

IFRS 17

Background

- **Europe is the biggest user of International Financial Reporting Standards (IFRS) in the world**, and applies not only to listed companies but in many member states is used for statutory reporting. Since 2005, European regulation has required IFRS for consolidated reporting for all insurers that have shares or bonds listed on regulated exchange markets. In many other large markets (USA, Japan) IFRS is not mandatory.
 - IFRS impacts more than only listed companies in the EU because many countries have opted to permit or require all companies, including unlisted insurers of any size, to apply IFRS. In fact, **IFRS is mandatory for unlisted companies consolidated financial statements in over half the EU member states.**
- The European insurance industry remains committed to the development of high-quality financial reporting standards and supports the IASB's process for finalising IFRS 17 amendments. Insurers have made significant contributions to the development of IFRS 17 'Insurance contracts' and are engaging significant efforts and considerable resources into its implementation.
- Insurers require accounting standards that appropriately represent their business model in order to offer appropriate products and services to customers and continue to act as long-term stable investors into the economy. This means additional effort needs to be made to ensure the standards recognise that insurance is a multiyear, long-term business, is based on portfolios and not single contracts, has assets and liabilities that interact, has risk and risk mitigation as core activities rather than side-effects.
- **While the industry broadly supports the goals of the IASB**, the IFRS 17 standard published in May 2017 was not good enough and **changes were needed** to achieve suitably high-quality global accounting standards that provide meaningful, consistent and reliable financial reporting and avoided excessive implementation costs.
- In its [Motion for a Resolution \(MfR\)](#) of June 2018, the European Parliament called on the European Commission and EFRAG to consider the specific aspects and impact of IFRS 17 on the insurance sector and potential effects on financial stability and competitiveness.
- Following the European field testing of the standard organised by EFRAG, the insurance industry identified a number of important issues that needed to be addressed and proposed solutions to them. The industry also called for implementation to be postponed to 1 January 2023 to allow time for the IASB to make the necessary improvements to the standard and to allow enough time for the wide range of European insurers affected to implement the standard. In September 2018, [EFRAG](#) also called for a number of changes to the standard, including on annual cohorts and identified 2023 as the realistic effective date.

Current situation

- The IASB published a revised IFRS 17 standard in June 2020. **We welcomed the IASB decision to postpone the effective date of IFRS 17** and to extend the exemption currently in place regarding the application of IFRS 9 – financial instruments – to 2023, which will enable insurers to implement both standards at the same time. However, while we appreciated that the effective dates of IFRS 17 and IFRS 9 were postponed and that progress has been made on a number of the industry's other issues, **we were disappointed that the IASB decided not to address concerns about the annual cohorts requirement and has also left other industry issues unresolved.**

- As part of the European endorsement process, EFRAG issued its draft endorsement advice on 30 September and is currently consulting stakeholders until the end of January 2021. The final advice by EFRAG to the European Commission is expected at the end of March 2021. In its draft advice, **EFRAG explained that its Board members are split into two groups about whether the requirement to apply annual cohorts meet the European endorsement criteria.** Nine EFRAG Board members believe that overcoming in a timely manner the issues of IFRS 4 brings sufficient benefits despite the concerns on annual cohorts, whereas seven EFRAG Board members consider that in many cases in Europe the requirement to apply annual cohorts will result in information that is neither relevant nor reliable.

- The European Commission's Accounting Regulatory Committee is also divided on the issue of annual cohorts, with representatives of France, Spain, Italy, Poland and Austria expressing very strong concerns about the issue of annual cohorts while Germany and the Netherlands arguing in favour of swift endorsement. Most other member states reserved their position to the issuance of EFRAG's Final Endorsement Advice (FEA).

- Insurance Europe's position on IFRS 17:
 - **The European Insurance industry continues to support IFRS international accounting standards** and the role they play in supporting international comparability among insurers and a global level playing field.

 - **Insurers regret that the IASB has decided not to address the concerns raised on the annual cohorts issue.**

 - This **remains a fundamental concern for the majority of our members** because it means for their companies that:
 - IFRS 17 will **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').
 - Failure to address this issue will **reduce the usefulness and relevance** of the reporting information and **increase the costs of compliance** with reporting.

 - **The CFO Forum, the French standard setter and the Spanish standard setter have provided potential solutions** and we are convinced that these can be used as the basis to create appropriate mechanisms to identify the contracts where annual cohorts should not be required.

 - Therefore, **the majority of our members**, given the IASB's decision not to address the annual cohorts issue and its significant impact on insurers, **support a European carve-in or carve-out** to ensure a solution to the annual cohort issue is applied for European insurers. Other members see the need to endorse IFRS 17 as-is to preserve the global nature of the standard and concerns about potential operational implications.

 - Against this background, any such carve-in/carve-outs **should not impact the effective date of 1 January 2023.**

Annex 1: Annual Cohorts in short

The annual cohort issue

The issue of level of aggregation has been of so great importance because it goes to the heart of the insurance business model. The insurance business model (and our ability to offer products to customers) is based around mutualisation and pooling of risks. This means aggregating individual contracts into portfolios and managing the aggregate risk. Unlike the selling of most other items (clothes, electronics, services) it is often impossible to determine if an individual insurance customer is profitable. For example with car insurance there is either a claim, and then the insurer almost certainly pays back more than the premium to the customer or there is no claim in which case the insurer gets to keep the premium (less costs). The insurer pools the car insurance customers together and aims to charge each customer a premium so that in aggregate the total premiums exceed the total claims (and costs) and the insurer can earn a profit. The profit can only be measured at aggregate portfolio level. The same applies for most insurance products including savings products such as profit sharing where investment performance is pooled across customers and across time so the customer gets a smoothed return based on long-term performance rather than the everyday ups and downs of the markets.

IFRS standards generally require accounting for individual contracts. This makes no sense for insurers and after a long process a few years ago, the IASB finally accepted this was economic reality and necessary for the accounts to be meaningful. They made an exception to the general contract rules for IFRS 17 so that insurers can aggregate contracts into portfolios for the financial reporting purposes.

However, IFRS 17 still requires all portfolios to split into annual cohorts. This goes against the business model because insurance products are often a multi-year and are not measured or managed on an annual basis. The costs of the system changes and additional data gathering needed to achieve this to allow the necessary data to be gathered and then the ongoing allocation of all data into such a grouping would be very high and the information simply not useful or useful enough to justify it.

This is why as well as the industry, the European Parliament in their Motion for Resolution raised the issue of aggregation, why it was one of the 6 key issues identified by EGRAG in their letter to the IASB and why EIOPA also in their analysis of IFRS 17 said they have "reservations on a few concepts that may affect comparability and relevance of IFRS 17 financial statements and should be duly addressed" and specifically noted that "Issues such as level of contracts' aggregation or gains from reinsurance contracts held may lead to further complexity of the financial statements"