# IFRS 17 *Insurance Contracts*

## Objective

1 The objective of this paper is to provide the EFRAG Board with an update on the discussions at the recent meeting of EFRAG TEG and seek the views of the EFRAG Board as to whether they have any questions to raise with EFRAG TEG.

2 The IFRS 17 *Insurance Contracts* topics discussed at the EFRAG TEG meeting comprised:

(a) A presentation from EIOPA on the EIOPA analysis of IFRS 17; and

(b) Provisional views of EFRAG TEG on issues/tentative decisions considered by the IASB at its December 2018 meeting, having noted the views of the EFRAG IAWG on these issues.

## EIOPA analysis of IFRS 17

3 Sandra Hack presented the EIOPA view on IFRS 17. A similar presentation is scheduled for the April EFRAG Board meeting.

4 EFRAG TEG members welcomed the report and the presentation as a useful input into their work on IFRS 17. Some members of EFRAG TEG expressed a view that the EIOPA conclusions may be overstated, including:

(a) There may be changes in product offerings arising from the implementation of Solvency II as it is difficult to separate responses to external economic forces and the capital requirements in Solvency II.

(b) The degree of cost savings in implementing IFRS 17 as a result of implementing Solvency II.

5 Some EFRAG TEG members expressed a view that the long-term goal should be to align Solvency II with IFRS 17 to the extent possible, given the different objectives of the two systems.

## EFRAG TEG February discussions

6 In its February meeting EFRAG TEG considered the December 2018 tentative decisions of the IASB. In doing so, EFRAG TEG was informed of the views of the EFRAG IAWG which considered these tentative decisions in its January meeting.

7 EFRAG TEG and EFRAG IAWG were asked to provide views on:

(a) Where the IASB tentatively decided to change IFRS 17, whether that change was supported, including the impact on the draft comment letter on the forthcoming exposure draft.

(b) Where the IASB tentatively decided not to change IFRS 17, how the underlying issue should be reflected in the forthcoming draft endorsement advice.

**IASB tentative decisions to amend IFRS 17**

*Separate presentation at portfolio level*

8 The IASB tentatively decided to amend IFRS 17 to require separate presentation at portfolio level rather than at group level of insurance contracts that are in an asset position from those that are in a liability position. Some EFRAG TEG members noted the consequent loss of information for users compared to separate presentation at group level but, on balance, EFRAG TEG supported the proposal.

9 On balance, EFRAG IAWG members had also supported this proposal.

10 Overall, the provisional view of EFRAG TEG is that this proposal from the IASB should be supported in the draft comment letter on the forthcoming exposure draft.

**Question for EFRAG Board**

11 Based on the information currently available, does the EFRAG Board agree that this proposal should be supported in the draft comment letter that will be brought to the EFRAG Board for approval at a public meeting?

**IASB tentative decisions to retain the requirements in IFRS 17**

12 The IASB has tentatively decided to retain certain requirements in IFRS 17. Comments from both EFRAG TEG and EFRAG IAWG (including the issues to be explored in the forthcoming draft endorsement advice) are summarised below.

13 EFRAG TEG also identified a number of issues where it would request further information from EFRAG IAWG.

*Separate presentation of premiums receivable and claims payable*

14 The IASB has tentatively decided not to require the separate presentation of premiums receivable and claims payable.

15 Some EFRAG TEG members, having noted the advice of the EFRAG IAWG, argued that any approach that does not allocate cash flows from premiums receivable and claims payable to the appropriate group of insurance contracts is likely to impact measurement as well as presentation. Others questioned this view and wanted more information.

16 Some EFRAG TEG members also argued that IFRS 17's approach is conceptually sound because it reflects the view that an insurance contract is a bundle of rights and obligations.

17 EFRAG TEG requested EFRAG IAWG to provide further information on premiums receivable and claims payable, including the extent to which premiums receivable reflect credit risk (which may affect the relevance of separate presentation).

18 Some members of the EFRAG IAWG considered that, by not amending IFRS 17:

(a) Costs of changing systems (specifically, greater integration of actuarial and cash systems) in order to provide the information that IFRS 17 requires would outweigh the benefits to users.

(b) Users would lose information as some entities currently provide disaggregated information on premiums receivable and claims payable, although not on a consistent basis.

(c) Although IAS 1 *Presentation of Financial Statements* permits disaggregation of line items such as the insurance contracts liability, analysts would want a harmonised approach to such disaggregation.

19 Overall, EFRAG IAWG members considered that this issue should be included in the draft endorsement advice as a cost-benefit issue.

*Discount rates*

20 The IASB has tentatively decided that IFRS 17 should continue to require the use of a locked-in rate for accretion of the contract service margin (CSM) under the general model.

21 EFRAG TEG, having noted the advice of the EFRAG IAWG, did not have major concerns on this issue. However, some EFRAG TEG members questioned the relevance of using a locked-in rate for the CSM. Some EFRAG TEG members noted that the CSM acts as a deferral mechanism for the effects of changes in estimates affecting the future, but that is does not defer all such effects.

22 A few EFRAG IAWG members were concerned about this requirement in IFRS 17. They suggested that it was not consistent with the IFRS 17 principle of treating rights and obligations arising from a group of insurance contracts as a single asset or liability and that the accounting policy choice on presentation of finance income and expense in profit or loss or OCI would not alleviate the concerns. A few EFRAG IAWG members considered that the current requirements impair relevance.

*Risk adjustment*

23 The IASB decided not to provide further guidance on the measurement of the risk adjustment.

24 EFRAG TEG, having noted the advice of the EFRAG IAWG, acknowledged that the lack of guidance would call on the need for judgement but did not consider this to be a significant issue for the draft endorsement advice.

25 One EFRAG IAWG member noted that this decision results in easier implementation.

*Subjectivity in determining discount rates and the risk adjustment*

26 IFRS 17 is a principles-based standard which provides different ways of determining discount rates and the risk adjustment.

27 EFRAG TEG, having noted the advice of the EFRAG IAWG, decided to ask the EFRAG IAWG for further information on discount rates.

28 A few EFRAG IAWG members continued to raise concerns about the subjectivity in determining discount rates and the risk adjustment and that there is a trade-off between relevance and reliability. Other EFRAG IAWG members consider that the principles in IFRS 17 result in relevant information and reflect economic reality.

*Option to disaggregate insurance financial income or expenses in OCI*

29 In order to avoid volatility in profit or loss, IFRS 17 permits the disaggregation of insurance finance income and expenses between profit or loss and OCI.

30 EFRAG TEG, having noted the advice of the EFRAG IAWG, acknowledged that the optionality might detract from comparability but did not consider this to be a significant issue for the draft endorsement advice.

31 EFRAG IAWG members had mixed views, with some considering that the option impairs comparability, although some noted that any impairment to comparability can be tempered by the proposed disclosures. Other EFRAG IAWG members noted that EFRAG had previously supported this approach.

*Variable fee approach – definition*

32 EFRAG TEG, having noted the advice of the EFRAG IAWG, did not consider this to be a significant issue for the draft endorsement advice.

33 Some EFRAG IAWG members consider that the scope of the variable fee approach (VFA) is too narrow. Individual members expressed different views as to whether Belgian contracts are, or are not, within the scope of the VFA.

*Variable fee approach – limited applicability of the risk mitigation exception*

34 The VFA includes a risk mitigation exception that is designed to avoid an accounting mismatch created by the VFA. That is, some changes in financial risk that otherwise would adjust the CSM may be recognised in profit or loss to match the change in the fair value of a derivative that mitigates that financial risk.

35 The IASB reconsidered this issue at its January meeting and the views of EFRAG TEG will be reported at a future meeting of the EFRAG Board.

*Business combinations*

36 IFRS 17 removes the exemption in IFRS 4 *Insurance Contracts* and requires insurers to apply IFRS 3 *Business Combinations*.

37 EFRAG TEG, having noted the advice of the EFRAG IAWG, generally supported the approach being taken by the IASB as this provided comparability of reporting under all IFRS Standards.

38 Most EFRAG IAWG members considered that the change to current practice would create operational challenges and would be costly to implement. They considered that this would not lead to relevant information. Other EFRAG IAWG members noted that there would be a trade-off between relevance and comparability (as IFRS 3 would only be applied prospectively).

*Future cash flows in the measurements of reinsurance contracts held*

39 IFRS 17 requires that, in measuring a reinsurance contract, cash flows should relate to all the underlying contracts covered by that reinsurance contract, whether or not the underlying contract has been written.

40 EFRAG TEG members, having noted the advice of the EFRAG IAWG, decided to ask the EFRAG IAWG for further information on the mismatches identified by the EFRAG IAWG.

41 Some EFRAG IAWG members considered that this requirement did not lead to relevant and reliable information as, with more complex reinsurance contracts, there is a lack of matching between the reinsurance contract and the underlying contract.

*Accounting estimates in interim financial statements*

42 EFRAG TEG, having noted the advice of the EFRAG IAWG, observed that the interim reporting requirements for insurers are consistent with other industries, and could also be seen as an operational relief for preparers.

43 Some EFRAG IAWG members considered that IAS 34 *Interim Financial Statements* should provide an exception to the discrete period approach in the case of insurance contracts. They noted that the effect of the discrete period approach would lead to different results depending on the frequency of financial reporting.

**Question for the EFRAG Board**

44 Does the EFRAG Board have any comments on the developments at EFRAG TEG?