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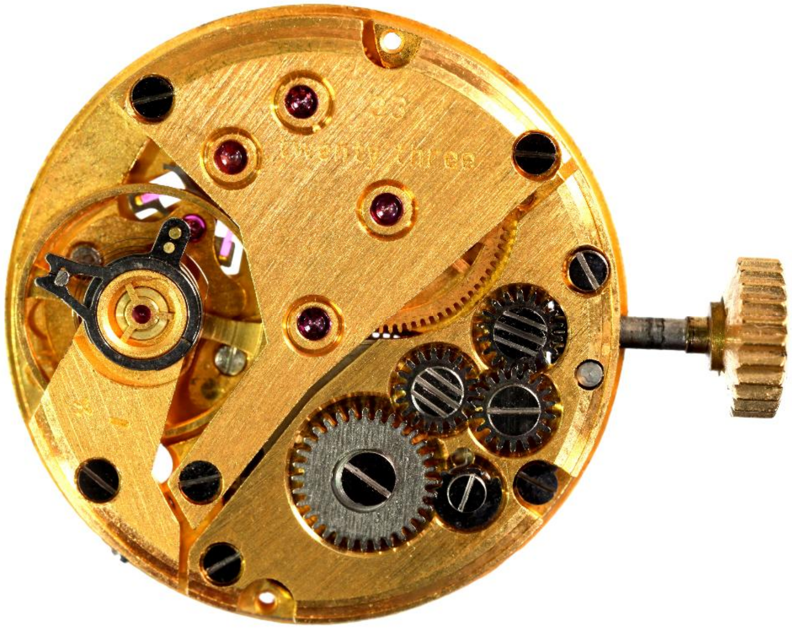

The IASB completes its final round of IFRS 17 amendments

Level of Aggregation does not change

Francesco Nagari, Deloitte Global IFRS Insurance Leader | 21 March 2019

Agenda

- Highlights of the IASB meeting on 14 March 2019
- Detailed analysis of the IASB discussion and of the decisions reached
- Next steps

Highlights of the IASB meeting on 14 March 2019

- The main highlight for the meeting is that the IASB has decided to retain the IFRS 17 requirements on the level of aggregation unchanged.
- The IASB amended the transition requirements in IFRS 17 to permit an entity to apply the risk mitigation option prospectively from the IFRS 17 transition date (1/1/21) instead of the date of initial application (1/1/22) and to be able to use the Fair Value Approach for those VFA contracts that are in the hedging relationship applied from transition.
- Certain credit card contracts that provide insurance coverage will be scoped out. Several sweep issues on the other scope exemption for loans with significant insurance risk transfer were also approved.
- Finally, the IASB amended several disclosure requirements derived from their tentative decisions to date and other implications for disclosure and transition requirements.

Level of aggregation—Stakeholder concerns, implementation challenges and Staff analysis

2—Level of aggregation of insurance contracts

- **IFRS 17 requires an entity to recognize and measure groups of insurance contracts, which are determined by:**
  - a) identifying portfolios of insurance contracts. A portfolio comprises contracts subject to similar risks and managed together.
  - b) dividing a portfolio into a minimum of three groups, i.e. 'profitability buckets':
    - group of contracts that are onerous at initial recognition, if any;
    - a group of contracts that at initial recognition have no significant possibility of becoming onerous subsequently, if any; and
    - a group of remaining contracts in the portfolio.
  - c) dividing the profitability buckets into groups of contracts not issued more than one year apart, i.e. annual cohorts.

- **Stakeholders are concerned mainly with the annual cohort requirement because they think:**
  - The requirement will not provide financial statements users with useful information as segregating portfolios does not depict business performance and accurately reflect pooling of risks
  - Implementing the requirement is a major challenge and the benefits do not outweigh costs, as significant changes to existing systems will be required
  - An entity can achieve the same outcome without applying those requirements

Level of aggregation—Stakeholder concerns, implementation challenges and Staff analysis

2—Level of aggregation of insurance contracts

- Some stakeholders have suggested amendments to IFRS 17. Those amendments are:
  a) reduce the number of profitability buckets by removing the profitability bucket 'a group of insurance contracts that at initial recognition have no significant possibility of becoming onerous subsequently'.
  b) replace the requirements for the level of aggregation with approaches that reflect more closely the entity's internal management.
  c) remove the requirement for annual cohorts for variable fee contracts or variable fee contracts that 'fully share risks' between policyholders.

Do you agree the Board should retain the IFRS 17 requirements on the level of aggregation unchanged?

- Some stakeholders have suggested a higher level of aggregation only for presentation purposes, which the Board tentatively decided to propose at its December 2018 meeting.

Level of aggregation—Stakeholder concerns, implementation challenges and Staff analysis

2—Level of aggregation of insurance contracts

- **Measuring insurance contracts at a too high a level of aggregation could obscure 3 types of information the IASB regards as fundamentally important:**
  - **Trends in the entity's profits from insurance contracts over time**
  - **Timely recognition of profit on profitable contracts so that all profit has been recognized by the end of the coverage period**
  - **Timely recognition of losses on onerous contracts**
- **Timely recognition of changes in profitability results in more transparent information, which contributes to improving investor understanding of insurance activity and long-term financial stability.**
- **The requirements in IFRS 17 strike a balance the Board found acceptable between the loss of useful information and the operational burden for entities.**

Level of aggregation—Stakeholder concerns, implementation challenges and Staff analysis

2—Level of aggregation of insurance contracts

- **In response to the stakeholders' suggested amendments:**

1. Reduce the number of profitability buckets by removing the profitability bucket 'a group of insurance contracts that at initial recognition have no significant possibility of becoming onerous subsequently'.

- **Onerous groups of contracts are more likely to arise from subsequent changes in expectations about groups of contracts that were initially expected to be profitable.**
- **Having only one bucket for all contracts that are profitable on initial recognition would increase the possibility of a subsequent change in expectations that would make some contracts onerous being absorbed by the remaining profitability on other contracts.**
- **A loss would only be created by subsequent changes in expectations that made all profitable contracts in an annual cohort onerous.**
- **Timing of loss recognition for onerous contracts would be significantly delayed.**
- **IASB Staff thought the loss of useful information in removing the requirement to distinguish two buckets for profitable contracts would be unacceptable.**

Level of aggregation—Stakeholder concerns, implementation challenges and Staff analysis

2—Level of aggregation of insurance contracts

- **In response to the stakeholders′ suggested amendments:**

2. Replace the requirements for the level of aggregation with approaches that reflect more closely the entity′s internal management, e.g. removing the requirement for annual cohorts

- **IASB Staff observed this suggestion is likely to result in groups being only the three profitability buckets, with no time-based cohorts.**
- **Three buckets of for a portfolio could last for the entire life of the portfolio, each with a contractual service margin that averages the profitability of all the contracts in the bucket.**
- **Effect of the averaging of the profits across the contracts in the bucket could be substantial leading to:**
  - **A greater possibility that the contractual service margin of contracts would outlast the coverage period of those contracts**
  - **A greater possibility of subsequent adverse changes in expectations that makes some contracts onerous being absorbed by continuing profitability of other contracts**
- **IASB Staff thought that the approaches suggested by stakeholders in having the level of aggregation requirements reflecting more closely to the entity′s internal management and without the annual cohorts requirements would lead to unacceptable loss of useful information.**

Level of aggregation—Stakeholder concerns, implementation challenges and Staff analysis

2—Level of aggregation of insurance contracts

- **In response to the stakeholders' suggested amendments:**

3. Remove the requirement for annual cohorts for variable fee contracts or variable fee contracts that 'fully share risks' between policyholders.

- **An example of two groups of variable fee contracts issued more than one year apart with intergenerational sharing of the returns of the underlying items stated in the contracts terms:**

	A	B	C		D		E
	Initial recognition of Group 1	Remeasurement of Group 1 before recognition of Group 2	Immediately after group 2 contracts issued, without applying paragraphs B67–B71 of IFRS 17		Immediately after Group 2 contracts issued, applying paragraphs B67–B71 of IFRS 17		Immediately after Group 2 contracts, if groups 1 and 2 were combined
	Group 1	Group 1	Group 1	Group 2	Group 1	Group 2	
FCF	9,567	11,734	10,828	15,761	11,734	14,855	26,589
CSM	433	531	1,437	(761)	531	145	676
Insurance contracts	10,000	12,265	12,265	15,000	12,265	15,000	27,265
Underlying items	10,000	12,265	12,265	15,000	12,265	15,000	27,265

- **Stakeholders thought determining the contractual service margin separately for each annual cohort does not provide useful information. Profit should be regarded as arising from the combined groups that share the returns of the underlying items.**

- **IASB Staff, in contrast, observed that keeping the profit of the annual cohorts separate is necessary to avoid deferring the recognition of profit beyond the coverage period of a group and obscuring trends in profitability for an entity from its insurance contracts over time.**

Level of aggregation—Stakeholder concerns, implementation challenges and Staff analysis

2—Level of aggregation of insurance contracts

Continued:
3. Remove the requirement for annual cohorts for variable fee contracts or variable fee contracts that 'fully share risks' between policyholders.

- The fact that the policyholders' share of underlying items is shared across all policyholders does not mean the entity receives an equal (average) profit from all contracts.
- IASB Staff thought removing the requirement for annual cohorts in this example with intergenerational returns between groups of contracts issued more than one year apart would lead to unacceptable loss of information.
- Averaging of the different profitability of contracts issued at different times would result in deferral of recognition of some of the profit of a group beyond its coverage period and a loss of information about trends in the entity's profitability over time.

Level of aggregation—Stakeholder concerns, implementation challenges and Staff analysis

2—Level of aggregation of insurance contracts

- The Board concluded that the requirements in IFRS 17 struck an appropriate balance between costs for preparers and useful information for users of financial statements. The Staff thinks that conclusion continues to be valid.
- The Board concluded that setting the boundary for an exception from the annual cohort requirement in IFRS 17 would add complexity to IFRS 17 and create the risk that the boundary would not be robust or appropriate in all circumstances.
- IASB Staff expected the stakeholders′ concerns about the difficulty of applying transition to insurance contracts issued many years ago due to lack of information, could be addressed by applying fair value approach, which provides an optional relief from applying the annual cohort requirement.
- The Staff thought all of the suggested changes to the requirements from stakeholders would result in an unacceptable loss of useful information, particularly in relation to information about trends in an entity′s profitability over time.
- Therefore, the Staff recommended the Board retain the IFRS 17 requirements on the level of aggregation unchanged.
- The Board voted unanimously to tentatively agree with the Staff recommendation to retain the IFRS 17 requirements on the level of aggregation unchanged.

Transition requirements—Risk mitigation option

25–Transition: Risk mitigation option

- The Staff considered two possible ways, other than retrospective application of the risk mitigation option tentatively decided to be retained in Feb 2019 IASB meeting, to address stakeholders' concerns.

Do you agree that the Board should amend the requirements of IFRS 17 to permit an entity to apply the risk mitigation option prospectively from the IFRS 17 transition date provided that an entity designates its risk mitigation relationships to apply the risk mitigation option no later than the IFRS 17 transition date?

- A prospective approach will permit entities to apply the risk mitigation option provided that an entity designates its risk mitigation relationships to apply the option no later than the IFRS 17 transition date, in addition to the criteria in IFRS 17 paragraph B116 being met at that date.
- Accounting mismatches will be eliminated in the comparative periods presented and will achieve comparability over time.
- Risk mitigation option can be applied prospectively from the date of initial application rather than from the transition date. This approach will not disrupt implementation process already underway.
- The Staff recommended the Board should amend the requirements of IFRS 17 to permit entities to apply the risk mitigation option prospectively from the transition date.
- The Board voted unanimously to tentatively agree with the Staff recommendation to amend the Standard.

Transition requirements—Risk mitigation option

25–Transition: Risk mitigation option

Do you agree that the Board should amend the requirements of IFRS 17 to permit an entity that can apply IFRS 17 retrospectively to a group of insurance contracts with direct participation features to use the fair value transition approach for the group if they:

a) choose to apply the risk mitigation option to the group prospectively from the transition date; and,

b) have used derivatives or reinsurance contracts held to mitigate financial risk arising from the group before the transition date

- For groups of contracts for which it is impracticable for an entity to apply a full retrospective approach, an entity is permitted to apply the fair value approach to transition.
- When applying the fair value approach to transition, the distortion on the equity of entities on transition and the revenue recognized for these groups of contracts in future periods, related to risk mitigating activities from previous periods does not exist.
- The fair value transition approach therefore could address stakeholders′ concerns in a way that does not involve the use of hindsight or risk ‵cherry picking′. However, IFRS 17 restricts its use to circumstances in which it is impracticable to apply a full retrospective approach.
- The Staff recommended the Board to amend the requirements of IFRS 17 to permit an entity that can apply IFRS 17 retrospectively to a group of insurance contracts with direct participating features to use the fair value transition approach for the group under certain circumstances.
- The Board voted unanimously to tentatively agree with the Staff recommendation to amend the Standard

Credit cards that provide insurance coverage

1—Scope of IFRS 17 | Credit cards that provide insurance coverage

- IFRS 17 applies to all insurance contracts as defined in IFRS 17, regardless of the type of entity issuing the contracts, with some specific exceptions.
- Some stakeholders are concerned that IFRS 17 requires an entity to account for some credit card contracts as insurance contracts, where the credit card contract meets the definition of an insurance contract in IFRS 4 and in IFRS 17 if the transfer of insurance risk is significant.
- Entities that currently account for a loan or a loan commitment in a credit card applying IFRS 9 would need to change the accounting for those contracts when IFRS 17 is effective.
- IASB Staff noted entities can choose to issue an insurance contract and a credit card contract as two separate contracts and therefore stakeholders′ concerns stated are not relevant for all entities issuing credit card contracts.

Do you agree the Board should amend IFRS 17 to exclude from the scope of the Standard credit card contracts that provide insurance coverage for which 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?

- The Board voted unanimously to tentatively agree with the Staff recommendation to amend the Standard.

Transition requirements—Loans that transfer significant insurance risk

1—Scope of IFRS 17 | Loans and other forms of credit that transfer insurance risk

- In its February 2019 meeting, the Board tentatively decided to amend the scope of IFRS 17 and IFRS 9 to permit an entity to apply either IFRS 17 or IFRS 9 to insurance contracts that provide insurance coverage only for the settlement of the policyholder's obligation created by the contract.
- The Staff produced a long list of small amendments for both IFRS 17 and IFRS 9 to make sure that the two standards were operating transition as intended against the possible combinations of transition scenarios:
  - Entity elects the use of IFRS 17
  - Entity elects the use of IFRS 9 and initially applies it together with IFRS 17
  - Entity elects the use of IFRS 9 and it has already adopted it before applying IFRS 17
- For all these small changes the Staff explained the detailed amendments or the basis for retaining the current transition requirements.
- The Board voted unanimously to tentatively agree with the Staff recommendations on all of these items

Implications for disclosure and transition requirements

Amendments the Board has tentatively decided to propose in response to the concerns and implementation challenges identified by stakeholders during their implementation processes:

		Staff recommendation to change?	
Topic	**Amendment tentatively decided**	**Disclosures**	**Transition**
1- Scope of IFRS 17 (Feb-2019)	Amendment of the scope of IFRS 17 and IFRS 9 for insurance contracts that provide insurance coverage only for the settlement of the policyholder's obligation created by the contract to enable entities issuing such contracts to account for those contracts applying either IFRS 17 or IFRS 9.	Yes. Several small changes.	Yes. Several small changes.

Implications for disclosure and transition requirements

Amendments the Board has tentatively decided to propose in response to the concerns and implementation challenges identified by stakeholders during their implementation processes:

		Staff recommendation to change?	
Topic	**Amendment tentatively decided**	**Disclosures**	**Transition**
2—Insurance acquisition cash flows for renewals outside the contract boundary (Jan-2019)	Allocation of part of the insurance acquisition cash flows to expected contract renewals.	Yes. The Staff recommended: a) A reconciliation of the asset created by insurance acquisition cash flows not yet included in the measurement of a group of insurance contracts at the beginning and the end of the reporting period and its changes, specifically the recognition of any impairment loss or reversals; and b) Quantitative disclosure, in appropriate time bands, of the expected inclusion of these acquisition cash flows in the measurement of related insurance contracts when the related insurance contracts are recognized.	No. An entity would treat insurance acquisition cash flows for renewals outside of the contract boundary in a similar way as other insurance acquisition cash flows relating to a group of issued insurance contracts before the group is recognized

Implications for disclosure and transition requirements

Amendments the Board has tentatively decided to propose in response to the concerns and implementation challenges identified by stakeholders during their implementation processes:

<table>
<tr><th></th><th></th><th colspan="2">Staff recommendation to change?</th></tr>
<tr><th>Topic</th><th>Amendment tentatively decided</th><th>Disclosures</th><th>Transition</th></tr>
<tr><td>3—CSM: coverage units in the general model (Jan-2019)</td><td>Allocation of the CSM of some general model contracts based on coverage units determined considering both insurance coverage and any investment return service.</td><td rowspan="2">Yes.

The Staff recommended to amend to require quantitative disclosure, in appropriate time bands, of the expected recognition in profit or loss of the CSM remaining at the end of the reporting period; and specific disclosure of the approach to assessing the relative weighting of the benefits provided by insurance coverage and investment-related services or investment return services.</td><td rowspan="2">No.

The Staff have not identified any implications.</td></tr>
<tr><td>4-CSM: coverage units in the VFA (Jun-2018)</td><td>Clarification that the definition of the coverage period for insurance contracts with direct participation features includes periods in which the entity provides investment-related services.</td></tr>
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Implications for disclosure and transition requirements

Amendments the Board has tentatively decided to propose in response to the concerns and implementation challenges identified by stakeholders during their implementation processes:

		Staff recommendation to change?	
Topic	**Amendment tentatively decided**	**Disclosures**	**Transition**
5-Risk mitigation exception (Jan-2019)	Application of the risk mitigation exception in the VFA when an entity uses reinsurance contracts held to mitigate financial risks.	No. The amendment expands the scope of the existing risk mitigation exception in paragraph B115 of IFRS 17.	No.
6-Reinsurance contracts held—onerous underlying insurance contracts (Jan-2019)	If an insurer recognizes losses on underlying insurance contracts at initial recognition, it would also recognize a gain at the same time on proportionate reinsurance contracts held.	No. IFRS 17 requires the disclosure requirements to be adapted to reflect the features of reinsurance contracts held.	No. When drafting the amendments to IFRS 17, the Staff will consider whether, for reinsurance contracts held, it is necessary to adapt the wording of the specified modifications that an entity applying the MRA can use.

Implications for disclosure and transition requirements

Amendments the Board has tentatively decided to propose in response to the concerns and implementation challenges identified by stakeholders during their implementation processes:

		Staff recommendation to change?	
Topic	**Amendment tentatively decided**	**Disclosures**	**Transition**
7-Presentation of insurance contracts in the statement of Financial Position (Dec-2018)	Presentation of insurance contract assets and liabilities in the statement of financial position determined using portfolios of insurance contracts rather than groups of insurance contracts.	Yes. The Staff expect the Exposure Draft to propose a consequential amendment to paragraph 99 of IFRS 17 so that when an entity discloses the reconciliations required by paragraphs 100–105 of IFRS 17, the entity presents, for each reconciliation, the net carrying amounts at the beginning and at the end of the period, disaggregated into a total for portfolios (rather than groups) of contracts that are assets and a total for portfolios (rather than groups) of contracts that are liabilities, that equal the amounts presented in the statement of financial position applying paragraph 78 of IFRS 17	No.

Implications for disclosure and transition requirements

Amendments the Board has tentatively decided to propose in response to the concerns and implementation challenges identified by stakeholders during their implementation processes:

		Staff recommendation to change?	
Topic	**Amendment tentatively decided**	**Disclosures**	**Transition**
8—Date of initial application of IFRS 17 (Nov-2018)	One-year deferral of the mandatory effective date of IFRS 17, so that entities would be required to apply IFRS 17 for annual periods beginning on or after 1 January 2022.	No. The Staff note that paragraphs 30 and 31 of IAS 8 detail the disclosure requirements for the expected impact of new IFRS which have not yet been adopted. An entity that does not early apply IFRS 17 would be required to provide those disclosures for one additional year.	No.
9—Temporary exemption from applying IFRS 9 (Nov-2018)	Amendment of the fixed expiry date for the temporary exemption in IFRS 4 Insurance Contracts from applying IFRS 9, so that all entities would be required to apply IFRS 9 for annual periods beginning on or after 1 January 2022.	No. The Staff note that entities that continue to apply IAS 39 are already required by IFRS 4 to make additional disclosures to enable users of financial statements to make comparisons with entities applying IFRS 9. An entity that defers the application of IFRS 9 by one additional year would provide those disclosures for that additional year.	No.

Implications for disclosure and transition requirements

Amendments the Board has tentatively decided to propose in response to the concerns and implementation challenges identified by stakeholders during their implementation processes:

		Staff recommendation to change?	
Topic	**Amendment tentatively decided**	**Disclosures**	**Transition**
10 – Transition (Feb-2019)	Additional specified modification to the transition approaches for the classification of a liability that relates to the settlement of claims incurred before an insurance contract was acquired.	No. Paragraph 115 of IFRS 17 already requires an entity to explain how it determined the measurement of insurance contracts at the transition date.	Not applicable.

- The Board voted unanimously to tentatively agree with the Staff recommendation to amend the Standard.

Next steps

IASB

- The IASB will discuss any sweep issues over its meeting during the week beginning on 8-12 April 2019. The Board plans to consider the package of amendments tentatively decided by the Board as a whole.
- The next TRG meeting will be held on 4 April 2019 in the IASB office in London.
- The IASB Technical Plan states that the ED amending IFRS 17 will be published by the end of Q2 2019.
- The Due Process Oversight Board has agreed to a short comment period (less than 120 days) for the responses to the questions in the upcoming ED.

Contact details

Francesco Nagari

Deloitte Global IFRS Insurance Leader

+852 2852 1977 or fnagari@deloitte.co.uk

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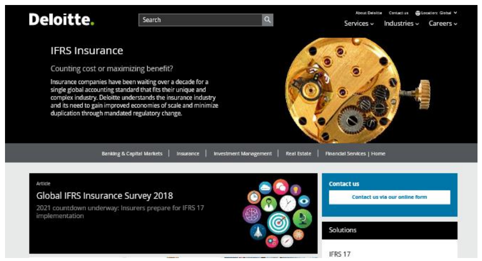

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