European Financial Reporting Advisory Group

Risk & Finance/WG Financial Reporting & Accounting/2021-010

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:

Assuralia

(b) Are you a:

☐ Preparer ☐ User ☐ Other (please specify)

Industry federation

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

Lobbyist

(d) Country where you are located:

Belgium

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

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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 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)

[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.

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.

Agree with the overall assessment but comment that the while **remaining issues** (other than annual cohorts) would not prohibit endorsement it is very regrettable that they were not addressed as they will impact the accuracy and usefulness of IFRS 17. **These issues should be included in the post implementation review (PIR).**

The remaining issues that should be included in the post implementation review (PIR) of IFRS 17, by order of priority, are the following:

- **Presentational issue : Cash basis for the measurement of the liabilities -** Under IFRS 17, the insurance contract liabilities or assets are measured on a cash basis and therefore include all receivables and payables to counterparties and expenses modelled in the future cash flows, until they are actually paid. Most insurance entities account for premium receivables and claim payables separately on an accrual basis. Therefore, those entities have to implement new systems or to modify their existing systems for IFRS 17 (while local accounts will remain on an accrual basis) to include premiums and claims on a cash basis in the measurement of their groups of contracts.

Operational challenges and technical issues associated with the implementation of the cash basis approach concern actuarial accounting and cash management systems and would result in unreasonable additional costs compared to a very limited benefit, if any. In this situation, insurers are inclined to use arbitrary allocations and other simplifications, that would not improve the quality of the financial information produced. We continue to believe that IFRS 17 would need to be improved to require the separate presentation of premium receivables and claim payables and their inclusion on an accrual basis in the measurement of the related groups of insurance contracts. It would increase the usefulness of information provided to users while significantly reducing the cost for entities.

- **Business Combinations** : **Insurance contract in settlement phase acquired in a business combination/transfer –** IFRS 17 requires an entity to classify a liability for settlement of claims as a liability for remaining coverage if the entity acquired the insurance contract during the claim settlement period and, at the acquisition date, the amount of claims is still uncertain. The requirement applies to contracts acquired both in a business combination within the scope of IFRS 3 and in a transfer of insurance contracts that do not form a business (for example, in a portfolio transfer). This implies that the liabilities for incurred claims (LIC) previously generated in the acquiree's statement of financial position become liabilities for remaining coverage (LRC) in the acquirer's accounts, with the consideration received on the business combination / transfer used as a proxy for the premiums received.

By consequence, the whole amount of consideration received is to be released in the insurance revenue over the coverage period, via the release of the present value of fulfilment cash flows (PVFCF) and of the CSM. This is consistent with the general measurement requirements of IFRS 17 for new contracts issued by the entity, however, it results in an artificial increase of insurance revenues during the coverage period.

In fact, economically, this approach appears contrary to §B5 of IFRS 17 which stays that for insurance contracts covering events that have already occurred but the financial effect of which is still uncertain, "the insured event is the determination of the ultimate cost of those claims." So, in the case of a business combination / transfer, the insurance risk should correspond to the risk of deviation of the actual ultimate cost of claims from the expected one. As such, the insurance revenue should only reflect the risk of deviation, that is not the case under the IFRS 17 requirements. In order to compensate for the misrepresentation effect of such a treatment and to provide relevant financial information to stakeholders, additional non-GAAP disclosures on adjusted insurance revenue will have to be produced in the financial statements.

From the operational point of view, transforming liabilities for claims settlement acquired into liabilities for remaining coverage may require significant additional cost and efforts as it implies developing calculation and accounting models proper to the General Measurement Model for the portfolios that otherwise should have been treated using a simplified method.

We therefore believe that IFRS 17 should be modified in a manner that the insurance revenues of all contracts acquired in their settlement period reflect only the risk of deviation of the actual ultimate cost of claims from the expected one.

Presentational issue – 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.

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.

Scope of hedging adjustment – 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 the date of initial application.

Discount rates – There are a number of issues arising in the use of discount rates:

- the use of a locked in discount rate for the CSM in general model;

- 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.

- there is uncertainty regarding whether changes in asset mix will result in changes to the discount rate using a top down approach.

(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

The requirements to apply annual cohorts to intergenerationally-mutualised contracts (within the context of paragraphs B67-B71 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 and are not contrary to the true and fair view principle.

(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

The application of annual cohorts to cash-flow matched contracts is not a relevant question for the Belgian insurance sector since those techniques are not applied in Belgium.

(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?

IFRS 17 as published by the IASB in June 2020 is not perfect and some reported issues remained unaddressed, however **given:**

a) The need for replacing IFRS 4 and to go ahead with IFRS 9 implementation;

b) The significant resources spent by the industry on implementation;

c) The fact that some helpful improvements were made

IF other reported issues are put forward for including in the PIR, **then** the requirements for endorsement can be considered to be met.

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.

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

The issue related to the requirement to apply annual cohorts to such contracts could have been tackled by the IASB during IFRS 17's amendment process. After a long period of uncertainties regarding the requirements and application date of IFRS 17, insurance companies are now relying on the official version of the standard as issued by the IASB. **New modifications to the standard before the official application date would disrupt the implementation processes and would be costly**. Belgian insurers are **asking for a stable standard that will not be amended anymore**.

The **Belgian insurance sector does not support any carving-out initiative which would make the application of IFRS standards in the EU different from elsewhere and which would intrude on comparability.** Even an optional temporary difference between IFRS standards as endorsed in EU and IFRS standards as applied in the rest of the world risks being complex for large international groups and confusing for users of financial information. Such differences would go against the main objectives of International Financial Reporting Standards which is bringing comparability amongst financial statements.

(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

The application of annual cohorts to cash-flow matched contracts is not a relevant question for the Belgian insurance sector since those techniques are not applied in Belgium.

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.

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.

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.

(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.

(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.

[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.

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

EFRAG's analysis on SME insurers affected by IFRS 17 is highly misleading. The EFRAG analysis fails to cover all insurers impacted by IFRS 17 and does only focuses on extremely "small" insurers using EIOPA's definition in its Draft Endorsement advice work. We note that the definition EFRAG used for small insurers is the one used in SII for insurers that are so small that they are exempted from Solvency II requirements. We also **note that for those small and medium size insurers for whom SII does apply – there are a range of exemptions and proportionality principles which are intended to allow 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**.

We are convinced that when the European Parliament and the European Commission asked to identify the effect of the standard on 'small insurers', the intention was to go beyond the listed insurers covered by the IASB, and account for all the other European insurers who are impacted by IFRS 17.

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.

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.

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.

(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.

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.

(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.

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.

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.

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.

Belgian insurers welcome the IASB decision to delay the official implementation date of IFRS 17 to 1 January 2023 but like to emphasize that **any additional delay is not desirable.** Several companies have already started the long implementation process of the amended standard. Additional modifications at the European level are not supported as these would risk disrupting this process while increasing the already high **implementation costs.**

(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.

Some **Belgian insurance companies would like to benefit from the early adoption option** by implementing the standard as per **1 January 2022**. Therefore, it is **crucial that the endorsement process of the standard as amended by the IASB in the European Union is done in due time without any additional delay or modifications**.

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.

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.

(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.

(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).

(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.

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

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?

(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.

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

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?

The Belgian insurance industry appreciates the efforts by the IASB and the EFRAG in considering the concerns raised by the insurance industry about IFRS 17 'Insurance Contracts', which resulted in the amendments published by the IASB in June 2020.

While there **remain some issues that could have been solved by the IASB** before the official implementation date of IFRS 17, the Belgian market welcomes the proposed amendments and is **satisfied with the current version of the amended standard**.

The version of **IFRS 17** as published by the IASB in June 2020 is **acceptable** but is **not yet perfect.** Issues that, in our view, **merit further consideration** by the IASB during **post-implementation reviews,** by order of priority**,** are the following:

- **Presentational issue : Cash basis for the measurement of the liabilities -** Under IFRS 17, the insurance contract liabilities or assets are measured on a cash basis and therefore include all receivables and payables to counterparties and expenses modelled in the future cash flows, until they are actually paid. Most insurance entities account for premium receivables and claim payables separately on an accrual basis. Therefore, those entities have to implement new systems or to modify their existing systems for IFRS 17 (while local accounts will remain on an accrual basis) to include premiums and claims on a cash basis in the measurement of their groups of contracts.

Operational challenges and technical issues associated with the implementation of the cash basis approach concern actuarial accounting and cash management systems and would result in unreasonable additional costs compared to a very limited benefit, if any. In this situation, insurers are inclined to use arbitrary allocations and other simplifications, that would not improve the quality of the financial information produced. We continue to believe that IFRS 17 would need to be improved to require the separate presentation of premium receivables and claim payables and their inclusion on an accrual basis in the measurement of the related groups of insurance contracts. It would increase the usefulness of information provided to users while significantly reducing the cost for entities.

- **Business Combinations** : **Insurance contract in settlement phase acquired in a business combination/transfer** – IFRS 17 requires an entity to classify a liability for settlement of claims as a liability for remaining coverage if the entity acquired the insurance contract during the claim settlement period and, at the acquisition date, the amount of claims is still uncertain. The requirement applies to contracts acquired both in a business combination within the scope of IFRS 3 and in a transfer of insurance contracts that do not form a business (for example, in a portfolio transfer). This implies that the liabilities for incurred claims (LIC) previously generated in the acquiree's statement of financial position become liabilities for remaining coverage (LRC) in the acquirer's accounts, with the consideration received on the business combination / transfer used as a proxy for the premiums received.

By consequence, the whole amount of consideration received is to be released in the insurance revenue over the coverage period, via the release of the present value of fulfilment cash flows (PVFCF) and of the CSM. This is consistent with the general measurement requirements of IFRS 17 for new contracts issued by the entity, however, it results in an artificial increase of insurance revenues during the coverage period.

In fact, economically, this approach appears contrary to §B5 of IFRS 17 which stays that for insurance contracts covering events that have already occurred but the financial effect of which is still uncertain, "the insured event is the determination of the ultimate cost of those claims." So, in the case of a business combination / transfer, the insurance risk should correspond to the risk of deviation of the actual ultimate cost of claims from the expected one. As such, the insurance revenue should only reflect the risk of deviation, that is not the case under the IFRS 17 requirements. In order to compensate for the misrepresentation effect of such a treatment and to provide relevant financial information to stakeholders, additional non-GAAP disclosures on adjusted insurance revenue will have to be produced in the financial statements.

From the operational point of view, transforming liabilities for claims settlement acquired into liabilities for remaining coverage may require significant additional cost and efforts as it implies developing calculation and accounting models proper to the General Measurement Model for the portfolios that otherwise should have been treated using a simplified method.

We therefore believe that IFRS 17 should be modified in a manner that the insurance revenues of all contracts acquired in their settlement period reflect only the risk of deviation of the actual ultimate cost of claims from the expected one.

Presentational issue – 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.

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.

Scope of hedging adjustment – 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 the date of initial application.

Discount rates – There are a number of issues arising in the use of discount rates:

- the use of a locked in discount rate for the CSM in general model;

- 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.

- there is uncertainty regarding whether changes in asset mix will result in changes to the discount rate using a top down approach.

Belgian insurers welcome the IASB decision to delay the official implementation date of IFRS 17 to 1 January 2023 but like to emphasize that **any additional delay is not desirable.** Several companies have already started the long implementation process of the amended standard. Additional modifications at the European level are not supported as these would risk disrupting this process while increasing the already high **implementation costs**.

Some **Belgian insurance companies would like to benefit from the early adoption option** by implementing the standard as per **1 January 2022**. Therefore, it is **crucial that the endorsement process of the standard as amended by the IASB in the European Union is done in due time without any additional delay or modifications**.

While the sector acknowledges that the requirement to manage insurance contracts on an annual cohort basis might constitute an issue for certain type of contracts, Belgian companies believe that, 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**.

Belgian insurance companies **do not support the (partial) non-endorsement of the requirement in IFRS 17 to apply annual cohorts to some specific insurance contracts** (i.e. intergenerationally mutualised and cash-flow matched contracts).