS 17 indicate that in recognising a group of insurance contracts in a reporting period an entity shall include only contracts that individually meet one of the criteria set out in paragraph 25 of the amendments to IFRS 17. That is, based on:*

- (a) the beginning of the coverage period of the group of contracts;*
- (b) the date when the first payment from a policyholder in the group becomes due; and*
- (c) for a group of onerous contracts, when the group becomes onerous.*

103 *However, in paragraph 22 of IFRS 17, an entity shall not include contracts issued more than one year apart in the same group.*

104 *Using the issue date in paragraph 25 of the amendments to IFRS 17 instead of the recognition date for the grouping would have implications on, for example, the discount rate and could create difficulties in terms of data availability causing operational issues and undue costs.*

105 *If you agree with either of the above two issues, please explain why this is an issue for you and the prevalence of the issue, including volumes and jurisdictions where the issue arises?*

Response to EFRAG:

We support the comments made by EFRAG in its draft comment letter. We refer to our response to the IASB. We have included additional comments in our response to the IASB that we believe require further amendment or clarification. With regard to our comments related to mutual entities, we believe that in Europe this is extremely important because mutuals differ considerably. For example, on the dissolution of a mutual or demutualisation, in some cases the net assets may be distributed among member policyholders but in other cases the net assets may not be distributed to the policyholders and are instead transferred to another mutual insurance company or to a foundation.

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’ 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?

Response to the IASB:

Whilst we understand the rationale for such change, we are concerned that the necessary changes would be widespread throughout the standard and accompanying documents, educational material, etc. This might be confusing, lead to unintended consequences and be unduly disruptive in this late stage of finalising IFRS 17.

EFRAG Additional questions to constituents:

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

Response to EFRAG:

We refer to our comments to the IASB.

Responses to the comments included in Appendix 2 of the draft comment letter of EFRAG (“Other comments on EFRAG’s September 2018 letter to the IASB on issues that have not been addressed by the ED”)

Topic 1 – Annual Cohorts

EFRAG questions to constituents:

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

- (a) *EFRA G 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 on 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 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 annual 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?

Response to EFRAG:

We strongly support EFRAG’s recommendation to the IASB to reconsider the requirements to restrict the grouping of contracts using annual cohorts. Many insurers issuing long term insurance contracts do not manage their business on an annual cohort basis. Measuring insurance contracts using groups that are inconsistent with the way the contracts are managed and regulated may not generate useful information. This is true under both the variable fee approach and the general model.

As set out in our “IFRS 17 Priorities” document, which has been discussed with EFRAG and the IASB, we believe that as a minimum:

- IFRS 17 should include an exception to the requirement to restrict the grouping of contracts using annual cohorts for mutualised portfolios measured using the variable fee approach ;
- Relief from the use of annual cohorts is needed for in-force business in transition, under all transition approaches; this would result in a significant reduction in the cost and effort of completing IFRS 17 transition using a retrospective approach.

We propose that annual cohorts should not be required for VFA contracts with significant intergenerational risk sharing. These intergenerational sharing contracts are a significant line of business in many countries. The VFA model requires that changes in the fair value of the underlying items can be attributed to individual groups. For many contracts with significant intergenerational risk sharing this is not possible, other than in a subjective manner, as both the timing of the distribution of fair value gains and losses on the underlying items, and how these will be allocated between cohorts is uncertain. Because VFA contracts with significant intergenerational risk sharing are managed at a portfolio rather than cohort level, any judgements required to allocate fair value gains and losses on the underlying items to annual cohorts would be made only for IFRS reporting, and are unlikely to be either reliable or uniform between different entities. This would lead to considerable diversity in reporting practice.

With regard to the need for transparency about trends in profitability, we note that such information is already provided by the combination of the existing requirements to disclose the amount of CSM contributed by new business and to disclose movements in the CSM balance for in-force portfolios.

For more information, please see our response to the IASB's Question 3.

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

EFRAG Questions 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.*

Response to EFRAG:

As highlighted in our response to the IASB's Question 8, we believe that the current requirements for the modified retrospective approach will result in a very limited ability to apply the modified retrospective approach in practice. Our response to that question includes examples of limitations in applying the modified retrospective approach in practice.

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

EFRAG 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?

Response to EFRAG:

As highlighted in our response to the IASB Question 5, we believe the proposed amendments do not address the concerns previously raised by the CFO Forum regarding the inclusion of premiums, claims and other associated cash flows in insurance liabilities on a cash basis. At present, accounting and reserving for insurance companies is typically done on an accrual basis, meaning that cash flows are included on their due date, rather than the date they are actually paid or received. Premiums receivable, claims payable and the related cash flows are currently managed in separate systems from the actuarial cash flow systems. The impact of the IFRS 17 requirement to measure premiums, claims and other associated cash flows on a cash basis would require significant investment in actuarial and finance systems to ensure financial information is prepared on the theoretical cash basis.

In addition, the removal of insurance receivables from the balance sheet reduces the value of information presented by insurers. For general insurers, basing liabilities on premium received rather than premium receivable will have a significant impact on financial statement presentation.

We believe that IFRS 17 should be amended to include premiums, claims and other associated cash flows on an accrual basis in the measurement of insurance liabilities, with premiums receivable and claims payable balances included separately on the balance sheet. Benefits of this change include reduced implementation efforts and improvements in the quality of financial information presented.

We believe a distinction should be made between premiums due to be paid by the policyholder after the financial reporting date, and those premiums which the policyholder is already due, and are either in the process of being collected, are late or are with an intermediary. Premiums due to be paid by the policyholder after the financial reporting date relate to remaining coverage, and we agree with the IASB that these should be included within the liability for remaining coverage (LRC). Premiums which are already due would normally relate to coverage already provided, and we consider these should be presented as a financial receivable.

We consider this also better represents an entity’s counterparty risk, as there would usually be no clear right of offset between financial receivables in respect of premiums already due and other liabilities of the entity.

Topic 4 - Reinsurance contracts: contract boundary

EFRAG 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 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.*

Response to EFRAG:

We do not support the IASB's tentative decision not to amend IFRS 17 for the contract boundary of reinsurance contracts held. We believe that reflecting potential future insurance contracts in the reinsurance asset, when these are not yet reflected in the underlying insurance liability, does not provide useful information. For example, the unit of account for the reinsurance contract (net gain or net cost) is dependent on a forecast of future new underlying business, which adds significant complexity. As such, including the impact on reinsurance of expected future underlying contracts in the CSM for reinsurance contracts held would not provide useful information for investors. We believe that this issue is important, both because of its conceptual nature and the impact on operational complexity.

For more information, see our response to the IASB's Question 4,