

To: Financial Reporting Working Group

From: Philippe Angelis

Meeting: 16 April 2019

Reference: ECO-FRG-19-057

Subject: IFRS 17 Update – FRWG 16 April

Objective
For discussion

Summary

Insurance Europe continues to lobby based on Financial Reporting issues based on the positions summarised below:

IFRS 17

- There is a need for a two-year delay to fix the 11 issues with the standard that need addressing and cope with the operational challenges of implementation.
- The EFRAG field testing and the extensive implementation planning companies have done has produced new evidence justifying the need for the delay and improvements to IFRS 17
- IFRS 9 should be implemented simultaneously with IFRS 17 for operational reasons and to avoid accounting mismatches.

We seek discussion and input from FRWG members on the following:

- Strategy going forward: issues and timing (we recognise this may be an initial discussion given need for consultation with members and CFO Forum meeting coming up on 24th April)
- Planning for consultation response (EFRAG and IASB)
- Coordination with CFO Forum

Background

Insurance Europe has, since the summer, been supporting the CFO Forum's call for IASB to address the 11 areas of key concern and we have called for a 2-year delay – both to provide the time to make the necessary improvements but also to give all companies sufficient time for implementation. Six out of the 11 areas were also highlighted by EFRAG in a letter to the IASB. One of the areas of concern appears to have been addressed through Transition Resource Group (TRG) decision, leaving 10 remaining priority areas. Insurance Europe has been engaging with the Commission, EFRAG, IASB and Parliament while working closely with the CFO Forum and coordinating with other associations worldwide to provide a united industry message to the IASB.

The industry has been successful in forcing the IASB, in October 2018, to accept that improvements are needed and to delay IFRS 17 (and IFRS 9 for insurers), although only for 1 year rather than the two Insurance Europe is pushing for.

Since December, the IASB have been using their monthly Board meetings to work through a list of 25 issues they selected from those raised by various stakeholders and make tentative decisions on whether any changes



are needed. The 25 issues cover 11 the areas of concern identified by the European industry, but also includes changes the industry does not want – for example calls from the ESAs to reduce flexibility on setting discount rates for valuing liabilities.

In March 2018, the IASB finished making recommendations on all of the 25 issues. See Annex 2 for an assessment of the degree to which the IASB has addressed the industry concerns but in summary there are very few points where the IASB has indicated an intention to address the issue. Fortunately, the IASB has rejected changes sought by other stakeholders that we would not want, such as reducing the current flexibility on setting of discount rates sought by the European Supervisory Authorities.

The IASB Board meeting in April will be used to finalise the review process and assess the overall package of proposed changes. The Board will assess whether on the whole, the benefits of the amendments outweigh the costs and whether the amendments wouldn't unduly disrupt ongoing implementation projects.

In December, the EC's Accounting Regulatory Committee (ARC) discussed the timing of the endorsement process. It provided an indication that the Commission shares some of the industry's concerns. The secretariat's understanding is that ARC was supportive of EFRAG working proactively on the six issues it identified to the IASB and discussed that a further deferral to the application of IFRS 17 could occur if the amendments proposed by the IASB are not completed quickly enough.

At EFRAG level, the IFRS 17 endorsement process remains paused until there is clarity on the changes the IASB will propose and there the standard is stable enough to resume endorsement. Following the ARC discussions, there was disappointment that EFRAG is not engaging more actively on the 6 issues they raised.

EFRAG is currently working on gathering views with its expert groups to respond to the IASB Exposure Draft (expected by end of June 2019) and to draft the EFRAG Draft Endorsement Advice (expected by H1 2020). The CFO Forum presented their [assessment](#) of the IASB proposed changes to IFRS 17 to the EFRAG TEG on 21 March.

On 4 April, the EFRAG Board held a strategic discussion on how to respond to the upcoming IASB ED and on what to include in the draft endorsement advice. The Board decided that the draft comment letter on the forthcoming Exposure Draft should address all the changes to IFRS 17 proposed by the IASB; and the topics raised by EFRAG in the letter of 3 September 2018 to the IASB where the IASB does not propose to change IFRS 17.

The European Parliament (EP) held an exchange of views with Erkki Liikanen, Chair of the IFRS Foundation Trustees and Hans Hoogervorst, Chair of the IASB on 26 February. In addition to preparing an analysis of IASB proposed amendments to date, the secretariat highlighted that the application of IFRS 17 for mutual entities is conceptually complex and has become an issue following the publication of an educational material by the IASB in July 2018, which was picked up by MEPs. The secretariat provided a summary of the exchange of views here [ECO-FRG-19-038](#).

Getting the IASB to make some changes is already a significant achievement but it is disappointing that many of the 11 areas of concern have been so far disregarded or only partially addressed.

The secretariat has put together a tentative IFRS 17 adoption timeline, which can be found in Annex 3. The timeline is based on the assumption the IASB will publish the new standard between mid Q1 and end Q2 2020 and with optimistic assumptions for the European endorsement process. It indicates that even with publication at the earliest date by the IASB the current 1-year delay could result in timing problems within Europe. If the IASB publishes mid 2020 then the risk of timing issues within Europe increases significantly. The timeline has been discussed with the EC, which confirmed the secretariat's understanding.



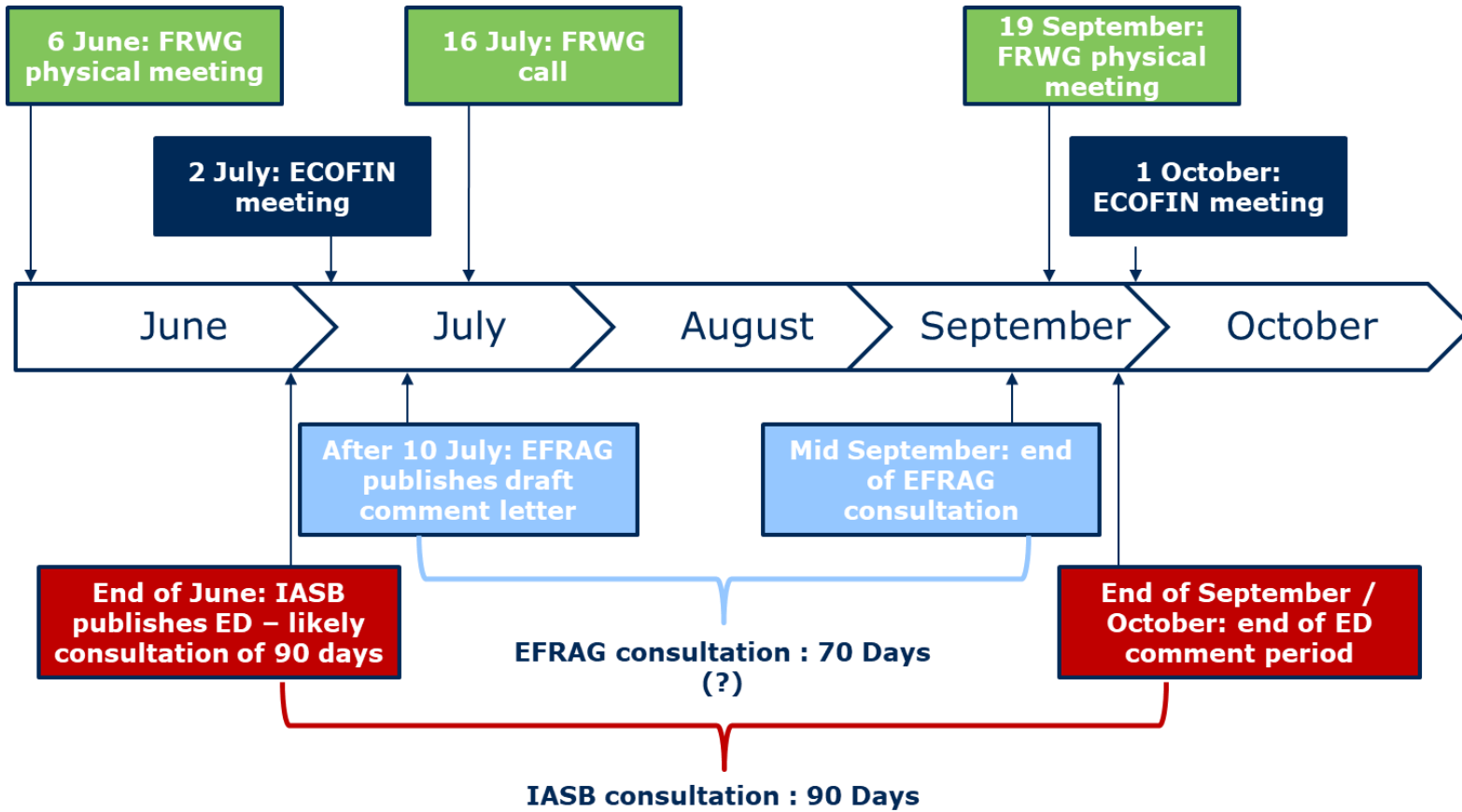
The secretariat updated its IFRS 17 position on its [website](#) (and communicated to EFRAG and the EC) in order to clarify that while the IASB's proposals for improvements are welcome, many issues remain unaddressed. There is pressure from both EFRAG and the EC to prioritize the list of issues in the hope of pushing the IASB to include those in the ED before its release. The CFO Forum will discuss their strategy going forward on 10 April – members are kindly requested to consult their members on their position as to potential prioritization and indication of the 2 or 3 most important issues that remain unresolved.

The secretariat has prepared a workplan overview of this summer's IFRS 17 consultations (see Annex 1). The secretariat also seeks member's views on potential seeking joint CFO Forum / Insurance Europe responses to the EFRAG and IASB consultations. Members will be invited to provide their views on the proposed next steps and preferred way to organize for the upcoming EFRAG and IASB consultations.

Next steps

- EFRAG
 - 16-17 April: EFRAG TEG meeting
 - 7 May EFRAG Board meeting
 - 16 May: EFRAG TEG meeting
- IASB
 - 13-17 May: IASB Board meeting
 - 17-19 June: IASB Board meeting

Annex 1: IFRS 17 consultations timeline



Annex 2: IASB proposed amendments analysis (updated for latest IASB board decisions)

Part 1: Issues raised by the Industry and in the Motion for Resolution

Issue	Description of specific concerns	IASB Board decision
Presentation	The standard requires that groups of contracts be presented as asset or liability based on its entirety. In reality, different components, such as claims liabilities to be settled, unearned premiums, etc are managed separately and administered in different systems. Groups of contracts may frequently switch from an asset to liability position.	Partly addressed– limited changes proposed (December 2018).
	The standard requires premiums and claims to be included in the insurance provision on a cash paid/received basis. In reality, these are reflected on an accrual basis and payments/receipts are managed and administered separately.	Discussed and changes rejected (December 2018).
	The standard requires, for presentation of revenue only, segregation of non-distinct investment components, even for contract that do not have a specified account balance or component.	Not Considered by the IASB -
	When 'rolling forward' the CSM, paragraph B137 requires insurers to take the latest published CSM balance, for example the balance included in interim results, as the opening position.	Discussed and changes rejected (December 2018)
Level of aggregation	The prohibition to aggregate contracts that are issued more than one year apart is unduly complex. We believe that it should be replaced by a principle according to which the insurer determines based on its internal business and risk management the way it defines its portfolios. This determination should reflect mutualisation effects when they exist. In addition, the second profitability bucket (no significant possibility of becoming onerous) is highly subjective and adds to the complexity.	Discussed and changes rejected (March 2018)
Transition	The modified retrospective approach is very restrictive and will not provide the simplifications that make retrospective application possible in practice.	Discussed and changes –rejected (February 2019)
	The option to set OCI to nil under the fair value approach is not available to assets accounted at fair value through OCI, though a similar treatment is allowed on liabilities side	Discussed and changes rejected – (February 2019).
	The hedging adjustment (risk mitigation option) cannot be applied retrospectively on the date of initial application.	The Board propose that prospective application of the risk mitigation option starts at the transition date, instead of effective date (March 2019)

Reinsurance	The approach to reinsurance gives rise to several accounting mismatches. Examples include; For an onerous contract a cedant has to recognise a loss component though P/L at inception whereas the relief from a corresponding reinsurance contract held has to be deferred over the coverage period.	Addressed for proportionate reinsurance, non-proportionate reinsurance not covered (January 2019).
	Reinsurance held cannot be accounted for under the VFA model, even if the VFA model is applied to the underlying insurance contracts.	Discussed and changes rejected (January 2019).
	Contract boundaries for reinsurance are inconsistent with those for the underlying insurance contracts, meaning that the reinsurance accounting requires the inclusion of an estimate of cash flows for underlying insurance business that is not yet written/ recognised.	Discussed and changes rejected (January 2019).
Implementation timeline concerns	IFRS 17 involves significant changes to systems and processes for insurance companies. The lack of resource and expertise to implement this comprehensive standard also make meeting the IASB application date extremely challenging, especially for smaller insurance companies. In addition, the requirement to restate comparatives really means companies will have to apply the standard by 1 January 2020.	Partially addressed by IASB (November 2018) – one-year delay rather than two, and no change to the mandatory restatement of comparatives.
IFRS 9 / IFRS 17 Link	IFRS 17 and IFRS 9 affect valuation both on the asset and liabilities side of insurers balance sheet. It is therefore important that those two standards' application dates be aligned for insurers and that consistency between the two standards is respected.	IASB delayed IFRS 9 as well as IFRS 17 (November 2018 decision) Industry remains committed to the reintroduction of equity recycling under IFRS 9.

Part 2: Additional issues raised by EFRAG, the Industry and referred to in Motion for resolution

Issue	Description of specific concerns	IASB Board decision
CSM amortization	The requirements on coverage units to be used for the CSM amortisation are not appropriate for all types of contracts. A key issue is that the CSM (of which the initial amount is impacted by investment spreads) cannot be amortised over the period in which the investment spread is earned and investment services/activity provided. This issue was mainly identified in the testing for GMM annuity contracts (particularly deferred annuities), savings and participating contracts.	Change for VFA contracts approved tentatively in June 2018.

	It is acknowledged that this is a topic under discussion by the IASB for contracts in scope of the VFA. However, the issue is equally relevant for the general measurement model.	A change for general model proposed (January 2019) addresses issue only for certain products
Acquisition Cost	Acquisition cash flows on new business that is expected to renew cannot be allocated to future periods. This is inconsistent with other industries which capitalise acquisition costs over multiple contracts. This was particularly evidenced in the testing of P&C contracts.	Addressed by IASB (January 2019)

Part 3: The remaining Industry priority issues identified during EFRAG's testing exercise

Issue	Description of specific concerns	IASB Board decision
Multi-component contracts	Certain contracts exposing the issuer to credit risk that are in substance loans (for example equity release mortgages in the UK) contain a small insurance element which causes the entire contract to be subject to Insurance accounting under IFRS 17.	Addressed by IASB (February 2019) – credit card issue solved (March 2019)
Scope of hedging adjustment	This was highlighted as part of the testing for a material book of business with guarantees that are hedged. Whilst IFRS 17 includes a specific hedging adjustment, its use is limited to specific circumstances: It is only available for contracts in scope of the VFA.	Discussed and changes rejected (December 2018).
	Hedging adjustment can only be used when derivatives are used as hedging instrument.	Partly addressed–reinsurance added to scope of risk mitigation; other financial instruments not (January 2019)
Scope of the VFA model vs General model vs PAA	The testing has shown that the results are very different depending on the measurement model applied, whilst there is a continuum in the nature of insurance products. There are several elements in the VFA model that deal more appropriately with specific elements of insurance products but these are not available under the general model or premium allocation approach. These include the alignment of liability discount rates with (accounting for) asset returns and the transitional amounts in OCI.	Discussed and changes rejected (December 2018)

Discount rates	The use of a locked in discount rate for the CSM in the general model. The impact of assumption updates is absorbed in the CSM at the locked-in rate. The Best estimate liability (BEL) is measured at the current rate. The difference between the locked-in and the current rate is reflected in the P&L and will significantly distort the current period result. In the situation where the BEL component of the insurance liability is an asset and the CSM component is a liability, inconsistencies arise due to the different discount rates for BEL (current rate) and CSM (locked-in rate).	Discussed and changes rejected (December 2018).
Business Combination	There are several elements in accounting for insurance business combinations that add significantly to complexity, including: the requirement to assess classification at the acquisition date instead of the original inception date.	Discussed and changes rejected (December 2018).
	The treatment of claims in payment at the acquisition date.	Discussed and changes rejected (December 2018).
		Relief on transition for business combinations (February 2019)

Annex 3: Tentative IFRS 17 Adoption Timeline

If IFRS 17 is re-issued toward the middle of Q1 2020, then even under optimistic assumptions, the EU endorsement process would be at risk and there is more than a remote chance of inconsistent adoption dates. If the standard is re-issued around mid 2020 there is a high chance of having a timing problem

