1 October 2019

Hans Hoogervorst
Chair
International Accounting Standards Board
7 Westferry Circus
Canary Wharf
London, E14 4HD
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Dear Hans

AOSSG comments on IASB Exposure Draft Amendments to IFRS 17

The Asian-Oceanian Standard-Setters Group (AOSSG) would like to express its views on the proposed amendments to IFRS 17.

The AOSSG currently has 27 member standard-setters from the Asian-Oceanian region: Australia, Bangladesh, 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 ten questions in the ED.

AOSSG highly appreciates the IASB's significant efforts in proposing the amendment to IFRS. AOSSG hopes that AOSSG's feedbacks are taken into account to reach a constructive solution.

If you have any questions regarding this submission, please contact either one of us.

Yours sincerely,

Yibin Gao
Chair of the AOSSG

Eui-Hyung Kim
Leader of the AOSSG Insurance Working Group

General Comments from the AOSSG members

Given the 10 questions, members generally supported the IASB’s amendments. However, there have been comments on several issues that require further amendments and clarification of the Board's intentions. We have summarized these issues below that we have not been able to resolve through the proposal in the Exposure Draft:

- The Exposure Draft is silent on the determination of the amount of pre-coverage asset on transition to IFRS 17. We suggest that Appendix C be amended to include explicit allowance for the recognition of the asset proposed in paragraph 28B(b) as part of the modified retrospective and fair value transition approaches.
  We also recommend some changes to the proposed wordings regarding recognition of insurance acquisition cash flows. The wording adopted by the IASB has potential unintended consequences for entities that underwrite new business with an expectation that there will be renewals but do not recover acquisition costs through future expected renewals from a commercial perspective. [Question 2]

- We believe that the recognition of contractual service margin attributable to investment-return service and investment-related service needs to be clarified for preparers. As such, the IASB’s intent can be delivered better. We also believe that the assessment of relative weighting of benefits may pose operational challenges. Hence, we suggest that for a group of contracts that contain both insurance and investment services, where a weighted measure of the services cannot be determined reliably and practicably, the entity should be allowed to allocate the contractual service margin in a practical and consistent manner, for example using the passage of time basis.[Question 3]

- The proposed change to reduce the accounting mismatch between reinsurance contracts held and recognition of underlying onerous contracts is insufficiently wide in scope to deal with the variety of reinsurance contracts that are used in practice. Changes to the proposed wording of IFRS 17 are required to widen the scope of this change. We have set out an alternative approach which would provide a principles-based approach and apply consistency across different types of reinsurance contracts held and which does not require further arbitrary assumptions to be introduced. [Question 4]

- We believe that the risk mitigation option should be extended to the insurance contracts under general model, rather than being restricted to the insurance contracts with direct participation features. In the case where the entity hedges financial risks with derivatives for the insurance contracts under general model, accounting mismatches occur in the income statements, as the effects of changes in the fair values of derivatives are recognised in profit or loss while the changes in the insurance contracts caused by the financial risk are reflected in OCI. This does not show the results of entities' hedging management and will cause volatility in profit or loss. The IASB recommended the entities having the insurance contracts under general model to apply the hedge accounting under IFRS 9, but the entities note that they cannot use the hedge accounting due to the strict criteria of IFRS 9. [Question 6]

- We believe that the treatment of acquired contracts under IFRS 17 (whether through a business combination under IFRS 3 or through an acquisition of insurance contracts) results in an overly complex accounting approach for acquired insurance contracts which, in many transactions, will not reflect the business model of the entity and will potentially confuse users. We recommend adopting a similar approach to that summarised in IFRS 3.15: "*The acquirer shall make those classifications or designations on the basis of the contractual terms, economic conditions, its operating or accounting policies and other pertinent conditions as they exist at the acquisition date.*" This will allow recognition of the insurers' business model when accounting for acquired insurance contracts and aligns more closely to the approach adopted for IFRS 9: Financial Instruments. [Question 8]

- We remain concerned with the override of IAS 34 which is included in IFRS 17.B137. Whilst we understand this was included to assist some preparers it has a significant impact on other preparers, requiring dual reporting by subsidiaries within a consolidated Group which have a different reporting cadence to the Group parent. As such we consider IFRS 17.B137 should be optional.

Specific Comments on the Questions

Question 1—Scope exclusions—credit card contracts and loan contracts that meet the definition of an insurance contract (paragraphs 7(h), 8A, Appendix D and BC9–BC30)

(a) Paragraph 7(h) proposes that an entity would be required to exclude from the scope of IFRS 17 credit card contracts that meet the definition of an insurance contract if, and only if, the entity does not reflect an assessment of the insurance risk associated with an individual customer in setting the price of the contract with that customer.

Do you agree with the proposed amendment? Why or why not?

(b) If not excluded from the scope of IFRS 17 by paragraphs 7(a)–(h), paragraph 8A proposes that an entity would choose to apply IFRS 17 or IFRS 9 to contracts that meet the definition of an insurance contract but limit the compensation for insured events to the amount required to settle the policyholder's obligation created by the contract (for example, loans with death waivers). The entity would be required to make that choice for each portfolio of insurance contracts, and the choice for each portfolio would be irrevocable.

Do you agree with the proposed amendment? Why or why not?

(Comments)

All the members agreed with the proposed amendments. One member commented that keeping the insurance aspects of these contracts within the scope of IFRS 17 could create substantial costs for the effected entities for little or no benefit to users.

Question 2—Expected recovery of insurance acquisition cash flows (paragraphs 28A– 28D, 105A–105C, B35A–B35C and BC31–BC49)

Paragraphs 28A−28D and B35A−B35C propose that an entity: (a) allocate, on a systematic and rational basis, insurance acquisition cash flows that are directly attributable to a group of insurance contracts to that group and to any groups that include contracts that are expected to arise from renewals of the contracts in that group; (b) recognise as an asset insurance acquisition cash flows paid before the group of insurance contracts to which they are allocated is recognised; and (c) assess the recoverability of an asset for insurance acquisition cash flows if facts and circumstances indicate the asset may be impaired. Paragraphs 105A−105C propose disclosures about such assets. Do you agree with the proposed amendments? Why or why not?

(Comments)

Most of the members agreed that the proposed amendments will provide more useful information to users of the financial statements in the situations described where insurance acquisition costs are recovered by the entity through future expected contract renewals. However we have highlighted four items the IASB should consider further. We also have one member who is concerned about the proposed amendments.

1. Unintended consequences of paragraph B35A

Based on the Basis for Conclusions it appears the intention of the change is to require acquisition costs to be amortised over the period expected to recover the costs. The wording adopted by the IASB has potential unintended consequences for entities that underwrite new business with an expectation that there will be renewals but do not recover acquisition costs through future expected renewals from a commercial perspective (for example, many general insurance contracts).

The existence, or not, of renewals may have no bearing on the commission structure and other acquisition costs incurred (including internal cost allocations) but the wording in the proposed IFRS 17.B35A includes the very broad term “expected to arise from renewal of the insurance contracts”, which has the potential to capture a much wider scope of costs beyond those contemplated by the IASB as evidenced in the Basis for Conclusions. The Basis for Conclusions to ED/2019/4 notes at paragraph BC39 (emphasis added):

*… The Board was persuaded that the payment of the commissions creates an asset that may **be expected to be recovered through expected renewals of contracts**. The resulting information would also be comparable to the information provided by IFRS 15 for the incremental costs of obtaining a contract.*

The term "expected to be recovered through expected renewals" is not currently used in the proposed IFRS 17 requirements but is significant to achieve the intended outcome.

2. Determination of asset on transition to IFRS 17

The Exposure Draft is silent on the determination of the amount of asset on transition to IFRS 17. Paragraph 28B(b) proposes the recognition of an asset in respect of future groups of insurance contracts to which insurance acquisition cash flows are allocated. In order to calculate the value of this asset upon transition to IFRS 17, historical information relating to the insurance contracts will be required. Feedback from one member's jurisdiction noted that this information may be difficult to obtain without significant cost or effort because it relates to contracts originally issued and lapsed many years ago and includes:

- Historic insurance acquisition costs relating to contracts previously originated.
- Expected lapse and renewal profile of contracts issued many years prior to transition to IFRS 17, and their subsequent actual experience.

One member suggested that Appendix C be amended to include explicit allowance for the recognition of the asset proposed in paragraph 28B(b) as part of the modified retrospective and fair value transition approaches. Explicit allowance for 28B(b) under the modified retrospective and fair value approaches will provide entities an alternative where it is impracticable to apply a full retrospective approach.

The member suggested the following amendments and insertions to Appendix C:

C7 Paragraphs C9-C19 set out the permitted modifications to retrospective application in the following areas:

(a) …

(b) amounts related to the contractual service margin,or loss component <u>or recognition of any asset relating to insurance acquisition cash flows paid before a group of insurance contracts is recognised</u> for insurance contracts without direct participation features.

(c) Amounts related to the contractual service margin,or loss component <u>or</u>

recognition of any asset relating to insurance acquisition cash flows paid before a group of insurance contracts is recognised for insurance contracts with direct participation features.

C16A To the extent permitted by paragraph C8, for contracts without direct participation features, an entity shall determine the asset recognised under 28B(b) based on an estimate of insurance acquisition cash flows arising prior to the transition date, adjusted for portions derecognised prior to the transition date on a systematic and rational basis.

C17A To the extent permitted by paragraph C8, for contracts with direct participation features, an entity shall determine the asset recognised under 28B(b) based on an estimate of insurance acquisition cash flows arising prior to the transition date, adjusted for portions derecognised prior to the transition date on a systematic and rational basis.

C20B To apply the fair value approach, an entity shall determine the amounts related to the recognition of any asset relating to insurance acquisition cash flows paid before a group of insurance contracts is recognised for insurance contracts at transition date as zero.

3. Clarification of the number of assets under 28B

Paragraph 28B(b) requires that "*An entity shall recognise such an asset for each **existing or future group** of insurance contracts to which insurance acquisition cash flows are allocated.*" (emphasis added).

We understand that the Board's intention was for a single asset to be recognised in respect of all existing or future groups for which insurance acquisition cash flows are paid before recognition of the group. However, we are concerned that the *words "each existing or future group"* could be interpreted to require a different asset for each existing or future group. This would add significant operational complexity due to the number of assets that would require tracking, storing and regular testing for impairment.

4. Reconsider the disclosure requirement in paragraph 105B

The disclosure requirement in paragraph 105B states an entity shall disclose quantitatively, in appropriate time bands, when it expects to derecognise an asset for insurance acquisition cash flows applying paragraph 28C. This proposed disclosure requirement will involve the use of forward looking information which may be indicative of the entity's future business projections. As such information is commercially sensitive, we believe that the IASB ought to consider removing this requirement from the Standard. Furthermore, such information pertaining to the recoverability of the acquisition asset is already addressed in paragraphs B35B(b) and B105C.

One member note that entities have some concerns about how this proposed amendments can be implemented and the member suggest that the Board consider the following: (a) some preparers prefer to have an (irrevocable) option to recognize immediately in profit or loss for the reporting period as the acquisition costs relating to expected renewals are incurred, especially when first-year commission rates are relatively low; (b) unless the entity's expected persistency ratio is guaranteed to be fixed, the expectation of persistency ratio involves estimates. More guidance is needed from the Board regarding how to reasonably ensure the fair determination of expected persistency ratio, and how to perform impairment tests on the acquisition costs yet to be allocated; (c) More guidance is needed for the accounting treatment for the subsequent changes in the estimate of the expected renewals, for example, the renewals last longer or shorter than expected.

Question 3—Contractual service margin attributable to investment-return service and investment-related service (paragraphs 44–45, 109 and 117(c)(v), Appendix A, paragraphs B119–B119B and BC50–BC66)

(a) Paragraphs 44, B119−B119A and the definitions in Appendix A propose that an entity identify coverage units for insurance contracts without direct participation features considering the quantity of benefits and expected period of investment-return service, if any, in addition to insurance coverage. Paragraph B119B specifies criteria for when contracts may provide an investment-return service.

Do you agree with the proposed amendment? Why or why not?

(b) Paragraphs 45, B119−B119A and the definitions in Appendix A clarify that an entity is required to identify coverage units for insurance contracts with direct participation features considering the quantity of benefits and expected period of both insurance coverage and investment-related service.

Do you agree with the proposed amendment? Why or why not?

(c) Paragraph 109 proposes that an entity disclose quantitative information about when the entity expects to recognise in profit or loss the contractual service margin remaining at the end of a reporting period. Paragraph 117(c)(v) proposes an entity disclose the approach used to determine the relative weighting of the benefits provided by insurance coverage and investment-return service or investment-related service.

Do you agree with the proposed disclosure requirements? Why or why not?

(Comments)

We agree with the IASB's proposals in (a) and (b) (i.e. changes to 44(e), 45(e) and B119) clarifying that the contractual service margin (CSM) should include future expected investment services (as well as future insurance services) whenever relevant (that is, whether or not the contracts have direct participation features). Feedback from preparers highlights this is particularly important when, later in their lifecycle, some 'insurance contracts' become substantively investment-only contracts and IFRS 17.B25 prohibits them from being reclassified out of IFRS 17. As the CSM will now also represent investment services, a relevant portion of the CSM will be available to be allocated to later periods in the lifecycle of such a contract. Otherwise, CSM is recognised too early.

The IASB's proposals will ensure that the CSM allocated to profit or loss will reflect both insurance and investment services provided to the policyholder to enable insurers to faithfully represent the investment services they provide in the relevant periods.

However, we have different responses for the Question 3 (c) which is about the disclosure requirements. One member support the proposals to require disclosure of:

- quantitative (rather than qualitative) information about when the entity expects to recognise in profit or loss the CSM remaining at the end of a reporting period [IFRS 17.109], in appropriate time bands; and
- the approach used to determine the relative weighting of the benefits provided by insurance coverage and investment-return service or investment-related service [IFRS 17.117(c)(v)].

The member considers that the quantitative disclosures about the amount of CSM expected to be recognised over time are important as these disclosures enable users of financial statements to monitor the profitability pattern, allowing informed comparisons across entities. The member considers that an entity needs to determine this release pattern for its own purposes (including estimation of that release pattern in the future). Therefore, preparers should be able to provide this quantitative information without undue cost or effort.

The member acknowledges that there will be subjectivity in applying the proposed amendment, and determining the weighting between the insurance coverage services and either the investment-return services or the investment-related services, in order to determine the coverage units and the release pattern of the CSM. However, an entity is already required to make similar assessments and judgments for contracts which provide more than one type of insurance coverage. These disclosures will enable users to better understand the sources of profit and to make comparisons both between types of contracts and across entities and over time and, therefore, the member considers that this proposal will not require the excessive use of judgment and will facilitate users' understanding of the impact of all relevant services on the amortisation of CSM.

On the other hand, two of our members commented that the assessment of relative weighting of benefits may pose operational challenges. Hence, they suggest that for a group of contracts that contain both insurance and investment services, where a weighted measure of the services cannot be determined reliably and practicably, the entity should be allowed to allocate the contractual service margin in a practical and consistent manner, for example using the passage of time basis.

One member suggests a minor proposal to amend the definition of investment return service.
The definition of an investment-return service in B119B(b) requires a 'positive investment

return' to be provided. Feedback from preparers has identified the following issues related to this requirement:

- It is not clear what a 'positive investment return' is (and B119B(b) indicates that it could even be negative).
- The inclusion of a 'positive investment return' implies the explicit addition of some amount to deposits made by the policyholder. Yet, a typical surrender value (which would often represent the value of an investment component) for a traditional product is often calculated prospectively, being the present value of future cash flows – past investment returns are irrelevant, and future expectations for determining a present value may not immediately reflect 'positive returns' earned in the past. It is not clear what the inclusion is in those circumstances.
- The reference to a 'positive investment return' implies that if an investment component does not provide a 'positive investment return' then you may have an investment component that does not provide an investment-return service. As the component of a contract must provide some service (the policyholder would not enter a contract where no service was provided to it), this raises the question of what service is provided by an investment component (in a contract without discretionary participation features) if it is not an investment-return service?

The member believes that simply requiring an 'investment return', without specifying that it be 'positive', would be sufficient, and consistent with other products that provide either an 'investment-related service' or the service provided by an investment funds management contract (i.e. providing a service to the policyholder which they are unable to provide to themselves due to amounts invested (being too small), expertise, etc.).

Question 4—Reinsurance contracts held—recovery of losses on underlying insurance contracts (paragraphs 62, 66A–66B, B119C–B119F and BC67–BC90)

Paragraph 66A proposes that an entity adjust the contractual service margin of a group of reinsurance contracts held that provides proportionate coverage, and as a result recognise income, when the entity recognises a loss on initial recognition of an onerous group of underlying insurance contracts, or on addition of onerous contracts to that group. The amount of the adjustment and resulting income is determined by multiplying: (a) the loss recognised on the group of underlying insurance contracts; and (b) the fixed percentage of claims on the group of underlying contracts the entity has a right to recover from the group of reinsurance contracts held. Do you agree with the proposed amendment? Why or why not?

(Comments)

All the members support amending IFRS 17 to allow the recognition of reinsurance recovery income when the entity recognises losses on onerous underlying contracts. We consider that this reflects the nature of a reinsurance contract as a risk mitigation tool and provides essential information for users of financial statements by fairly representing the economic substance of the reinsurance protection purchased.

However, we disagree with the scope of the proposed amendment, specifically, its limitation to "reinsurance contracts held that provide proportionate coverage" ('proportionate reinsurance') as defined in paragraph B119C. In our view, the proposed amendment should be applied to all reinsurance contracts where there is a direct link between the expected recoveries and the claims (and therefore, onerous losses) of the underlying contracts they cover because:

1) The proposed amendment is insufficient in scope to deliver value for users of financial statements because reinsurance transactions that provide the same economic outcomes would be accounted for differently depending on whether:

- the reinsurance contracts provide 'proportionate' or 'non-proportionate coverage'; and
- the underlying contracts were expected to be onerous on inception, or subsequently.

This issue arises because the proposed definition of "proportionate coverage" in B119C excludes a significant portion of reinsurance contracts in the market which are of the same nature and substance.

2) The reinsurance recoveries on non-proportionate reinsurance contracts that relate to a loss recognised on underlying insurance contracts can be identified without making arbitrary assumptions beyond the existing assumption already set out by the IASB, i.e. that the onerous loss is caused only by claims. In section 2 below, we propose a method for allocating recoveries to the onerous underlying losses that can be applied consistently by all entities for all types of reinsurance contracts and does not require subjective judgment.

1. Inconsistent accounting treatment of reinsurance transactions with the same economic outcomes

1.1 The current scope of the proposed amendment would significantly limit the usefulness of information to users of financial statements because the limitation:

(a) Will result in different accounting treatment of reinsurance transactions that have the same economic effect;

(b) Will result in an inconsistent treatment across reinsurance contracts of the same nature and substance and where there is an equally direct link between the expected reinsurance recoveries and the losses on the underlying contracts;

(c) Is inconsistent with the subsequent measurement requirement set out in IFRS 17.66(c)(ii) which allows a gain on reinsurance held to be recognised in profit or loss where they relate to underlying contracts that become onerous (or more onerous) after initial recognition because of adverse changes in estimates regardless of the type of reinsurance contract held; and

(d) May give rise to inconsistent interpretations as the proposed amendment adds a new distinction ('proportionate' vs 'non-proportionate') that may be difficult to apply.

This may result in non-GAAP measures being used by preparers to mitigate the reduced understandability brought about by the different treatment across reinsurance contracts held.

1.2 The narrow definition of "proportionate coverage" means that the proposed amendment will have limited application in practice as a significant portion of reinsurance contracts in the market will not meet the definition set out in in B119C. In summary:

(a) The proposed amendment excludes a significant body of reinsurance contracts held which are used in practice in global reinsurance such as excess of loss (XOL) and surplus reinsurance contracts that are widely used in the life and general insurance market globally. These include simple facultative reinsurance contracts that cover only one risk/underlying contract. For some of these reinsurance contracts, the reinsurance retention / deductible may apply to specific individual underlying claims and therefore, for each claim the insurer expects to incur there is a direct link to the reinsurance recoveries the insurer expects to receive. These contracts would not appear to meet the definition of 'proportionate' as they do not cover a fixed percentage but may vary for each claim based on the claim size;

(b) Proportional reinsurance contracts (such as simple quota shares (QS)) are often subject to specified limits - e.g. a quota share reinsurance contract that will pay the cedant recoveries of 50% of all underlying claims subject to a limit of CU1m. These reinsurance contracts do not cover a fixed percentage of all claims, and would therefore, appear not to meet the definition of "proportionate" in paragraph B119C, even if they cover a fixed proportion of claims at the individual contract level;

(c) Proportional reinsurance contracts which have contract terms that do not align with the underlying cohorts in a group (e.g. reinsurance contracts in force from July to June covering underlying contracts in groups comprising contracts issued between January and December) will not be in scope of the proposed amendment if those reinsurance contracts do not cover all contracts in a group, even though all claims in the group may have the right to a fixed percentage of reinsurance recoveries if the reinsurance contracts covering the group are considered collectively (e.g. a January . December annual cohort covered by 2 back to back reinsurance contracts which have July to June contract terms); and

(d) A group of underlying contracts issued may be covered by more than one reinsurance contract, e.g. a facultative excess of loss (XOL) reinsurance contract (non-proportionate) that provides coverage for claims above a deductible and up to a limit, and a quota share (QS)(proportional) that covers a fixed percentage of all claims not covered by the XOL reinsurance contract. The QS in this scenario would appear not to meet the definition of 'proportionate' in paragraph B119C as it does not cover a fixed percentage of all claims of the group of underlying contracts.

Whilst we understand that the example provided in pages 11-12 of *the Snapshot: Amendments to IFRS 17* is intended to be illustrative, we note that it is not reflective of the majority of reinsurance contracts in the market. The reinsurance contracts described in (a)~(d) above may be used to achieve the same economic outcomes as those that are in scope of B119C but would be accounted for differently under the IASB's proposed amendment - Appendix D. Section 1 (of this submission) sets out examples of various reinsurance transactions and structures that demonstrate this.

2. Identifying reinsurance recoveries related to a loss recognised on underlying insurance contracts

2.1 We consider it to be clear that both proportionate and non-proportionate reinsurance contracts held provide a direct link between the expected recoveries and the loss recognised on underlying onerous contracts. This is acknowledged by the IASB in Basis for Conclusions on ED Amendments BC79.

2.2 The underlying expected cash flows, including expected claims, are estimated in accordance with IFRS 17.33, in an unbiased way using reasonable and supportable information, and by applying appropriate methods (e.g. probability weighted mean). The total reinsurance recoveries which an entity is entitled to recover in respect of those expected underlying claims can be reliably and factually determined for both proportionate and non-proportionate reinsurance based on the terms of the reinsurance contract (e.g. by applying the fixed percentage agreed in a proportionate reinsurance contract, or by applying the deductible / limits / surplus percentages / any other relevant terms agreed in a non-proportionate reinsurance contract). We note that many preparers already determine expected reinsurance recoveries on insurance contracts issued at all stages of the contract life cycle. This is done for local regulatory calculations, existing IFRS and other bases such as Market Consistent Embedded Value and will also need to be calculated for the application of the IFRS 17 measurement requirements.

2.3 We note that the IASB's reason for the limitation of the proposed amendment is based on a perceived inability to identify the amounts that the entity has the right to recover from the reinsurer in respect of the underlying onerous losses recognised ('corresponding reinsurance recoveries'). We consider that the corresponding reinsurance recoveries in relation to non-proportionate reinsurance can be determined without making additional arbitrary assumptions by applying the recovery percentage (determined as the total expected reinsurance recoveries as a proportion of the total expected underlying claims) to the onerous loss recognised in profit or loss. Every dollar of underlying claims is considered an equal contributor to the onerous loss recognised and therefore, an equal contributor to the calculation of the expected recovery percentage. That is, the recovery percentage is the allocation of the insurer's right to recover under the reinsurance contract to each underlying claim. This is also the basis on which compensation required from policyholders would be determined, i.e. prices charged to policyholders would not differ based on whether the relevant contracts are expected to trigger the deductible or not.

The examples in Appendix D – Section 2 (of this submission) address the specific concerns expressed by the IASB in *Basis for Conclusions on ED Amendments* BC86(a) and (b) and demonstrate that the extent to which reinsurance recoveries relate to a loss recognised on underlying contracts can be determined by using a simple methodology that:

• can be applied consistently by all entities for all types of reinsurance contracts;

• does not require subjective judgment; and

• is well-established as it is currently applied by many entities to estimate reinsurance recoveries.

The methodology we have proposed also does not result in reinsurance income being recognised early in respect of underlying groups of contracts that are profitable.

3. Recommendation

3.1 One member recommends an amendment to the proposals in paragraphs 66A–66B, B119C–B119F and BC67–BC90 of the ED to allow for application to all reinsurance contracts held for which there is a direct link between the expected recoveries and the loss recognised on underlying onerous contracts. The member considers that this can be achieved by removing references to 'proportionate coverage' and have provided some suggested wording changes underlined below:

66A An entity shall adjust the contractual service margin of a group of reinsurance contracts held *~~that provides proportionate coverage~~* and as a result recognise income when the entity recognises a loss on initial recognition of an onerous group of underlying insurance contracts or on addition of onerous underlying insurance contracts to that group. The amount of the adjustment and resulting income is determined applying paragraph B119D.*

~~B119C Paragraph 66A applies to reinsurance contracts held that provide proportionate coverage. Such reinsurance contracts provide the entity with the right to recover from the issuer a fixed percentage of all claims incurred on a group of underlying insurance contracts. Such reinsurance contracts can also include cash flows, other than claims, that are not proportionate to cash flows of the underlying groups of insurance contracts issued. For example, in such reinsurance contracts, the premiums due to the reinsurer might not be proportionate to premiums due from the policyholders of the groups of underlying insurance contracts.~~

B119D An entity shall determine the adjustment to the contractual service margin and the resulting income recognised applying paragraph 66A by multiplying:

(a) the loss recognised on the group of underlying insurance contracts; and

(b) the ~~fixed~~ percentage of claims on the group of underlying insurance contracts the entity has a right to recover from the group of reinsurance contracts held, determined as the total expected reinsurance recoveries as a proportion of the total expected underlying claims for the group of underlying insurance contracts.

3.2 The member recommends the following consequential amendments to paragraphs 62, B95B and C15A to reflect the proposed amendment above:

62 Instead of applying paragraph 25, unless paragraph 62A applies, an entity shall recognise:

(a) a group of reinsurance contracts held that provide proportionate coverage, ~~(i) unless paragraph 62(a)(ii) applies~~ – at the beginning of the coverage period of the group of reinsurance contracts held or at the initial recognition of any underlying contract, whichever is later; or ~~(ii) if the entity recognises an onerous group of underlying contracts before the beginning of the coverage period of the group of reinsurance contracts held – at the same time as the onerous group of underlying contracts.~~

(b) ~~in~~ all other groups of reinsurance contracts held ~~cases~~ from the beginning of the coverage period of the group of reinsurance contracts held.

62A If before the beginning of the coverage period of a group of reinsurance contracts held, the entity recognises an onerous group of underlying contracts in accordance with paragraph 25(c), the entity shall recognise the group of reinsurance contracts held at the same time as the onerous group of underlying contracts.

B95B For a group of reinsurance contracts held to which paragraphs 66A-66B apply at the date of the transaction, an entity shall determine the loss-recovery component of the asset for remaining coverage by multiplying:

(a) the loss component of the liability for remaining coverage of the group of underlying insurance contracts at the date of the transaction; and

(b) the ~~fixed~~ percentage of claims the entity has a right to recover from the group of reinsurance contracts held, determined as the total expected reinsurance recoveries as a proportion of the total expected underlying claims for the group of underlying insurance contracts.

C15A For a group of reinsurance contracts held that provides ~~proportionate~~ coverage for an onerous group of insurance contracts and was acquired before or at the same time *that the insurance contracts were issued, an entity shall establish a loss-recovery component of the asset for remaining coverage at the transition date (see paragraphs 66A-66B). To the extent permitted by paragraph C8, an entity shall determine the loss-recovery component by multiplying:*

(a) the loss component of the liability for remaining coverage for the group of underlying insurance contracts at the transition date (see paragraphs C16 and C20); and

(b) the ~~fixed~~ percentage of claims for the group of underlying insurance contracts the entity has a right to recover from the group of reinsurance contracts held, determined as the total expected reinsurance recoveries as a proportion of the total expected underlying claims for the group of underlying insurance contracts. The total expected underlying claims and reinsurance recoveries used to determine this percentage is measured in accordance with the measurement requirements of IFRS 17 as set out in paragraphs 32 to 38 and 63 to 68 respectively.

Furthermore, one of our members notes that, though the reinsurance contract commercially results in a net increase in the operating loss of the retrocedant (as illustrated by the example in the ED), applying the proposed amendment would result in an income being reported for the reinsurance contract held in its initial reporting period, and the operating loss being reflected only in subsequent periods through amortization. In this way, some insurers may have the incentive to recognize an income in a period in exchange for a relatively low cost to buy reinsurance. The member suggests the Board consider its economic consequences.

Question 5—Presentation in the statement of financial position (paragraphs 78–79, 99, 132 and BC91–BC100)

The proposed amendment to paragraph 78 would require an entity to present separately in the statement of financial position the carrying amount of portfolios of insurance contracts issued that are assets and those that are liabilities. Applying the existing requirements, an entity would present the carrying amount of groups of insurance contracts issued that are assets and those that are liabilities. The amendment would also apply to portfolios of reinsurance contracts held that are assets and those that are liabilities. Do you agree with the proposed amendment? Why or why not?

(Comments)

All the members agree with the proposed change to require separate presentation of insurance assets and liabilities at a higher level of aggregation than 'group'.

However, preparers from two member jurisdictions contend that there would be no loss of useful information for users because portfolios will be inconsistent between entities as they are based around the management construct of the entity, which can differ significantly by entity. Prepares can see no benefit for users in providing this information at portfolio level and, given the increased implementation costs of delivering this information it is strongly recommended aggregation at entity level is adopted to facilitate comparability.

Question 6—Applicability of the risk mitigation option (paragraphs B116 and BC101–BC109)

The proposed amendment to paragraph B116 would extend the risk mitigation option available when an entity uses derivatives to mitigate financial risk arising from insurance contracts with direct participation features. That option would apply in circumstances when an entity uses reinsurance contracts held to mitigate financial risk arising from insurance contracts with direct participation features. Do you agree with the proposed amendment? Why or why not?

(Comments)

All the members support the proposal to extend the scope of the risk mitigation exception to financial risk changes mitigated by reinsurance contracts held on the basis that it will help to mitigate accounting mismatches in affected jurisdictions [paragraph BC105].

However, one member thinks that the risk mitigation option should be extended to the insurance contracts under general model, rather than being restricted to the insurance contracts with direct participation features. In the case where the entity hedges financial risks with derivatives for the insurance contracts under general model, accounting mismatches occur in the income statements, as the effects of changes in the fair values of derivatives are recognised in profit or loss while the changes in the insurance contracts caused by the financial risk are reflected in OCI. This does not show the results of entities' hedging management and will cause volatility in profit or loss. The IASB recommended the entities having the insurance contracts under general model to apply the hedge accounting under IFRS 9, but the entities note that they cannot use the hedge accounting due to the strict criteria of IFRS 9.

Question 7—Effective date of IFRS 17 and the IFRS 9 temporary exemption in IFRS 4 (paragraphs C1, [Draft] Amendments to IFRS 4 and BC110–BC118)

IFRS 17 is effective for annual reporting periods beginning on or after 1 January 2021. The amendments proposed in this Exposure Draft are such that they should not unduly disrupt implementation already under way or risk undue delays in the effective date. (a) The proposed amendment to paragraph C1 would defer the effective date of IFRS 17 by one year from annual reporting periods beginning on or after 1 January 2021 to annual reporting periods beginning on or after 1 January 2022. Do you agree with the proposed amendment? Why or why not? (b) The proposed amendment to paragraph 20A of IFRS 4 would extend the temporary exemption from IFRS 9 by one year so that an entity applying the exemption would be required to apply IFRS 9 for annual reporting periods beginning on or after 1 January 2022. Do you agree with the proposed amendment? Why or why not?

(Comments)

1. Comment on question 7 (a)

All the members welcome the proposed deferral to the effective date as the additional time will allow entities to reflect the impact of the amendments as proposed in this ED.

However, one of our members would specifically support a further one year deferral of IFRS 17 to 1 January 2023 to allow for a more strategic implementation approach to be adopted.

The other member is supportive of the IASB's aim to have a truly global standard which is uniformly adopted in terms of both effective date and technical interpretation and application. The member urges the IASB to continue working with the major markets to ensure IFRS 17 is applied consistently and in a timely manner, without unduly affecting or impacting the position of the early adopters of the Standard.

Another member commented that IFRS 17 needs to be implemented simultaneously worldwide in order to become a uniform accounting standard for insurance contracts across the world. However, if the amendments to IFRS 17 delay the Europe's implementation, it may be difficult for Europe to implement them by the year of 2022. As such, other jurisdictions may delay their implementation. They understand that the timing of implementation is up to individual countries, but they are concerned that it could be a problem for the fairness of insurance companies if all countries do not adopt it at the same time.

2. Comment on question 7 (b)

All the members support the proposed extension of the IFRS 9 exemption being in line with the mandatory application date of IFRS 17 on the basis that business models may need to be re-assessed and could, therefore, affect IFRS 9 measurement approaches adopted (or revised) on applying IFRS 17. However, feedback from preparers in one member jurisdiction notes that a consistent mandatory application date for IFRS 9 and IFRS 17 is not relevant for all their constituents, particularly given that on transition to IFRS 17 decisions made on measurement model under IFRS 9 can be reconsidered as specified in paragraphs C29-C33.

Question 8—Transition modifications and reliefs (paragraphs C3(b), C5A, C9A, C22A and BC119–BC146)

(a) Paragraph C9A proposes an additional modification in the modified retrospective approach. The modification would require an entity, to the extent permitted by paragraph C8, to classify as a liability for incurred claims a liability for settlement of claims incurred before an insurance contract was acquired. Paragraph C22A proposes that an entity applying the fair value approach could choose to classify such a liability as a liability for incurred claims.

Do you agree with the proposed amendments? Why or why not?

(b) The proposed amendment to paragraph C3(b) would permit an entity to apply the option in paragraph B115 prospectively from the transition date, rather than the date of initial application. The amendment proposes that to apply the option in paragraph B115 prospectively on or after the transition date, an entity would be required to designate risk mitigation relationships at or before the date it applies the option.

Do you agree with the proposed amendment? Why or why not?

(c) Paragraph C5A proposes that an entity that can apply IFRS 17 retrospectively to a group of insurance contracts be permitted to instead apply the fair value approach to that group if it meets specified criteria relating to risk mitigation.

Do you agree with the proposed amendment? Why or why not?

(Comments)

Comments on question 8 (a) only

One of our members supports the amendment to the modified retrospective approach requiring entities, subject to certain criteria, to classify as a liability for incurred claims (and not as a liability for remaining coverage) a liability for settlement of claims incurred before an insurance contract was acquired.

Feedback from preparers in relation to this issue of the member's jurisdiction, has highlighted the practical difficulties and high costs of applying IFRS 17.B5 to acquired contracts on an ongoing basis after transition to IFRS 17 based on the wide-ranging meaning of the term in IFRS 17.B5 "an insurance contract that provides coverage against an adverse development of an event that has already occurred" now conferred by paragraph BC120 to the Basis for Conclusions to ED/2019/4. Preparers consider that an adverse development cover is a specific type of cover underwritten to provide cover in the future for development of claims incurred in the past. This contrasts with acquired contracts which are generally not issued or underwritten to provide such cover but are often acquired as part of a broader strategic transaction with no intent to earn profit from the claims run-off element.

They consider that IFRS 17.B5 should be amended such that, on an ongoing basis, consistent with IFRS 3.15 *Business Combinations*, insurers are required to determine the nature of what they have acquired on the basis of the "**contractual terms, economic conditions, the entities operating or accounting policies and other pertinent conditions as they exist at the acquisition date".**

Accordingly, when an insurer acquires contracts in their claims settlement period, unless the insurer acquires insurance contracts that, on acquisition, are intended to be in the nature of adverse development covers (e.g. purchase of a run-off portfolio for the purpose of making profit from that portfolio as opposed to the future renewal rights of that portfolio), they would be classified as a liability for incurred claims. This is consistent with the original wording of IFRS 17.B5; however, in proposing the addition of IFRS 17.C9A, paragraph BC120 could be inferred as implying that all contracts acquired in their claims settlement period (after transition) should be treated as adverse development covers. If this were the case, it would create potentially inconsistent accounting treatments for identical contracts purely due to the timing of when the portfolio was purchased, which is unhelpful for users of financial statements and creates additional complexity and cost in both applying and explaining the results of an insurer.

Furthermore, the treatment of the acquired portfolio could be potentially misleading for users by changing the classification of the contract. For example, an entity that measures its issued insurance contracts using the premium allocation approach may be required to apply the general model to identical contracts which have been acquired rather than issued (depending on the settlement period of the claims and the related volatility). Reclassifying the portfolio in this way may distort the business transaction for users by indicating the entity has changed its business focus to the management of run-off portfolios, as opposed to acquiring contracts as a means of increasing market share or entry into a new market through the rights to the renewal business. In addition, this approach would add significant operational complexity and cost with minimal benefit for users. Equally, a contract accounted for under the general model or the premium allocation approach could cease to meet the definition of an insurance contract if acquired later in the coverage period and be required to be measured under IFRS 9 Financial Instruments. Such **changes in classification would be confusing to users and investors as well as costly to apply**.

They contrast this treatment with the acquisition of financial instruments. On acquisition of financial instruments in a business combination, IFRS 3 requires re-measurement of financial instruments, but the **"classification"** of the financial instrument is determined by the acquirer based on the characteristics of the instrument and the acquirer's business model, whereas the application of IFRS 3, in conjunction with IFRS 17B5 potentially **"reclassifies"** the insurance contract. This change in classification will confuse users and drive up costs of IFRS 17 implementation on an ongoing and lasting basis.

Feedback from preparers has emphasised that there is a clear distinction between underwriting contracts that provide adverse development coverage and entering into the acquisition of insurance contracts that are either partly or fully within their claim settlement stage. Such acquired contracts are often pooled with other contracts originated by the insurer to diversify the pool of risks and/or make good use of surplus claims management capacity. That is, they are managed and pose the same economic costs and benefits as originated contracts in their claim settlement period. These acquired contracts are still considered insurance contracts with the original policyholders, not adverse development contracts, and the nature of the underlying contract has not changed.

They therefore request the IASB to clarify IFRS 17.B5 to ensure that insurers account consistently for contracts acquired fully or partially in their claims-settlement stage in a manner that reflects their business model and which, whilst requiring the remeasurement requirements of IFRS 3, does not force unnecessary re-classification of insurance contracts.

They consider that only treating contracts in the nature of adverse development covers as being within IFRS 17.B5 is consistent with the work conducted by the IASB at its IFRS 17 Transition Resource Group (TRG) meeting noted below.

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The work the IASB conducted through its TRG in September 2018 in respect of Agenda paper 1 *Group insurance policies*) involved identifying the policyholder when individual policies are sold under master arrangement and the flow-on consequences for determining contract boundaries. All the criteria applied in that Agenda paper relate to the original contract10 which set the contract boundary. When an insurer acquires a contract in its settlement period, the policyholder does not change and nor should the contract boundary. IFRS 17.B5 should, therefore, only be read as being a limited exception to this principle when the contract acquired takes on the character of an adverse development cover from the perspective of the acquiring insurer.

Question 9—Minor amendments (BC147–BC163)

This Exposure Draft also proposes minor amendments (see paragraphs BC147−BC163 of the Basis for Conclusions). Do you agree with the Board's proposals for each of the minor amendments described in this Exposure Draft? Why or why not?

(Comments)

All the members agree with the proposed amendments. However, the amendment to paragraph 71(a) and paragraph 28 suggest that the eligibility criteria for the variable fee approach have been changed from being assessed at a group of contracts to an individual contract. One member wishes to seek clarification whether it is the intention of the IASB to change this requirement as this change could result in significant disruption to the implementation timeline of the Standard.

Another member supports the amendment to specify that IFRS 17.39 applies only to business combinations within the scope of IFRS 3 Business Combinations on the basis that contracts acquired in business combinations under common control (BCUCC) should not be accounted for as if they had been acquired on the date of a BCUCC [ED/2019/4. BC151]. BCUCC may occur simply as part of an internal restructuring and it would pose an unnecessary cost to have to presume contracts are newly acquired at the time of a BCUCC.

Question 10—Terminology

This Exposure Draft proposes to add to Appendix A of IFRS 17 the definition 'insurance contract services' to be consistent with other proposed amendments in this Exposure Draft. In the light of the proposed amendments in this Exposure Draft, the Board is considering whether to make a consequential change in terminology by amending the terms in IFRS 17 to replace 'coverage' with 'service' in the terms 'coverage units', 'coverage period' and 'liability for remaining coverage'. If that change is made, those terms would become 'service units', 'service period' and 'liability for remaining service', respectively, throughout IFRS 17. Would you find this change in terminology helpful? Why or why not?

(Comments)

All members agree with the proposed amendments. However, one member considers that the level of aggregation (annual cohorts) requirement may lead to unnecessary costs being incurred, in particular, for contracts with cash flows that affect or are affected by cash flows to policyholders of other contracts. We believe that it is worth re-considering whether the annual cohorts requirement is justified for such contracts and recommend that the IASB consider developing an exception for them, starting from paragraph BC138; the exception should be reflective of the reporting objectives of the level of aggregation requirements in IFRS 17.