

STAFF PAPER

December 2019

IASB[®] meeting

Project	Amendments to IFRS 17		
Paper topic	Cover note		
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This paper has been prepared for discussion at a public meeting of the International Accounting Standards Board (Board) and does not represent the views of the Board or any individual member of the Board. Comments on the application of IFRS[®] Standards do not purport to set out acceptable or unacceptable application of IFRS Standards. Technical decisions are made in public and reported in IASB[®] *Update*.

Introduction

1. This cover note provides:
 - (a) background information about the tentative decisions made by the International Accounting Standards Board (Board) at its recent meetings about amendments to IFRS 17 *Insurance Contracts*;
 - (b) an overview of the papers for this meeting, including a summary of staff recommendations;
 - (c) an outline of next steps; and
 - (d) an appendix listing the topics that the Board decided at its November 2019 meeting to discuss at future meetings.

Background

2. At its October and November 2019 meetings, the Board discussed the feedback from outreach and comment letters on the Exposure Draft *Amendments to IFRS 17*.

3. In the light of that feedback, at its November 2019 meeting, the Board decided on its plan for redeliberating some of the matters raised by respondents on the Exposure Draft. The Board tentatively decided:
 - (a) the proposed amendments the Board will confirm at a future meeting without substantive redeliberation;
 - (b) the topics for which the Board will consider further the feedback from respondents; and
 - (c) the topics for which the Board will not consider further the feedback from respondents.

4. The Board noted that its tentative decision about the topics that it will not consider further should reduce uncertainty about any possible additional amendments to IFRS 17 and, therefore, limit disruption to implementation processes under way.

5. IFRS 17 is urgently needed to address many inadequacies in the wide range of insurance accounting practice used in applying IFRS 4 *Insurance Contracts* and significant implementation activities are underway. Accordingly, the Board decided that, in considering further the feedback from respondents, the Board will apply the same criteria that it applied when developing the Exposure Draft. The Board decided that any amendments to IFRS 17 must not:
 - (a) change the fundamental principles of the Standard because that would result in a significant loss of useful information for users of financial statements relative to that which would otherwise result from applying IFRS 17;
 - (b) unduly disrupt implementation already underway; or
 - (c) further delay the effective date of IFRS 17.

6. The Board noted that a small number of respondents included new concerns and implementation questions in their comment letters on the Exposure Draft. The staff will analyse the new concerns and implementation questions and report to the Board at a future meeting so that the Board can decide what, if any, action is needed to address them. The staff think that, at this stage, further changes to IFRS 17 are more likely to disrupt rather than help the implementation process. However, other action such as educational material might be appropriate to continue to support implementation of IFRS 17.

Papers for this meeting and summary of the staff recommendations

7. The papers for this meeting provide an analysis of the following topics:
- (a) proposed amendments to confirm without substantive redeliberation—see Agenda Paper 2A *Proposed amendments to be finalised*;
 - (b) insurance acquisition cash flows—see Agenda Paper 2B *Expected recovery of insurance acquisition cash flows*; and
 - (c) reinsurance contracts held—see Agenda Paper 2C *Reinsurance contracts held—recovery of losses*.
8. The following paragraphs summarise the staff recommendations in these papers.

Proposed amendments to be finalised (Agenda Paper 2A)

9. In Agenda Paper 2A the staff recommend the Board finalise the following amendments to IFRS 17 as proposed in the Exposure Draft:
- (a) scope exclusion for loans;
 - (b) contractual service margin attributable to investment services—coverage units for insurance contracts with direct participation features;
 - (c) presentation in the statement of financial position—portfolio instead of group level;
 - (d) applicability of the risk mitigation option—reinsurance contracts held;
 - (e) transition reliefs for business combinations; and
 - (f) transition reliefs for the risk mitigation option—application from the transition date and the option to apply the fair value approach.

Expected recovery of insurance acquisition cash flows (Agenda Paper 2B)

10. In Agenda Paper 2B the staff recommend the Board:
- (a) finalise the proposed amendment to IFRS 17 that would require an entity to allocate insurance acquisition cash flows that are directly attributable to a group of insurance contracts applying a systematic and rational method:
 - (i) to that group; and

- (ii) to any groups that include contracts that are expected to arise from renewals of the contracts in that group.
- (b) confirm that the unit of account for an asset for insurance acquisition cash flows is the group of insurance contracts to which those cash flows have been allocated.
- (c) finalise the proposed requirements for an entity to assess the recoverability of an asset for insurance acquisition cash flows if facts and circumstances indicate the asset may be impaired.
- (d) finalise the proposed requirements for an entity to disclose:
 - (i) a reconciliation from the opening to the closing balance of assets for insurance acquisition cash flows, showing separately any recognition of impairment losses and reversals of impairment losses; and
 - (ii) quantitative information, in appropriate time bands, about when an entity expects to derecognise an asset for insurance acquisition cash flows and include those cash flows in the measurement of the group of insurance contracts to which they are allocated.
- (e) retain, unchanged, the requirement in IFRS 17 for an entity to present any asset for insurance acquisition cash flows in the carrying amount of the related portfolios of insurance contracts issued.

Reinsurance contracts held—recovery of losses (Agenda Paper 2C)

11. In Agenda Paper 2C the staff recommend the Board:
- (a) extend the scope of the proposed amendment to IFRS 17 to require an entity to adjust the contractual service margin of a group of reinsurance contracts held, 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.
 - (b) amend the proposed calculation of the income, as a consequence of the extension of the scope of the proposed amendment, to require an entity to

determine the amount of a loss recovered from a reinsurance contract held by multiplying:

- (i) the loss recognised on the group of underlying insurance contracts;
and
 - (ii) the percentage of claims on underlying insurance contracts the entity expects to recover from the reinsurance contract held.
- (c) not add the proposed footnote to paragraph BC304 of the Basis for Conclusions on IFRS 17.
- (d) confirm that the amendment to IFRS 17 described in paragraph 11(a) of this paper would apply only when the reinsurance contract held is recognised before or at the same time as the loss is recognised on the underlying insurance contracts.
- (e) clarify, in the final amendments to IFRS 17, that paragraph 66(c)(ii) of IFRS 17—for subsequent measurement of a group of reinsurance contracts held when a group of underlying insurance contracts become onerous—applies when underlying insurance contracts are measured applying the premium allocation approach.

Next steps

12. The staff expect to present papers to the Board on the remaining topics for discussion at future meetings. The staff anticipate presenting a paper to the Board regarding the proposed effective date of IFRS 17 and the proposed extension of the IFRS 9 *Financial Instruments* temporary exemption in IFRS 4 towards the end of redeliberations.
13. The staff expect that the timetable will allow sufficient time for the Board to consider further the feedback on the remaining topics and to finalise any resulting amendments, in line with the Board's plan as stated in the Exposure Draft, in mid-2020.

Appendix A—topics the Board decided at its November 2019 meeting to discuss at future meetings

Topic	Agenda Paper
Scope exclusion for loans	AP2A December 2019
Contractual service margin attributable to investment services—coverage units for insurance contracts with direct participation features	AP2A December 2019
Presentation in the statement of financial position—portfolio instead of group level	AP2A December 2019
Applicability of the risk mitigation option—reinsurance contracts held	AP2A December 2019
Transition reliefs for business combinations	AP2A December 2019
Transition reliefs for the risk mitigation option—application from the transition date and the option to apply the fair value approach	AP2A December 2019
Scope exclusion for credit cards	Future meeting
Expected recovery of insurance acquisition cash flows	AP2B December 2019
Contractual service margin attributable to investment services—coverage units for insurance contracts without direct participation features, disclosures and terminology	Future meeting
Reinsurance contracts held—recovery of losses	AP2C December 2019
Applicability of the risk mitigation option—non-derivative financial instruments at fair value through profit or loss	Future meeting
Effective date of IFRS 17	Future meeting
Extension of the IFRS 9 temporary exemption in IFRS 4	Future meeting
Transition—the prohibition from applying the risk mitigation option retrospectively	Future meeting
Minor amendments	Future meeting
Level of aggregation—annual cohorts for some specific insurance contracts	Future meeting
Business combinations—contracts acquired in their settlement period	Future meeting
Interim financial statements	Future meeting
Additional specific transition modifications and reliefs (including transition requirements for insurance acquisition cash flows)	Future meeting

STAFF PAPER

December 2019

IASB[®] meeting

Project	Amendments to IFRS 17		
Paper topic	Proposed amendments to be finalised		
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Purpose of the paper

1. This paper discusses the proposed amendments to IFRS 17 *Insurance Contracts* that the International Accounting Standards Board (Board) tentatively decided, at its November 2019 meeting, to confirm at a future meeting without any substantive redeliberation.
2. The proposed amendments that the Board is asked to finalise at this meeting are the following:
 - (a) scope exclusion for loans (paragraphs 6–13 of this paper);
 - (b) contractual service margin attributable to investment services—coverage units for insurance contracts with direct participation features (paragraphs 14–16 of this paper);
 - (c) presentation in the statement of financial position—portfolio instead of group level (paragraphs 17–21 of this paper);
 - (d) applicability of the risk mitigation option—reinsurance contracts held (paragraphs 22–24 of this paper);
 - (e) transition reliefs for business combinations (paragraphs 25–29 of this paper);and

- (f) transition reliefs for the risk mitigation option—application from the transition date and the option to apply the fair value approach (paragraphs 30–35 of this paper).

Summary of staff recommendations

- 3. The staff recommend the Board finalise the amendments listed in paragraph 2 of this paper as proposed in the Exposure Draft *Amendments to IFRS 17*.

Structure of the paper

- 4. For each of the proposed amendments listed in paragraph 2 of this paper, the paper provides:
 - (a) an overview of the proposals in the Exposure Draft;
 - (b) an overview of the feedback; and
 - (c) the staff analysis, recommendations and questions for Board members.
- 5. Appendix A to this paper include extracts from the Basis for Conclusions on the Exposure Draft relevant for those proposed amendments.

Scope exclusion for loans

Proposals in the Exposure Draft

- 6. The Exposure Draft proposed that an entity would choose to apply IFRS 17 or IFRS 9 *Financial Instruments* 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, using the IFRS 17 definition of a portfolio. The choice for each portfolio would be irrevocable.

7. The Exposure Draft also proposed transition requirements in IFRS 9 for entities that will:
- (a) choose, applying the amended IFRS 17, to apply IFRS 9 to the loan contracts discussed in paragraph 6 of this paper; and
 - (b) apply the amended IFRS 17 after they have already applied IFRS 9 and for which the transition requirements in IFRS 9 would not be applicable (ie entities that do not apply the temporary exemption in IFRS 4 *Insurance Contracts* and, therefore, are required to apply IFRS 9 (as issued in 2014) for annual reporting periods beginning on or after 1 January 2018).

Feedback

8. Of the respondents who provided comments on the proposed scope exclusion for the loan contracts discussed in paragraph 6 of this paper:
- (a) most respondents generally agreed with the Board’s proposal and rationale for proposing the amendment to IFRS 17; and
 - (b) a small number of respondents:
 - (i) disagreed with the scope exclusion because they believe that an entity should be required to apply IFRS 17 to all loan contracts that meet the definition of an insurance contract to appropriately reflect the insurance feature of those contracts; or
 - (ii) suggested the Board amend the proposal so that an entity would be *required* to apply IFRS 9 to the loan contracts that would be captured by the proposed scope exclusion because they believe that mandating the use of the same accounting requirements for the same type of contracts would ensure consistency and comparability between entities, without imposing IFRS 17 implementation costs to entities issuing those contracts.

9. Of the respondents who agreed with the Board’s proposal:
- (a) a small number of respondents:
 - (i) commented on the implications of accounting for such loan contracts applying IFRS 9. Those respondents suggested the Board confirm that the contractual cash flows of such loan contracts are not solely payments of principal and interest (SPPI) and, therefore, applying IFRS 9, such loan contracts would be accounted for at fair value through profit or loss.
 - (ii) highlighted the importance for an entity to disclose, in the notes to the financial statements, whether the entity has elected to apply IFRS 9 to such loan contracts.
 - (b) one respondent expressed concerns that requiring an entity to make the proposed choice portfolio by portfolio using the IFRS 17 definition of a portfolio would be burdensome to apply. This is because an entity that chooses to apply IFRS 9 to such loan contracts would be required to first apply IFRS 17 to identify a portfolio of contracts.
 - (c) one respondent provided a drafting suggestion about the wording of the proposed amendment that, in the view of this respondent, would reduce the risk of misinterpretation of the type of contracts that would be captured by the proposed scope exclusion. This respondent noted that in some mortgage contracts the amount of compensation under the insurance feature of the contract is limited to the amount required to settle what would have been the policyholder’s obligation absent the insurance feature. This respondent, therefore, suggested the Board amend the wording of the proposed scope exclusion as follows: ‘Some contracts meet the definition of an insurance contract but limit the compensation for insured events to the amount otherwise required to settle the policyholder’s obligation created by the contract (for example, loans with death waivers).’

10. A small number of respondents commented on the proposed transition requirements in IFRS 9. Those respondents expressed support for those proposed transition requirements.

Staff analysis and recommendations

11. The staff note that the Board considered the concerns and suggestions from respondents discussed in paragraphs 8(b) and 9(a)(i) of this paper when developing the Exposure Draft. Specifically, at the February 2019 Board meeting, the Board considered whether to:
- (a) propose an amendment to IFRS 17 so that entities would be required, rather than permitted, to apply IFRS 9 to the loan contracts discussed in paragraph 6 of this paper. The Board agreed with staff recommendations in Agenda Paper 2A *Loans that transfer significant insurance risk* of the February 2019 Board meeting not to require an entity to apply IFRS 9 to such loan contracts for the following reasons:
 - (i) amending IFRS 17 to require entities to apply IFRS 9 to such loan contracts might introduce a significant change for entities that currently account for those contracts applying IFRS 4 and are preparing to implement IFRS 17. Some entities might need to develop systems to account for contracts with insurance and non-insurance components in accordance with IFRS 9, while they are already developing systems to implement IFRS 17 to account for those contracts.
 - (ii) prohibiting entities from applying IFRS 17 to those loan contracts would not enable entities that issue those loan contracts and other types of insurance contracts to account for both types of contracts in the same way.
 - (iii) those loan contracts meet the definition of an insurance contract because they transfer significant insurance risk. IFRS 17 was developed with the objective that entities issuing contracts that transfer significant insurance risk faithfully represent those

contracts. The accounting model in IFRS 17 appropriately reflects the features of these contracts.

- (b) specify that, if an entity chooses to apply IFRS 9 to such loan contracts, the entity would always measure them at fair value through profit or loss. The Board concluded that such specification was not necessary noting that IFRS 9 is a principle-based and sufficiently robust Standard to handle complex financial instruments.

12. Regarding the concerns discussed in paragraph 9(b) of this paper, the staff note that, to avoid incurring costs to implement IFRS 17, entities that do not issue insurance contracts other than such loan contracts would elect to apply IFRS 9 to all such loan contracts. Therefore, those entities would not need to apply IFRS 17 to identify portfolios of insurance contracts.

13. The staff recommend the Board finalise the amendment discussed in paragraphs 6–7 of this paper as proposed in the Exposure Draft, reflecting the drafting suggestion discussed in paragraph 9(c) of this paper, because:

- (a) the feedback from outreach and comment letters provides support for the Board to finalise that amendment; and
- (b) the staff have not identified points the Board has not considered previously.

Question 1 for Board members

Do you agree that the Board should finalise:

- (a) the proposed amendment that would permit an entity to choose, portfolio by portfolio, 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 otherwise required to settle the policyholder’s obligation created by the contract?
- (b) the proposed transition requirements in IFRS 9 for entities that choose to apply IFRS 9 to insurance contracts that limit the compensation for insured events to the amount otherwise required to settle the policyholder’s obligation created by the contract?

Contractual service margin attributable to investment services—coverage units for insurance contracts with direct participation features

Proposals in the Exposure Draft

14. The Exposure Draft proposed to 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.

Feedback

15. All respondents who commented on the proposed clarification discussed in paragraph 14 of this paper supported the clarification.

Staff analysis and recommendations

16. The staff recommend the Board finalise the amendment discussed in paragraph 14 of this paper as proposed in the Exposure Draft because the feedback from outreach and comment letters provides support for the proposed clarification for identifying coverage units for insurance contracts with direct participation features.

Question 2 for Board members

Do you agree that the Board should finalise the proposed amendment to 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?

Presentation in the statement of financial position—portfolio instead of group level

Proposals in the Exposure Draft

17. The Exposure Draft proposed that an entity present separately in the statement of financial position the carrying amount of portfolios (rather than groups) of insurance contracts issued that are assets and those that are liabilities. The proposed amendment

would also apply to portfolios of reinsurance contracts held that are assets and those that are liabilities.

Feedback

18. Overall, respondents expressed support for the proposed amendment to the presentation of insurance contracts in the statement of financial position and agreed with the Board’s conclusion that the proposed amendment would decrease operational complexity and IFRS 17 implementation costs.
19. However, consistent with feedback during the development of the Exposure Draft, a small number of respondents continued to express the view that they would prefer the Board to require an entity to present insurance contract assets and liabilities at an entity level, rather than at a portfolio level. Some of those respondents:
 - (a) noted that different entities will identify portfolios in different ways and, therefore, those respondents think that a higher level of presentation in the statement of financial position would provide more useful information for users of financial statements to compare entities; or
 - (b) expressed the view that presenting separately insurance contract assets and liabilities does not provide useful information to users of financial statements.

Staff analysis and recommendations

20. The staff note that the Board considered the concerns and suggestions from respondents discussed in paragraph 19 of this paper when developing the Exposure Draft. Specifically, as explained in paragraph BC97 of the Basis for Conclusions on the Exposure Draft, when developing the Exposure Draft, the Board considered but rejected some stakeholders’ suggestions that presentation of insurance contracts in the statement of financial position should be at an entity level because that would risk a significant loss of useful information for users of financial statements.
21. The staff recommend the Board finalise the amendment discussed in paragraph 17 of this paper as proposed in the Exposure Draft because:

- (a) the feedback from outreach and comment letters provides support for the Board to finalise the proposal for the presentation of insurance contracts in the statement of financial position; and
- (b) the staff have not identified points the Board has not considered previously.

Question 3 for Board members

Do you agree that the Board should finalise the proposed amendment that would require an entity to present separately in the statement of financial position the carrying amount of portfolios of insurance contracts issued and of reinsurance contracts held that are assets and those that are liabilities?

Applicability of the risk mitigation option—reinsurance contracts held

Proposals in the Exposure Draft

22. The Exposure Draft proposed to extend the risk mitigation option available when an entity uses derivatives to mitigate financial risk arising from insurance contracts with direct participation features (ie contracts to which the variable fee approach applies). In accordance with the proposal, the option would also apply in circumstances in which an entity uses reinsurance contracts held to mitigate financial risk arising from insurance contracts with direct participation features. The entity would be permitted to include in profit or loss some or all of the changes in the effect of financial risk on insurance contracts with direct participation features that usually adjust the contractual service margin. Doing so reduces accounting mismatches because the change resulting from financial risk in a reinsurance contract held is included in profit or loss.

Feedback

23. All respondents who commented on the proposal to extend the risk mitigation option to circumstances in which an entity uses reinsurance contracts held to mitigate financial risk arising from insurance contracts with direct participation features:
- (a) supported the proposal; and

- (b) agreed with the Board’s view that the proposal would reduce accounting mismatches.

Staff analysis and recommendations

24. The staff recommend the Board finalise the amendment discussed in paragraph 22 of this paper as proposed in the Exposure Draft because the feedback from outreach and comment letters provides support for the proposal that would permit an entity to apply the risk mitigation option when the entity uses reinsurance contracts held to mitigate financial risk arising from insurance contracts with direct participation features.

Question 4 for Board members

Do you agree that the Board should finalise the proposed amendment that would permit an entity to also apply the risk mitigation option when the entity uses reinsurance contracts held to mitigate financial risk arising from insurance contracts with direct participation features?

Transition reliefs for business combinations

Proposals in the Exposure Draft

25. IFRS 17 requires an entity to classify a liability for settlement of claims as a liability for remaining coverage if the entity acquired the insurance contract during the claims settlement period and, at the acquisition date, the amount of claims is still uncertain.
26. The Exposure Draft proposed that, when applying IFRS 17 for the first time, an entity:
- (a) applying the modified retrospective approach, to the extent the entity cannot apply the requirement discussed in paragraph 25 of this paper retrospectively, classify as a liability for incurred claims a liability for settlement of claims incurred before an insurance contract was acquired;
and

- (b) applying the fair value approach be permitted to classify such a liability as a liability for incurred claims.

Feedback

- 27. Overall, respondents expressed support for the proposed amendment to the IFRS 17 transition requirements discussed in paragraph 26 of this paper. Some respondents agreed with the Board's view that the proposed amendment would provide practical relief when an entity does not have information to apply the requirements of IFRS 17 retrospectively.
- 28. A small number of respondents suggested the Board confirm whether the proposed amendment would apply to all contracts acquired, rather than just to contracts acquired in a business combination within the scope of IFRS 3 *Business Combinations*. One of those respondents suggested the Board amend the wording of the proposed transition reliefs to clarify that those reliefs would apply to a transfer of insurance contracts that do not form a business or a business combination within the scope of IFRS 3, consistent with the wording in paragraph B93 of IFRS 17.

Staff analysis and recommendations

- 29. The staff recommend the Board:
 - (a) finalise the amendment to IFRS 17 transition requirements discussed in paragraph 26 of this paper because the feedback from outreach and comment letters provides support for the Board to finalise the proposed additional transition reliefs for insurance contracts acquired; and
 - (b) confirm that the proposed amendment would apply to contracts acquired in a transfer of insurance contracts that do not form a business or in a business combination within the scope of IFRS 3, in the light of the feedback discussed in paragraph 28 of this paper.

Question 5 for Board members

Do you agree that the Board should finalise the proposed amendment discussed in paragraph 26 of this paper that would provide transition reliefs for insurance contracts acquired in a transfer of insurance contracts that do not form a business or in a business combination within the scope of IFRS 3?

Transition reliefs for the risk mitigation option—application from the transition date and the option to apply the fair value approach***Proposals in the Exposure Draft***

30. IFRS 17 allows an entity that meets specified conditions not to recognise a change in the contractual service margin for some or all of the effect of financial risk on a group of insurance contracts with direct participation features (the risk mitigation option).
31. The Exposure Draft proposed that an entity:
 - (a) apply the risk mitigation option prospectively from the transition date, rather than the date of initial application. An entity would be required to designate risk mitigation relationships at or before the date it applies the option.
 - (b) that can apply IFRS 17 retrospectively to a group of insurance contracts with direct participation features be permitted to instead apply the fair value approach to that group if it meets specified criteria relating to risk mitigation.

Feedback

32. Overall, respondents expressed support for the proposed amendments to the IFRS 17 transition requirements discussed in paragraph 31 of this paper.
33. Some respondents who supported the proposed amendments would prefer that the Board amend IFRS 17 to allow retrospective application of the risk mitigation option, in addition, or as an alternative, to the proposed transition requirements discussed in paragraph 31 of this paper.

Staff analysis and recommendations

34. The staff note that the Board tentatively decided, at its November 2019 meeting, to consider further suggestions from respondents to allow a retrospective application of the risk mitigation option. Even if the Board were to amend IFRS 17 to allow retrospective application of the risk mitigation option, the staff think that the amendments to IFRS 17 transition requirements discussed in paragraph 31 of this paper would still provide relief for entities that would not be able to apply the risk mitigation option retrospectively.
35. The staff recommend the Board finalise the amendments to the IFRS 17 transition requirements discussed in paragraph 31 of this paper because the feedback from outreach and comment letters provides support for the Board to finalise the proposed additional transition reliefs for the use of the risk mitigation option.

Question 6 for Board members

Do you agree that the Board should finalise the proposed amendment discussed in paragraph 31 of this paper that would provide transition reliefs relating to the use of the risk mitigation option?

Appendix A—relevant extracts from the Basis for Conclusions on the Exposure Draft

Scope exclusions—loan contracts that meet the definition of an insurance contract (paragraph 8A and Appendix D)

Proposed amendment

- BC9 IFRS 17 applies to all contracts that transfer significant insurance risk, regardless of the type of entity issuing the contracts, with some specific scope exclusions. The Board has been made aware that some credit card contracts and loan contracts transfer significant insurance risk and, consequently, are within the scope of IFRS 17. Examples are:
- (a) ...
 - (b) loan contracts such as a loan contract with a death waiver and a lifetime mortgage with a no-negative-equity-guarantee.
- BC10 The Exposure Draft proposes two additional scope exclusions to the requirements in IFRS 17:
- (a) ...
 - (b) paragraph 8A proposes that an entity may choose to apply IFRS 9 *Financial Instruments* instead of IFRS 17 to contracts that meet the definition of an insurance contract but that limit the compensation for insured events to the amount required to settle the policyholder's obligation created by the contract (for example, loan contracts 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.
- BC11 The Board decided it would not be necessary to propose additional disclosure requirements in IFRS 17 or IFRS 9 related to the proposed amendments in paragraphs 7(h) and 8A of the Exposure Draft (other than on transition in some circumstances, see paragraph BC30(b)). Both IFRS 17 and IFRS 9 already specify sufficient disclosure requirements for such contracts.

Rationale for changing the requirements

- BC12 The definition of an insurance contract in IFRS 17 is unchanged from IFRS 4, and so the contracts described in paragraph BC9 already meet the definition of an insurance contract applying IFRS 4. However, IFRS 4 permits an entity to separate from a host insurance contract some non-insurance components and apply other IFRS Standards to the non-insurance components. IFRS 4 also allows a wide range of accounting practices for components that are not separated. As a result, some entities may be applying IFRS 9 or IAS 39 *Financial Instruments: Recognition and Measurement*, or an accounting policy similar to the requirements

in those Standards, to such contracts. IFRS 17 is more restrictive on the separation of non-insurance components and is more specific in its requirements for accounting for all aspects of insurance contracts in their entirety. The Board was persuaded that for some entities that apply accounting policies consistent with IFRS 9 or IAS 39 to some credit card contracts and loan contracts that transfer significant insurance risk, the costs of applying IFRS 17 might exceed the benefits of changing to applying IFRS 17, as described in paragraphs BC13–BC22.

Proposed amendment to permit an entity to apply IFRS 9, instead of IFRS 17, to specified contracts that meet the definition of an insurance contract (paragraph 8A)

- BC18 Some contracts meet the definition of an insurance contract but limit the compensation for insured events to the amount required to settle the policyholder’s obligation created by the contract (for example, loan contracts with death waivers). An entity would provide useful information about such contracts applying either IFRS 17 or IFRS 9. Both credit risk and insurance risk are prominent features in such contracts and, as noted in paragraph BC14, both Standards have requirements that can address these risks, albeit with a different focus.
- BC19 Hence, the Board concluded:
- (c) requiring an entity to apply IFRS 17 to those contracts, when the entity had previously been applying an accounting policy consistent with IFRS 9 or IAS 39 to those contracts (or vice versa), could impose cost without a corresponding benefit; and
 - (d) more useful information for users of financial statements might be provided if an entity were to apply the same Standard to those contracts as it applies to other similar contracts it issues.
- BC20 Accordingly, the Board concluded that, for such contracts, an entity would be required to make the choice between applying IFRS 17 or IFRS 9 for each portfolio of insurance contracts and the choice for each portfolio would be irrevocable.
- BC21 The Board considered whether the proposed amendment in paragraph 8A of the Exposure Draft should be applied on a contract-by-contract basis, rather than on a portfolio of insurance contracts basis. Requiring a contract-by-contract basis would be consistent with the scope exclusion for fixed-fee service contracts in paragraph 8 of IFRS 17. However, the Board concluded that applying the proposed amendment in paragraph 8A of the Exposure Draft on a portfolio basis would mitigate the lack of comparability that might otherwise arise between similar contracts issued by the same entity, and between similar contracts issued by different entities.
- BC22 The Board considered a suggestion that IFRS 17 be amended to require an entity to separate a loan component from such an insurance contract, consistent with existing accounting practice for some contracts. However, the Board confirmed the approach in paragraphs 10–13 of IFRS 17—that components of a contract should

not be separated if they are highly interrelated. As explained in paragraph BC10(a) of the Basis for Conclusions on IFRS 17, it would be difficult for an entity to separate such components routinely and setting requirements to do so would result in complexity. Such separation would also ignore interdependencies between components, with the result that the sum of the values of the components may not always equal the value of the contract as a whole, even on initial recognition.

Transition requirements when an entity chooses to apply IFRS 9 to contracts specified in paragraph 8A (Appendix D)

- BC23 Entities that do not apply the temporary exemption in IFRS 4 are required to apply IFRS 9 (as issued in 2014) for annual periods beginning on or after 1 January 2018. Accordingly, some entities will apply the amended IFRS 17 after they have already applied IFRS 9.
- BC24 The Exposure Draft proposes transition requirements for such entities that choose, applying paragraph 8A of the Exposure Draft, to apply IFRS 9 to insurance contracts that limit the compensation for insured events to the amount required to settle the policyholder’s obligation created by the contract.
- BC25 Without those proposed requirements in the Exposure Draft, the transition requirements in Section 7.2 of IFRS 9 (as issued in 2014) would not be applicable for entities that have already applied IFRS 9. Accordingly, an entity would be required to apply the proposed amendments in the Exposure Draft retrospectively applying IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*.
- BC26 Retrospective application in such circumstances would be consistent with the general requirement that an entity applies the classification and measurement requirements in IFRS 9 retrospectively. However, in some circumstances, an entity may not be able to apply the proposed amendments in the Exposure Draft retrospectively without the use of hindsight.
- BC27 When the Board developed the transition requirements in IFRS 9, it provided requirements to address scenarios in which it would be impracticable for entities to apply particular requirements retrospectively. The Board expects that similar scenarios might arise when an entity first applies IFRS 9 to contracts addressed by paragraph 8A of the Exposure Draft. Accordingly, the Exposure Draft proposes that an entity would apply the relevant transition requirements in IFRS 9 that are necessary to initially apply the proposed amendment in paragraph 8A of the Exposure Draft.
- BC28 The Board also considered specific transition requirements related to the fair value option in IFRS 9. An entity’s decision to apply IFRS 9 to insurance contracts that limit the compensation for insured events to the amount required to settle the policyholder’s obligation created by the contract could change, either partially or in full, the classification and measurement of such contracts. Such changes may

create or eliminate accounting mismatches between the contracts and financial liabilities an entity might consider to be related to the contracts. Therefore, the Board decided to propose amendments to the IFRS 9 transition requirements that would permit an entity to designate, or that would require an entity to revoke its previous designation of, a financial liability at the date of initial application of the proposed amendments to the extent that a new accounting mismatch is created, or a previous accounting mismatch no longer exists, as a result of applying the proposed amendment in paragraph 8A of the Exposure Draft.

- BC29 The Board noted that paragraph C29 of IFRS 17 already permits an entity to designate a financial asset and requires an entity to revoke its previous designation of a financial asset at the date of initial application of IFRS 17. In addition, paragraphs C32–C33 of IFRS 17 require disclosures about those assets. Accordingly, the Board decided it is unnecessary to propose further requirements for the designation or de-designation of financial assets under the fair value option in IFRS 9.
- BC30 The Exposure Draft also proposes the following amendments for consistency with the transition requirements in IFRS 9 and IFRS 17:
- (a) an entity would not be required to restate prior periods to reflect the effect of the proposed amendments, and could choose to do so only if such restatement is possible without the use of hindsight and if the restated financial statements reflect all the requirements in IFRS 9 for the affected financial instruments;
 - (b) an entity would disclose, in addition to any disclosures required by other IFRS Standards, information about the changes in the classification and measurement of contracts as a result of applying the proposed amendments in paragraph 8A of the Exposure Draft; and
 - (c) an entity would not be required to disclose, for the current period or any prior period presented, the quantitative information otherwise required by paragraph 28(f) of IAS 8.

Contractual service margin attributable to investment-related service

Proposed amendment

- BC50 IFRS 17 requires an entity to recognise the contractual service margin, which is the unearned profit in a group of insurance contracts, in profit or loss over time on the basis of coverage units. The number of coverage units in a group of contracts is determined by considering, for each contract, the quantity of the benefits provided under the contract and the expected period over which those benefits will be provided. The Exposure Draft proposes two amendments relating to the identification of coverage units applying paragraph B119:
- (a) ...

- (b) the second proposed amendment would 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.

Rationale for changing the requirements

- BC54 A question submitted to the Transition Resource Group for IFRS 17 indicated that it would be useful to clarify that an entity is required to consider investment-related service when determining coverage units for insurance contracts with direct participation features. Transition Resource Group members thought coverage units for contracts with direct participation features should include investment-related service because those contracts are substantially investment-related service contracts. However, Transition Resource Group members held different views on whether IFRS 17 requires, permits or prohibits such an approach. Hence, the Board decided to clarify that such an approach is required.

Presentation in the statement of financial position (paragraphs 78–79, 99 and 132)

Proposed amendment

- BC91 The Exposure Draft proposes to amend paragraph 78 of IFRS 17, which requires an entity to present separately in the statement of financial position the carrying amount of groups of insurance contracts issued that are assets and those that are liabilities and the carrying amount of groups of reinsurance contracts held that are assets and those that are liabilities.
- BC92 The proposed amendment to paragraph 78 of IFRS 17 would require an entity to instead present separately in the statement of financial position the carrying amounts of portfolios of insurance contracts issued that are assets and those that are liabilities and portfolios of reinsurance contracts held that are assets and those that are liabilities. There are no proposed changes to the measurement requirements of IFRS 17 as a result of this proposed amendment.
- BC93 The Exposure Draft proposes consequential amendments to paragraph 79 of IFRS 17 and to the disclosure requirements in paragraphs 99 and 132 of IFRS 17 to reflect a portfolio rather than a group level of presentation.

Rationale for changing the requirements

- BC94 The requirements in IFRS 17 for presenting groups of insurance contracts are consistent with the requirements for recognising and measuring groups of insurance contracts. The fulfilment cash flows included in the measurement of insurance contracts are the same regardless of the level at which they are measured. However, an entity is required to allocate fulfilment cash flows that

relate to remaining coverage at a group level to determine and recognise the contractual service margin (or loss on onerous contracts).

- BC95 Some stakeholders expressed concerns that identifying fulfilment cash flows for each group of insurance contracts typically requires integrating independent systems, such as cash management systems and actuarial systems at a level of a group of contracts. Some of those fulfilment cash flows do not need to be allocated to groups to apply the measurement requirements of IFRS 17, for example, amounts related to the settlement of incurred claims. Those stakeholders explained that new systems would need to be implemented to apply this aspect of IFRS 17, at significant cost. Those stakeholders suggested that presenting insurance contracts at a level that is higher than a group level would provide them with a meaningful practical relief that, in their view, would not significantly diminish the usefulness of information for users of financial statements.
- BC96 Feedback from initial outreach with users of financial statements supports the stakeholder views set out in paragraph BC95—that presenting insurance contracts at a level that is higher than a group level would not significantly diminish the usefulness of information when compared to presentation at a group level. Considering this information, the Board concluded that the benefit of the proposed amendment to paragraph 78 of IFRS 17 (operational relief for preparers of financial statements) would outweigh the cost (potential limited loss of useful information for users of financial statements).

Other approaches considered and rejected

- BC97 The Board considered some stakeholders' suggestions that presentation of insurance contracts in the statement of financial position should be at an entity level and rejected that suggestion because that would risk a greater loss of useful information for users of financial statements.

Applicability of the risk mitigation option (paragraph B116)

Proposed amendments

- BC101 The Exposure Draft proposes to extend the option in paragraphs B115–B116 of IFRS 17 relating to the accounting treatment of some types of risk mitigation. That option permits an entity to reflect some or all of the changes in the effect of financial risk on insurance contracts with direct participation features that usually adjust the contractual service margin immediately in profit or loss. An entity may apply that option if, and only if, the entity mitigates those financial risks using derivatives and meets the conditions in paragraph B116 of IFRS 17. Without that exception, the variable fee approach would create an accounting mismatch when an entity uses derivatives to mitigate financial risk in insurance contracts. Specifically:

- (a) the change in the fair value of the derivative would be recognised in profit or loss applying IFRS 9; but
- (b) the change in the insurance contract, the risk of which was mitigated by the derivative, would adjust the contractual service margin applying paragraph 45 of IFRS 17.

BC102 The proposed amendment in paragraph B116 of the Exposure Draft would extend that option to be available when an entity mitigates financial risk on insurance contracts with direct participation features using reinsurance contracts held.

BC103 The Board concluded that additional disclosures as a result of this amendment would not be needed because the existing disclosures relating to paragraphs B115–B116 of IFRS 17 would be sufficient.

Rationale for changing the requirements

BC104 Some entities purchase reinsurance contracts that cover insurance contracts with direct participation features that the entities issue. Those reinsurance contracts transfer both non-financial risk and financial risk to the reinsurer.

BC105 All reinsurance contracts held are accounted for applying the general measurement requirements in IFRS 17. Similar to previous feedback about derivatives, stakeholders expressed concern that an accounting mismatch arises because:

- (a) the change resulting from financial risk in a reinsurance contract held would be recognised in profit or loss applying paragraph 87 of IFRS 17; but
- (b) the change resulting from financial risk in underlying insurance contracts with direct participation features would adjust the contractual service margin applying paragraph 45 of IFRS 17.

BC106 The Board acknowledged that the concern expressed by stakeholders for reinsurance contracts held is similar to the concern previously raised in relation to derivatives—the identified accounting mismatches are created by the variable fee approach. The Board decided to propose an amendment to IFRS 17 that extends the scope of the risk mitigation option in paragraph B116 of IFRS 17 to address this concern. As a consequence of the proposed amendment, the accounting for insurance contracts with direct participation features may be different depending on whether the entity has purchased a reinsurance contract. However, the Board concluded that such an amendment would be acceptable because it is consistent with the option introduced previously to address a similar concern for derivatives.

Transition modifications and reliefs (paragraphs C3(b), C5A, C9A and C22A)

- BC119 The Exposure Draft proposes amendments that would provide additional transition modifications and reliefs for entities applying IFRS 17 for the first time for:
- (a) the classification of contracts acquired in their settlement period (paragraphs BC120–BC124); and
 - (b) the risk mitigation for insurance contracts with direct participation features (paragraphs BC125–BC133).

Classification of contracts acquired in their settlement period

Proposed amendment

- BC120 Liabilities that relate to the settlement of claims for insured events are generally treated as liabilities for incurred claims. However, if an entity acquires the insurance contract after the insured event occurred and the amount for which it will be settled is uncertain, IFRS 17 requires an entity to classify the liability that relates to the settlement of claims for that insured event as a liability for remaining coverage. For the acquiring entity, the insured event is the determination of the ultimate cost of those claims.
- BC121 Paragraph C9A of the Exposure Draft proposes an additional modification to the modified retrospective approach that would permit an entity to classify such liabilities for insurance contracts acquired before the transition date as a liability for incurred claims rather than a liability for remaining coverage. Consistent with the other requirements for the modified retrospective approach, an entity would be permitted to apply this modification only to the extent that it does not have reasonable and supportable information to apply a retrospective approach. Paragraph C22A of the Exposure Draft proposes that an entity applying the fair value approach would have an option to classify such a liability as a liability for incurred claims.
- BC122 No additional disclosures are proposed as a result of the proposed amendments in paragraphs C9A and C22A of the Exposure Draft. Paragraph 115 of IFRS 17 requires an entity to explain how it determined the measurement of insurance contracts at the transition date to enable users of financial statements to understand the nature and significance of the methods used and judgements applied in determining the transition amounts.

Rationale for changing the requirements

- BC123 The Board set the requirements in the modified retrospective approach to achieve the closest outcome to retrospective application possible using reasonable and supportable information available without undue cost or effort. Each modification

addresses specific areas of the requirements the Board expected would often be impracticable to apply retrospectively.

- BC124 Since IFRS 17 was issued, the Board has heard that it will often be impracticable for an entity to classify contracts acquired in their settlement period before the transition date as either a liability for remaining coverage or a liability for incurred claims. At the time those contracts were acquired, the entity may have managed the claims for those contracts with other contracts it issued and may have gathered data at a higher level than is required to distinguish between claims from contracts issued and claims from contracts acquired. The Board noted that the existing requirements in the modified retrospective approach and reliefs in the fair value approach do not resolve this challenge. Accordingly, the Board concluded that a new specific modification and new relief should be proposed for transition to IFRS 17.

Risk mitigation for insurance contracts with direct participation features

Proposed amendment

- BC125 Paragraph B115 of IFRS 17 allows an entity an accounting policy choice to reflect some or all of the changes in the effect of financial risk on insurance contracts with direct participation features that usually adjust the contractual service margin immediately in profit or loss. An entity can apply the option if, and only if, the entity mitigates those financial risks using derivatives and meets the conditions in paragraph B116 of IFRS 17 (or mitigates those financial risks using reinsurance contracts held applying the proposed amendment in paragraph B116 of the Exposure Draft). Applying paragraph C3(b) of IFRS 17, an entity is not permitted to apply the risk mitigation option for periods before the date of initial application, because the Board concluded that doing so would give rise to the risk of the use of hindsight.
- BC126 The Exposure Draft proposes two amendments to the transition requirements relating to the risk mitigation option:
- (a) the proposed amendment to paragraph C3(b) of IFRS 17 would permit an entity to apply the option in paragraph B115 of IFRS 17 prospectively from the transition date, rather than the date of initial application. To apply the option in paragraph B115 of IFRS 17 from the transition date, an entity would be required to designate risk mitigation relationships at or before the transition date.
 - (b) paragraph C5A of the Exposure Draft proposes that an entity that can apply IFRS 17 retrospectively to a group of insurance contracts would be permitted to instead apply the fair value approach to that group if, and only if:

- (i) the entity chooses to apply the risk mitigation option in paragraph B115 of IFRS 17 to the group prospectively from the transition date; and
- (ii) before the transition date, the entity has been using derivatives or reinsurance contracts held to mitigate financial risk arising from the group of insurance contracts.

BC127 The Board concluded that additional disclosures as a result of those amendments would not be needed because the disclosures in paragraphs 114–116 of IFRS 17 already require an entity to explain how it determined the measurement of insurance contracts at the transition date.

Rationale for changing the requirements

BC128 Some stakeholders stated that permitting retrospective application of the risk mitigation option in paragraph B115 of IFRS 17 would enhance comparability of information before and after the date of initial application of IFRS 17. In the Board's view, permitting an entity to apply the risk mitigation option consistently for risk mitigation activities that take place before and after the date of initial application of IFRS 17 could increase comparability between reporting periods and, therefore, provide users of financial statements with useful information. However, as the risk mitigation option can be applied to particular risks in a group of insurance contracts, permitting application of the option retrospectively would risk the use of hindsight and create opportunities for entities to decide the risk mitigation relationships to which to apply the option based on the known accounting outcome. Accordingly, the Board disagreed with a suggestion by stakeholders that an entity should be permitted to apply the risk mitigation option retrospectively.

BC129 Despite concluding that an entity should not be allowed to apply the risk mitigation option retrospectively, the Board sought to address stakeholders' concerns about a lack of consistency in the treatment of risk mitigation activities before and after the date of initial application of IFRS 17. The Board noted that the risk mitigation option is a choice and so an entity could avoid this inconsistency. However, the Board understood that some entities want to use the risk mitigation option, as intended, to address the accounting mismatch between insurance contracts with direct participation features and derivatives that meet specified conditions. As a result, the Board considered whether an alternative approach would allow an entity to avoid the mismatch without risking the use of hindsight.

BC130 The Board concluded it should be possible for an entity to apply the risk mitigation option from a date earlier than the date of initial application of IFRS 17 without risking the use of hindsight. Accordingly, to address concerns about inconsistency between the first reporting period applying IFRS 17 and the restated comparative information, the Board decided to allow an entity to apply the risk mitigation option in the comparative period if it does so prospectively. Applying the option prospectively requires the entity to designate the risk mitigation relationships to

which it will apply the option at or before the transition date.

- BC131 The Board also noted that an entity that uses the fair value transition approach in IFRS 17 avoids the situation in which changes in the fair value of derivatives being used for risk mitigation are reflected in opening retained earnings or equity but the corresponding changes in the insurance contracts are reflected in the contractual service margin. At the transition date, the fair value of derivatives will include only expectations about future cash flows. In the fair value approach, the fair value of insurance contracts at transition would also include only expectations about future cash flows. Any past gains or losses on derivatives and any effects on insurance contracts of past changes in financial risk would be reflected in opening retained earnings. However, applying the existing requirements in IFRS 17, an entity is only permitted to apply the fair value approach if it is impracticable to apply IFRS 17 retrospectively.
- BC132 In the Board's view, applying IFRS 17 retrospectively provides the most useful information about insurance contracts both on transition to IFRS 17, and in future reporting periods. However, the Board concluded that the loss of information would be acceptable if entities with risk mitigation activities were permitted to apply the fair value approach instead of retrospective application. The Board noted that those entities are unable to apply a full retrospective approach because paragraph C3(b) of IFRS 17 prohibits them from applying paragraph B115 of IFRS 17. Furthermore, the Board views the fair value approach as also providing useful information. However, the Board decided to limit the groups of insurance contracts to which this proposed amendment could apply, because it is intended to address only contracts for which stakeholders' concerns relating to risk mitigation apply.

STAFF PAPER

December 2019

IASB® meeting

Project	Amendments to IFRS 17		
Paper topic	Expected recovery of insurance acquisition cash flows		
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Purpose of the paper

1. This paper discusses staff analysis and recommendations about the amendment proposed in the Exposure Draft *Amendments to IFRS 17* relating to insurance acquisition cash flows. This paper follows the tentative decision of the International Accounting Standards Board (Board), at its November 2019 meeting, to consider further the feedback from outreach and comment letters on this proposed amendment.

Summary of staff recommendations

2. The staff recommend the Board:
 - (a) finalise the proposed amendment to IFRS 17 *Insurance Contracts* that would require an entity to allocate insurance acquisition cash flows that are directly attributable to a group of insurance contracts applying a systematic and rational method:
 - (i) to that group; and
 - (ii) to any groups that include contracts that are expected to arise from renewals of the contracts in that group.
 - (b) confirm that the unit of account for an asset for insurance acquisition cash flows is the group of insurance contracts to which those cash flows have been allocated.

- (c) finalise the proposed requirements for an entity to assess the recoverability of an asset for insurance acquisition cash flows if facts and circumstances indicate the asset may be impaired.
- (d) finalise the proposed requirements for an entity to disclose:
 - (i) a reconciliation from the opening to the closing balance of assets for insurance acquisition cash flows, showing separately any recognition of impairment losses and reversals of impairment losses; and
 - (ii) quantitative information, in appropriate time bands, about when an entity expects to derecognise an asset for insurance acquisition cash flows and include those cash flows in the measurement of the group of insurance contracts to which they are allocated.
- (e) retain, unchanged, the requirement in IFRS 17 for an entity to present any asset for insurance acquisition cash flows in the carrying amount of the related portfolios of insurance contracts issued.

Structure of the paper

- 3. This paper provides:
 - (a) an overview of the proposals in the Exposure Draft;
 - (b) an overview of the feedback;
 - (c) the specific feedback, staff analysis, recommendations and questions for Board members on each of the following areas:
 - (i) allocation of insurance acquisition cash flows;
 - (ii) recognition of an asset;
 - (iii) impairment test;
 - (iv) disclosures;

- (v) presentation; and
 - (vi) transition.
4. Appendix A to this paper provides an example of applying the two impairment tests proposed in the Exposure Draft.

Proposals in the Exposure Draft¹

5. Appendix A of IFRS 17 defines insurance acquisition cash flows as cash flows arising from the costs of selling, underwriting and starting a group of insurance contracts that are directly attributable to the portfolio of insurance contracts to which the group belongs. IFRS 17 requires an entity to recognise an asset for any insurance acquisition cash flows relating to a group of insurance contracts that the entity pays before the group is recognised.
6. The Exposure Draft proposed 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:
 - (i) to that group; *and*
 - (ii) to any groups that include contracts that are expected to arise from renewals of the contracts in that group.
 - (b) consistent with the existing requirements of IFRS 17, recognise as an asset insurance acquisition cash flows paid before the group of insurance contracts to which they are allocated is recognised.
 - (c) assess the recoverability of an asset for insurance acquisition cash flows if facts and circumstances indicate the asset may be impaired.
 - (d) provide the following disclosures about such assets:
 - (i) a reconciliation from the opening to the closing balance of assets for insurance acquisition cash flows, showing separately

¹ See paragraphs 28A–28D, 105A–105C and B35A–B35C of the Exposure Draft and paragraphs BC31–BC49 of the Basis for Conclusions on the Exposure Draft.

any recognition of impairment losses and reversals of impairment losses; and

- (ii) quantitative information, in appropriate time bands, about when an entity expects to derecognise an asset for insurance acquisition cash flows and include those cash flows in the measurement of the group of insurance contracts to which they are allocated.

Overview of the feedback

- 7. Most respondents who commented on the proposed amendment relating to insurance acquisition cash flows agreed with the Board’s proposal and rationale for proposing the amendment to IFRS 17 as set out in the paragraph 6 of this paper.
- 8. A small number of respondents, including one insurer, one user of financial statements, one national standard-setter and one regulator, from different jurisdictions, disagreed with the proposal because, in their view, it would:
 - (a) impair comparability between entities, in the light of the significant judgement they think would be involved in allocating insurance acquisition cash flows to expected renewals; and
 - (b) add complexity to IFRS 17 implementation and application.

Specific feedback, staff analysis and recommendations

Allocation of insurance acquisition cash flows

- 9. Some respondents commented on the following aspects of the proposal to allocate insurance acquisition cash flows to groups of insurance contracts:
 - (a) guidance on allocating insurance acquisition cash flows (paragraphs 10–12 of this paper);

- (b) reallocation of insurance acquisition cash flows between groups of insurance contracts (paragraphs 13–14 of this paper);
- (c) allocation on a systematic and rational basis (paragraphs 15–17 of this paper); and
- (d) interaction between the wording of the proposed amendment and the requirements in IFRS 17 (paragraphs 18–19 of this paper).

Guidance on allocating insurance acquisition cash flows

10. Some respondents suggested the Board provide guidance on allocating, on a systematic and rational basis, insurance acquisition cash flows that are directly attributable to a group of insurance contracts:
 - (a) to that group; and
 - (b) to any groups that include contracts that are expected to arise from renewals of the contracts in that group.
11. The staff think that providing guidance on, or specific examples of, a systematic and rational basis of allocation could:
 - (a) have unintended consequences by unduly restricting an entity’s ability to apply judgement in specific facts and circumstances (see paragraph 16 of this paper).
 - (b) disrupt implementation given that systematic and rational allocation is required by other paragraphs of IFRS 17. For example, paragraph B65(l) of IFRS 17 requires an allocation of fixed and variable overheads to groups of contracts using methods that are systematic and rational and are consistently applied to all costs that have similar characteristics.
12. Therefore, the staff think the Board should not provide guidance on, or specific examples of, a systematic and rational basis of allocation of insurance acquisition cash flows.

Reallocation of insurance acquisition cash flows between groups of insurance contracts

13. One respondent asked whether an entity would be required or permitted to reallocate insurance acquisition cash flows between groups of insurance contracts each reporting period. For example, this respondent questioned whether an entity would be required or permitted to reallocate insurance acquisition cash flows allocated to expected renewals if there was a change in the entity's expectation about the number of renewals.
14. The staff note that a systematic and rational allocation would be required at the end of each reporting period. The staff think that an entity should apply the same systematic and rational method of allocation consistently over time. However, that method of allocation could result in changes in the amounts being allocated to groups if there are changes in facts and circumstances upon which the method depends. To clarify this approach, the staff intend to revise the wording to refer to 'methods that are systematic and rational', consistent with the wording of B65(l) of IFRS 17.

Allocation on a systematic and rational basis

15. Some respondents expressed the view that a requirement to allocate insurance acquisition cash flows to renewals on a systematic and rational basis would be unduly complex. A small number of those respondents provided the following alternative suggestions:
 - (a) requiring an entity to allocate insurance acquisition cash flows to groups based on expected recovery—that is, based on how the entity expects to recover the insurance acquisition cash flows; and
 - (b) permitting, rather than requiring, an entity to allocate insurance acquisition cash flows to expected renewals to reduce the complexity and cost of applying IFRS 17.
16. In the staff view, an allocation to groups based on expected recovery is one systematic and rational basis of allocation. However, it is not the only systematic and rational basis. The staff think that a requirement to allocate insurance acquisition cash flows based on expected recovery as suggested in paragraph 15(a) of this paper could be

restrictive and burdensome for some entities to apply. Instead, in the staff view, requiring allocation on a systematic and rational basis allows an entity to use judgement to decide whether to allocate on an expected recovery basis, or a different basis. Such judgement would allow an entity to consider both the usefulness of information that would be provided to users of financial statements applying different allocation bases and the costs and benefits of different allocation bases. In addition, the staff note that any lack of recoverability of an asset for insurance acquisition cash flows would be identified by the proposed impairment test (see paragraph 33 of this paper).

17. In regard to the suggestion from respondents discussed in paragraph 15(b) of this paper, in the staff view, the proposed amendment does not necessarily add operational complexity as explained in paragraph 16 of this paper. In addition, the staff note that renewals often arise from short-term insurance contracts, many of which could be accounted for applying the premium allocation approach. Applying that approach an entity is permitted to recognise insurance acquisition cash flows as expenses when incurred rather than recognising an asset, and so the proposed amendment would not be applicable.

Interaction between the wording of the proposed amendment and the requirements in IFRS 17

18. Some respondents suggested the Board clarify the interaction between the wording of the proposed amendment and the requirements in IFRS 17. This is because:
- (a) in defining insurance acquisition cash flows, Appendix A of IFRS 17 refers to costs that are directly attributable to the *portfolio* of insurance contracts to which the group belongs; whereas
 - (b) the proposed amendment refers to an allocation of insurance acquisition cash flows that are directly attributable to a *group* of insurance contracts.
19. The staff note that the proposed allocation requirement refers only to the insurance acquisition cash flows that are directly attributable to a *group* because the proposed amendment is not relevant to those attributable to a *portfolio*. An entity is already required by IFRS 17 to allocate insurance acquisition cash flows attributable to a

portfolio to groups of contracts on a systematic and rational basis. When finalising any amendments to IFRS 17, the staff will consider whether drafting changes are needed to align the proposed amendments and the definition of insurance acquisition cash flows.

Staff recommendation

20. Considering the analysis in paragraphs 10–19 of this paper, the staff recommend the Board finalise the proposed amendment to IFRS 17 that would require an entity to allocate insurance acquisition cash flows that are directly attributable to a group of insurance contracts applying a systematic and rational method:
- (a) to that group; and
 - (b) to any groups that include contracts that are expected to arise from renewals of the contracts in that group.

Question 1 for Board members

Do you agree the Board should finalise the proposed amendment to IFRS 17 that would require an entity to allocate insurance acquisition cash flows that are directly attributable to a group of insurance contracts applying a systematic and rational method:

- (a) to that group; and
- (b) to any groups that include contracts that are expected to arise from renewals of the contracts in that group?

Recognition of an asset

21. Some respondents suggested the Board clarify the unit of account for an asset for insurance acquisition cash flows. A small number of those respondents expressed the view that the unit of account should be an entity level asset, similar to the unit of account used by entities applying some existing insurance accounting practices to recognise deferred acquisition costs as assets.
22. Applying IFRS 17, the unit of account for any asset recognised for insurance acquisition cash flows is the group of insurance contracts to which the insurance

acquisition cash flows have been allocated. This is consistent with the recognition and measurement requirements of IFRS 17.

23. The staff note that applying IFRS 17 as originally issued, an entity that recognises an asset for insurance acquisition cash flows is required to identify the future groups to which those insurance acquisition cash flows relate. Applying the proposed amendment, an entity would be required to identify groups further into the future—because the entity would be required to identify the future groups that will include expected renewals. The staff acknowledge that this could be complex. However, the staff think that an entity must identify the future group to which insurance acquisition cash flows paid have been allocated in order to recognise those insurance acquisition cash flows as an asset.
24. In addition, the staff note that if the unit of account for the asset was at an entity level, as suggested by some respondents, the proposed impairment test would be performed at an entity level. If the impairment test was performed at an entity level, the asset for insurance acquisition cash flows would relate to a specific subset of insurance contracts but it would be tested for impairment against the expected net cash inflows of all insurance contracts the entity expects to issue. Therefore, the staff expect that it would be highly unlikely that an impairment test at an entity level would identify any impairment losses. Consequently, the staff view is that setting the unit of account at an entity level would result in a significant loss of useful information.

Staff recommendation

25. The staff recommend the Board confirm that the unit of account for an asset for insurance acquisition cash flows is the group of insurance contracts to which those cash flows have been allocated.

Question 2 for Board members

Do you agree the Board should confirm that the unit of account for an asset for insurance acquisition cash flows is the group of insurance contracts to which those cash flows have been allocated?

Impairment test

26. Some respondents commented on the following aspects of the proposal to assess the recoverability of an asset for insurance acquisition cash flows:
- (a) frequency of the impairment test (paragraphs 27–30 of this paper); and
 - (b) application of the impairment test (paragraphs 31–34 of this paper).

Frequency of the impairment test

27. A small number of respondents suggested that an entity should be required to assess the recoverability of an asset for insurance acquisition cash flows annually, regardless of the existence of facts and circumstances indicating the asset may be impaired.
28. The staff note that requiring an entity to test an asset for insurance acquisition cash flows for impairment only when facts and circumstances indicate the asset may be impaired is consistent with:
- (a) paragraph 26 of IFRS 17 for the recognition of a group of onerous contracts before the beginning of the coverage period or the date when the first payment from a policyholder in the group becomes due; and
 - (b) IAS 36 *Impairment of Assets*, which requires that an entity assess at the end of each reporting period whether there is any indication that an asset may be impaired.
29. In the staff view, requiring an entity to test the recoverability of an asset for insurance acquisition cash flows annually, regardless of whether facts and circumstance indicate the asset may be impaired, could lead to an unnecessary operational burden for entities.
30. Therefore, the staff think that, as proposed in the Exposure Draft, the Board should require an entity to test the recoverability of an asset for insurance acquisition cash flows at the end of a reporting period if facts and circumstances indicate the asset may be impaired.

Application of the impairment test

31. Some respondents expressed concerns that the proposed requirements to assess the recoverability of an asset for insurance acquisition cash flows, if facts and circumstances indicate the asset may be impaired, are unduly complex. Specifically, those respondents noted that the Exposure Draft proposes a two-step impairment test. Those steps are:
- (a) an impairment test at the level of a group of insurance contracts (group level impairment test); and
 - (b) an additional impairment test specific to insurance acquisition cash flows allocated to expected contract renewals (additional impairment test).
32. Those respondents suggested the Board not require the additional impairment test discussed in paragraph 31(b) of this paper because, in their view, the group impairment level test discussed in paragraph 31(a) of this paper would be sufficient to identify any impairment loss. In addition, some of those respondents noted that the information that would be required to perform the additional impairment test is more detailed than the information about expected renewals that entities typically maintain applying some existing insurance accounting practices.
33. As explained in paragraph BC45 of the Basis for Conclusions on the Exposure Draft, the proposed group level impairment test compares the carrying amount of an asset for insurance acquisition cash flows allocated to a group with the expected net cash inflow of that group. That net cash inflow includes cash flows for expected renewals of contracts with current policyholders and cash flows for contracts with future policyholders expected to be in that same group. The Board decided to require an additional impairment test specific to cash flows for expected contract renewals. The additional impairment test results in the recognition of any impairment losses on expected future renewals when the entity no longer expects those renewals to occur. Without the additional impairment test, cash flows from future policyholder contracts might prevent the recognition of such an impairment loss.
34. Appendix A to this paper provides an example illustrating how an entity would apply the impairment test requirements discussed in paragraphs 31(a) and 31(b) of this

paper. In that example, an impairment loss is identified by both tests. In other examples, either test could identify an impairment loss that would not be identified by the other test, for example:

- (a) the group impairment level test could identify an impairment loss when entities do not expect any renewals (so the additional impairment test would not apply) and fewer contracts have been issued than expected initially; or
- (b) the additional impairment test could identify an impairment loss when entities allocate insurance acquisition cash flows to a future group of expected renewals, subsequently no longer expect those renewals but do expect to issue profitable contracts to new policyholders (as discussed in paragraph 33 of this paper).

Staff recommendation

35. The staff acknowledge that the impairment tests are an additional operational task for entities. However, as discussed in paragraph 30 of this paper, the staff continue to recommend that any impairment test would be required only when facts and circumstances indicate an asset may be impaired. In those circumstances, the staff view is that the benefit of identifying potential impairment losses outweighs the operational cost. The staff also recommend the Board confirm that the impairment test includes two steps as set out in paragraph 31 of this paper.

Question 3 for Board members

Do you agree the Board should finalise the proposed requirements to assess the recoverability of an asset for insurance acquisition cash flows if facts and circumstances indicate the asset may be impaired?

Disclosures

36. Some respondents agreed with the Board’s view that the following proposed disclosure requirements would provide useful information:

- (a) a reconciliation from the opening to the closing balance of assets for insurance acquisition cash flows, showing separately any recognition of impairment losses and reversals of impairment losses; and
 - (b) quantitative information, in appropriate time bands, about when an entity expects to derecognise an asset for insurance acquisition cash flows and include those cash flows in the measurement of the group of insurance contracts to which they are allocated.
37. A small number of respondents expressed concerns that the proposed disclosure described in paragraph 36(b) of this paper would require entities to disclose commercially sensitive information about projections of future business. Some of those respondents think that information about the recoverability of an asset for insurance acquisition cash flows is sufficiently addressed by the proposed impairment test requirements.
38. As explained in paragraph BC46 of the Basis for Conclusions on the Exposure Draft, the proposed amendment would extend the period for which an asset for insurance acquisition cash flows would be recognised compared to IFRS 17 as originally issued. In the light of this extended period, the Board’s view is that it would be useful for users of financial statements to know when that asset is expected to be derecognised and the insurance acquisition cash flows are expected to be included in the measurement of a group of insurance contracts.
39. In the staff view:
- (a) the Board’s view discussed in paragraph 38 of this paper continues to hold. Feedback from outreach with users of financial statements supports the Board’s view.
 - (b) the proposed recoverability assessment identifies when an impairment loss exists, it does not provide users of financial information with information about when an asset for insurance acquisition cash flows is expected to be derecognised.
 - (c) the proposed disclosure requirements are similar to disclosures required by other IFRS Standards (for example, IFRS 15 *Revenue from Contracts with*

Customers requires entities to disclose when they expect to recognise as revenue the amounts allocated to unsatisfied performance obligations).

Staff recommendation

40. The staff recommend the Board finalise the proposed amendment that would require an entity to disclose:
- (a) a reconciliation from the opening to the closing balance of assets for insurance acquisition cash flows, showing separately any recognition of impairment losses and reversals of impairment losses; and
 - (b) quantitative information, in appropriate time bands, about when an entity expects to derecognise an asset for insurance acquisition cash flows and include those cash flows in the measurement of the group of insurance contracts to which they are allocated.

Question 4 for Board members

Do you agree the Board should finalise the proposed amendments that would require an entity to disclose:

- (a) a reconciliation from the opening to the closing balance of assets for insurance acquisition cash flows, showing separately any recognition of impairment losses and reversals of impairment losses; and
- (b) quantitative information, in appropriate time bands, about when an entity expects to derecognise an asset for insurance acquisition cash flows and include those cash flows in the measurement of the group of insurance contracts to which they are allocated?

Presentation

41. A small number of respondents suggested that any asset for insurance acquisition cash flows should be presented separately in the statement of financial position (rather than as part of the carrying amount of the related portfolios of insurance contracts issued as required by the proposed amendment). In their view, separate presentation would provide useful information because it would be aligned with the proposed disclosure

requirements for assets for insurance acquisition cash flows described in paragraph 6(d) of this paper.

42. The staff note that the proposed amendment could extend the period for which an asset for insurance acquisition cash flows would be recognised and could increase the amount of the asset compared to IFRS 17 as originally issued. For that reason, the staff understand why some respondents think that separate presentation would provide useful information.
43. However, the staff note that an asset for insurance acquisition cash flows will subsequently be included in the measurement of a group of insurance contracts. Therefore, in the staff view, presenting any such asset in the carrying amount of the related portfolio of insurance contracts would provide useful information.
44. In addition, the disclosures would provide further information about assets for insurance acquisition cash flows. This is consistent with other IFRS 17 balances that an entity is required to present as a part of the portfolio of insurance contracts rather than separately in the statement of financial position (for example, the contractual service margin).

Staff recommendation

45. Therefore, the staff recommend the Board retain, unchanged, the requirement to present any asset for insurance acquisition cash flows in the carrying amount of the related portfolio of insurance contracts issued.

Question 5 for Board members

Do you agree the Board should retain, unchanged, the requirement to present any asset for insurance acquisition cash flows in the carrying amount of the related portfolios of insurance contracts issued?

Transition

46. Some respondents suggested the Board provide transition reliefs to determine an asset for insurance acquisition cash flows when applying IFRS 17 for the first time.
47. The staff analysis and recommendations about respondents' feedback on transition reliefs for insurance acquisition cash flows will be provided in a separate paper of a future Board meeting.

Appendix A—example of applying the two impairment tests proposed in the Exposure Draft

A1. The following example illustrates how the two impairment tests proposed in the Exposure Draft would identify any impairment losses on an asset for insurance acquisition cash flows.

Fact pattern

A2. At the beginning of Year 1 an entity pays commissions of CU38² relating to a group of insurance contracts yet to be issued. Those commissions meet the definition of insurance acquisition cash flows.

Allocation and recognition

A3. The commission of CU38 is directly attributable to insurance contracts the entity expects to issue later in Year 1 (Group 1). The entity expects that some policyholders of those insurance contracts that will be issued in Year 1 will renew those contracts in Year 2 (Group 2), Year 3 (Group 3) and Year 4 (Group 4). Accordingly, applying the proposed amendment, at the beginning of Year 1, the entity allocates the commissions of CU38 on a systematic and rational basis to the expected future groups of insurance contracts as follows:

	Year 1 (Group 1– initial contracts)	Year 2 (Group 2– expected renewals)	Year 3 (Group 3– expected renewals)	Year 4 (Group 4– expected renewals)	Total
Assets for insurance acquisition cash flows at the beginning of Year 1	25	5	5	3	38

A4. The entity recognises assets for insurance acquisition cash flows of CU38 at the beginning of Year 1.

² In this paper amounts are denominated in ‘currency units’ (CU).

- A5. At the end of Year 1, the entity derecognises the asset of CU25 allocated to Group 1 and includes the insurance acquisition cash flows in the measurement of Group 1. At the end of Year 1 there are no facts and circumstances indicating that the assets for insurance acquisition cash flows allocated to each of Groups 2 to 4 may be impaired. Therefore, at the end of Year 1 the carrying amount of the assets for insurance acquisition cash flows is CU13:

	Year 1 (Group 1– initial contracts)	Year 2 (Group 2– expected renewals)	Year 3 (Group 3– expected renewals)	Year 4 (Group 4– expected renewals)	Total
Assets for insurance acquisition cash flows at the end of Year 1	-	5	5	3	13

Impairment

- A6. At the end of Year 2, the entity derecognises the asset of CU5 allocated to Group 2, and includes the insurance acquisition cash flows in the measurement of Group 2. At the end of Year 2, facts and circumstances indicate that the assets for insurance acquisition cash flows for Groups 3 and 4 may be impaired. The carrying amount of the assets for insurance acquisition cash flows subject to impairment testing is CU8:

	Year 1 (Group 1– initial contracts)	Year 2 (Group 2– expected renewals)	Year 3 (Group 3– expected renewals)	Year 4 (Group 4– expected renewals)	Total
Assets for insurance acquisition cash flows at the end of Year 2	-	-	5	3	8

- A7. Applying the proposed amendment, the entity performs a group level impairment test to each of the assets for the two future groups. In addition, because the entity has allocated amounts to expected renewals, the entity performs the additional impairment test specific to expected renewals.
- A8. To perform the two impairment tests, the entity estimates the following amounts:

Expected net cash inflows	Year 3 (Group 3)	Year 4 (Group 4)
(a) expected renewals	3	1
(b) other than renewals	6	1
Total expected net cash inflows	9	2

- A9. Applying the group level impairment test the entity compares the asset for insurance acquisition cash flows for each future group to the expected net cash inflows for that group, as follows:

Group level impairment test	Year 3 (Group 3)	Year 4 (Group 4)
Assets for insurance acquisition cash flows	5	3
Total expected net cash inflows	9	2
Impairment	-	(1)

- A10. Applying the additional impairment test specific to insurance acquisition cash flows allocated to expected contracts renewals, the entity compares the amount of insurance acquisition cash flows allocated to expected renewals to the total expected net cash inflows for those expected renewals, as follows:

Additional impairment test specific to expected renewals	Year 3 (Group 3)	Year 4 (Group 4)	Total
Amount of insurance acquisition cash flows allocated to expected renewals	5	3	8
Expected net cash inflows for expected renewals	3	1	4
Impairment			(4)

- A11. Accordingly, the entity recognised as an expense in profit or loss an impairment of CU4 comprising of:

- (a) CU1 identified applying paragraph B35B(a) of the Exposure Draft; and
- (b) CU4 identified applying paragraph B35B(b)(i) of the Exposure Draft less CU1 identified in A11(a) applying paragraph B35B (b)(ii) of the Exposure Draft.

- A12. After recognising the impairment loss described in paragraph A11 of this paper the entity will allocate the total amount of insurance acquisition cash flows remaining in the assets of CU4 to the groups of contracts still to be recognised (Group 3 and Group 4 in this example) on a systematic and rational basis.

STAFF PAPER

December 2019

IASB® meeting

Project	Amendments to IFRS 17		
Paper topic	Reinsurance contracts held—recovery of losses		
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This paper has been prepared for discussion at a public meeting of the International Accounting Standards Board (Board) and does not represent the views of the Board or any individual member of the Board. Comments on the application of IFRS® Standards do not purport to set out acceptable or unacceptable application of IFRS Standards. Technical decisions are made in public and reported in IASB® *Update*.

Purpose of the paper

1. This paper discusses staff analysis and recommendations about the amendment proposed in the Exposure Draft *Amendments to IFRS 17* relating to reinsurance contracts held. This paper follows the tentative decision of the International Accounting Standards Board (Board), at its November 2019 meeting, to consider further the feedback from outreach and comment letters on this proposed amendment.

Summary of staff recommendations

2. The staff recommend the Board:
 - (a) extend the scope of the proposed amendment to IFRS 17 *Insurance Contracts* to require an entity to adjust the contractual service margin of a group of reinsurance contracts held, 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.
 - (b) amend the proposed calculation of the income, as a consequence of the extension of the scope of the proposed amendment, to require an entity to determine the amount of a loss recovered from a reinsurance contract held by multiplying:

- (i) the loss recognised on the group of underlying insurance contracts;
and
 - (ii) the percentage of claims on underlying insurance contracts the entity expects to recover from the reinsurance contract held.
- (c) not add the proposed footnote to paragraph BC304 of the Basis for Conclusions on IFRS 17.
- (d) confirm that the amendment to IFRS 17 described in paragraph 2(a) of this paper would apply only when the reinsurance contract held is recognised before or at the same time as the loss is recognised on the underlying insurance contracts.
- (e) clarify, in the final amendments to IFRS 17, that paragraph 66(c)(ii) of IFRS 17—for subsequent measurement of a group of reinsurance contracts held when a group of underlying insurance contracts become onerous—applies when underlying insurance contracts are measured applying the premium allocation approach.

Structure of the paper

3. This paper provides:
- (a) an overview of the proposals in the Exposure Draft;
 - (b) an overview of the feedback; and
 - (c) the staff analysis, recommendations and questions for Board members.
4. Appendix A to this paper provides three examples of applying the proposed amendment in the Exposure Draft.

Proposals in the Exposure Draft

5. The Exposure Draft proposed an amendment to the measurement of a group of reinsurance contracts held.¹ The proposed amendment would require an entity to adjust the contractual service margin of a group of reinsurance contracts held that provide 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.

6. The amount of the adjustment and resulting income would be 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 insurance contracts the entity has a right to recover from the group of reinsurance contracts held.

7. The Exposure Draft proposed the amendment would apply only when:
 - (a) a reinsurance contract held provides proportionate coverage. That is, as noted in the calculation in paragraph 6 of this paper, when the entity has the right to recover from the reinsurer a percentage of all claims incurred on groups 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.
 - (b) the reinsurance contract held is recognised before or at the same time as the loss is recognised on the underlying insurance contracts.

8. Applying the proposed amendment, an entity would:
 - (a) recognise income in the statement of financial performance (credit); and
 - (b) increase the reinsurance contract held asset on the statement of financial position (debit) by increasing the net cost that will be recognised over the coverage period or decreasing the net gain that will be recognised over the

¹ See paragraphs 66A–66B and B119C–B119F of the Exposure Draft and paragraphs BC67–BC90 of the Basis for Conclusions on the Exposure Draft.

coverage period, depending on whether the reinsurance contract held is in a net cost or net gain position.

9. The Exposure Draft proposed adding a footnote to paragraph BC304 of the Basis for Conclusions on IFRS 17 to explain that if a reinsurance contract held covers claims in excess of a specified amount on an individual insurance contract that reinsurance contract does not provide proportionate coverage.²

Feedback

10. Most respondents expressed support for the objective of the proposed amendment. However, they expressed the view that the proposed amendment requires refinement to achieve the Board's objective of making it easier for entities to explain their results to investors. Respondents expressed concerns about:
 - (a) the proposed population of reinsurance contracts held to which the amendment would apply (see paragraphs 12–20 of this paper); and
 - (b) the proposed calculation of income on the reinsurance contract held (see paragraphs 21–23 of this paper).
11. Respondents also commented on other aspects of the proposed amendment (see paragraphs 24–27 of this paper).

Proposed population

12. Most respondents, particularly preparers, expressed concerns that the proposed amendment would apply only to a limited population of reinsurance contracts held. Those respondents expressed the view that either:
 - (a) the definition of a reinsurance contract held that provides proportionate coverage should be extended; or
 - (b) the proposed amendment should apply to all reinsurance contracts held.

² Paragraph BC304 of the Basis for Conclusions on IFRS 17 explains that, in some cases, a reinsurance contract held covers the losses of separate contracts on a proportionate basis.

Definition of proportionate coverage

13. Some respondents did not disagree with the proposed amendment applying only to reinsurance contracts held that provide proportionate coverage. However, many of those respondents expressed the view that the definition of proportionate coverage proposed in the Exposure Draft is too narrow. Those respondents noted only a few reinsurance contracts held would meet that proposed definition and, therefore, expressed the view that the proposed amendment would not address the concerns previously raised by stakeholders.

14. Examples of reinsurance contracts held that respondents explained are commonly described in practice as proportional but would not meet the definition of proportionate coverage proposed in the Exposure Draft include:
 - (a) reinsurance contracts held that provide an entity with the right to recover from the reinsurer a fixed percentage of claims, but with either a *minimum retention*, a *maximum limit* or both. For example, a right to recover 40% of any claims above CU20.³ The existence of a minimum retention, a maximum limit or both would preclude the reinsurance contract held from meeting the proposed definition.

 - (b) reinsurance contracts held that provide an entity with the right to recover from the reinsurer claims above a minimum retention on an *individual* underlying insurance contract. For example, a right to recover any claims above CU10 on each underlying insurance contract. The existence of a minimum retention would preclude the reinsurance contract held from meeting the proposed definition.

 - (c) reinsurance contracts held that provide an entity with the right to recover from the reinsurer a fixed percentage of some, but not all, types of claims covered by the underlying insurance contracts. For example, an entity sells insurance contracts providing coverage in the event of accidental fire, flood or earthquake. The reinsurance contract held provides the entity with a right to recover a fixed percentage of any claims arising from an earthquake event only. The reinsurance contract held does not provide coverage for a fixed

³ In this paper amounts are denominated in ‘currency units’ (CU).

percentage of all claims on the underlying insurance contract and therefore would not meet the proposed definition.

- (d) reinsurance contracts held that provide an entity with the right to recover from the reinsurer a fixed percentage of all claims on each individual underlying insurance contract, but the percentage is different for each underlying contract and the entity includes the underlying contracts in the same group. The percentage the entity has a right to recover is not fixed for all contracts in a single group of underlying contracts and, therefore, the reinsurance contract held would not meet the proposed definition.

15. Some respondents suggested the Board amend the proposed definition of a reinsurance contract held that provides proportionate coverage to include the contracts described in paragraph 14 of this paper. To achieve this, some respondents suggested the definition should be 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.

All reinsurance contracts held

16. Consistent with feedback during the development of the Exposure Draft, some respondents continued to express the view that the proposed amendment should apply to *all* reinsurance contracts held. For example, in addition to the reinsurance contracts discussed in paragraph 14 of this paper, those respondents think the amendment should apply to reinsurance contracts held that provide an entity with the right to recover from the reinsurer the aggregate amount of claims from a number of underlying insurance contracts in excess of an aggregate retention amount. For example, a right to recover all claims above a CU200 aggregate retention on all underlying insurance contracts issued in a specified period.
17. In those respondents' view, the same accounting mismatch between a reinsurance contract held and onerous underlying insurance contracts would arise regardless of whether the reinsurance contract held provides proportionate coverage or coverage that is not proportionate. Those respondents expressed the view that the proposed amendment would result in an inconsistent accounting treatment of reinsurance contracts that are entered into to achieve the same economic outcome.

18. Those respondents noted that IFRS 17 already includes an exception which addresses a similar accounting mismatch between a reinsurance contract held and onerous underlying insurance contracts on *subsequent measurement*. That exception applies to all reinsurance contracts held. In their view, extending the proposed amendment to apply also to all reinsurance contracts held would improve consistency within the Standard by making the accounting at initial recognition consistent with the subsequent accounting.
19. Those respondents acknowledged the Board’s rationale for limiting the proposed amendment to reinsurance contracts held that provide proportionate coverage. The Board was concerned that the timing mismatch between the recognition of claims on underlying insurance contracts and the recognition of claim recoveries on the reinsurance contract held could not be directly identified for reinsurance contracts held that do not provide proportionate coverage. However, those respondents suggested an alternative amendment that they think would:
- (a) resolve the accounting mismatch for all types of reinsurance contracts held.
 - (b) address the Board’s concerns. In the view of those respondents, the suggested amendment would result in the income on the reinsurance contract held being identified in a direct and consistent way, without arbitrary assumptions or subjective judgements.
20. Those respondents suggested the proposed amendment should apply to all reinsurance contracts held by requiring an entity to:
- (a) identify the percentage of *all* underlying claims the entity *expects* to recover through the reinsurance contract held; and
 - (b) recognise income (loss recovery) on the reinsurance contract held by multiplying the loss on the underlying insurance contracts by that percentage.

Proposed calculation

21. Most respondents that commented on the proposed amendment did not comment on the proposed calculation of income on the reinsurance contract held (loss-recovery calculation). Of those respondents who commented on the proposed loss-recovery

calculation, a small number of respondents expressed support for the calculation and noted that it would be a practical solution.

22. As discussed in paragraph 20 of this paper, some respondents suggested the Board amend the loss-recovery calculation to reflect the extension of the scope of the proposed amendment to all reinsurance contracts held suggested by those respondents.
23. Some respondents expressed concerns about the proposed calculation. Particularly:
- (a) some respondents, including some reinsurance brokers and some insurance industry representative bodies, expressed concerns that the calculation of the loss recovery is determined considering only the connection between claims on the underlying insurance contracts and claims recoveries on the reinsurance contract held. In those respondents' view, although practical to apply, such an approach might not be appropriate. For example, those respondents said that a loss on underlying insurance contracts might result from acquisition costs, rather than claims, and acquisition costs are typically not recoverable from the reinsurer. In their view, an entity should be required to apply judgement to identify the extent to which the net fulfilment cash flows of the reinsurance contract held result from the onerous underlying insurance contracts. Such an approach would require an entity to identify the connections, if any, between:
 - (i) all fulfilment cash flows that contribute to the *loss on the underlying insurance contracts* (for example, premiums, claims, acquisition costs, other expenses and the risk adjustment for non-financial risk); and
 - (ii) all fulfilment cash flows that contribute to the *net cost or net gain on the reinsurance contract held* (for example, reinsurance premiums, claims recoveries, reinsurance commissions and the risk adjustment for non-financial risk).
 - (b) some respondents, including a regulator and a national standard-setter, expressed concerns that the proposed amendment could result in an entity recognising income on a reinsurance contract held that is in a net cost position. In those respondents' view, the proposed amendment would not reflect the economics of a reinsurance contract that is in a net cost position and would be open to abuse to achieve an accounting outcome. Those respondents expressed

concerns that applying the proposed amendment when a reinsurance contract held is in a net cost position would result in the entity deferring losses because the entity would recognise income and, at the same time, increase the net cost it will recognise on the reinsurance contract held over time. In addition, those respondents were concerned that losses would not be visible to users of financial statements. Those respondents suggested the loss recovery should be limited to the amount of any net gain on the reinsurance contract held.

Other feedback

Proposed footnote in the Basis for Conclusions on IFRS 17

24. Some respondents think the proposed footnote to paragraph BC304 of the Basis for Conclusions on IFRS 17 discussed in paragraph 9 of this paper narrows the Board’s previous explanation of proportionate reinsurance contracts in that paragraph. Those respondents suggested the Board does not add the proposed footnote because they think doing so would disrupt implementation of the requirements in paragraph 62 of IFRS 17 for the recognition of reinsurance contracts held, which distinguishes between reinsurance contracts held that provide proportionate coverage and other reinsurance contracts held.

Timing of entering into the reinsurance contract held

25. A small number of respondents commented on the proposal that, for the proposed amendment to apply, the reinsurance contract held would need to be recognised before or at the same time as the loss is recognised on the underlying insurance contracts (see paragraph 7(b) of this paper). Some of those respondents expressed concerns and suggested the Board consider permitting application of the proposed amendment also when the reinsurance contract held is recognised *after* the loss is recognised on the underlying insurance contracts. In contrast, other respondents agreed with the Board’s rationale for requiring the reinsurance contract held to be recognised before or at the same time as the loss is recognised.

Guidance on the loss-recovery component

26. A small number of respondents asked for clarification or guidance on the accounting treatment for the loss-recovery component of a group of reinsurance contracts held. One respondent suggested that guidance could be provided by extending the illustrative example accompanying the Exposure Draft.

Premium allocation approach

27. A small number of respondents expressed support for the proposed amendment applying when either the reinsurance contract held or underlying insurance contracts are accounted for applying the premium allocation approach. Some of those respondents asked the Board to clarify that the existing exception in paragraph 66(c)(ii) of IFRS 17 for *subsequent measurement* of a reinsurance contract held when a group of underlying insurance contracts becomes onerous applies when underlying insurance contracts are accounted for applying the premium allocation approach. Those respondents noted that paragraph refers to the contractual service margin of the underlying insurance contracts and that the measurement of insurance contracts applying the premium allocation approach does not include a contractual service margin.

Staff analysis and recommendations

28. The staff analysis in this paper is structured as follows:
- (a) proposed population (paragraphs 29–42 of this paper);
 - (b) proposed calculation (paragraphs 43–58 of this paper); and
 - (c) other feedback (paragraphs 59–64 of this paper).

Proposed population

29. The Board limited the scope of the proposed amendment to contracts that meet both the following criteria:
- (a) reinsurance contracts held for which an entity could identify a known reinsurance claim recovery for each CU1 of underlying insurance claim. For

example, if an entity has the right to recover 40% of all claims from the reinsurer, the entity can identify a known recovery of CU0.4 for each CU1 of claim. With the scope of the proposed amendment limited in this way, the Board concluded that an entity could identify the loss recovery on the reinsurance contract held by assuming that the loss on the underlying insurance contracts results solely from claims. In the example, if the loss was CU20, the loss recovery would be CU8.

- (b) reinsurance contracts held that provide the entity with the right to recover a fixed percentage of *all* claims incurred on a group of underlying insurance contracts and for which the percentage the entity has a right to recover is fixed for *all* contracts in that group. The Board proposed limiting the scope of the amendment in this way to minimise the operational complexity that would result from applying the proposed amendment.

30. Accordingly, a reinsurance contract held is excluded from the scope of the proposed amendment if one or both of the following apply:

- (a) the reinsurance contract held includes a feature such as a minimum retention or maximum limit. Such features mean that it is not possible to identify a known reinsurance claim recovery for each CU1 of underlying insurance claim. The Board decided not to include such contracts in the scope of the proposed amendment because the Board was concerned that for those contracts an entity would be required to use estimates to identify the loss recovery which may require a more complex loss-recovery calculation compared to the simple calculation proposed by the Board.
- (b) the reinsurance contract held does not cover, at the same fixed percentage, *all* claims incurred on a *group* of underlying insurance contracts.

31. Although the scope of the proposed amendment was limited, the amendment would address stakeholder concerns about the examples of reinsurance contracts held that stakeholders previously provided to the Board to demonstrate an accounting mismatch on initial recognition of onerous underlying insurance contracts.⁴ The proposed

⁴ Those examples were included in Agenda Paper 2C *Appendix to reinsurance contracts held—onerous underlying insurance contracts* of the January 2019 Board meeting.

amendment would also apply to a wider population of reinsurance contracts held than the examples of reinsurance contracts held provided to the Board. This is because the examples provided to the Board included both premiums and claims that are proportionate, whereas the proposed amendment would require only that claims be proportionate. For reinsurance contracts held to which the proposed amendment would apply, the proposed amendment would address stakeholder concerns in a manner that could be consistently and robustly applied without significant operational implications.

32. However, the feedback from outreach and comment letters provides additional information about common features of reinsurance contracts in practice that would mean that many reinsurance contracts held would not be within the scope of the proposed amendment. In the light of the feedback that the proposed amendment would apply only to a few reinsurance contracts held, the staff analysis considers whether the Board should extend the scope of the proposed amendment.

Definition of proportionate coverage

33. Some respondents suggested the Board extend the definition of proportionate coverage proposed in the Exposure Draft to include reinsurance contracts held that are commonly described in practice as proportional, as discussed in paragraph 14 of this paper. The staff expect that, if the Board were to extend the definition in that way, the amendment might apply to a much larger population of reinsurance contracts held than proposed in the Exposure Draft.
34. However, the reasons for which the Board decided to exclude many reinsurance contracts held from the scope of the proposed amendment (as discussed in paragraph 30 of this paper) apply as much to reinsurance contracts held that are commonly described in practice as proportional (as discussed in paragraph 14 of this paper) as to other reinsurance contracts held. The staff have not identified a reason to consider amending the definition of a reinsurance contract held that provides proportionate coverage. Therefore, the staff analysis in paragraphs 35–42 of this paper considers whether the Board should extend the scope of the proposed amendment to apply to all reinsurance contracts held.

All reinsurance contracts held

35. As noted in paragraphs 29–31 of this paper, the Board limited the scope of the proposed amendment to apply only when a loss on an underlying insurance contract has a *known* recovery from the reinsurance contract held. The Board concluded that the limitation was appropriate, considering that the proposed amendment would be an exception to the principles of the Standard and would result in the recognition of income immediately in profit or loss before any service is received. In addition, the proposed limited scope meant that the loss recovery could be calculated applying a simplified approach.

36. The staff note that the respondents who suggested the proposed amendment apply to all reinsurance contracts held suggested the calculation should be applied based on the *total expected* recovery from the reinsurance contract held. Those respondents expressed the view that such an approach would be consistent with the measurement requirements in IFRS 17 which are based on expected cash flows.

37. In those respondents' view, such an approach would address the Board's concerns that, for reinsurance contracts held that do not provide proportionate coverage, the timing mismatch between the recognition of claims on underlying insurance contracts and the recognition of claim recoveries on the reinsurance contract held could not be directly identified. Those respondents think that the mismatch can be identified based on estimates that are required by IFRS 17.

38. Consider an example of a reinsurance contract held that provides the entity with the right to recover from the reinsurer 40% of the aggregate of claims above CU200 on a number of underlying insurance contracts. Assume the entity expects total claims of CU1,200 on the underlying insurance contracts and accordingly expects total reinsurance claim recoveries of CU400. The percentage of all underlying claims the entity expects to recover from the reinsurance contract held is 33%. Those respondents suggested that if a loss of CU15 is recognised on an individual underlying insurance contract, an entity should recognise a loss recovery of CU5 (CU15 x 33%).

39. The staff are persuaded by the view that a loss-recovery calculation based on total expected reinsurance recoveries would be consistent with the general measurement requirements of IFRS 17 that are comprehensively based on expectations about future

cash flows.⁵ In addition, the staff agree with some respondents that requiring the proposed amendment to apply to all reinsurance contracts held would increase comparability between reinsurance contracts held that are entered into to achieve the same outcome.

40. The suggestion from respondents in paragraph 36 of this paper would maintain some of the simplicity of the amendment proposed in the Exposure Draft because it builds on the proposed loss-recovery calculation whereby an entity would assume the loss on underlying insurance contracts is caused by claims and multiple the loss by a loss-recovery percentage to determine the loss recovery.
41. The consequence of the suggestion is that the proposed loss-recovery calculation may not be as simple to apply for reinsurance contracts held that are outside the scope of the proposed amendment in the Exposure Draft. This was one of the reasons the Board limited the scope of the proposed amendment in the Exposure Draft. In some circumstances, to determine the total percentage of claims an entity expects to recover from the reinsurance contract held, the entity would be required to identify all expected claims across more than one group of underlying insurance contracts, including expected claims on insurance contracts expected to be issued in the future. However, the staff note that IFRS 17 already requires an entity to have that information for the purpose of determining the cash flows in the measurement of the reinsurance contract held. In addition, some respondents expressed the view that applying the proposed loss-recovery calculation based on the total percentage of claims an entity expects to recover from a reinsurance contract held would not add significant operational complexity.
42. In the light of the feedback from outreach and comment letters, the staff view is that, on balance, the benefit of extending the proposed amendment to apply to all reinsurance contracts held would outweigh the cost. Therefore, the staff recommend the Board extend the scope of the proposed amendment to IFRS 17 to require an entity to adjust the contractual service margin of a group of reinsurance contracts held, and as a result recognise income, when the entity recognises a loss on initial

⁵ For example, IFRS 17 requires the measurement of insurance contracts to include expected cash outflows over which the entity has discretion (see paragraph B65 of IFRS 17 and paragraphs BC169–BC170 of the Basis for Conclusions on IFRS 17).

recognition of an onerous group of underlying insurance contracts, or on addition of onerous contracts to that group.

Question 1 for Board members

Do you agree the Board should extend the scope of the proposed amendment to IFRS 17 to require an entity to adjust the contractual service margin of a group of reinsurance contracts held, 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?

Proposed calculation

43. Some respondents expressed concerns about the proposed loss-recovery calculation. Specifically, as discussed in paragraph 23 of this paper, some respondents expressed concerns about:
- (a) the assumption that a loss on underlying insurance contracts is caused by claims, without considering any other cash flows that contribute to the loss; and
 - (b) the calculation being based on the connection between insurance claims and reinsurance claim recoveries, without considering whether the reinsurance contract held is in an overall net gain or net cost position.

Assumption that a loss on underlying insurance contracts is caused by claims

44. In regard to the concern discussed in paragraph 43(a) of this paper, the staff note that the loss on underlying insurance contracts results from all fulfilment cash flows. This includes premiums, claims, insurance acquisition cash flows, other expenses allocated to the group of insurance contracts and the risk adjustment for non-financial risk. The staff think that any attempt to identify a loss as arising from specific cash flows would be arbitrary.
45. In developing the proposed amendment, the Board decided that it was necessary to make a simplified assumption about the cause of a loss when identifying how much of the loss is recovered through a reinsurance contract held. Without that assumption, an

entity would be required to identify the connection between all fulfilment cash flows in the measurement of the insurance contract issued and all fulfilment cashflows in the measurement of the reinsurance contract held. In the Board’s view, doing so would often be complex and burdensome, and could itself require arbitrary assumptions—in particular, this would be difficult when a reinsurance contract held covers many underlying insurance contracts. In addition, because arbitrary assumptions would be required, the result would not be comparable between entities.

46. In the staff view, the Board’s rationale for proposing a simplified approach continues to hold. An assumption that the loss on insurance contracts is caused solely by claims would be operationally simple and would reflect fully the connection between insurance claims and reinsurance claim recoveries.

Calculation based on the connection between insurance claims and reinsurance claim recoveries

47. In regard to the concern discussed in paragraph 43(b) of this paper, the staff note that those respondents were supportive of the result of applying the proposed amendment in scenarios in which the loss recovery is equal to the net gain on a reinsurance contract held. That would be the result of applying the proposed amendment in scenarios in which both premiums and claims are proportionate. However, those respondents disagreed with the result of applying the proposed amendment in scenarios in which the loss recovery is more than the net gain, or the reinsurance contract held is in a net cost position. That would be the result of applying the proposed amendment in scenarios in which premiums are not proportionate.
48. Example 1 in Appendix A to this paper demonstrates the result of applying the proposed amendment in the Exposure Draft when both premiums and claims are proportionate. The amounts recognised in profit or loss are included in the following tables.

IFRS 17 as originally issued	Recognised immediately	Recognised over time
Insurance contracts issued	(50)	-
Reinsurance contracts held	-	20
Profit/(loss)	(50)	20

Proposed amendment in the Exposure Draft	Recognised immediately	Recognised over time
Insurance contracts issued	(50)	-
Reinsurance contracts held	20	-
Profit/(loss)	(30)	-

49. The result of applying the proposed amendment in Example 1 reflects that, when both premiums and claims are proportionate, a reinsurance contract held acts similarly to a profit-sharing contract.
50. Example 2 and Example 3 in Appendix A to this paper demonstrate the results of applying the proposed amendment when premiums are not proportionate. In Example 3, the reinsurance contract held is in a net cost position and the amounts recognised in profit or loss are included in the following tables.

IFRS 17 as originally issued	Recognised immediately	Recognised over time
Insurance contracts issued	(50)	-
Reinsurance contracts held	-	(5)
Profit/(loss)	(50)	(5)

Proposed amendment in the Exposure Draft	Recognised immediately	Recognised over time
Insurance contracts issued	(50)	-
Reinsurance contracts held	20	(25)
Profit/(loss)	(30)	(25)

51. Some respondents expressed concerns that in Example 2 and Example 3, the result of applying the proposed amendment could be viewed as the deferral of a loss. In these examples, the premiums are not proportionate and, in contrast to Example 1, the reinsurance contract held does not act like a profit-sharing contract. In Example 3, the loss recovery of CU20 recognised immediately reflects the amount of the CU50 loss the entity expects to recover from the reinsurer. The net cost of CU25 recognised over time reflects the amount the reinsurer charges the entity for *all* reinsurance coverage the entity will receive. That reinsurance coverage includes:
- (a) the right to recover CU20 of the CU50 expected loss;

- (b) the right to recover CU40 of CU100 expected claims in addition to the expected loss; and
 - (c) the right to recover amounts relating to any *unexpected* claims.
52. In addition, the cost could relate, in part, to recovery of expenses other than claims.
53. Some respondents expressed concerns that in Example 2 and Example 3 losses would not be visible to users of financial statements. However, the staff note that applying the reconciliation requirement in paragraph 100 of IFRS 17, an entity would disclose both the loss component on underlying insurance contracts and the loss-recovery component on a reinsurance contract held. Those disclosures would provide users of financial statements with information about the amount of losses on insurance contracts issued and the extent to which those losses are recoverable through reinsurance contracts held.
54. Some respondents expressed concerns that, in Example 2 and Example 3, the proposed amendment would be open to abuse. Consider the following example. An entity issues an insurance contract with premiums of CU280 and expected claims of CU300. The insurance contract is onerous and the entity recognises a loss of CU20. At the same time, the entity purchases a reinsurance contract held to recover 100% of underlying claims for a reinsurance premium of CU300. In that example, if claims occur as expected, the reinsurance contract held has no overall effect on the net cash flows of the entity. With or without the reinsurance contract held the entity has a net cash outflow of CU20. However, applying the proposed amendment, the entity would recognise a loss recovery of CU20 at the same time it recognised the loss of CU20 (net effect of zero in profit or loss on day one) and a net cost of CU20 would be recognised over time.
55. The staff note that in the example in paragraph 54 of this paper, the entity has a right to recover from the reinsurer both expected claims and any unexpected claims and that the entity will receive service from the reinsurer over time. The CU20 net cost that would be recognised over time would reflect the net cost of the service the entity is receiving from the reinsurer. In addition, the proposed amendment would apply only when the reinsurance contract held is recognised before or at the same time as the loss is recognised on the underlying insurance contract. In the staff view, that

requirement, in addition to the requirement to disclose the loss component and the loss-recovery component, should limit the possibility of abuse.

56. The staff understand why some respondents think that useful information would be provided by limiting the amendment to the amount of any net gain on a reinsurance contract held so that the amendment would apply only in scenarios such as Example 1. However, the staff note that such an approach would apply only when the reinsurance contract held covers only one underlying insurance contract. When a reinsurance contract held covers many underlying insurance contracts, it is often not possible to identify the extent to which the overall net gain or net cost relates to each individual underlying insurance contract. The staff think the Board should not require an entity to separate a reinsurance contract held in this way, for the reasons set out in paragraph 45 of this paper.
57. Considering the analysis in paragraphs 43–56 of this paper, the staff continue to hold the view that the proposed loss-recovery calculation (amended to reflect the recommended extension of the scope of the proposed amendment in paragraph 42 of this paper) would:
- (a) address stakeholder concerns about an accounting mismatch on initial recognition of onerous underlying insurance contracts;
 - (b) be operationally simple for entities to apply; and
 - (c) provide comparable, transparent and useful information for users of financial statements.
58. Therefore, the staff recommend the Board amend the proposed calculation of income, as a consequence of the extension of the scope of the proposed amendment, to require an entity to determine the amount of a loss recovered from a reinsurance contract held by multiplying:
- (a) the loss recognised on the group of underlying insurance contracts; and
 - (b) the percentage of claims on underlying insurance contracts the entity expects to recover from the reinsurance contract held.

Question 2 for Board members

Do you agree the Board should amend the proposed calculation of income, as a consequence of the extension of the scope of the proposed amendment, to require an entity to determine the amount of a loss recovered from a reinsurance contract held by multiplying:

- (a) the loss recognised on the group of underlying insurance contracts; and
- (b) the percentage of claims on underlying insurance contracts the entity expects to recover from the reinsurance contract held?

Other feedback*Proposed footnote in the Basis for Conclusions on IFRS 17*

59. As discussed in paragraph 24 of this paper, some respondents think the proposed footnote to paragraph BC304 of the Basis for Conclusions on IFRS 17 narrows the Board's previous explanation of proportionate reinsurance in that paragraph. A distinction between reinsurance contracts held that provide proportionate coverage and other reinsurance contracts held already exists in IFRS 17 for the purpose of the requirements to recognise reinsurance contracts held in paragraph 62 of IFRS 17. As a simplification to the general recognition requirements in IFRS 17, paragraph 62 of IFRS 17 requires an entity to recognise a reinsurance contract held that provides proportionate coverage at the later of the beginning of the coverage period or initial recognition of the first underlying insurance contract.
60. When developing the proposed amendment, the Board observed that some stakeholders had interpreted the explanation of proportionate coverage in paragraph BC304 of the Basis for Conclusions on IFRS 17 differently to what the Board intended. The proposed footnote was intended to clarify the Board's original intention and would be consistent with the proposed definition of proportionate coverage in the Exposure Draft. However, the staff note that the footnote would no longer be necessary in the context of the proposed amendment if the Board were to agree with the staff recommendation that the proposed amendment apply to all reinsurance contracts held (see paragraph 42 of this paper). In addition, in the light of the feedback from outreach and comment letters, the staff think that adding the footnote at this

stage of implementation would likely disrupt rather than support implementation. Therefore, the staff recommend the Board does not add the proposed footnote to paragraph BC304 of the Basis for Conclusions on IFRS 17.

Timing of entering into the reinsurance contract held

61. As discussed in paragraph 25 of this paper, a small number of respondents expressed concerns that the proposed amendment would not apply when a reinsurance contract held is recognised after a loss is recognised on initial recognition of an underlying insurance contract. As explained in paragraph BC85 of the Basis for Conclusions on the Exposure Draft, the Board concluded that such a condition is necessary to ensure that the recovery of losses is recognised at the same time as the losses. In the staff view, the Board’s rationale continues to hold. An accounting mismatch cannot exist on initial recognition of a loss on an underlying insurance contract if the reinsurance contract held does not exist at the time the loss is recognised. In addition, as discussed in paragraph 54 of this paper, this condition would limit the possibility of abuse of the proposed amendment. Therefore, the staff recommend the Board confirm that the amendment to IFRS 17 would apply only when the reinsurance contract held is recognised before or at the same time as the loss is recognised on the underlying insurance contracts.

Guidance on the loss-recovery component

62. As discussed in paragraph 26 of this paper, a small number of respondents asked for guidance on the loss-recovery component of a group of reinsurance contracts held. Tracking a loss-recovery component of a group of reinsurance contracts held is necessary both when applying:
- (a) the proposed amendment in the Exposure Draft; and
 - (b) paragraph 66(c)(ii) of IFRS 17 for subsequent measurement.
63. The loss-recovery component of a group of reinsurance contracts held is akin to the loss component of a group of insurance contracts issued and, therefore, is accounted for in a consistent manner. The staff will consider either extending the illustrative example accompanying the Exposure Draft or providing educational material on the

treatment of a loss-recovery component to provide guidance on the measurement of the loss-recovery component.

Premium allocation approach

64. As discussed in paragraph 27 of this paper, a small number of respondents said that while the proposed amendment would apply when underlying insurance contracts are measured applying the general model or the premium allocation approach, the requirement in paragraph 66(c)(ii) of IFRS 17 for subsequent measurement appears to apply only when underlying insurance contracts are measured applying the general model. That paragraph refers to the contractual service margin of the underlying insurance contracts. The measurement of insurance contracts applying the premium allocation approach does not include a contractual service margin. In the staff view, the Board intended that paragraph to apply also when underlying insurance contracts are measured applying the premium allocation approach. However, the staff think the premium allocation approach was overlooked in the drafting. Therefore, the staff recommend the Board clarify, in the final amendments to IFRS 17, that paragraph 66(c)(ii) of IFRS 17—for subsequent measurement of a group of reinsurance contracts held when a group of underlying insurance contracts become onerous—applies when underlying insurance contracts are measured applying the premium allocation approach.

Question 3 for Board members
<p>Do you agree the Board should:</p> <ul style="list-style-type: none"> (a) not add the proposed footnote to paragraph BC304 of the Basis for Conclusions on IFRS 17; (b) confirm that the amendment to IFRS 17 would apply only when the reinsurance contract held is recognised before or at the same time as the loss is recognised on the underlying insurance contracts; and (c) clarify, in the final amendments to IFRS 17, that paragraph 66(c)(ii) of IFRS 17—for subsequent measurement of a group of reinsurance contracts held when a group of underlying insurance contracts become onerous—applies when underlying insurance contracts are measured applying the premium allocation approach?

Appendix A—three examples of applying the proposed amendment in the Exposure Draft

Introduction

- A1. This appendix provides three examples:
- (a) Example 1—loss recovery is equal to net gain on reinsurance contract held;
 - (b) Example 2—loss recovery is more than net gain on reinsurance contract held;
and
 - (c) Example 3—reinsurance contract held is in net cost position.
- A2. In all three examples:
- (a) a reinsurance contract held provides coverage for 40% of all claims on an underlying insurance contract that is onerous;
 - (b) the risk adjustment for non-financial risk and discounting are ignored for simplicity; and
 - (c) it is assumed that events occur as expected at initial recognition.
- A3. For ease of reading, the amounts which differ between the three examples are shown in blue.

Example 1—loss recovery is equal to net gain on reinsurance contract held

A4. The premium charged by the reinsurer is proportionate to the premium charged by the entity. Expected cash flows at initial recognition are as follows:

Insurance contract issued	Reinsurance contract held	Total			
Premiums	100	Reinsurance premiums	(40)	Net premiums	60
Claims	(150)	Claim recoveries	60	Net claims	(90)
Loss	(50)	Net gain	20	Net position	(30)

A5. Applying IFRS 17 as originally issued, the amounts recognised in profit or loss would be calculated as follows:

IFRS 17 as originally issued	Recognised immediately	Recognised over time
Insurance revenue	-	100
Insurance service expenses	(50)	(100)
Insurance contracts issued	(50)	-
Reinsurance premiums	-	(40)
Amounts recovered from reinsurance	-	60
Reinsurance contracts held	-	20
Profit/(loss)	(50)	20

A6. Applying the proposed amendment in the Exposure Draft, the loss recovery would be CU20 (CU50 x 40%) and the amounts recognised in profit or loss would be calculated as follows:

Proposed amendment in the Exposure Draft	Recognised immediately	Recognised over time
Insurance revenue	-	100
Insurance service expenses	(50)	(100)
Insurance contracts issued	(50)	-
Reinsurance premiums	-	(40)
Amounts recovered from reinsurance	20	40
Reinsurance contracts held	20	-
Profit/(loss)	(30)	-

Example 2—loss recovery is more than net gain on reinsurance contract held

A7. The premium charged by the reinsurer is not proportionate to the premium charged by the entity. Instead the reinsurer charges a higher premium than in Example 1.

Expected cash flows at initial recognition are as follows:

Insurance contract issued	100	Reinsurance contract held	(52)	Total	
Premiums	100	Reinsurance premiums	(52)	Net premiums	48
Claims	(150)	Claim recoveries	60	Net claims	(90)
Loss	(50)	Net gain	8	Net position	(42)

A8. Applying IFRS 17 as originally issued, the amounts recognised in profit or loss would be calculated as follows:

IFRS 17 as originally issued	Recognised immediately	Recognised over time
Insurance revenue	-	100
Insurance service expenses	(50)	(100)
Insurance contracts issued	(50)	-
Reinsurance premiums	-	(52)
Amounts recovered from reinsurance	-	60
Reinsurance contracts held	-	8
Profit/(loss)	(50)	8

A9. Applying the proposed amendment in the Exposure Draft, the loss recovery would be CU20 (CU50 x 40%) and the amounts recognised in profit or loss would be calculated as follows:

Proposed amendment in the Exposure Draft	Recognised immediately	Recognised over time
Insurance revenue	-	100
Insurance service expenses	(50)	(100)
Insurance contracts issued	(50)	-
Reinsurance premiums	-	(52)
Amounts recovered from reinsurance	20	40
Reinsurance contracts held	20	(12)
Profit/(loss)	(30)	(12)

Example 3—reinsurance contract held is in net cost position

A10. The premium charged by the reinsurer is not proportionate to the premium charged by the entity. Instead the reinsurer charges a higher premium than in Example 1 and Example 2. Expected cash flows at initial recognition are as follows:

Insurance contract issued	100	Reinsurance contract held	(65)	Total	
Premiums	100	Reinsurance premiums	(65)	Net premiums	35
Claims	(150)	Claim recoveries	60	Net claims	(90)
Loss	(50)	Net cost	(5)	Net position	(55)

A11. Applying IFRS 17 as originally issued, the amounts recognised in profit or loss would be calculated as follows:

Applying IFRS 17 as originally issued	Recognised immediately	Recognised over time
Insurance revenue	-	100
Insurance service expenses	(50)	(100)
Insurance contracts issued	(50)	-
Reinsurance premiums	-	(65)
Amounts recovered from reinsurance	-	60
Reinsurance contracts held	-	(5)
Profit/(loss)	(50)	(5)

A12. Applying the proposed amendment in the Exposure Draft, the loss recovery would be CU20 (CU50 x 40%) and the amounts recognised in profit or loss would be calculated as follows:

Proposed amendment in the Exposure Draft	Recognised immediately	Recognised over time
Insurance revenue	-	100
Insurance service expenses	(50)	(100)
Insurance contracts issued	(50)	-
Reinsurance premiums	-	(65)
Amounts recovered from reinsurance	20	40
Reinsurance contracts held	20	(25)
Profit/(loss)	(30)	(25)