CFOFORUM

insurance europe

Mr. Jean-Paul Gauzès
EFRAG Board President
EFRAG
35 Square de Meeûs
B-1000 Brussels
Belgium

21 January 2021

Dear Mr. Gauzès,

EFRAG Draft Endorsement Advice on IFRS 17 'Insurance Contracts' as amended in June 2020

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

We would like to thank EFRAG for its extensive work on IFRS 17 and believe that these efforts have significantly contributed to the ongoing process to improve the standard. We continue to support a high-quality standard for insurance contract accounting and have contributed significant efforts in your testing of IFRS 17, in particular through responding to the EFRAG IFRS 17 Case Study in 2018 and the EFRAG Limited Update in 2020. In this context, we welcome the opportunity to comment on EFRAG's Draft Endorsement Advice on IFRS 17 'Insurance Contracts' as amended in June 2020.

We support endorsement provided there is a solution for annual cohorts with a 2023 effective date
We support the endorsement of IFRS 17 in the European Union, provided that there is an adequate solution to the issue of 'annual cohorts' as part of the endorsement process. Such a solution should be optional and should not impact the 1 January 2023 effective date of IFRS 17.

Annual cohorts must be resolved as part of the endorsement process with a 2023 effective date
While we welcome the improvements made by the IASB in the final version of IFRS 17, the final standard still contains a number of unresolved issues that we have highlighted earlier. Of particular importance is the application of annual cohorts to intergenerationally-mutualised and cash flow-matched contracts. In May 2020, the CFO Forum submitted a document to EFRAG outlining its view that the requirement in IFRS 17 to use annual cohorts to measure the contractual service margin is not aligned to the fundamentals of such contracts, and doing so will significantly reduce the usefulness of reported information and increase the cost of compliance. A copy of this document is provided in Appendix 3 to this letter. We believe this significant issue should be resolved as part of the endorsement of IFRS 17 in the European Union. However, we believe that the solution developed to resolve this annual cohorts issue should be optional (to allow insurers to also comply with IFRS as issued by the IASB) and furthermore should not delay IFRS 17's effective date of 1 January 2023. We hope that, at some point in the future, the IASB will accommodate such European solution for annual cohorts so that the European difference from IFRS 17 would be temporary.

Several other issues remain unresolved, but should not impact the endorsement process
Whilst these other issues should not impact the endorsement process of IFRS 17 in the European Union, several priority issues identified by us in 2018 (including CSM amortisation, reinsurance, multi-component contracts, scope of hedging and business combinations), for which we proposed solutions, have also not been resolved by the IASB in the final IFRS 17 published in June 2020. We have included a

list of these issues, together with their current status, in Appendix 2 to this letter. We have also encountered several other issues during our work in implementing IFRS 17 and we disagree with a number of assessments in the Draft Endorsement Advice (as highlighted in Appendix 1). Addressing these concerns in line with our earlier proposed solutions would have significantly improved the quality and usefulness of IFRS 17 and would produce financial results that would better reflect the economics of the underlying businesses. However, we do not believe that these issues should block the endorsement of IFRS 17 in the European Union in time for the 2023 effective date and, therefore, should not lead to amendments to IFRS 17 as part of the European endorsement process. We believe a thorough post implementation review, addressing all these issues (excluding issues only relevant at transition), will be needed.

Our detailed responses are included in Appendix 1
We have included our responses to your 'Invitation to comment' in Appendix 1. We highlight that it is difficult to answer several questions: while we do not fully agree with EFRAG's assessment with regard to all issues other than annual cohorts for the reasons set out above (which would lead to a 'No' response to the questions), we do agree with EFRAG's assessment that topics should not block the endorsement of IFRS 17 in the European Union in time for the 2023 effective date, as overall IFRS 17 is an improvement (which would result in a 'Yes' response). Our 'Yes and No' responses should be viewed in this context.

We appreciate the opportunity to provide comments on the Draft Endorsement Advice and would be pleased to discuss them with you at your earliest convenience.

Yours sincerely,

Delfin Rueda
Chair
European Insurance CFO Forum

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

Appendix 1 – Response to EFRAG ‘Invitation to comment’

EFRAG European Financial Reporting Advisory Group	

INVITATION TO COMMENT ON EFRAG’S ASSESSMENTS ON IFRS 17 INSURANCE CONTRACTS AS AMENDED IN JUNE 2020

Once filled in, this form should be submitted by 29 January 2021 using the ‘Comment publication link’ available at the bottom of the respective news item. All open consultations can be found on EFRAG’s web site: Open consultations: express your views.

EFRAG has been asked by the European Commission to provide it with advice and supporting material on IFRS 17 *Insurance Contracts* as amended in June 2020 (‘IFRS 17’ or ‘the Standard’). In order to do so, EFRAG has been carrying out an assessment of IFRS 17 against the technical criteria for endorsement set out in Regulation (EC) No 1606/2002 and has also been assessing the costs and benefits that would arise from its implementation in the European Union (the EU) and European Economic Area.

A summary of IFRS 17 is set out in Appendix I.

Before finalising its assessment, EFRAG would welcome your views on the issues set out below. Please note that all responses received will be placed on the public record, unless the respondent requests confidentiality. In the interests of transparency, EFRAG will wish to discuss the responses it receives in a public meeting, so it is preferable that all responses can be published.

In order to facilitate the EFRAG process, it is strongly recommended to use the structure below in your responses.

EFRAG’s initial assessments, summarised in this questionnaire, will be updated for comments received from constituents when EFRAG is in the process of finalising its Letter to the European Commission regarding endorsement IFRS 17.

Your details

1 Please provide the following details:

(a) Your name or, if you are responding on behalf of an organisation or company, its name:

Joint response by:

- European Insurance CFO Forum; and
- Insurance Europe

(b) Are you a:

☐ Preparer ☐ User ☒ Other (please specify)

Industry organisations representing European insurance and reinsurance companies.

(c) Please provide a short description of your activity:

The European Insurance CFO Forum ("CFO Forum") is a group representing 23 of Europe's largest insurance companies. Insurance Europe is the European insurance and reinsurance federation, comprising 37 national insurance associations. Its members represent 95% of the premium income of the European insurance market.

(d) Country where you are located:

Both the CFO Forum and Insurance Europe are pan-European organisations, representing insurance entities and associations in multiple countries.

(e) Contact details, including e-mail address:

CFO Forum: cfoforum.vpo@uk.pwc.com Insurance Europe: reporting@insuranceeurope.eu

Part I: EFRAG's initial assessment with respect to the technical criteria for endorsement

Note to the respondents: *Appendix II presents EFRAG's reasoning with reference to all requirements in IFRS 17 apart from the application of the annual cohorts requirement to some contracts specified in paragraph 6 of Annex A within Annex 1 (those contracts are conventionally referred to in this questionnaire, in the Cover Letter, in its Appendices and Annex as 'contracts with intergenerationally mutualisation and cash-flow matched contracts'[1], or 'intergenerationally mutualised and cash flow matched contracts'. Annex 1 presents content of this requirement that contribute positively or negatively to the technical criteria on this matter.*

2 EFRAG's initial assessment of IFRS 17 is that:

- The EFRAG Board has concluded on a consensus basis that, apart from the requirement to apply annual cohorts to intergenerationally-mutualised and cash-flow matched contracts, as explained in the attached Cover Letter, on balance, all the other requirements of IFRS 17 meet the qualitative characteristics of relevance, reliability, comparability and understandability required to support 'economic decisions and the assessment of stewardship and raise no issues regarding prudent accounting. EFRAG has concluded that all the other requirements of IFRS 17 are not contrary to the true and fair view principle.
- EFRAG Board members were split into two groups about whether the requirement to apply annual cohorts to intergenerationally mutualised and cash-flow matched contracts meet the qualitative characteristics described above.
  - (i) Nine EFRAG Board members consider that overcoming in a timely manner the issues of IFRS 4 brings sufficient benefits despite the concerns on annual cohorts. They believe that, in the absence of an

[1] For a description of the affected contracts please refer to paragraphs 8 to 28 of Annex A to Annex 1 of the endorsement package relating to IFRS 17.

alternative principles-based approach to grouping of contracts, on balance the annual cohorts requirement provides an acceptable conventional approach that enables to meet the reporting objectives of the level of aggregation of IFRS 17.

(ii) Seven EFRAG Board members consider that in many cases in Europe the requirement to apply annual cohorts for insurance contracts with intergenerational mutualisation and cash-flow matched contracts will result in information that is neither relevant nor reliable. This is because the requirement does not depict an entity's rights and obligations and results in information that represents neither the economic characteristics of these contracts nor the entity's underlying business model. These EFRAG Board members also consider that this requirement is not conducive to the European public good because it (i) adds complexity and cost and does not bring benefits in terms of the resulting information, (ii) may lead to unintended incentives to change the way insurers cover insurance risks and (iii) may produce pro-cyclical reporting effects.

EFRAG's reasoning and observations are set out in Appendix II, Annex 1 and the Cover Letter regarding endorsement of IFRS 17.

(a) Do you agree with this assessment for all the other requirements of IFRS 17 apart from the requirement to apply annual cohorts to intergenerationally mutualised and cash-flow matched contracts?

☒ Yes ☒ No

If you do not agree, please provide your arguments and what you believe the implications of this could be for EFRAG's endorsement advice.

While we do not completely agree with EFRAG's assessment with regard to the details of the specific topic raised in the question for the reasons set out below (which would lead to a 'No' response to this question), we do agree with EFRAG's assessment that this topic should not block the endorsement of IFRS 17 in the European Union in time for the 2023 effective date and, therefore, should not lead to amendments to IFRS 17 as part of the European endorsement process; this would lead to a 'Yes' response if the question is considered in relation to the overall endorsement advice. Our response should be seen in this context.

In 2018, the CFO Forum identified 11 priority issues with the drafting of the proposed IFRS 17 standard as well as proposed solutions for each of these issues. We have included a list of these issues, together with their current status, in Appendix 2 to our comment letter.

Other than the annual cohorts issue noted by EFRAG, several of the other remaining priority issues identified in 2018 have also not been resolved by the IASB in the 'Amendments to IFRS 17' published in June 2020. We acknowledge that these remaining unresolved priority issues should not block the endorsement of IFRS 17 by the European Union but note that the final proposed standard does not address our members' concerns in several areas. As we have highlighted before, each of these issues is important to at least a number of our members. Therefore, addressing the concerns on these unresolved issues with our proposed solutions would have significantly improved the quality and usefulness of

IFRS 17. However, we agree that these remaining issues (including CSM amortisation, reinsurance, multi-component contracts, scope of hedging and business combinations) should not block the endorsement of IFRS 17 by the European Union in time for the 2023 effective date and, therefore, should not lead to amendments to IFRS 17 as part of the European endorsement process. We recommend to re-evaluate these issues in the context of a post implementation review of IFRS 17.

(b) Having considered the technical arguments for those that support and those that oppose the application of annual cohorts to intergenerationally-mutualised contracts, as described in Annex 1, and having considered the two views from the EFRAG Board above does the requirement to apply annual cohorts to intergenerationally-mutualised contracts (within the context of paragraphs B67-B71 of IFRS 17) meet the qualitative characteristics described above? Please explain your technical reasons for supporting your view.

☐ Yes ☒ No

In May 2020, the CFO Forum submitted a document to EFRAG outlining its view that the requirement in IFRS 17 to use annual cohorts to measure the contractual service margin is not aligned to the fundamentals of intergenerationally-mutualised or cash flow-matched contracts. A copy of this document is provided in Appendix 3 to our comment letter.

Whilst the issue regarding the use of annual cohorts in principle relates to all insurance contracts, it is specifically relevant to contracts with risk sharing between generations and contracts that are cashflow-matched over different generations. As the CFO Forum stated in May 2020, the requirement in IFRS 17 to use annual cohorts for such contracts will significantly reduce the usefulness of reported information and increase the cost of compliance. We believe this significant issue should be resolved as part of the endorsement of IFRS 17 by the European Union. However, we believe that the solution developed to resolve this annual cohorts issue should be optional (to allow users to also comply with IFRS as issued by the IASB) and furthermore should not delay IFRS 17's effective date of 1 January 2023.

(c) Having considered the technical arguments for those that support and those that oppose the application of annual cohorts to cash-flow matched contracts, as described in Annex 1, and having considered the two views from the EFRAG Board above does the requirement to apply annual cohorts to cash-flow matched contracts meet the qualitative characteristics described above? Please explain your technical reasons for supporting your view.

☐ Yes ☒ No

In May 2020, the CFO Forum submitted a document to EFRAG outlining its view that the requirement in IFRS 17 to use annual cohorts to measure the contractual service margin is not aligned to the fundamentals of intergenerationally-mutualised or cash flow-matched contracts. A copy of this document is provided in Appendix 3 to our comment letter.

Whilst the issue regarding the use of annual cohorts in principle relates to all insurance contracts, it is specifically relevant to contracts with risk sharing between generations and contracts that are cashflow-matched over different generations. As the CFO Forum stated in May 2020, the requirement in IFRS 17 to use annual cohorts for such contracts will significantly reduce the usefulness of reported information and increase the cost of compliance. We believe this significant issue should be resolved as part of the endorsement of IFRS 17 by the European Union. However, we believe that the solution developed to resolve this annual cohorts issue should be optional (to allow users to also comply with IFRS as issued by the IASB) and furthermore should not delay IFRS 17's effective date of 1 January 2023.

(d) Are there any issues that are not mentioned in Appendix II, Annex 1 and the Cover Letter regarding the endorsement of IFRS 17 that you believe EFRAG should take into account in its technical evaluation of IFRS 17? If there are, what are those issues and why do you believe they are relevant to the evaluation?

During our work in implementing IFRS 17 (in combination with IFRS 9) we have encountered several issues that demonstrate the (unnecessary) complexity of IFRS 17 and the misalignment between the detailed requirements in IFRS 17 and the fundamental nature of insurance business in certain areas. Whilst this implies that financial results under IFRS 9 and IFRS 17 will not always be reflective of the economics of the underlying businesses, we do not believe that these issues are sufficient to block the endorsement of IFRS 17 by the European Union in time for the 2023 effective date. However, we do believe that a thorough post implementation review will be needed.

Part II: The European public good

Note to the respondents: *EFRAG's reasoning and conclusions with reference to all the other requirements of IFRS 17 is presented in Appendix III, apart from the observations on the requirement to apply annual cohorts to intergenerationally mutualised and cash flow matched contracts, which are presented in Annex 1 (refer to the section titled Appendix III in Annex 1).*

3 In its assessment of the impact of IFRS 17 on the European public good, EFRAG has considered a number of issues that are addressed in Appendix III and Annex 1 regarding the endorsement of IFRS 17.

- The EFRAG Board has on a consensus basis assessed that, apart from the requirement to apply annual cohorts to intergenerationally-mutualised and cash-flow matched contracts, all the other requirements of IFRS 17 would improve financial reporting and would reach an acceptable cost-benefit trade-off. EFRAG has not identified any other requirements of IFRS 17 that could have major adverse effect on the European economy, including financial stability and economic growth. Accordingly, EFRAG assesses that all the other requirements in IFRS 17 are, on balance, conducive to the European public good.

(a) Do you agree with this assessment for all the other requirements apart from the requirement to apply annual cohorts to intergenerationally mutualised and cash-flow matched contracts?

☒ Yes ☐ No

If you do not agree, please provide your arguments and what you believe the implications of this could be for EFRAG's endorsement advice.

In 2018, the CFO Forum identified 11 priority issues with the drafting of the proposed IFRS 17 standard as well as proposed solutions for each of these issues. We have included a list of these issues, together with their current status, in Appendix 2 to our comment letter.

Other than the annual cohorts issue noted by EFRAG, several of the other remaining priority issues identified in 2018 have also not been resolved by the IASB in the 'Amendments to IFRS 17' published in June 2020. We acknowledge that these remaining unresolved priority issues should not block the endorsement of IFRS 17 by the European Union but note that the final proposed standard does not address our members' concerns in several areas. As we have highlighted before, each of these issues is important to at least a number of our members. Therefore, addressing the concerns on these unresolved issues with our proposed solutions would have significantly improved the quality and usefulness of IFRS 17. However, we agree that these remaining issues (including CSM amortisation, reinsurance, multi-component contracts, scope of hedging and business combinations) should not block the endorsement of IFRS 17 by the European Union in time for the 2023 effective date and, therefore, should not lead to amendments to IFRS 17 as part of the European endorsement process. We recommend to re-evaluate these issues in the context of a post implementation review of IFRS 17.

- EFRAG Board members were split between two groups, as described in the Cover Letter and above, with reference to the requirement to apply annual cohorts for contracts with intergenerational mutualisation and cash-flow matched contracts.

(b) Having considered the technical arguments for those that support and those that oppose the application of annual cohorts to intergenerationally-mutualised contracts, as described in Annex 1, and having considered the two views from the EFRAG Board above, is the requirement to apply annual cohorts to intergenerationally-mutualised contracts (within the context of paragraphs B67-B71 of IFRS 17) conducive to the European public good? Please explain your technical reasons for supporting your view.

☐ Yes ☒ No

In May 2020, the CFO Forum submitted a document to EFRAG outlining its view that the requirement in IFRS 17 to use annual cohorts to measure the contractual service margin is not aligned to the fundamentals of intergenerationally-mutualised or cash flow-matched contracts. A copy of this document is provided in Appendix 3 to our comment letter.

Whilst the issue regarding the use of annual cohorts in principle relates to all insurance contracts, it is specifically relevant to contracts with risk sharing between generations and contracts that are cashflow-matched over different generations. As the CFO Forum stated in May 2020, the requirement in IFRS 17 to use annual cohorts for such contracts will significantly reduce the usefulness of reported information and increase

the cost of compliance. We believe this significant issue should be resolved as part of the endorsement of IFRS 17 by the European Union. However, we believe that the solution developed to resolve this annual cohorts issue should be optional (to allow users to also comply with IFRS as issued by the IASB) and furthermore should not delay IFRS 17's effective date of 1 January 2023.

(c) Having considered the technical arguments for those that support and those that oppose the application of annual cohorts to cash-flow matched contracts, as described in Annex 1, and having considered the two views from the EFRAG Board above, is the requirement to apply annual cohorts to cash-flow matched contracts conducive to the European public good? Please explain your technical reasons for supporting your view.

☐ Yes ☒ No

In May 2020, the CFO Forum submitted a document to EFRAG outlining its view that the requirement in IFRS 17 to use annual cohorts to measure the contractual service margin is not aligned to the fundamentals of insurance business. A copy of this document is provided in Appendix 3 to our comment letter. Whilst the issue regarding the use of annual cohorts in principle relates to all insurance contracts, it is specifically relevant to contracts with risk sharing between generations and contracts that are cashflow-matched over different generations. As the CFO Forum stated in May 2020, the requirement in IFRS 17 to use annual cohorts for such contracts will significantly reduce the usefulness of reported information and increase the cost of compliance. We believe this significant issue should be resolved before IFRS 17 is endorsed by the European Union. However, we believe that the solution developed to resolve this annual cohorts issue should be optional (to allow users to also comply with IFRS as issued by the IASB) and furthermore should not delay IFRS 17's effective date of 1 January 2023.

Part III: The questions in Part III relate to all the other requirements in IFRS 17 apart from the requirement to apply annual cohorts to intergenerationally mutualised and cash-flow matched contracts

Notes to the respondents: *In this Part, "IFRS 17" or "requirements in IFRS 17" or "the Standard" is intended to be referred to all the other requirements in IFRS 17 apart from the requirement to apply annual cohorts to intergenerationally mutualised and cash-flow matched contracts (your views on the latter requirement are to be covered in Part IV).*

The European Commission and the European Parliament asked EFRAG to provide its views on a number of specific matters, that are presented below.

Improvement in financial reporting

4 EFRAG has identified that, in assessing whether the endorsement of IFRS 17 is conducive to the European public good, it should consider whether the Standard is an improvement over current requirements across the areas which have been subject to changes (see paragraphs 15 to 27 of Appendix III). To summarise, for all the other requirements in IFRS 17 apart from the requirement to apply annual cohorts to intergenerationally mutualised and cash-flow matched contracts, EFRAG considers that they provide better financial information than IFRS 4.

Do you agree with this assessment?

☒ Yes ☒ No

If you do not agree, please provide your arguments and indicate how this could affect EFRAG's endorsement advice.

Both yes and no have been selected due to an uncertainty on the scope of the question.

We believe that, excluding the annual cohorts issues for intergenerationally mutualised and cash-flow-matched contracts, the remaining IFRS 17 requirements provide better overall financial information than IFRS 4. However, some specific requirements of IFRS 17 do not provide better information than IFRS 4 for that specific topic (see Appendix 2) and therefore we do not agree that <u>all</u> other requirements of IFRS 17 provide better information. As overall these other requirements do provide better financial information, the requirements which do not provide better financial information should not block the endorsement of IFRS 17 by the European Union in time for the 2023 effective date.

Costs and benefits

5 EFRAG's initial assessment is that taking into account the evidence obtained from the various categories of stakeholders, the benefits of all the other IFRS 17 requirements in IFRS 17 exceeds the related costs.

Do you agree with this assessment?

☒ Yes ☐ No

If you do not agree, please provide your arguments and indicate how this could affect EFRAG's endorsement advice.

We believe that the requirements in IFRS 17 are unnecessarily complex and that the benefits of more consistency in financial reporting amongst insurers could have been achieved at a much lower cost. At the same time, we find it very difficult to quantify and measure the benefits of IFRS 17 and believe that the benefits of IFRS 17 may be more visible at an industry level than for individual companies. In any case, given the significant implementation work that has already been undertaken, with the related significant costs having already been incurred, we do not believe that the cost/benefit assessment should block the endorsement of IFRS 17 by the European Union in time for the 2023 effective date, other than in the context of annual cohorts as set out above.

Other factors

Potential effects on financial stability

6 EFRAG has assessed the potential effects on financial stability based on the ten criteria set out in the framework developed by the European Central Bank "*Assessment of accounting standards from a financial stability perspective*" in December 2006. Based on this assessment, EFRAG is of the view that, on balance, IFRS 17 does not negatively affect financial stability (Appendix III paragraphs 428 to 482).

Do you agree with this assessment?

☒ Yes ☐ No

If you do not agree, please provide your arguments and indicate how this could affect EFRAG's endorsement advice.

We agree with the assessment that, on balance, IFRS 17 does not negatively affect financial stability.

Potential effects on competitiveness

(Appendix III paragraphs 227 to 286)

7 EFRAG has assessed how IFRS 17 could affect the competitiveness of European insurers taking into account the diversity in their business models vis-à-vis their major competitors outside Europe.

EFRAG concludes that the underlying economics and profitability will always be more decisive in taking up a business in a particular region or a particular insurance product than changes to the accounting that is used to report on it.

Do you agree with this assessment?

☒ Yes ☐ No

If you do not agree, please provide your arguments and indicate how this could affect EFRAG's endorsement advice.

We disagree with the assessment that accounting is not relevant to the competitiveness of European insurers vis-à-vis their major competitors outside Europe. We regret that the implementation of IFRS 17 will not lead to world-wide harmonisation in accounting for insurance contracts and, as such, may put some European insurers at a competitive disadvantage to their competitors that are not required to apply IFRS 17. However, we do not believe that the assessment of competitiveness should block the endorsement of IFRS 17 by the European Union in time for the 2023 effective date, other than in the context of annual cohorts as set out above.

Potential impact on the insurance market (including impact on social guarantees)

8 EFRAG has assessed the potential impact on the insurance market in Appendix III paragraphs 287 to 325.

EFRAG commissioned a study from an economic consultancy. This study ('Economic Study') stated that entities may re-consider both their pricing methodologies and product offers when applying IFRS 17 for the first time. The effect on pricing may be more significant than the effect on product offers. However, EFRAG does not have any quantification of the extent of changes in pricing or product design that would result from it.

As per the Economic Study, a majority of stakeholders interviewed (i.e. supervisory authorities, insurers and external investors) agreed that IFRS 17 alone would not impact the asset allocation of insurance undertakings, because this activity is more driven by risk management and/or asset/liability management.

Furthermore, EFRAG has considered how IFRS 17 could affect small and medium-sized entities (SMEs). EFRAG concludes that the number of small insurers that would be affected by IFRS 17 in producing their individual financial statements is very limited (between 27 and 35 depending on the option chosen based on the proposed[2] EIOPA quantitative thresholds).

(a) Do you agree with the assessment on pricing and product offerings?

☒ Yes ☐ No

(i) If you do not agree, please provide your arguments and indicate how this could affect EFRAG's endorsement advice.

(ii) Do you have any other observations that you think is relevant for EFRAG's endorsement assessment on this topic? Please explain.

N/A

(b) Do you agree with the assessment on asset allocation?

☒ Yes ☐ No

(i) If you do not agree, please provide your arguments and indicate how this could affect EFRAG's endorsement advice.

(ii) Do you have any other observations that you think is relevant for EFRAG's endorsement assessment on this topic? Please explain.

N/A

(c) Do you agree with the assessment on SMEs?

☒ Yes ☒ No

(i) If you do not agree, please provide your arguments and indicate how this could affect EFRAG's endorsement advice.

(iii) Do you have any other observations that you think is relevant for EFRAG's endorsement assessment on this topic? Please explain.

While this matter should not block the endorsement of IFRS 17 with a 1 January 2023 effective date, EFRAG's analysis on SMEs affected by IFRS 17 is misleading. To define "small" insurers, EFRAG uses EIOPA's definition of small insurers for which Solvency II requirements do not apply. This means that EFRAG's analysis focuses only on extremely small insurers and fails to consider the large number of small and medium unlisted insurers which apply IFRS as part of the option under article 5 of the IAS regulation in Europe. In addition, for those small and medium sized insurers for whom Solvency II does apply there are a range of exemptions and proportionality principles which are intended to facilitate a significant reduction in burden. There is no such relief in IFRS 17, so all insurance companies in Europe who will be under IFRS 17 will have to apply the full standard irrespective of their size.

[2] Reference is made to EIOPA's publicly consulted Consultation Paper on the Opinion on the 2020 review of Solvency II to amend the thresholds for applying Solvency II.

Presentation of general insurance contracts

9 EFRAG is of the view the presentation requirements of IFRS 17 would provide relevant information. EFRAG also concludes that providing separate information for contracts that are in an asset, from those in a liability, position would provide useful information to users. (Appendix II paragraphs 118 to 125, 360 to 362).

Do you agree with this assessment?

☒ Yes ☒ No

If you do not agree, please provide your arguments and indicate how this could affect EFRAG's endorsement advice.

While we do not completely agree with EFRAG's assessment with regard to the details of the specific topic raised in the question for the reasons set out below (which would lead to a 'No' response to this question), we do agree with EFRAG's assessment that this topic should not block the endorsement of IFRS 17 in the European Union in time for the 2023 effective date and, therefore, should not lead to amendments to IFRS 17 as part of the European endorsement process; this would lead to a 'Yes' response if the question is considered in relation to the overall endorsement advice. Our response should be seen in this context.

We refer to the earlier communicated issues (that remain largely unresolved) and proposed solutions that, amongst others, also relate to the separate presentation of contracts that are in an asset and in a liability position. However, we do not believe that these should block the endorsement of IFRS 17 by the European Union in time for the 2023 effective date.

Interaction between IFRS 17 and Solvency II

10 EFRAG concludes that in implementing IFRS 17, there are possible synergies with Solvency II, but the extent of such synergies varies between insurers. In addition, no synergies are expected for building blocks that are specific to IFRS 17 such as the contractual service margin which is not an element of the measurement approach for insurance liabilities under Solvency II. Synergy potential is available in areas that have a high degree of commonality under the two frameworks, i.e. the building blocks for the measurement of the insurance liability needed to establish the cash flow projections, and actuarial systems to measure insurance liabilities. The potential depends, to an extent, on the differences in the starting position of insurers and the investments already made in the implementation of Solvency II. It also depends on the amount of effort to adapt existing actuarial systems, that were developed for the Solvency II environment, to the IFRS 17 reporting requirements. (Appendix III paragraphs 401 to 412).

Do you agree with this assessment?

☒ Yes ☐ No

If you do not agree, please provide your arguments and indicate how this could affect EFRAG's endorsement advice.

N/A

Impact of the new Standard on financial stability, long-term investment in the EU, procyclicality and volatility

11 On financial stability, refer to the conclusions in paragraph 6 of this Invitation to Comment.

On long-term investment in the EU, EFRAG's view is that asset allocation decisions are driven by a variety of factors, among which external financial reporting requirements might play some part but do not appear to be a key driver. There is no indication that IFRS 17 in isolation would lead to any significant changes in European insurers' decisions on asset allocation or holding periods (Appendix III paragraphs 96 to 123).

On procyclicality and volatility, EFRAG believes that IFRS 17 has mixed effects on procyclicality. IFRS 17 may result in more volatile financial performance measures because of the use of a current measurement. However, from the evidence collected, it is not likely that this volatility has the potential to play a specific role in producing pro-cyclical or anti-cyclical effects. EFRAG also assesses that IFRS 17 does not have the potential to reinforce economic cycles, such as overstating profits and thus allowing dividends and bonus distributions in good times, as there is no linkage between the accounting equity (cumulative retaining earnings) and amounts available for distributions, which are defined within the requirements of Solvency II or within the requirements at national level, independently from the IFRS accounting. Finally, EFRAG notes that the transparent nature of the IFRS 17 information has the benefit for investors to be able to react timely to any changes at hand, thereby avoiding cliff-effects. (Appendix III paragraphs 483 to 507).

(a) Do you agree with the assessment on long-term investment?

☒ Yes ☐ No

(i) If you do not agree, please provide your arguments and indicate how this could affect EFRAG's endorsement advice.

(ii) Do you have any other observations that you think is relevant for EFRAG's endorsement assessment on this topic? Please explain.

N/A

(b) Do you agree with the assessment on procyclicality and volatility?

☒ Yes ☐ No

(i) If you do not agree, please provide your arguments and indicate how this could affect EFRAG's endorsement advice.

(ii) Do you have any other observations that you think is relevant for EFRAG's endorsement assessment on this topic? Please explain.

N/A

IFRS 17 and IFRS 9

12 EFRAG is of the view that mismatches reported by preparers that contributed to EFRAG's assessment do not arise solely from the application of IFRS 17 and

IFRS 9 but are mostly economic in nature. EFRAG considers that reporting the extent of the economic mismatches in profit or loss provides useful information.

In EFRAG's view, asset allocation decisions are driven by a variety of factors and disentangling the impact of accounting requirements from other factors is difficult. When defining the accounting for financial assets under IFRS 9, an insurer would not apply business models determined in isolation, but rather business models that are supportive of or complementary to their business model for managing insurance contracts. EFRAG notes that the interaction between each of an entity's internal policy decisions will determine the importance of any accounting mismatches remaining in the financial statements and this may differ largely from one insurer to another.

EFRAG has assessed the different tools that both standards offer to mitigate accounting mismatches. EFRAG assesses that:

(a) there is no conceptual barrier against the application of hedge accounting in the context of IFRS 17. However, given the lack of experience and systems by the industry, it would require significant investment both in time and systems development to achieve hedge accounting in this context (Appendix III, Annex 5);

(b) the treatment of OCI balances and risk mitigation at transition will not, on balance, negatively impact the usefulness of the resulting information.

(a) Do you agree with the assessment on the application of hedge accounting?

☒ Yes ☒ No

(i) If you do not agree, please provide your arguments and indicate how this could affect EFRAG's endorsement advice.

(ii) Do you have any other observations that you think is relevant for EFRAG's endorsement assessment on this topic? Please explain.

While we do not completely agree with EFRAG's assessment with regard to the details of the specific topic raised in the question for the reasons set out below (which would lead to a 'No' response to this question), we do agree with EFRAG's assessment that this topic should not block the endorsement of IFRS 17 in the European Union in time for the 2023 effective date and, therefore, should not lead to amendments to IFRS 17 as part of the European endorsement process; this would lead to a 'Yes' response if the question is considered in relation to the overall endorsement advice. Our response should be seen in this context.

We do not agree with the assessment that the application of hedge accounting is only hindered by the lack of experience and systems in the insurance industry and could be resolved by investing significant time and systems development. As we have demonstrated before, applying the hedge accounting requirements in IFRS 9 to insurance liabilities as the hedged item results in several fundamental issues that are caused by the limitations and constraints in IFRS and not just by the lack of experience and systems. However, we do not believe that this issue should block the endorsement of IFRS 17 by the European Union in time for the 2023 effective date.

(b) Do you agree with the assessment on the treatment of OCI-balances and risk mitigation?

☒ Yes ☒ No

(i) If you do not agree, please provide your arguments and indicate how this could affect EFRAG's endorsement advice.

(ii) Do you have any other observations that you think is relevant for EFRAG's endorsement assessment on this topic? Please explain.

While we do not completely agree with EFRAG's assessment with regard to the details of the specific topic raised in the question for the reasons set out below (which would lead to a 'No' response to this question), we do agree with EFRAG's assessment that this topic should not block the endorsement of IFRS 17 in the European Union in time for the 2023 effective date and, therefore, should not lead to amendments to IFRS 17 as part of the European endorsement process; this would lead to a 'Yes' response if the question is considered in relation to the overall endorsement advice. Our response should be seen in this context.

We disagree with the assessment for both OCI balances and risk mitigation at transition that these would not negatively impact the usefulness of the resulting information.

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

While the fair value and modified retrospective approaches allow the accumulated OCI balance on insurance liabilities to be set to nil on transition, as stated in paragraph C24(b) of IFRS 17, no such relief is available to assets measured at fair value through OCI. Setting OCI on the liabilities to nil at transition, whilst maintaining the historical OCI on related assets may significantly distort equity at transition and future results. Assets will generate a yield based on the historical effective interest rate, whilst liabilities will unwind at the market rate at transition date.

As we have indicated before, both of these issues could lead to material distortion of financial results under IFRS 17 and we have already provided proposed solutions to both. However, we do not believe that this issue should block the endorsement of IFRS 17 by the European Union in time for the 2023 effective date.

Application of IFRS 15

13 In some instances, an entity (including insurers) may choose to apply IFRS 15 instead of IFRS 17 to contracts that meet the definition of an insurance contract but that have as their primary purpose the provision of services for a fixed fee. EFRAG concludes that this option would probably be made by those entities that do not operate in the insurance business. EFRAG concludes that for these entities accounting for these contracts in the same way as for other contracts would provide useful information and that applying IFRS 17 to these contracts would impose costs for no significant benefit (Appendix III paragraphs 68 to 76).

Do you agree with this assessment?

☒ Yes ☐ No

If you do not agree, please provide your arguments and indicate how this could affect EFRAG's endorsement advice.

N/A

Implications of transitional requirements

14 Considering the extent of the information available for each particular group of insurance contracts at transition, EFRAG assesses that the existence of three transition approaches does not result in a lack of relevant information. The alleviations granted under the modified retrospective approach are still leading to relevant information as they enable achieving the closest outcome to a full retrospective application without undue cost or effort. In addition, EFRAG acknowledges that the possible use of three different transition methods may affect comparability among entities and, for long-term contracts, over time. However, the practical benefits of the modified retrospective and fair value approach, which were introduced by the IASB to respond to operational concerns of the preparers, may justify the reduced comparability (Appendix II paragraphs 129 to 155, 228 to 237, 300 to 303, 372 to 374, 398 to 400).

Do you agree with this assessment?

☒ Yes ☒ No

If you do not agree, please provide your arguments and indicate how this could affect EFRAG's endorsement advice.

While we do not completely agree with EFRAG's assessment with regard to the details of the specific topic raised in the question for the reasons set out below (which would lead to a 'No' response to this question), we do agree with EFRAG's assessment that this topic should not block the endorsement of IFRS 17 in the European Union in time for the 2023 effective date and, therefore, should not lead to amendments to IFRS 17 as part of the European endorsement process; this would lead to a 'Yes' response if the question is considered in relation to the overall endorsement advice. Our response should be seen in this context.

We support the existence of the modified retrospective approach and fair value approach as practical expedients for transition where obtaining the information required for the fully retrospective approach is impracticable. However, we believe that the modifications permitted under the modified retrospective approach, as set out in paragraphs C9 to C19 of IFRS 17, are too restrictive and do not provide the simplifications that make retrospective application possible in practice. Insurers will be forced to use the fair value approach for many portfolios, potentially reducing the level of comparability between the basis of reporting for in-force business at the date of transition and new business written thereafter. However, we do not believe that these issues should block the endorsement of IFRS 17 by the European Union in time for the 2023 effective date.

Impact on reinsurance

15 EFRAG concludes that the separate treatment under IFRS 17 of reinsurance contracts held and underlying direct contracts reflects the rights and obligations of different and separate contractual positions. Furthermore, EFRAG acknowledges

that reinsurance contracts issued or held may meet the variable fee criteria even though IFRS 17 states that they cannot be insurance contracts with direct participation features. However, EFRAG assesses that the risk mitigation option would largely address the accounting mismatches, thereby balancing relevant information. In addition, for reinsurance contracts held that are used to recover losses from the underlying contracts, EFRAG considers that the Amendments provide relevant information as they aim at reducing accounting mismatches which is present under the original version of the Standard (Appendix II paragraphs 63 to 74, 210 to 216, 274 to 275, 349 to 352, 395 to 397).

Do you agree with this assessment?

☒ Yes ☒ No

If you do not agree, please provide your arguments and indicate how this could affect EFRAG's endorsement advice.

While we do not completely agree with EFRAG's assessment with regard to the details of the specific topic raised in the question for the reasons set out below (which would lead to a 'No' response to this question), we do agree with EFRAG's assessment that this topic should not block the endorsement of IFRS 17 in the European Union in time for the 2023 effective date and, therefore, should not lead to amendments to IFRS 17 as part of the European endorsement process; this would lead to a 'Yes' response if the question is considered in relation to the overall endorsement advice. Our response should be seen in this context.

Despite the welcome recent improvements made by the IASB in IFRS 17, we still have remaining concerns about the IFRS 17 reinsurance requirements that result in significant accounting mismatches in several areas. We have provided proposed solutions to each of these issues before. However, we do not believe that these concerns should block the endorsement of IFRS 17 by the European Union in time for the 2023 effective date.

Implementation timeline

16 Feedback from the Limited Update to the Case Studies shows that the delay to the effective date of IFRS 17 to 1 January 2023 results in higher one-off implementation costs for preparers. However, the delay is also helping preparers to adjust their project approaches to the operational difficulties of the Covid-19 crisis. EFRAG understands from preparers that they may choose to avoid these costs by revisiting solution designs or may make more use of internal (cheaper) resources. Furthermore, according to the Limited Update to the Case Studies and other feedback from insurance associations, most of the participants did not intend to early apply IFRS 17, whereas a small minority wanted to have this possibility. EFRAG is not aware of any European insurer having taken a firm commitment to early apply the Standard. Finally, EFRAG notes that IFRS 17 requires a presentation of restated comparative information when applying the Standard for the first time. However, IFRS 9 does not have similar requirements for financial assets and liabilities (Appendix III paragraphs and 609 to 613).

(a) Do you agree with the assessment relating to delay of IFRS 17 implementation till 2023?

☒ Yes ☐ No

(i) If you do not agree, please provide your arguments and indicate how this could affect EFRAG's endorsement advice.

(ii) Do you have any other observations that you think is relevant for EFRAG's endorsement assessment on this topic? Please explain.

N/A

(b) Do you agree with the assessment relating to early application?

☒ Yes ☐ No

(i) If you do not agree, please provide your arguments and indicate how this could affect EFRAG's endorsement advice.

(ii) Do you have any other observations that you think is relevant for EFRAG's endorsement assessment on this topic? Please explain.

N/A

17 Do you agree that there are no other factors to consider in assessing whether the endorsement of the Standard is conducive to the European public good?

☒Yes ☐ No

If you do not agree, please identify the factors, provide your views on these factors and indicate how this could affect EFRAG's endorsement advice.

N/A

Part IV: The questions in Part IV aim at collecting constituents' inputs (Questions to constituents in Annex 1) and views relating to the requirement in IFRS 17 to apply annual cohorts to intergenerationally mutualised and cash-flow matched contracts

Notes to the respondents: *Respondents are reminded that responses to this Invitation to Comment will be made public on EFRAG's website. EFRAG is also inviting respondents to share quantitative data and to allow confidentiality of this information, constituents are kindly invited to submit these data separately from the Invitation to Comment. Such quantitative data can be sent to ifrs17secretariat@efrag.org. Only aggregated resulting data will be made public in the subsequent steps of the due process and will be presented in an anonymous way.*

The intergenerationally-mutualised and cash-flow matched contracts are specified in paragraph 6 of Annex A within Annex 1.

18 As stated in paragraphs 5 to 9 of Annex 1:

(a) What is the portion of intergenerationally-mutualised contracts and cash-flow matched contracts of all life insurance liabilities and all insurance liabilities? Please report the results for these two types of contracts separately where relevant.

> Please refer to information submitted by CFO Forum and Insurance Europe members in response to the 2018 Case Study and 2020 Limited Update.

(b) Please indicate the proportion of contracts with intergenerational mutualisation (within the context of paragraphs B67-B71 of IFRS 17) for which the requirement around annual cohorts is considered a significant issue. Please specify the share that would qualify for VFA.

> Please refer to information submitted by CFO Forum and Insurance Europe members in response to the 2018 Case Study and 2020 Limited Update.

(c) Please describe the approach you envisage to implement the annual cohorts requirement to contracts with intergenerationally-mutualised contracts (within the context of paragraphs B67-B71 of IFRS 17).

> We are unable to answer this question as we do not envisage an approach to implementing the current annual cohort requirements for these types of contracts. We believe this significant issue should be resolved as part of the endorsement of IFRS 17 by the European Union.

(d) Please indicate the proportion of cash-flow matching contracts for which the requirement around annual cohorts is considered a significant issue. Please specify how the features of the contracts compare with the description provided in Annex A of Annex 1.

> Please refer to information submitted by CFO Forum and Insurance Europe members in response to the 2018 Case Study and 2020 Limited Update.

(e) Please describe the approach you envisage to implement the annual cohorts requirement to cash-flow matched contracts.

> We are unable to answer this question as we do not envisage an approach to implementing the current annual cohort requirements for these types of contracts. We believe this significant issue should be resolved as part of the endorsement of IFRS 17 by the European Union.

Part V: Questions to Constituents raised in Appendix III

19 As stated in paragraphs 532 to 534 of Appendix III:

(a) In your view, how will the Covid-19 pandemic affect the impacts of IFRS 17 on the insurance market (see a description of some expected impacts in paragraphs 518 to 527 in Appendix III) and indirectly, on the European economy as a whole?

> In our opinion, at this time, the Covid-19 pandemic should not impact the decision on endorsement of IFRS 17 by the European Union in time for the 2023 effective date.

(b) Is the Covid-19 pandemic affecting your implementation process for IFRS 17 and IFRS 9? Please explain in detail the impacts such as project ambitions, budget for implementation and ongoing costs, resources, speed of implementation. Please also explain whether this relates to the IT systems implementation, or rather the actuarial or accounting aspects of implementation.

> No. In our opinion, at this time, the Covid-19 pandemic should not impact the decision on endorsement of IFRS 17 by the European Union in time for the 2023 effective date.

(c) Are there other aspects around the implications of Covid-19, not yet addressed in the DEA that you want to expand on?

> No. In our opinion, at this time, the Covid-19 pandemic should not impact the decision on endorsement of IFRS 17 by the European Union in time for the 2023 effective date.

Part VI: EFRAG's overall advice to the European Commission

20 Do you have any other comment on, or suggestion for, the advice that EFRAG is proposing to give to the European Commission?

> In 2018, the CFO Forum identified 11 priority issues with the drafting of the proposed IFRS 17 standard as well as proposed solutions for each of these issues. We have included a list of these issues, together with their current status, in Appendix 2 to our comment letter. Of particular importance is the application of annual cohorts to intergenerationally-mutualised and cash flow-matched contracts. In May 2020, the CFO Forum submitted a document to EFRAG outlining its view that the requirement in IFRS 17 to use annual cohorts to measure the contractual service margin is not aligned to the fundamentals of these contracts. This document is included in Appendix 3 to our letter. We strongly believe that the solution developed to resolve the annual cohorts issue should be optional (to allow users to also comply with IFRS as issued by the IASB) and furthermore should not delay IFRS 17's effective date of 1 January 2023.
>
> Other than the annual cohorts issue noted above, several of the other remaining priority issues identified in 2018 have also not been resolved by the IASB in the 'Amendments to IFRS 17' published in June 2020. We acknowledge that these remaining unresolved priority issues should not block the endorsement of IFRS 17 by the European Union but note that the final proposed standard does not address our members' concerns in several areas. As we have highlighted before, each of these issues is important to at least a number of our members. Therefore, addressing the concerns on these unresolved issues with our proposed solutions would have improved the quality and usefulness of IFRS 17. However, we agree that these remaining issues (including CSM amortisation, reinsurance, multi-component contracts, scope of hedging and business combinations) should not block the endorsement of IFRS 17 by the European Union in time for the 2023 effective date and, therefore, should not lead to amendments to IFRS 17 as part of the

European endorsement process. We recommend to re-evaluate these issues in the context of a post implementation review of IFRS 17.

Appendix 2 – Status of the CFO Forum's Priority Issues

On 17 October 2018, the CFO Forum sent a letter to EFRAG and the IASB, outlining 11 priority issues in IFRS 17 identified by members during testing. A copy of the letter is provided in Appendix 4.

The current status of these issues, following the publication of the *Amendments to IFRS 17* by the IASB in June 2020, is outlined in the following table:

Issue	**Description of issue**	**Current Status**
Acquisition cash flows	Acquisition cash flows on new business that is expected to renew, cannot be allocated to future periods.	Addressed
CSM amortisation	The requirements on coverage units to be used for the CSM amortisation are not appropriate for all types of contracts. The CSM cannot be amortised over the period in which investment services are provided.	Partially addressed
Reinsurance	The approach to reinsurance gives rise to several accounting mismatches. Examples include: i. For an onerous contract a cedant must recognise a loss component though P/L at inception whereas relief from a corresponding reinsurance contract held must be deferred over coverage period. ii. Reinsurance held cannot be accounted for under the VFA model. iii. Contract boundaries for reinsurance are inconsistent with those for the underlying insurance contracts.	Partially addressed
Transition	The modified retrospective approach is restrictive and will not provide simplifications to make retrospective application possible. In addition, the option to set OCI to nil under the fair value approach is not available to assets accounted at fair value through OCI.	Partially addressed
Multi-Component contracts	i. 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. ii. Certain products change significantly in nature during their life due to the exercise of an option by the policyholder. For example, a policy with a savings phase with profit sharing may become an annuity in payment or remain paid-up without any participation if elected by the policyholder. As the classification between general model and VFA is done at inception and is irrevocable, certain products may be measured using the VFA whereas, after the execution of the option, the VFA model is not suitable.	i. Addressed ii. Not addressed

Issue	Description of issue	Current Status
Level of aggregation	**Annual Cohorts issue:** 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 cohorts. 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. On the contrary, the requirement to group contracts in their entirety prohibits the insurer to group components of an insurance contract (e.g. the host contract and individual riders) in line with how the business and risks are managed in some cases. While the annual cohorts issue is important for most insurance contracts, in May 2020, the CFO Forum highlighted the critical need for a solution in relation to contracts with risk sharing between generations and contracts that are cashflow-matched over different generations.	Not addressed
Presentational issues	i. The standard requires that groups of contracts be presented as asset or liability based on its entirety. ii. The standard requires premiums and claims to be included in the insurance provision on a cash paid/received basis. iii. The standard requires, for presentation of revenue only, segregation of non-distinct investment components, even for contracts that do not have a specified account balance or component. iv. The CSM must be "locked-in" at interim reporting, meaning that that any differences in external reporting frequency between group and subsidiary entities would result in different CSMs.	i. Partially addressed ii. Not addressed iii. Not addressed iv. Addressed
Scope of hedging adjustment	Whilst IFRS 17 includes a specific hedging adjustment, its use is limited to specific circumstances: i. It is only available for contracts in scope of the VFA. ii. It cannot be applied retrospectively on the date of initial application. iii. It can only be used when derivatives are used as hedging instrument.	i. Not addressed ii. Not addressed iii. Addressed
Scope of VFA model vs General Model and PAA	Results are very different depending on the measurement model applied, whilst there is a continuum in the nature of insurance products.	Not addressed

Issue	Description of issue	Current Status
Discount rates	There are a number of issues arising in the use of discount rates: i. The use of a locked in discount rate for the CSM in general model. ii. 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 and CSM. iii. There is uncertainty regarding whether changes in asset mix will result in changes to the discount rate using top down approach.	Not addressed
Business Combinations	There are several elements in accounting for insurance business combinations that add significantly to complexity, including: i. the requirement to assess classification at the acquisition date instead of the original inception date. ii. the treatment of claims in payment at the acquisition date.	i. Not addressed ii. Partially addressed

CFO Forum - Exemption from Annual Cohorts Discussion Document

Table of Contents:

1. Introduction

The European Insurance CFO Forum ("CFO Forum") supports the development of a high-quality standard for insurance contracts accounting and has contributed significant effort in responding to Exposure Drafts, participating in EFRAG's testing of IFRS 17 and proposing solutions to issues identified.

Our members believe the requirement in IFRS 17 to use annual cohorts to measure the contractual service margin is not aligned to the fundamentals of insurance business. Whilst this in principle relates to all insurance contracts, the issue is specifically relevant to contracts with risk sharing between generations and contracts that are cashflow-matched over different generations.

We believe that:

- The current Exposure Draft still **does not adequately reflect the true economic nature** of insurance contracts with risk sharing between generations and contracts that are cashflow-matched over different generations (together referred to as 'mutualisation') and the specific nature, performance and risks of these types of contract cannot be captured under an annual cohorts measure.

- The IASB staff, in a document for the February 2020 Board Meeting, established a list of four features of contracts "that increase the costs of applying the annual cohort requirement compared to other contracts and/or reduce the usefulness of the resulting information". The CFO Forum's view is that mutualised contracts exhibit these features, therefore **reducing the usefulness of the reporting information and increasing the costs of compliance with reporting under the annual cohorts measure**.

- **Our proposed solution more accurately represents** the intergenerational sharing nature of these contracts and is closely aligned to the current European regulatory requirements for territories where this business is actively sold.

Therefore, to assist with the finalisation of IFRS 17, the CFO Forum has proposed revised wording in this document to reflect the principle of these changes.

2. Proposed amendments to IFRS 17

To assist with the finalisation of IFRS 17, the CFO Forum has proposed the following revised wording to reflect the principle of the changes proposed by the CFO Forum. The proposed changes to the current IFRS 17 wording (existing wording, prior to revisions to be issued by the IASB by mid-2020, which are not yet available) are in italicised underlined text below.

22 An entity shall not include contracts issued more than one year apart in the same group, *<u>except for the contracts mentioned in paragraphs 22A and 22B</u>.* To achieve this the entity shall, if necessary, further divide the groups described in paragraphs 16–21.

[New] 22A *<u>An entity does not have to apply paragraph 22 to contracts that fulfill the conditions of paragraphs B67 (and B68), when:</u>*

- *<u>(a) the contracts share the return of the same specified pool of underlying items; and</u>*
- *<u>(b) their cash flows substantially affect or are affected by cash flows to policyholders of other contracts. In that case, the groups of contracts shall be established as to reflect the substantial effect of their respective cash flows. This substantial effect is on the cash flows that vary based on the return mentioned in (a), including the guarantees mentioned in B67(b) if any.</u>*

[New] 22B *<u>An entity does not have to apply paragraph 22 to contracts that are managed under cash flow matching techniques that include contracts issued more than one year apart. The cash flow matching techniques applied should be consistent with the objective of having a replicating portfolio as described in B46. For these insurance contracts, a portfolio of assets with similar cash-flow characteristics as the liabilities that this support has been assigned and maintained over the life of the obligations. Significant changes to the portfolio of assets are only made for the purpose of maintaining the replication of expected cash flows between assets and liabilities where the cash flows have materially changed. The portfolio of assets and liabilities should be identified, organised and managed separately from other portfolios of the insurer and the expected asset and liability cash flows are well-matched (i.e. the expected cash flow of the assigned portfolio of assets replicate each of the expected cash flows of the group of insurance contracts in the same currency, and any mismatch does not give rise to material financial and insurance risk). In this case, groups of contracts can be established reflecting how the insurance contracts are managed through the cash flow matching techniques.</u>*

***[*New]109A** *<u>For insurance contracts which have been grouped together using paragraphs 22A and B, an entity shall disclose a description of such groups, an explanation how the cash flows are substantially shared, how groups have been determined, the effect of the new contracts added to the existing groups, and provide the information required by paragraph 109 separately from that for other contracts.</u>*

3. Basis for conclusion

3.1 Paragraph 22A

Contracts in scope of the Paragraph 22A exemption – references to existing criteria in IFRS 17

The IFRS 17 Standard as issued in May 2017 already recognises the existence of "contracts with cash flows that affect or are affected by cash flows to policyholders of other contracts". The relevant paragraphs are B67 to B71.

- B67 presents the characteristics of such contracts:
  "B67 Some insurance contracts affect the cash flows to policyholders of other contracts by requiring:
    - (a) the policyholder to share with policyholders of other contracts the returns on the same specified pool of underlying items; and
    - (b) either:
      - (i) the policyholder to bear a reduction in their share of the returns on the underlying items because of payments to policyholders of other contracts that share in that pool, including payments arising under guarantees made to policyholders of those other contracts; or
      - (ii) policyholders of other contracts to bear a reduction in their share of returns on the underlying items because of payments to the policyholder, including payments arising from guarantees made to the policyholder."

- B68 states that the fulfilment cash flows of contracts belonging to such a group shall:
    - (a) include payments arising from the terms of existing contracts to policyholders of contracts in other groups, regardless of whether those payments are expected to be made to current or future policyholders; and
    - (b) exclude payments to policyholders in the group that, applying (a), have been included in the fulfilment cash flows of another group."

- An illustration of the conditions set in B67 is given in B69 with a group benefitting from a guaranteed amount, which reduces the returns of the underlying items for the policyholders of another group.

- B70 indicates that in some cases, the interaction between the cash flows may have to be calculated at a higher level than the groups and should then be allocated to those groups on "a systematic and rational basis".

- Lastly, B71 indicates that fulfilment cash flows may include payments expected to be made to current policyholders in other groups or future policyholders. In that case, an entity is not required to continue to allocate such fulfilment cash flows to specific groups but can instead recognize and measure a liability for such fulfilment cash flows arising from all groups.

There is a common belief that these paragraphs cover the case of contracts for which an intergenerational and substantial risk sharing exists, but fall short of providing a complete solution. In fact, annual cohorts require arbitrary allocations for contracts with discretionary cash flows where management exercises discretion as to the timing and the allocation of the policyholders' profit share to individual policyholders. This is because the discretionary cash flows are fully shared across the different generations of policyholders so that profitability is not relevant on a cohort by cohort basis.

Contracts in scope of the Paragraph 22A exemption – references to AP2B §27 of the February 2020 Board meeting

The characteristics of the contracts that would be in scope of the new paragraph 22A are as follows:

- The contracts are participating contracts, which share the same pool of underlying items. This pool is either a segregated pool of assets or identified through regulatory or contractual terms.
- The regulatory or contractual formula is usually discretionary yet provides for a minimum right to participation.
- There is an intergenerational sharing of the risks and rewards corresponding to the participation, because the return is shared between the policyholders with the same participation formula, whatever their underwriting date.
- For such contracts, the cash flows that vary based on the underlying items' return are substantial for the policyholders.
- If some contracts benefit from a guaranteed amount, then the other policyholders sharing the return of the same pool of underlying items are affected by the benefits related to that guaranteed amount. The insurer will only contribute to the guaranteed amount in the last resort, if the return of the pool is not sufficient.

Currently, these contracts are managed together for both accounting and regulatory purposes. The concept of annual cohorts is not currently applied, because it is irrelevant for the measurement of the liability corresponding to the variable return. It is also irrelevant for assessing the profitability of these contracts, which will become onerous as a whole if the global asset return does not provide for both the costs of all policyholders, and the guaranteed amount of only some of them.

In the AP2B of the February 2020 Board meeting §27, the IASB staff established a list of four features of contracts "that increase the costs of applying the annual cohort requirement compared to other contracts and/or reduce the usefulness of the resulting information":

Feature	Cost of implementation and benefit of resulting information
1. Paragraphs B67 and B68 of IFRS 17 apply and the contract shares in the same pool of underlying items as other contracts in the group. In addition, the entity has discretion over how it shares the returns from underlying items between itself and the policyholders as a whole.	Cost is potentially relatively high and the benefits of the resulting information potentially reduced.
2. The contract meets the criteria in paragraph B101 of IFRS 17. This is the scope of the variable fee approach.	Cost is potentially relatively high.

Feature	Cost of implementation and benefit of resulting information
3. If there are financial guarantees over returns on underlying items in the contract: (a) their effect is shared with other policyholders across generations; and (b) the entity's remaining share is small.	The benefits of the resulting information are potentially reduced.
4. The contract includes only small amounts of 'fixed cash flows' the effect of changes in which is not shared with other policyholders.	The benefits of the resulting information are potentially reduced.

For the contracts described above, at least 3 of these features are met, and all 4 if the contracts are in scope of the Variable Fee Approach (i.e. if conditions of B101 are met):

- All these contracts share the same pool of underlying items and paragraphs B67 (and sometimes B68) will apply;
- Most of these contracts are in scope of the Variable Fee Approach (i.e. comply with B101);
- If there are financial guarantees over returns on underlying items in the contract, their effect is substantially shared with other policyholders across generations, and the remaining exposure for the insurer is relatively small;
- These contracts include only small amounts of "fixed cash flows" not shared with other policyholders.

Whilst most contracts eligible for 22A will be in scope of the Variable Fee Approach, it may also apply to General Measurement Model contracts which have cash flows that affect or are affected by cash flows to policyholders of other contracts as per paragraphs B67-B68.

An exception based on these features would fit these particular contracts with intergenerational risk sharing (mutualisation).

3.2 Paragraph 22B

A key characteristic of the particular contracts in scope of paragraph 22B is that these contracts and the related assets are managed on a cash-flow matching basis without a distinction between generations. Cash flows on the related assets are matched with the overall portfolio of contracts, and not on an issue year basis. As such, there is intergenerational sharing in the cash-flow matching and as such we have proposed the wording in Paragraph 22B.

The criteria should be based on the existence of cash flow matching techniques with the same objective as the one described in paragraph B46.

Cash flow matching techniques are applied to different generations of insurance contracts since the same issue year might contain different profiles of ages among policyholders (e.g. annuitants) in the case of a long term annuity portfolio which consequently lead to different longevity risk exposures.

These cash flow matching groups are defined and created for the cash flows that arise from a group of insurance contracts with similar insurance (e.g. longevity) and financial risks (e.g. guaranteed interest rates embedded in the insurance portfolios). The main objective of the cash flow matching is to exactly match in amount and timing the liabilities arising from a group of insurance contracts.

It is worth noting that those contracts do not fulfill the characteristics described in paragraph B67-B71 and are accounted for under the general measurement model. Insurance companies do not have the discretion of modifying the interest rate granted to policyholders since it is contractually guaranteed upfront.

The application of the annual cohort requirement by policy year is not in line with the mutualisation effect embedded in the cash flow matching grouping. In the context of an asset liability management strategy, in case that the cash flow matching groups had to be broken down by annual cohorts, artificial volatility in the allocation of assets to liability is expected to arise.

4. Further arguments for exemption to annual cohorts

Do annual cohorts fail to reflect intergenerational sharing of risk?
Contracts in scope of the proposed exception have cash flows that affect or are affected by cash flows to policyholders of other contracts as outlined in IFRS 17.B67-B71 or have cash flows that are matched to asset cash flows over policy generations. Relying on existing provisions of IFRS 17, the cash flows are interdependent across groups, meaning that different generations of policies share risks of changes in cash flows.

Moreover, under the contracts in scope of 22A, individual policyholders jointly share in the profits of a common pool of underlying items. This implies that no single group/generation of policyholders within the portfolio is entitled to a separable profit share in a subset of the underlying items until the benefit is individually allocated to each policyholder.

In this regard, in the February 2020 Board meeting AP2B §21 (a), the IASB "*does not expect to track specific underlying items for each annual cohort if the contract requires the policyholder to share with policyholders of other annual cohorts the returns on the same specified pool of underlying items [as] that would not be practicable, nor would it depict the nature of the sharing of the returns on the total pool of underlying items across the annual cohorts*".

When the sharing of returns is determined for policyholders as a whole and an allocation on a cohort by cohort basis is not objectively determinable as cash flows are shared across (existing and new) generations of policyholders, the use of annual cohorts does not provide useful information about changes in the profitability of contracts over time because profitability is not measurable at that level. As a consequence, the allocation to annual cohorts cannot "appropriately" reflect the legal and economic features of such contracts.

Do annual cohorts result in arbitrary allocations?
The proposed scope exception would apply to contracts with intergenerational mutualisation. In absence of such exception, the requirement in IFRS 17.24 otherwise arbitrarily requires the entity to allocate to each group of contracts future cash flows expected to be paid to current and future policyholders. These allocations would be totally arbitrary in the sense that if identifying the subsidization effect of the current contracts to new business is determinable and it is a fundamental principle for contracts with intergenerational risk sharing mechanism, assigning those allocations to

different groups and track these allocations overtime introduce artificial element in the performance measurement and reporting. In a low interest rates scenario, the risk is to favor pro-cycling reporting effects linked to artificial and arbitrary allocations rather than reflecting the capability of managing risks and reporting meaningful profitability trends.

On the contrary for such contracts, the CSM roll forward is a powerful tool to understand how the expected profits emerge and change over time. This is achieved through the disclosure of the impact at inception of new contracts on the existing group, as well as details on the computation of the CSM effect of new business on the groups eligible to the exception to the annual cohorts and on the detailed features of such groups meeting the exception criteria . An additional disclosure is proposed to that effect.

Are annual cohorts too costly for contracts with intergenerational sharing of risks?
Intergenerational mutualisation is a key feature of life-saving business in many European jurisdictions hence the exception would apply to a large portion of Life business for many entities.

The CFO Forum believes that the scope of the proposed exception adequately captures the characteristics of contracts for which applying the annual cohort requirement would not provide relevant information to users of the financial statements. In case such a requirement persists, complex process and IT implementation would be required to perform, track and manage over time the allocations described above, all the more since this information does not currently exist. As the CSM is calculated retrospectively, outputs will need to be stored, referenced and updated in each subsequent reporting period. In order to achieve this, projected fulfilment cash flows will need to be segmented and stored at an annual cohort level. The changes to systems and processes that are required in order to achieve this functionality require significant effort and cost.

Cash flow matching techniques – An example
This section provides further information on the nature of Spanish long-term insurance products, which would meet the criteria for exemption from annual cohorts set out in paragraph 22B.

According to local regulation and since 1999, Spanish insurance undertakings are required to apply an Asset and Liability Management (ALM) framework to manage the insurance and financial risks arising from long term savings products. Over the last twenty years these cash flow matching techniques have proven to be robust in providing a risk management tool for those undertakings offering long term guarantees to its policyholders.

The main objective of the cash flow matching techniques is to ensure the matching of the future proceeds expected from the asset cash flows to mimic the movements of the probability weighted liability cash flows, aiming at ensuring the matching of both the timing and the quantity of liability cash flows. Calculations are required to be performed in monthly buckets until the depletion of future expected liabilities of an in-force portfolio. These adequacy checks are performed and monitored on a frequent basis. External auditors perform regular reviews on the adequacy of those tests which are also reviewed by the local regulator.

In terms of the assets used for ALM techniques, typically fixed asset cash flows are used and are managed and held to maturity (mostly debt instruments and other cash assets which are classified as Available for Sale). Additionally, in certain cases also derivatives are used in order to mimic the projection of the liability cash flows based on the expected duration of those contracts. Those derivatives are not used for speculative purposes as it is not permitted by the local regulator.

In terms of the approach used for defining the grouping of the cash flow matching portfolios, insurance undertakings create asset portfolios for those insurance liability portfolios which have homogeneous insurance and financial risks. Mutualization of risks among generations is demonstrated by the following facts:

1. Insurance risks: typically, a liability portfolio within the same cash flow matching group contains policyholders with different ages, thus with different exposure to longevity risks. Given its long-term nature, longevity risk is managed through the mutualization of risk exposures within the same group.

2. Financial risks: typically, the cash flow matching group contains different levels of guaranteed interest rates, within a range. The asset portfolio is created in order to provide coverage to those rates guaranteed to policyholders. Insurance undertakings shall manage assets to ensure that the proceeds from financial assets are sufficient to pay policyholders 'benefits at any projected period of time based on the contractual obligations.

The most common life insurance product subject to cash flow matching techniques relate to life-long annuities. Probability weighted liability cash flows are estimated until those are expected to be depleted (i.e. upon death of the policyholder) based on best-estimate assumptions. Surrender benefits are also considered in the projection of liability cash flows, including the corresponding market-value adjustment, where necessary, based on the contractual terms and conditions.

These cash flow matching techniques have been the fundamental pillar in order to obtain the regulatory approval to use the Matching Adjustment under the Solvency II framework. This mechanism permits insurance undertakings to adjust the risk-free rate term structure used for the valuation of liabilities aiming at ensuring the removal of volatility of Solvency II Own Funds. Additionally, cash flow matching techniques are fundamental in order to ensure the correct level of reserves to cover future life policyholder benefits.

Based on the above-mentioned facts, substantial intergenerational risk sharing is proved and, consequently, the adoption of the annual cohort requirements would lead to artificial volatility in the allocation of assets covering liabilities. Thus, a proposal is presented to provide an exemption to insurance companies as noted above in paragraph 22B of the proposed amendment.

Mr. Jean-Paul Gauzes
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Mr. Hans Hoogervorst
IASB Board Chair
IASB
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London, UK, E14 4HD

17 October 2018

Re: Proposed solutions to IFRS 17 issues discussed on 3 July 2018

Dear Mr Gauzes and Mr. Hoogervorst,

As indicated in our letter dated 3 August 2018, we have prepared proposed solutions for the issues in IFRS 17 identified during our testing and presented to you in your meeting on 3 July 2018. The proposed solutions are attached to this letter.

We have been able to address the issues presented on 3 July through the combination of the attached proposed solutions and further implementation discussions, including the recent IASB's Transition Resource Group. Resolution of all these issues is important and the proposed solutions are supported by the members of the CFO Forum.

We continue to appreciate the work done to obtain a high quality accounting standard for insurance contracts and we would like to maintain the momentum on developing and agreeing the necessary changes to IFRS 17. We would welcome discussion of the proposed solutions and the next steps in the process with both EFRAG and the IASB.

Yours faithfully

Matthew Rider Chairman
European Insurance CFO Forum

Copy CC:

- Mr. Olivier Guersent – Director-General, Financial Stability, Financial Services and Capital Markets Union, European Commission
- Mr. Alain Deckers – Head of Unit, Accounting and Financial Reporting at DG Financial Stability, Financial Services and Capital Markets Union, European Commission
- Mr. Theodor Stolojan MEP – Chair of the IFRS Permanent Team, ECON Committee, European Parliament
- Mr. Gabriel Bernardino - Chairman of the European Insurance and Occupational Pensions Authority
- Mr. Olav Jones – Deputy Director General, Insurance Europe
- Mr. Patrick Raaflaub – Chairman, CRO Forum
- Mr. Thomas Buberl – Chairman, Pan-European Insurance Forum
- Mr. Steven Maijoor - Chair, European Securities and Markets authority

Topic name:	**Acquisition cash flows**
Description of issue:	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.
Implications of issue	This results in incorrect matching of income and expenses over time. The implications are intensified if the inability to allocate acquisition costs to future periods results in contracts being onerous in accounting (but not in economic reality).
Explanation of the proposed solution	The proposed solution is to amend the wording to permit acquisition costs to be amortised over the expected economic benefit period (initial contract and expected renewals), in combination with an impairment test. This approach would be consistent with the amortisation of acquisition costs under IFRS 15.
Proposed amendments to IFRS 17 text to resolve issue:	The starting point is the wording of IFRS 17.27 as amended by the IASB Meeting of 21 June 2018. IFRS 17.27: "An entity shall recognise an asset or liability for any *insurance acquisition cash flows* relating to a group of insurance contracts issued or expected to be issued that the entity pays or receives before the group is recognised, unless it chooses to recognise them as expenses or income applying paragraph 59(a). Insurance contracts expected to be issued include expected future renewals of contracts. An asset for insurance cash flows that relate to future renewals must be tested for impairment in accordance with IAS 36. An entity shall derecognise the asset or liability resulting from such insurance acquisition cash flows when the group of insurance contracts to which the cash flows are allocated is recognised (see paragraph 38(b))."

<table>
<tr><td>Topic name:</td><td>CSM amortisation</td></tr>
<tr><td>Description of issue:</td><td>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 investment services are provided. This issue was mainly identified in the testing for savings and participating contracts.

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.</td></tr>
<tr><td>Implications of issue</td><td>Profit recognition over the life of the contract is not appropriate. For certain contracts, profit recognition is strongly frontloaded or backloaded. For example, on a simple annuity contract profit is not appropriately recognised in the accumulation and deferral phases.</td></tr>
<tr><td>Explanation of the proposed solution</td><td>The proposed solution is to expand the ‘coverage units’ to include more than only insurance benefits. This is achieved by adding the proposed wording which would permit coverage units to include “related activities performed to deliver those benefits”. This is intended to cover key non-insurance benefits such as investment activities. In order to narrow the scope of “related activities” two criteria were added:

i. that are required to be performed by law or regulation; or

ii. that were assumed in the pricing of the contract, and performance or non-performance of those activities would have had a significant impact on either the premium charged or benefits offered under the contract.</td></tr>
<tr><td>Proposed amendments to IFRS 17 text to resolve issue:</td><td>B119 An amount of the contractual service margin for a group of insurance contracts is recognised in profit or loss in each period to reflect the services provided under the group of insurance contracts in that period (see paragraphs 44(e), 45(e) and 66(e)). The amount is determined by:

(a) identifying the coverage units in the group. The number of coverage units in a group is the quantity of coverage provided by the contracts in the group, determined by considering for each contract <u>both</u> the quantity of the benefits provided <u>and the related activities performed to deliver those benefits</u> under a contract and its expected coverage duration. <u>Related activities performed to deliver benefits are those:</u>

<u>i. that are required to be performed by law or regulation; or</u>
<u>ii. that were assumed in the pricing of the contract, and performance or non-performance of those activities would have had a significant impact on either the premium charged or benefits offered under the contract.</u>

Appendix A

coverage period The period during which the entity provides coverage for insured events <u>or investment related services</u>. This period includes the coverage that relates to all premiums within the boundary of the insurance contract.

Basis of conclusions

BC 279 As discussed in paragraph BC21, the Board views the contractual service margin as depicting the unearned profit for coverage and other services provided over the coverage period. Insurance coverage is <u>often</u> the defining service provided by insurance contracts <u>but may not be the sole driver in all cases, for example where there are significant activities performed by the entity to deliver those services or where the contract includes an investment related service</u>. The Board noted that an entity provides this service over the whole of the coverage period, and not just when it incurs a claim. Consequently, IFRS 17 requires the contractual service margin to be</td></tr>
</table>

	recognised over the coverage period in a pattern that reflects the provision of services, including both the contractual benefits ~~coverage~~ and the activities performed to deliver those benefits ~~as~~ required by the contract. To achieve this, the contractual service margin for a group of insurance contracts remaining (before any allocation) at the end of the reporting period is allocated over the coverage provided in the current period and expected remaining future coverage, on the basis of coverage units, reflecting the expected duration, ~~and~~ quantity of benefits provided and the activities performed to deliver the benefits ~~by~~ of the contracts in the group. The Board considered whether: (a) the contractual service margin should be allocated based on the pattern of expected cash flows or on the change in the risk adjustment for non-financial risk caused by the release of risk. However, the Board decided the pattern of expected cash flows and the release of the risk adjustment for non-financial risk are not relevant factors in determining the satisfaction of the performance obligation of the entity. They are already included in the measurement of the fulfilment cash flows and do not need to be considered in the allocation of the contractual service margin. Hence, the Board concluded that coverage units better reflect the provision of ~~insurance~~ coverage.

<table>
<tr><td>Topic name:</td><td>Discount rates</td></tr>
<tr><td>Description of issue:</td><td>• 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 BEL is measured at the current rate. The difference between the locked-in and the current rate is reflected in the P&L or OCI and may 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).</td></tr>
<tr><td>Implications of issue</td><td>The result is significantly distorted by the discount rate components of the impact of assumption changes that are otherwise absorbed in the CSM.

The P&L and/or OCI is distorted by the use of different discount rates for different components of the insurance liability. This is particularly exacerbated when the BEL component is an asset.</td></tr>
<tr><td>Explanation of the proposed solution</td><td>For those portfolios where changes in discount rates are recognised directly in the income statement (the ‘FVPL model’), it is proposed to amend the Standard such that the current discount rate should always be utilised for all CSM measurements, re-measurements and movements. As such also the impact of changes in non-financial assumptions would be recognised in the CSM and not be split between the CSM and the income statement. All components of the liability would be measured consistently at the current interest rate when applying the FVPL model.

It is noted that no change is proposed to the OCI model. This implies that in the OCI model the impact of changes in non-financial assumptions is partly absorbed in the CSM (the impact at the locked-in rate) and partly in OCI (the effect of the difference between the locked-in rate and the current rate).</td></tr>
<tr><td>Proposed amendments to IFRS 17 text to resolve issue:</td><td><u>Use of locked-in discount rate</u>

44 For insurance contracts without direct participation features, the carrying amount of the contractual service margin of a group of contracts at the end of the reporting period equals the carrying amount at the start of the reporting period adjusted for:

(a) the effect of any new contracts added to the group (see paragraph 28);

(b) interest accreted on the carrying amount of the contractual service margin during the reporting period, measured:

(i) where an entity applies paragraph 88(a), at the current discount rates applying paragraph 36;
(ii) where an entity applies paragraph 88(b), at the discount rates specified in paragraph B72(b);

(c) the changes in fulfilment cash flows relating to future service as specified in paragraphs B96–B100, except to the extent that:

(i) such increases in the fulfilment cash flows exceed the carrying amount of the contractual service margin, giving rise to a loss (see paragraph 48(a)); or

(ii) such decreases in the fulfilment cash flows are allocated to the loss component of the liability for remaining coverage applying paragraph 50(b).

(d) where an entity applies paragraph 88(a), the effect of remeasuring the contractual service margin for the change in discount rate over the reporting period (see paragraph B96B);

(~~d~~e) the effect of any currency exchange differences on the contractual service margin; and

(~~e~~f) the amount recognised as insurance revenue because of the transfer of services in the period, determined by the allocation of the contractual service</td></tr>
</table>

margin remaining at the end of the reporting period (before any allocation) over the current and remaining coverage period applying paragraph B119.

66 Instead of applying paragraph 44, an entity shall measure the contractual service margin at the end of the reporting period for a group of reinsurance contracts held as the carrying amount determined at the start of the reporting period, adjusted for:

(a) the effect of any new contracts added to the group (see paragraph 28);

(b) interest accreted on the carrying amount of the contractual service margin, measured:

(i) where an entity applies paragraph 88(a), at the current discount rates applying paragraph 36;
(ii) where an entity applies paragraph 88(b), at the discount rates specified in paragraph B72(b);

(c) changes in the fulfilment cash flows measured where an entity applies paragraph 88(a), at the current discount rates applying paragraph 36; or where an entity applies paragraph 88(b), at the discount rates specified in paragraph B72(b) , to the extent that the change:

(i) relates to future service; unless

(ii) the change results from a change in fulfilment cash flows allocated to a group of underlying insurance contracts that does not adjust the contractual service margin for the group of underlying insurance contracts.

(d) where an entity applies paragraph 88(a), the effect of remeasuring the contractual service margin for the change in discount rate over the reporting period (see paragraph B96B)

(~~d~~e) the effect of any currency exchange differences arising on the contractual service margin; and

(~~e~~f) the amount recognised in profit or loss because of services received in the period, determined by the allocation of the contractual service margin remaining at the end of the reporting period (before any allocation) over the current and remaining coverage period of the group of reinsurance contracts held, applying paragraph B119.

B96 For insurance contracts without direct participation features paragraph 44(c) requires an adjustment to the contractual service margin of a group of insurance contracts for changes in fulfilment cash flows that relate to future service. These changes comprise:

(a) experience adjustments arising from premiums received in the period that relate to future service, and related cash flows such as insurance acquisition cash flows and premium-based taxes, measured at the discount rate specified in paragraph B96(e); ~~the discount rates specified in paragraph B72(c);~~

(b) changes in estimates of the present value of the future cash flows in the liability for remaining coverage, except those described in paragraph B97(a), measured at the discount rate specified in paragraph B96(e); ~~the discount rates specified in paragraph B72(c)~~

(c) differences between any investment component expected to become payable in the period and the actual investment component that becomes payable in the period, measured at the discount rates specified in paragraph B~~72(c)~~96(e); and

(d) changes in the risk adjustment for non-financial risk that relate to future service.

(e) in applying paragraph B96, the applicable discount rate to be utilised shall be:

i. where an entity applies paragraph 88(a), the current discount rates applying paragraph 36; or

	ii. where an entity applies paragraph 88(b), the discount rates specified in paragraph B72(c); B96B For insurance contracts without direct participation features where an entity applies paragraph 88(a), paragraph 44(d) and 66(d) require the contractual service margin to be remeasured for the change in discount rate over the reporting period. An entity shall apply paragraph B119 to determine a stream of notional cash flows whose discounted value at the reporting date using the discount rate applicable at the start of the reporting period applying paragraph 36 at that date equals the contractual service margin at the reporting date before this remeasurement. The effect of remeasuring the contractual service margin for the change in discount rate over the reporting period is then the difference between discounting these notional cash flows at the reporting date using the current discount rate applying paragraph 36 and discounting these notional cash flows at the reporting date using the current discount rate applicable at the start of the reporting period applying paragraph 36 at that date.

Topic name:	**Multi-component contracts**
Description of issue:	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. Certain products change significantly in nature during their life due to the execution of an option by the policyholder. For example, a policy with a savings phase with profit sharing may become an annuity in payment or remain paid-up without any participation if elected by the policyholder. As the classification between General Model and VFA is done at inception and is irrevocable, certain products may have to be accounted for under the VFA whereas, after the execution of the option, the VFA model is not suitable and not comparable to similar products with a different 'history'.
Implications of issue	Including these contracts in the scope of IFRS 17 is inconsistent with the treatment of similar products in other industries.
Explanation of the proposed solution	In the proposed solution, a scope exclusion is proposed whereby the issuer may elect to treat contracts that are in substance loans that expose the issuer primarily to credit risk as a financial instrument (under IFRS 9) rather than as an insurance contract (under IFRS 17). In addition, a solution is proposed for contracts which significantly change in nature due to an election by the policyholder, to treat that change as a contract modification which would permit the "new" contract to be re-assessed and treated under the appropriate measurement model (VFA or GMM) for that "new" contract.
Proposed amendments to IFRS 17 text to resolve issue:	**A – Loan-type contracts** It is proposed a new scope exemption should be added to IFRS 17 for loan type contracts. It is proposed the following wording should be added to the standard as paragraph 8A: "Some contracts meet the definition of an insurance contract but are in substance loans that expose the issuer to credit risk. An entity may choose to apply IFRS 9 instead of IFRS 17 to such contracts that it issues if, and only if, specified conditions are met. The entity may make that choice contract by contract, but the choice for each contract is irrevocable. The conditions are: a. The contract compensates the customer by reducing the customer's outstanding debt to the entity, rather than making cash payments to the customer; and b. The insurance risk transferred by the contract arises primarily from guarantees provided to the customer of the maximum amount of debt that is repayable if specified uncertain future events occur" **B – Contracts subject to significant change in nature** B24. For some contracts, the transfer of insurance risk to the issuer occurs after a period of time, and for some contracts, the nature of the contract changes significantly on the exercise of an option included in the terms of the contract. For example, consider a contract that provides a specified investment return and includes an option for the policyholder to use the proceeds of the investment on maturity to buy a life-contingent annuity at the same rates the entity charges other new annuitants at the time the policyholder exercises that option. Such a contract transfers insurance risk to the issuer only after the option is exercised, because the entity remains free to price the annuity on a basis that reflects the insurance risk that will be transferred to the entity at that time. Consequently, the cash flows that would occur on the exercise of the option fall outside the boundary of the contract, and before exercise there are no

	insurance cash flows within the boundary of the contract. However, if the contract specifies the annuity rates (or a basis other than market rates for setting the annuity rates), the contract transfers insurance risk to the issuer because the issuer is exposed to the risk that the annuity rates will be unfavourable to the issuer when the policyholder exercises the option. In that case, the cash flows that would occur when the option is exercised are within the boundary of the contract. The exception to this is where the conditions in B102A will be met on the exercise of the option included in the terms of the contract, in which case only the cost of providing the guaranteed option would be within the boundary of the original contract that is recognised before the option is exercised. B102. An entity shall assess whether the conditions in paragraph B101 are met using its expectations at inception of the contract and shall not reassess the conditions afterwards, unless: ~~the contract is modified, applying paragraph 72.~~ (a) the contract is modified, applying paragraph 72; or (b) the exercise of an option included in the terms of the contract leads to a significant and permanent change in the nature of the whole contract. An example of a significant and permanent change in the nature of a contract is when the exercised option results in the contract no longer having any direct participation features for the remainder of its term, or vice versa. B102A If an entity applies paragraph B102(b) it shall derecognise the original contract and recognise a contract including the exercised option as a new contract, applying IFRS 17. B129…. It may be appropriate to apply a different accounting policy choice in the different stages of a contract (e.g. before and after a significant change in the nature of the contract) to ensure that similar portfolios are accounted for on a consistent basis.

Topic name:	**Reinsurance**
Description of issue:	The approach to reinsurance gives rise to several accounting mismatches. Examples include; 1. For an onerous contract a cedant has to recognise a loss component though P/L whereas the relief from an corresponding reinsurance contract held has to be deferred over the coverage period 2. Reinsurance held cannot be accounted for under the VFA model, even if the VFA model is applied to the underlying insurance contracts 3. Contract boundaries for reinsurance are inconsistent with those of the underlying insurance contracts, meaning that the reinsurance accounting requires including an estimate of underlying insurance business that is not yet written/recognised
Implications of issue	The inconsistencies between insurance and reinsurance accounting create a number of accounting mismatches, meaning that the financial statements do not appropriately reflect the net risk position after reinsurance and, as a consequence, a distorted profit recognition pattern.
Explanation of the proposed solution	The proposed solutions would: 1. For proportionate reinsurance, permit the insurer to recognise a portion of the reinsurance benefit to offset the loss on the underlying contract. This ensures that the income statement reflects the economic mitigation of the reinsurance contract; 2. Permit the VFA model for reinsurance contracts when the underlying contracts are measured under the VFA model; and 3. Ensure that reinsurance would not be recognised until the underlying insurance contracts being reinsured are recognised.
Proposed amendments to IFRS 17 text to resolve issue:	**Mismatch at initial recognition** Amend IFRS 17.65 as follows: IFRS 17.65c: Only for groups of insurance contracts being reinsured on a proportionate basis, at inception of the reinsurance contract: (i) a proportionate share of the loss component for the group of underlying insurance contracts (IFRS 17.47) shall be replaced by a negative contractual service margin representing the reinsurer's share in the underlying contracts. This shall only apply if the reinsurance contract held is recognised prior to or at the same time as the underlying insurance contracts. (ii) a proportionate share of the contractual service margin for the group of underlying insurance contracts (IFRS 17.38) shall be released representing the reinsurer's share in the underlying contracts, after deducting net costs (IFRS 17.65b) resulting from these reinsurance contracts held. Regarding subsequent measurement of the underlying direct contracts reinsured in accordance with IFRS 17.65c, IFRS 17.66 needs to be extended as follows: IFRS 17.66A: For insurance contracts reinsured according to IFRS 17.65c(i) the following applies. (i) The carrying amount of the negative contractual service margin shall be adjusted for any changes in fulfilment cash flows relating to future service, notwithstanding IFRS 17.66. (ii) The amount recognised in profit or loss because of the transfer of services in the period determined by the allocation of the contractual service margin remaining at the end of the reporting period shall be presented in accordance with IFRS 17.84 and shall not change insurance revenue.

(iii) If the conditions of IFRS 17.65c cease to exist as either the reinsurance contracts held or the underlying insurance contracts are derecognised, IFRS 17.76 shall be applied accordingly.

Similarly, IFRS 17.69 needs to be extended as follows:

IFRS 17.69A: For insurance contracts under the scope of IFRS 17.65c, IFRS 17.65c and IFRS17.66A are applied consistently leading to an adjustment of the liability for remaining coverage when the entity expects not to differ materially from a comparable adjustment of the contractual service margin.

Mismatch in projected fulfilment cash flows of underlying contracts and reinsurance held

IFRS 17.62(a) should read:

if the reinsurance contracts held provide proportionate coverage—at the beginning of the coverage period of the group of reinsurance contracts held or at the initial recognition of ~~any underlying contract~~the underlying contracts, whichever is the later; and

Furthermore, IFRS 17.BC305(a) should read:

when the group of reinsurance contracts held covers the loss of a group of insurance contracts on a proportionate basis, the group of reinsurance contracts held is recognised at the later of the beginning of the coverage period of the group of reinsurance contracts held or the initial recognition of ~~any~~ the underlying contracts. This means that the entity will ~~not recognise the group of reinsurance contracts until it has recognised at least one of the underlying contracts~~only recognise the group of reinsurance contracts held to the extent that the underlying direct contracts are already recognised.

Retroactive reinsurance

IFRS 13.BC312 should be amended as follows:

The Board also decided that the net expense of purchasing reinsurance should be recognised over the coverage period as services are received unless the reinsurance covers events that have already occurred. For such reinsurance contracts held, the Board concluded that entities should recognise the whole of the net expense at initial recognition, to be consistent with the treatment of the net expense of purchasing reinsurance before an insured event has occurred. If, and only if, the insured event that triggers future cash outflows has already occurred, the corresponding net costs shall be recognised at initial recognition. The Board acknowledged that this approach does not treat the coverage period of the reinsurance contract consistently with the view that for some insurance contracts the insured event is the discovery of a loss during the term of the contract, if that loss arises from an event that had occurred before the inception of the contract. However, the Board concluded that consistency of the treatment of the net expense across all reinsurance contracts held would result in more relevant information

Reinsurance of financial risk where underlying contracts are measured by the variable fee approach

IFRS 17.B109 should be amended as follows:

~~Reinsurance contracts issued and reinsurance contracts held cannot be insurance contracts with direct participation features for the purpose of IFRS 17.~~ If and only if reinsurance contracts meet the criteria in B101 (a) to (c) and the underlying insurance contracts are contracts with direct participation features, entities may choose to account for reinsurance contracts as contracts with direct participation features. For

	reinsurance contracts issued this principle also applies to transactions under common control.

Topic name:	**Scope of hedging adjustment**
Description of issue:	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 • It cannot be applied retrospectively on from the date of initial application • It can only be used when derivatives are used as hedging instrument This was highlighted as part of the testing for a material book of business with guarantees that are hedged.
Implications of issue	The inability to use the hedge adjustment outside the narrowly defined scope will result in accounting mismatches if the fair value changes on hedging instruments are not recognised in the same category (P&L, OCI or CSM) as the changes on the hedged items). This will significantly distort the net result and create misalignment between accounting results and risk management. Paradoxically, a perfect hedge would cause a comparatively higher income statement volatility than a partial hedge.
Explanation of the proposed solution	The proposed solution would broaden the scope of the hedging adjustment to include contracts not measured under the VFA model. Furthermore, if the hedging existed at the time of adopting IFRS 17 then it would be allowed to be recognised retroactively. Hedging instruments would also be allowed to include instruments other than derivatives (including other financial instruments and reinsurance contracts).
Proposed amendments to IFRS 17 text to resolve issue:	**Contractual service margin (paragraphs B96—B119)** 44 For *insurance contracts without direct participation features*, the carrying amount of the contractual service margin of a group of contracts at the end of the reporting period equals the carrying amount at the start of the reporting period adjusted for: (a) the effect of any new contracts added to the group (see paragraph 28); (b) interest accreted on the carrying amount of the contractual service margin during the reporting period, measured at the discount rates specified in paragraph B72(b); (c) the changes in fulfilment cash flows relating to future service as specified in paragraphs B96–B100, except to the extent that: (i) such increases in the fulfilment cash flows exceed the carrying amount of the contractual service margin, giving rise to a loss (see paragraph 48(a)); ~~or~~ (ii) such decreases in the fulfilment cash flows are allocated to the loss component of the liability for remaining coverage applying paragraph 50(b); or (iii) paragraph B115A (on risk mitigation) applies in relation to the contractual service margin. (d) the effect of any currency exchange differences on the contractual service margin; and (e) the amount recognised as insurance revenue because of the transfer of services in the period, determined by the allocation of the contractual service margin remaining at the end of the reporting period (before any allocation) over the current and remaining coverage period applying paragraph B119. B97 An entity shall not adjust the contractual service margin for a group of insurance contracts without direct participation features for the following changes in fulfilment cash flows because they do not relate to future service: (a) the effect of the time value of money and changes in the time value of money and the effect of financial risk and changes in financial risk, (being the effect, if any, on estimated future cash flows and the effect of a change in discount rate), except to the extent paragraph B115A applies; (b) changes in estimates of fulfilment cash flows in the liability for incurred claims; and (c) experience adjustments, except those described in paragraph B96(a). **Risk mitigation** B115 For insurance contracts with direct participation features, ~~T~~to the extent that an entity meets the conditions in paragraphs B116 and /or B116A, it may choose not to recognise a change in the contractual service margin to reflect some or all of the changes in the effect of financial risk on the entity's share of the underlying

items (see paragraph B112) or the fulfilment cash flows set out in paragraph B113(b).

B115A For insurance contracts without direct participation features, to the extent that the entity meets the conditions in paragraph B116, it may choose not to recognise in other comprehensive income (where an entity applies paragraph 88(b)) or in the contractual service margin some or all of the effect of changes in the time value of money and financial risks arising from insurance contracts for the period.

B116 In respect to financial risk, ~~T~~to apply paragraphs B115 or B115A, an entity must have a previously documented risk-management objective and strategy ~~for using derivatives~~ to mitigate financial risk arising from the insurance contracts and, in applying that objective and strategy:
(a) the entity uses a ~~derivative~~ financial instrument to mitigate the financial risk arising from the insurance contracts.
(b) an economic offset exists between the insurance contracts and the financial instrument ~~derivative~~, ie the values of the insurance contracts and the financial instrument ~~derivative~~ generally move in opposite directions because they respond in a similar way to the changes in the risk being mitigated. An entity shall not consider accounting measurement differences in assessing the economic offset.
(c) credit risk does not dominate the economic offset.

B116A In respect of non-financial risk, to apply paragraph B115, an entity must have reinsurance contracts held to mitigate non-financial risk arising from the insurance contracts with direct participating features, and:
(a) an economic offset exists between the non-financial risk on the insurance contracts and the reinsurance contract held, ie the values of the insurance contracts and the reinsurance contract held generally move in opposite directions because they respond in a similar way to the changes in the risk being mitigated. An entity shall not consider accounting measurement differences in assessing the economic offset.
(b) credit risk does not dominate the economic offset.

B117 The entity shall determine the fulfilment cash flows in a group to which paragraphs B115 and B115A applies in a consistent manner in each reporting period.

B118 For insurance contracts with direct participation features, ~~I~~if any of the conditions in paragraphs B116 and B116A ceases to be met, an entity shall:
(a) cease to apply paragraph B115 from that date; and
(b) not make any adjustment for changes previously recognised in profit or loss.

B118A For insurance contracts without direct participation features, if any of the conditions in paragraph B116 ceases to be met, an entity shall:
(a) cease to apply paragraph B115A from that date; and
(b) not make any adjustment for changes previously recognised in profit or loss.

Insurance finance income or expenses (see paragraphs B128–B136)

88 Unless paragraph 89 applies, an entity shall make an accounting policy choice between:
(a) including insurance finance income or expenses for the period in profit or loss; or
(b) disaggregating insurance finance income or expenses for the period to include in profit or loss an amount determined by the total insurance finance income or expenses on the carrying amount of the group of insurance contracts to the extent that paragraph B115A applies (to remove accounting mismatches with income and expenses included in profit or loss on financial instrument to mitigate the financial risk arising from the insurance contracts) and a systematic allocation of the remaining expected total insurance finance income or expenses over the duration of the group of contracts, applying paragraphs B130–B133.

Insurance finance income or expenses (see paragraphs 87–92)

B130 If paragraph 88(b) applies, after consideration of the impacts of paragraph B115A, an entity shall include in profit or loss an amount determined by a systematic allocation of the expected total finance income or expenses over the duration of the group of insurance contracts. In this context, a systematic allocation is an allocation of the total expected finance income or expenses of a group of insurance contracts (after consideration of paragraph B115A) over the duration of the group that:

(a) is based on characteristics of the contracts, without reference to factors that do not affect the cash flows expected to arise under the contracts. For example, the allocation of the finance income or expenses shall not be based on expected recognised returns on assets if those expected recognised returns do not affect the cash flows of the contracts in the group.

(b) results in the amounts recognised in other comprehensive income over the duration of the group of contracts totalling zero. The cumulative amount recognised in other comprehensive income at any date is the difference between the carrying amount of the group of contracts and the amount that the group would be measured at when applying the systematic allocation.

Transition

C3 An entity shall apply IFRS 17 retrospectively unless impracticable, except that:

(a) an entity is not required to present the quantitative information required by paragraph 28(f) of IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*; and

(b) an entity shall not apply the option~~s~~ in paragraph B115 and B115A for periods before the date of initial application of IFRS 17 unless it can do so without the use of hindsight, for example where documentation exists that describes the hedging strategy and the hedge objective targets prior to the date of initial application of IFRS 17 and where the entity can compute the cumulative risk mitigation impact in other comprehensive income or on the contractual service margin using reasonable methods that will result in reliable and relevant financial results.

Topic name:	**Transition**
Description of issue:	Applying the fully retrospective approach to transition is expected to be impossible in many cases due to the need for detailed historical data for long historic periods. The modified retrospective approach is very restrictive and will not provide the simplifications that make retrospective application possible in practice. The option to set OCI to nil under the fair value approach is not available to assets accounted at fair value through OCI.
Implications of issue	If the modified retrospective method is not improved, insurers will be forced into the fair value approach for many portfolios. Whilst the fair value approach is a helpful practical expedient in some cases, it may not provide an appropriate profit recognition pattern in all cases. Depending on the final interpretation of the fair value, this could be the case for portfolios with significant in-force and significant new business. Setting OCI on the liabilities to nil at transition, whilst maintaining the historical OCI on related assets will distort equity at transition and results going forward significantly.
Explanation of the proposed solution	The proposed solution would provide a more principles based approach to the modified retrospective approach to transition, by replacing specific prescribed modifications by a more general principle to allow reasonable approximations. The proposed solutions would also address the distortion to equity at transition and P&L after transition that arises under the option to set OCI on liabilities to nil at transition. The proposed solutions permits setting OCI on liabilities equal to OCI on assets, also for the GMM. Finally, the proposed solution extends the transition relief on annual cohorts to all transition approaches.
Proposed amendments to IFRS 17 text to resolve issue:	**Issue 1** C5A Regardless of the transition approach applied, an entity is not required to apply paragraphs 15- 24, and may include in a group: (i) contracts issued more than one year apart; and (ii) contracts which would otherwise be divided by applying paragraph 16. C7 Paragraphs C9–C19 set out ~~permitted~~ modifications to retrospective application in the following areas: (a) assessments of insurance contracts or groups of insurance contracts that would have been made at the date of inception or initial recognition; (b) amounts related to the contractual service margin or loss component for insurance contracts without direct participation features; (c) amounts related to the contractual service margin or loss component for insurance contracts with direct participation features; and (d) insurance finance income or expenses. C8 To achieve the objective of the modified retrospective approach, an entity is permitted to make ~~use each~~ modifications, including but not limited to those set out in paragraphs C11~~9~~–C19, only to the extent that an entity does not have reasonable and supportable information to apply a retrospective approach. C9 In applying the modified retrospective approach, an entity may apply paragraph C10 to determine: ~~To the extent permitted by paragraph C8, an entity shall determine the following matters using information available at the transition date~~ (a) how to identify groups of insurance contracts, applying paragraphs 14–24; (b) whether an insurance contract meets the definition of an insurance contract with direct participation features, applying paragraphs B101–B109; and (c) how to identify discretionary cash flows for insurance contracts without direct participation features, applying paragraphs B98–B100.

C10 An entity may choose to determine the matters in paragraph C9 using:
(a) reasonable and supportable information for what the entity would have determined given the terms of the contract and the market conditions at the date of inception or initial recognition, as appropriate; or
(b) reasonable and supportable information available at the transition date.

C11 To the extent permitted by paragraph C8~~, for contracts without direct participation features,~~ an entity ~~shall~~ may determine the contractual service margin or loss component of the liability for remaining coverage (see paragraphs 49–52) at the transition date by applying paragraphs C12–C16.

C17 To the extent permitted by paragraph C8, for contracts with direct participation features an entity ~~shall~~ may choose to make specific modifications (for example, by applying paragraphs C12-C16) or may determine the contractual service margin or loss component of the liability for remaining coverage at the transition date as:

(a) the total fair value of the underlying items at that date; minus

(b) the fulfilment cash flows at that date; plus or minus

(c) an adjustment relating to service provided before that date. The entity shall estimate this amount taking into account distributions to the entity from the underlying items before that date and by comparing the remaining coverage units with the total coverage units of the group of contracts ~~for~~

(i) This adjustment can be determined as:

- amounts charged by the entity to the policyholders (including amounts deducted from the underlying items) before that date.
- amounts paid before that date that would not have varied based on the underlying items.
- the change in the risk adjustment for non-financial risk caused by the release from risk before that date. The entity shall estimate this amount by reference to the release of risk for similar insurance contracts that the entity issues at the transition date

(ii~~d~~) if (a), (b) and (c)(i)~~(c)~~ result in a contractual service margin—minus the amount of the contractual service margin that relates to services provided before that date. The total of (a)–(c) is a proxy for the total contractual service margin for all services to be provided under the group of contracts, ie before any amounts that would have been recognised in profit or loss for services provided. The entity shall estimate the amounts that would have been recognised in profit or loss for services provided by comparing the remaining coverage units at the transition date with the coverage units provided under the group of contracts before the transition date; or

(iii~~e~~) if (a), (b) and (c)(i)~~(c)~~ result in a loss component—adjust the loss component to nil and increase the liability for remaining coverage excluding the loss component by the same amount.

<u>Issue 2</u>

IFRS 17.C18 "For groups of insurance contracts that, applying paragraph C10, include contracts issued more than one year apart:
….
(b) if an entity chooses to disaggregate insurance finance income or expenses between amounts included in profit or loss and amounts included in other comprehensive income applying paragraphs 88(b) or 89(b), the entity needs to determine the cumulative amount of insurance finance income or expenses recognised in other comprehensive income at the transition date to apply paragraph 91(a) in future periods. The entity is permitted to determine that cumulative difference either by applying paragraph C19(b) or:

	(i) as nil, unless (ii) applies; and (ii) ~~for insurance contracts with direct participation features to which paragraph B134 applies,~~ as equal to the cumulative amount recognised in other comprehensive income on the underlying ~~items~~ assets." … … IFRS 17.C19 "For groups of insurance contracts that do not include contracts issued more than one year apart: … (b) if an entity chooses to disaggregate insurance finance income or expenses between amounts included in profit or loss and amounts included in other comprehensive income, applying paragraphs 88(b) or 89(b), the entity needs to determine the cumulative amount of insurance finance income or expenses recognised in other comprehensive income at the transition date to apply paragraph 91(a) in future periods. The entity shall determine that cumulative difference: (i) for insurance contracts for which an entity will apply the methods of systematic allocation set out in paragraph B131—if the entity applies paragraph C13 to estimate the discount rates at initial recognition—using the discount rates that applied at the date of initial recognition, also applying paragraph C13; (ii) for insurance contracts for which an entity will apply the methods of systematic allocation set out in paragraph B132—on the basis that the assumptions that relate to financial risk that applied at the date of initial recognition are those that apply on the transition date, i.e. as nil unless paragraph C19(b)(iv) applies; (iii) for insurance contracts for which an entity will apply the methods of systematic allocation set out in paragraph B133—if the entity applies paragraph C13 to estimate the discount rates at initial recognition (or subsequently)—using the discount rates that applied at the date of the incurred claim, also applying paragraph C13; and (iv) ~~for insurance contracts with direct participation features to which paragraph B134 applies,~~—as equal to the cumulative amount recognised in other comprehensive income on the underlying ~~items~~ assets." C24 In applying the fair value approach … (c) ~~for insurance contracts with direct participation features to which paragraph B134 applies,~~ — as equal to the cumulative amount recognised in other comprehensive income from the underlying ~~items~~ assets.

Topic name:	**Business combinations**
Description of issue:	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 • the treatment of claims in payment at the acquisition date
Implications of issue	This will result in a significantly different accounting treatment between the group and subsidiary financial statements. This adds significant unnecessary complexity and costs, particularly for GI business which may require GMM capability only if a future acquisition takes place.
Explanation of the proposed solution	Under the proposed solution the acquiring insurer would not be required to reassess the classification into accounting models and the determination of the insured event at acquisition date.
Proposed amendments to IFRS 17 text to resolve issue:	To remove the deletion in the consequential amendment to IFRS 3.17(b) and amend the IFRS 3.17(b) and B93 as follows: IFRS 3.17 This IFRS provides two exceptions to the principle in paragraph 15: (a)… (b) classification of ~~a~~ insurance contracts ~~as an insurance contract~~ and the determination of the insured event in accordance with IFRS 17 Insurance Contracts. The acquirer shall classify those contracts on the basis of the contractual terms and other factors at the inception of the contract […]. IFRS 17.B93 When an entity acquires insurance contracts issued or reinsurance contracts held in a transfer of insurance contracts that do not form a business or in a business combination, the entity shall apply paragraphs 14–24 to identify the groups of contracts acquired, as if it had entered into the contracts on the date of the transaction. When an entity acquires insurance contracts issued or reinsurance contracts held in a business combination, the entity is allowed to identify the groups of contracts acquired on the basis of the contractual terms and other factors at the inception of the contract, if the acquired business already applies IFRS 17 before the business combination.

Topic name:	**Level of aggregation**
Description of issue:	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 cohorts. 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.
Implications of issue	The standard's requirements on level of aggregation, including the annual cohorts, are too prescriptive and detailed, leading to an excessive level of granularity, major implementation challenges, as well as undue costs.
Explanation of the proposed solution	The proposed solution would remove the requirement to group contracts by annual cohorts, under the condition that contracts issued in different years would be in the same profitability group.
Proposed amendments to IFRS 17 text to resolve issue:	IFRS 17 para 22 is amended as follows: An entity shall not include contracts issued more than one year apart in the same group. The annual cohort application is not required when the entity has reasonable and supportable evidence to conclude that contracts issued more than 12 months apart would be classified into the same profitability group as defined in paragraph 16. To achieve this the entity shall, if necessary, further divide the groups described in paragraphs 16-21

Topic name:	**Presentation issues**
Description of issue:	• 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, receivables/payables, etc are managed separately and administered in different systems. Groups of contracts may frequently switch from an asset to liability position. • 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. • 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. • There are several elements in the accounting which lead to different accounting treatment between the group and subsidiary financial statements. One of these is the interpretation that the CSM must be "locked-in" at interim reporting means that that any differences in external reporting frequency between group and subsidiary entities would result in different CSMs.
Implications of issue	These requirements, that impact only presentation, would require major system changes compared to the current approach, which is a well-established industry practice. These changes will also lead to insurance receivables no longer being separately visible in the balance sheet, which is a deterioration in relevance of the financial statements for both life and general insurance insurers. Companies have considered the implications for implementation and maintenance of systems for these requirements and found that the complexity and costs will very significant
Explanation of the proposed solution	The proposed solution would ensure that all amounts due (e.g. premiums receivable and claims payable) continue to be accounted for separately from the insurance liability under IFRS 9. The proposed solutions would also remove the requirement to separately report components of groups of contracts that are entirety in an asset position from those in a liability position. The definition of 'non-distinct investment components' is proposed to be changed to only include components that have the characteristics of a deposit. Furthermore, the difference between consolidated and subsidiary reporting due to different reporting frequencies is proposed to be resolved by aligning the accounting in the subsidiary to the consolidated group.
Proposed amendments to IFRS 17 text to resolve issue:	**Receivables/Payables** IFRS 17.33 should be amended as follows: ***An entity shall include in the measurement of a group of insurance contracts all the future cash flows that are not due within the boundary of each contract in the group […]*** For clarification, IFRS 17.B66 should be amended as follows: ***[…]*** cash flows that are already due to be paid or received. Any rights or obligations to receive or to pay cash flows that are unconditional and due shall be accounted for in accordance with IFRS 9. **Assets/liabilities** IFRS 17.78 should be amended as follows: ***An entity shall present separately in the statement of financial position the carrying amount of ~~groups of:~~***

	(a) the liability for remaining coverage and the liability for incurred claims for insurance contracts issued ***(b) the expected recovery for remaining coverage and the recovery for incurred claims for reinsurance contracts held.*** ***~~insurance contracts issued that are assets;~~*** ***~~insurance contracts issued that are liabilities;~~*** ***~~reinsurance contracts held that are assets; and~~*** ***~~reinsurance contracts held that are liabilities~~*** **Investment components** Amend Appendix A, Defined terms for "investment component" as follows: "The amounts that an insurance contract requires the entity to repay to a policyholder even if an insured event does not occur and has the characteristics of a deposit, such as a specified account balance and the requirement to repay the amounts with interest." **Dual Accounting** **Interim financial statements** B137 Notwithstanding the requirement in IAS 34 *Interim Financial Reporting* that the frequency of an entity's reporting shall not affect the measurement of its annual results, an entity ~~shall not~~ is not required to change the treatment of accounting estimates made in previous interim financial statements when applying IFRS 17 in subsequent interim financial statements or in the annual reporting period.