European Financial Reporting Advisory Group

DRAFT FOR DISCUSSION BY THE EFRAG BOARD

Input for Planning of endorsement activity of IFRS 17

Summary of the activities performed from the issuance of the standard to date

1 The IASB issued IFRS 17 *Insurance Contracts* in May 2017.

2 EFRAG received the letter by the European Commission in January 2018, requesting to provide endorsement advice on the standard, and in October 2018 the European Parliament approved a Motion on the same topic. Appendix 1 and 2 of this document provide a summarised list of the topics that these two documents request to consider in the endorsement.

3 The EFRAG Secretariat has been working in preparation of the endorsement advice since the issuance of the standard. The following documents collect the results of the preparatory work performed until the first quarter 2018:

(a) Background briefing paper on Level of aggregation;

(b) Background briefing paper on Release of the contractual service margin; and

(c) Background briefing paper on the Transition requirements of IFRS 17.

4 In addition, the EFRAG Secretariat consulted a number of European investor and analyst users of financial statements through telephone/webcast meetings and some in person between April and May 2018. 31 users were interviewed – 24 specialists and 7 generalists.

5 The EFRAG Secretariat has also performed a structured case study, comprising an extensive case study (involving 11 preparers) and a simplified case study (involving 49 preparers). The findings of these case studies were presented to EFRAG TEG in July 2018. The evidence gathered through this exercise covers several European countries and segments (life, non-life), and focused on certain portfolios only, as (reflecting the status of the implementation projects) preparers did not have yet the opportunity to test the impact on their business as a whole.

6 In September 2018, the near final draft economic report on IFRS 17, prepared by the external consultant firm (LE Europe and VVA Consulting) was presented to the EFRAG Board.

7 The preparatory work performed in 2018 resulted as well in the identification of 6 topics included in the letter sent by to the IASB as meriting further consideration. Starting from November 2018, the IASB started to discuss targeted amendments to IFRS 17, to respond to concerns and challenges raised by stakeholders as IFRS 17

is being implemented. The 6 issues identified by EFRAG were included in the topics of the IASB deliberations.

8 Starting from the commencement of the re-deliberation process, the public due process of EFRAG has been focused on the contents of the Amendments that have been exposed for comments in the ED/2019/4 *Amendments to IFRS 17*, issued by the IASB on 26 June 2019. The final comment letter was sent on the 24th September 2019.

9 The EFRAG Secretariat has continued perform preparatory work for the endorsement advice in this period, compatibly with the available resources. In July 2019, a questionnaire on Hedge Accounting for insurers has been issued, with closing period for the responses on the 16th September. The evidence gathered through this exercise is intended to contribute to the understanding of risk mitigation practices and to the impact assessment for the interactions of IFRS 9 and IFRS 17.

Key assumption to plan technical activities for the endorsement advice

10 At the date of this document, there are uncertainties with reference to some elements of the endorsement process, including the outcome of the IASB deliberation process following the consultation completed in September 2019. Accordingly, the working assumptions for a plan of activities developed at this stage are subject to change and the final activity plan may be significantly different from what could be discussed today.

11 The length of the endorsement process for a standard with the complexity of IFRS 17 is difficult to predict with precision. IFRS 9 was published by the IASB in July 2014 and endorsed in the EU in November 2016. The overall length of the process may be different from the IFRS 9 process and may be as well reduced. In addition, substantial activities have been already performed by EFRAG.

12 The assessment of implications of IFRS 17 on financial stability will benefit from the conclusions of relevant authorities, including the work produced by the EIOPA and of the taskforce on IFRS 17 established at the ESRB upon the request in the EP resolution.

13 Several working assumptions have to be made at this stage of the planning. The table at the end of this page summarises the preparatory activity by the EFRAG Secretariat for the next 8 months. The EFRAG project plan envisages to update the Board regularly in the coming months and to present more detailed planning as soon as feasible; accordingly each of this assumption, together with the resulting planning, will be monitored and updated when needed.

IASB process

(a) We understand that at this stage the Standard might be issued mid-2020 (the IASB will discuss the outcome of the consultation starting from October);

(b) We assume that there will be clarity on the outcome of the IASB deliberations and their impact on the contents of the final Standard by March 2020;

(c) We assume that the IASB will issue a separate due process document for the amendments to IFRS 4 *Insurance Contracts* relating to the optional deferral of IFRS 9.

Scope of work and timing of EFRAG activity

(d) The EFRAG Secretariat will focus until the end of 2019 on the results of the Hedge Accounting questionnaire, including interactions with IFRS 9;

(e) The EFRAG Secretariat will update the existing preparatory material that will contribute to populate the Appendices of the Endorsement Advice to reflect the outcome of the IASB deliberations once the deliberation outcome will be sufficiently clear;

(f) Selected outreach with preparers, questionnaires to members of the EFRAG IAWG and possible public surveys on specific issues may be envisaged, including to update specific information that may result outdated considering the impacts of the Amendments; however the EFRAG Secretariat will not repeat the case-study exercise. Similarly, specific updates of the economic study may be envisaged, if appropriate;

(g) We assume at this stage that there will be no new issues, nor new requests by relevant stakeholders, in addition to the topics in the letter by the EC and in the EP Motion.

Target timeline

(h) The endorsement activities for the separate document dealing with the deferral of IFRS 9 will have to follow a fast-track procedure in order for the deferral to be available for entities before 1 January 2021. The preparatory activities for the endorsement of the deferral of IFRS 9 will be performed having March 2020 as targeted date for discussion of the DEA at EFRAG TEG;

(i) Consistent with the recommendation included in the final comment letter issued on 24 September 2019, the plan will assume that the effective date will be 1 January 2023. In order to allow entities to be able to voluntarily early apply in January 2022, the endorsement process will have to be completed by the end of 2021;

(j) Assuming that the IFRS 17 final standard is issued no later than August 2020, the timing left to the end of 2021 to complete the whole process would a maximum of 16 Months. At this stage it is difficult to assess if a shorter process could be feasible.

Period	Preparatory activity by the EFRAG Secretariat
4Q19	Feedback on Hedge Accounting questionnaire
1Q20	Endorsement advice of deferral of IFRS 9 (Amendments to IFRS 4)
1H20	Update material for endorsement advice on IFRS 17

Questions for EFRAG Board members

14 Please provide your feedback on the assumptions above and other input useful to finalise the plan.

15 In particular:

(a) once the contents of the final standard will be sufficiently clear (e.g. March 2020), would you advise that EFRAG TEG and Board discuss and approve preparatory Chapters of the DEA in advance of the issuance of the final Standard?

(b) would you advise that the public consultation process on the DEA is limited in order to speed up the process? How long would you advise this consultation to be?

Appendix 1

Summary of the EC request for advice, January 2018

IMPACTS

- What will be the benefits brought by IFRS 17 accounting harmonisation compared to the existing situation?
- Will IFRS 17 deliver consistent and understandable reporting of financial reporting performance for insurance contracts within a group?
- How does IFRS 17 take into account the specificities of the insurance sector?
- Do different accounting methods reflect properly the different business models and is the delineation between these different methods such as the scope of the VFA clear?
- How does the pattern of release of the CSM for insurance contracts with direct participation features reflect the business models of the insurance sector?

FINANCIAL STABILITY

- Will IFRS 17 endanger financial stability?
- Improved transparency resulting from IFRS 17 is expected to contribute to long term financial stability, as insurers are important long-term investors. How IFRS 17 is expected to affect financial stability? Include sensitivity analyses and stress testing of the impact on financial statements.
- Will IFRS 17 hinder economic development?

COMPETITIVENESS/ MARKET

- Analysis of how IFRS 17 could affect competitiveness of European insurers taking into account the diversity in business models versus major competitors outside Europe.
- Impact of IFRS 17 on the range of insurance products available to policyholders, design and pricing of insurance products, including prospective impact on demand for various products. Make a distinction between life and non-life.
- Potential impact of IFRS 17, considering interactions with IFRS 9, on long term investment including investments held by insurance groups.

Comparison between the existing situation and IFRS 17 (cost/benefits)

COSTS

- Comparison of the estimated impact of the financial statements with the information provided under Solvency II to understand the size of the differences between IFRS 17 and Solvency II
- Separately identify one-off costs of implementing the standard, ongoing incremental costs of applying it, possible cost saving e.g. simplifications, synergies with existing It systems, potential ability to benefit from Solvency II, possible synergies for companies operating in multiple jurisdictions.
- Is the complexity justified in terms of costs of application?
- Is the complexity justified in particular as regards the subdivision of products into subgroups (onerous-non onerous and remaining) and annual cohorts?

- Is the level of aggregation striking the right balance between the usefulness of the information and the complexity and costs of its implementation?
- Is the complexity justified as regard the requirement to provide comparative numbers for the year preceding the application date of IFRS 17?

BENEFITS

- Improved quality of the financial information
- Increase of comparability with the EU insurance industry and globally
- Accounting level playing field for companies
- Increased understanding of the sector by capital providers
- Possible increased attractiveness of the sector to investors
- Possible positive effect on the cost of capital of insurers

Appendix 2

Summary of the Motion of the EP on endorsement advice of IFRS 17

- Notes the concerns of the European Banking Authority (EBA) that IFRS 17 allows for inconsistent accounting treatment for similar transactions, depending on the industry of the issuers. EFRAG, therefore, shall liaise closely with the EBA in order to assess whether these concerns are still valid in the context of the final requirements of IFRS 17 and whether transactions of a similar economic substance are handled consistently under IFRS 17 (paragraph 6 of the Motion).
- Notes the concerns of ESMA on presenting the effects of changes in the discount rate partly in 'other comprehensive income (OCI)' and partly in profit or loss, which could make financial statements too difficult to understand and thus impair the comparability of contracts with similar features. EFRAG, therefore, shall liaise closely with the ESMA and consider these concerns, if still relevant, when drawing up its endorsement advice, as part of the final requirements of IFRS 17 and to conclude whether IFRS 17 meets the endorsement criterion of understandability (paragraph 7 of the Motion).
- Notes the concerns of ESMA that IFRS 17 may fall short of providing sufficient clarity in the presentation of revenue, and that the determination of the discount rate and risk adjustment may hamper effective enforcement; calls on the EFRAG, therefore, to liaise closely with the ESMA and consider these concerns, if still relevant, when drawing up its endorsement advice, as part of the final requirements of IFRS 17 (paragraph 7 of the Motion).
- Notes the EBA's concerns on IFRS 17 permitting an insurance entity to determine a discount rate using either a top-down or a bottom-up approach. EFRAG, therefore, shall liaise closely with the EBA, and consider these concerns, if still relevant, when drawing up its endorsement advice, as part of the final requirements of IFRS 17, notably whether this option might significantly increase the scope for judgement and inconsistency in application potentially leading to reduced comparability of financial information and subjective earnings' management (paragraph 7 of the Motion).
- In the wake of IFRS 17 and IFRS 9, two major changes in financial reporting standards are affecting accounting for insurance undertakings. Changes in valuation now occur on both the assets and the liabilities side of insurers' balance sheets, as investment assets are marked-to-market and the valuations of insurance contracts include forward-looking net cash flow estimates; calls on the EFRAG to assess the potential interaction and any mismatches between IFRS 9 and IFRS 17 (paragraph 9 of the Motion).
- Notes that exemptions to IFRS 17 and IFRS 9 allow for the application of IFRS 15 to relevant contracts; calls on the EFRAG to assess whether this treatment is appropriate (paragraph 10 of the Motion).
- Consider concerns relating to the level of aggregation, including requirements on how the business is run in practice and on grouping contracts into annual cohorts, which may give an unclear reflection of business management (paragraph 11 of the Motion).
- Clarification on certain potential negative implications of the transitional requirements, particularly in terms of the complexity of the retrospective approaches and the limited availability of data in this regard; consider the potential consequences on comparability and data issues of the need to apply multiple transition approaches for one portfolio of insurance contracts (paragraph 13 of the Motion).

- Consider the impact of IFRS 17 requirements on accounting for reinsurance, by taking into account both the interests of the beneficiaries and the business models of reinsurance providers (paragraph 15 of the Motion).
- Notes that the true scale and complexity of IFRS 17 will only become clear once the EFRAG has completed its impact assessment; calls on the Commission and the EFRAG to examine, subject to the results of this assessment, the achievability of the current implementation timeline of IFRS 17, and to consider potential interaction with implementation dates in other jurisdictions (paragraph 17 of the Motion).
- Check that all the core features of the insurance covers are reflected in a way that does not distort the social guarantees offered (paragraph 5 of the Motion).
- Consider the recommendations regarding the impact of new standards on financial stability and long-term investment in the EU, but also the risks entailed by the propensity of accounting provisions to cause pro-cyclical effects and/or higher volatility, particularly as IFRS 17 will shift the focus from historical cost to current values. Recalls the Maystadt recommendations on the expansion of the ‘public good’ criterion, namely that accounting standards should neither jeopardise the EU’s financial stability nor hinder its economic development (paragraph 8 of the Motion).
- Effects on financial stability, competitiveness, and insurance markets, for insurance SMEs in particular, and the need for a cost-benefit analysis (paragraph 5 of the Motion).
- Understand the interaction between IFRS 17, which employs a principles-based approach, and other regulatory requirements for insurance entities in the EU, in particular Solvency II, especially in relation to the cost of implementing IFRS 17 (paragraph 6 of the Motion).
- Cost of IFRS 17 and whether it will hinder understanding of the financial impact of general insurance contracts. Consider concerns relating to the presentation of general insurance contracts, including the risk of reduced quality of disclosure, undue increases in the expected cost of implementation and significant increases in the operational complexity of reporting under IFRS 17 (paragraph 3 of the Motion).
- Consider concerns relating to the level of aggregation insofar as the disaggregation of a portfolio on profitability criteria and annual cohorts may not reflect how the business is run, while possibly increasing costs, complexity and administrative burden for companies (paragraph 12 of the Motion).
- Effects on financial stability, competitiveness, and insurance markets, for insurance SMEs in particular, and the need for a cost-benefit analysis (paragraph 5 of the Motion).
- Consider the potential benefits for all stakeholders (paragraph 14 of the Motion).