February 23, 2016
Mr. Hans Hoogervorst, Chairman
International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

Dear Hans

AOSSG comments on IASB Exposure Draft ED/2015/11 *Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts*

The Asian-Oceanian Standard-Setters Group (AOSSG) would like to express its views on the interaction between the application of IFRS 9 Financial Instruments and the forthcoming insurance standard, and the approach to address concerns expressed thereto. The purpose of this letter is to provide AOSSG members' comments on the proposed amendments to IFRS 4 as outlined in the Exposure Draft ED/2015/11.

The AOSSG currently has 26 member standard-setters from the Asian-Oceanian region: Australia, Brunei, Cambodia, China, Dubai, Hong Kong, India, Indonesia, Iraq, Japan, Kazakhstan, Korea, Macao, Malaysia, Mongolia, Nepal, New Zealand, Pakistan, Philippines, Saudi Arabia, Singapore, Sri Lanka, Syria, Thailand, Uzbekistan and Vietnam.

To the extent feasible, this submission to the IASB reflects in broad terms the collective views of AOSSG members. Please note that the level of concerns from each AOSSG member jurisdiction varies, which reflects the extent of IFRS applied in our region. The attached appendix provides responses to each of the six questions in the ED.

AOSSG highly appreciates the IASB's ongoing significant efforts in proposing the overlay approach and the temporary exemption to address the accounting mismatch arising from different effective dates of IFRS 4 Phase II and IFRS 9. AOSSG endeavours to delineate the rationale behind each member's concern, including eligibility of the temporary exemption and pre-determined expiry date on the temporary exemption. AOSSG hopes that AOSSG's feedbacks are taken into account to reach a constructive solution. If you have any questions, please contact me.

Yours sincerely,

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Question 1—Addressing the concerns raised

Paragraphs BC9–BC21 describe the following concerns raised by some interested parties about the different effective dates of IFRS 9 and the new insurance contracts Standard:

(a) Users of financial statements may find it difficult to understand the additional accounting mismatches and temporary volatility that could arise in profit or loss if IFRS 9 is applied before the new insurance contracts Standard (paragraphs BC10–.BC16).

(b) Some entities that issue contracts within the scope of IFRS 4 have expressed concerns about having to apply the classification and measurement requirements in IFRS 9 before the effects of the new insurance contracts Standard can be fully evaluated (paragraph BC17–.BC18).

(c) Two sets of major accounting changes in a short period of time could result in significant cost and effort for both preparers and users of financial statements (paragraphs BC19–.BC21).

The proposals in this Exposure Draft are designed to address these concerns.

Do you agree that the IASB should seek to address these concerns? Why or why not?

1. The AOSSG members agree that the IASB should seek to address the concerns arising from the different effective dates of IFRS 9 and the forthcoming insurance standard.

Question 2 - Proposing both an overlay approach and a temporary exemption from applying IFRS 9

The IASB proposes to address the concerns described in paragraphs BC9–BC21 by amending IFRS 4:

(a) to permit entities that issue contracts within the scope of IFRS 4 to reclassify from profit or loss to other comprehensive income some of the income or expenses arising from designated financial assets that:

(i) are measured at fair value through profit or loss in their entirety applying IFRS 9 but

(ii) would not have been so measured applying IAS 39 (the 'overlay approach') (see paragraphs BC24–C25);

(b) to provide an optional temporary exemption from applying IFRS 9 for entities whose predominant activity is issuing contracts within the scope of IFRS 4 (the 'temporary exemption from applying IFRS 9') (see paragraphs BC26–C31).

Do you agree that there should be both an overlay approach and a temporary exemption from applying IFRS 9? Why or why not?

If you consider that only one of the proposed amendments is needed, please explain which and why.

2. Most AOSSG members agree that there should be both an overlay approach and a temporary exemption from applying IFRS 9 since the scope of the temporary exemption from applying IFRS 9 is restricted to an entity whose predominant activity is issuing contracts within IFRS 4.
3. However, they indicate that implementing the overlay approach would require insurers to operate the two systems in parallel, which would result in significant incremental operational efforts and costs. Some of those members mention that their constituents were particularly in favor of the deferral approach over the overlay approach.
4. Meanwhile, an AOSSG member expresses its view that it is deemed unnecessary for the IASB to propose both the overlay approach and the temporary exemption since the overlay approach will enhance the quality of 'profit or loss' information while addressing the accounting mismatch from the misalignment of the effective dates of IFRS 9 and the forthcoming insurance standard.
5. Also, the AOSSG member considers that the temporary exemption from applying IFRS 9 would result in undesirable consequences as follows:
   (a) The temporary exemption would significantly reduce the comparability of financial statements between entities that issue contracts within the scope of IFRS 4 and non-insurance financial institutions since entities that issue insurance contracts ordinarily hold a large volume of financial assets as a part of their investment portfolio.
   (b) The pre-determined expiry date of the temporary exemption might hinder the IASB's careful consideration that should be given to finalizing the process of the new insurance standard due to time constraints.

Question 3 - The overlay approach

Paragraphs 35A–5F and BC32–C53 describe the proposed overlay approach.

(a) Paragraphs 35B and BC35–C43 describe the assets to which the overlay approach can be applied. Do you agree that the assets described (and only those assets) should be eligible for the overlay approach? Why or why not? If not, what do you propose instead and why?

(b) Paragraphs 35C and BC48–C50 discuss presentation of amounts reclassified from profit or loss to other comprehensive income applying the overlay approach. Do you agree with the proposed approach to presentation? Why or why not? If not, what do you propose instead and why?

(c) Do you have any further comments on the overlay approach?

6. Most AOSSG members support the IASB's proposal regarding the financial assets to which the overlay approach can be applied since the IASB's proposal gives the entity discretion to designate financial assets as relating to contracts within the scope of IFRS 4.

7. In addition, an AOSSG member suggests two recommendations regarding the eligibility of financial assets for the overlay approach as follows:

   (a) Refining the eligibility requirements for the determination of qualified financial assets designated as relating to contracts that are within the scope of IFRS 4. A financial asset does not usually have a one to one relationship with an insurance contract, so the value of the asset may not be exactly equal to the insurance liability. Therefore, there may be an opportunity for entities applying the overlay approach to deliberately inflate the value of an asset that is associated with the insurance contract.

   (b) Adding substantiation requirements for financial assets transferred between insurance and non-insurance business segments so that it is challenging for entities to change the designation of their financial assets to achieve a favourable accounting outcome.

8. Most AOSSG members agree with the IASB's proposal that the amount reclassified from profit or loss to other comprehensive income shall be either presented on the face of statement of profit or loss or disclosed in the notes to the financial statements.

9. However, an AOSSG member expresses its concern regarding the unrestricted options in presentation since those options would cause a lack of comparability.

10. Lastly, some AOSSG members point out the operation burden in implementing the overlay approach. They believe that in applying the overlay approach, both IFRS 9 and IAS 39 would need to be run in parallel for the assets to which the overlay approach is applied. And, the overlay adjustment would imply maintaining IAS 39 information to determine the overlay adjustment for those very specific assets within the scope of the overlay approach, which would result in significant costs.

Question 4-The temporary exemption from applying IFRS 9

As described in paragraphs 20A and BC58–.BC60 the Exposure Draft proposes that only entities whose predominant activity is issuing contracts within the scope of IFRS 4 can qualify for the temporary exemption from applying IFRS 9.

(a) Do you agree that eligibility for the temporary exemption from applying IFRS 9 should be based on whether the entity's predominant activity is issuing contracts within the scope of IFRS 4? Why or why not? If not, what do you propose instead and why?

As described in paragraphs 20C and BC62–C66, the Exposure Draft proposes that an entity would determine whether its predominant activity is issuing contracts within the scope of IFRS 4 by comparing the carrying amount of its liabilities arising from contracts within the scope of IFRS 4 with the total carrying amount of its liabilities (including liabilities arising from contracts within the scope of IFRS 4).

(b) Do you agree that an entity should assess its predominant activity in this way? Why or why not? If you believe predominance should be assessed differently, please describe the approach you would propose and why.

Paragraphs BC55–C57 explain the IASB's proposal that an entity would assess the predominant activity of the reporting entity as a whole (ie assessment at the reporting entity level).

(c) Do you agree with the proposal that an entity would assess its predominant activity at the reporting entity level? Why or why not? If not, what do you propose instead and why?

11. Most AOSSG members support in principle the temporary exemption from applying IFRS 9.

12. However, most AOSSG members express their concerns regarding the IASB's proposal in paragraphs 20C and BC62-BC66 of the exposure draft in relation to the entity's predominance test. Especially, presenting a single quantitative threshold in the Basis of Conclusions could inadvertently scope out entities that are primarily engaged in insurance activities, which could lead to a counterintuitive result. Thus, most AOSSG members suggest that the IASB should consider more principle-based eligibility criteria for the temporary exemption that includes quantitative as well as qualitative conditions.

13. In relation to the level at which an entity should assess the predominant activity:

    (a) The AOSSG Islamic Finance Working Group supports the proposal that the predominance assessment should be made at the reporting entity level rather than below the reporting entity level since financial statements of Islamic insurers (takaful companies) are comprised of three different funds. If the predominant activity is assessed at each fund level, this would result in mixed accounting treatments in a single set of financial statements. So they urge the IASB to clarify that in such circumstances the assessment of predominant activity should be at the 'consolidated' takaful company level as a whole and not at the fund level.

    (b) Some of AOSSG member reported that some of their constituents are concerned about setting the predominance test at the reporting entity level will not provide a level playing field to insurance subsidiaries and/or equity-accounted investees that are held by banking entities. That is, an insurance subsidiary or equity-accounted investee held by a banking entity would have to prepare two sets of financial statements; one for its financial statements and the other for its parent or investor consolidated financial statements which increases implementation costs and efforts.

    (c) An AOSSG member disagrees with the proposal that an entity would assess its predominant activity at the reporting entity level. It suggests that an entity should assess its predominant activity at the reporting entity level at first. If it is not eligible, an entity should then assess its predominant activity below the reporting entity level. No matter entities take a temporary exemption at the reporting entity level or below the reporting entity level, they do not have to make adjustment at the consolidated level for uniform accounting policies. This will reduce the cost for preparers of financial statements, and avoid the entities from giving up to choose a temporary exemption because of the huge adjustment work and the different accounting policies both between the parent and its subsidiaries, and between the investors and its associates or joint ventures. Although this will lead to different accounting policies in the consolidated financial statements, the member thinks that this is just a temporary expediency. Entities should make explanation in the notes to the financial statements.

The member mentions that the IASB concerns about the transfers of financial instruments between parts of a reporting entity that would qualify for the temporary exemption and parts of the reporting entity that would not qualify. In order to seek a balance between preventing earnings management and maintaining economic behaviours, the member suggests that the best solution is to only admit the financial instruments to transfer from applying IAS 39 to IFRS 9. That means, if a financial instrument is transferred from a reporting entity that would not qualify for the temporary exemption to a reporting entity that would qualify for the temporary exemption, this financial instrument will still apply IFRS 9.

Question 5-Should the overlay approach and the temporary exemption from applying IFRS 9 be optional?

As explained in paragraphs BC78–BC81, the Exposure Draft proposes that both the overlay approach and the temporary exemption from applying IFRS 9 would be optional for entities that qualify. Consistently with this approach, paragraphs BC45 and BC76 explain that an entity would be permitted to stop applying those approaches before the new insurance contracts Standard is applied.

(a) Do you agree with the proposal that the overlay approach and the temporary exemption from applying IFRS 9 should be optional? Why or why not?

(b) Do you agree with the proposal to allow entities to stop applying the overlay approach or the temporary exemption from applying IFRS 9 from the beginning of any annual reporting period before the new insurance contracts Standards is applied? Why or why not?

14. All AOSSG members are of the view that the overlay approach and temporary exemption from applying IFRS 9 should be optional.

15. Most AOSSG members agree with the IASB's proposal to allow an entity stop applying the overlay approach or the temporary exemption before the new insurance contracts. However, an AOSSG member is concerned that the IASB's proposal would cause the period-to-period comparability of financial statements of an entity to deteriorate by giving choice to an entity for determining when to stop the options.

Question 6-Expiry date for the temporary exemption from applying IFRS 9

Paragraphs 20A and BC77 propose that the temporary exemption from applying IFRS 9 should expire at the start of annual reporting periods beginning on or after 1 January 2021.

Do you agree that the temporary exemption should have an expiry date? Why or why not?

Do you agree with the proposed expiry date of annual reporting periods beginning on or after 1 January 2021? If not, what expiry date would you propose and why?

16. All AOSSG members disagree with the pre-determined expiry date on the temporary exemption from applying IFRS 9. The AOSSG members suggest that IASB should set the expiry date only after the IASB finalises the new insurance contract Standard.

Other Comments

17. One AOSSG member disagrees with the IASB's proposal for first-time adopters of IFRS. Under IFRS 1 *First-time Adoption of IFRS,* the transitions for insurance contracts and financial instruments already emphasised not disadvantaging first-time adopters over achieving comparability. Moreover, paragraph BC82(b) of the ED appears unrealistic because of the short period between the completion of technical deliberations on the new insurance contract Standard and the mandatory effective date of IFRS 9. IFRS should maintain a level playing field across capital markets as long as the IASB recognises that jurisdictions adopt IFRS at different points in time.