25 September 2019

Mr Hans Hoogervorst
Chairman
International Accounting Standards Board
Columbus Building
7 Westferry Circus
Canary Wharf
London E14 4HD
United Kingdom

Submission via ifrs.org

Dear Hans

Exposure Draft ED/2019/4 Amendments to IFRS 17

As the representatives of over 200,000 professional accountants in Australia, Chartered Accountants Australia and New Zealand (Chartered Accountants ANZ) and CPA Australia would like to thank you for the opportunity to comment on the above Exposure Draft (the ED). Our responses to specific questions raised in the ED are provided in the Appendix to this letter.

Our response has been informed by the Australian Accounting Standards Board Transition Resource Group (AASB TRG), which has been facilitating discussion of IFRS 17 implementation issues locally, monitoring and discussing IFRS 17 issues raised by the IASB TRG and IASB and has previously submitted responses to the IASB. We therefore encourage the IASB to consider the recommendations set out in the AASB's submission, as it addresses the issues raised in our responses.

If you have any questions about our submission, please contact either Gerrie Burger (Chartered Accountants ANZ) gerrie.burger@charteredaccountantsanz.com or Ram Subramanian (CPA Australia) at ram.subramanian@cpaaustralia.com.au.

Simon Grant FCA
Group Executive – Advocacy, Professional Standing and International Development
Chartered Accountants Australia and New Zealand

Gary Pflugrath CPA
Head of Policy and Advocacy
CPA Australia

Appendix

Responses to specific 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?

We support the proposed scope exclusions in (a) above. Where the inclusion of an insurance component is ancillary to the core services being provided through a financial instrument such as a credit card contract, we believe the costs of separately identifying the insurance component outweigh the benefits arising from doing so in accordance with IFRS 17.

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?

We agree with the proposed amendments for reasons set out in the ED and its Basis for Conclusions. We believe the proposals are generally appropriate, especially regarding insurance acquisition costs being recovered through future expected contract renewals. However, we would like to highlight three issues:

- The broad term, “expected to arise from renewal of the insurance contracts” in the proposed IFRS 17 paragraph B35A may potentially widen the ambit by including costs beyond those intended by the Basis for Conclusions. This may excessively increase the complexity of applying IFRS 17 regarding the amortisation of acquisition costs for insurance products that do not use the commission structures identified in the Basis for Conclusions. Entities that do not recover acquisition costs through future expected renewals would have to split between new and renewing contracts to expense acquisition costs over different amortisation periods of expected renewals. We believe the costs of changing reporting processes to split these would exceed the benefits and would not appropriately reflect the economics of the transactions.

  We suggest changing the wording in the proposed IFRS 17 paragraph B35A as follows:

  B35A
  To apply paragraph 28A, an entity allocates insurance acquisition cash flows that are directly attributable to a group of insurance contracts:
  a) *to that group; and*
  b) *to groups that include insurance contracts that are expected to arise from renewal of the insurance contracts in that group and are expected to recover the insurance acquisition cash flows.*

- 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. When applying IFRS 17 for the first time, historical information relating to the insurance contracts will be needed in order to measure this asset. We believe obtaining this information (including past expectations) retrospectively would be impracticable for many entities.

  We suggest that Appendix C be amended to provide exemption through a transitional provision:

  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 or recognition of any asset relating to insurance acquisition cash flows paid before a group of insurance contracts is recognised for insurance contracts without direct participation features.

Representatives of the Australian Accounting Profession

cpaaustralia.com.au

charteredaccountantsanz.com

(c) *Amounts related to the contractual service margin~~,or~~ loss component or 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.

- The wording in paragraph 28B(b) requiring entities to recognise an asset for "each existing or future group" is ambiguous in terms of aggregation. We believe the IASB intended the recognition of a single asset to represent the insurance acquisition cashflows in respect of all existing or future groups, before recognition of the group.

  We suggest amending the wording in paragraphs 28C, 28D and B35B to address this potential inconsistency. If, however, the intention was to create an asset for each group, we note this is a significant process redesign and would unduly disrupt implementation projects.

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?

We agree with the proposals as they will enable the entity to faithfully represent the investment services they provide in the relevant periods. However, in respect of the proposals in paragraph B119B(b), we suggest referring to an “investment return” rather than a “*positive* investment return.” It is not clear why there is a reference to a “positive” investment return.

We also have an additional request in relation to paragraph B65(1a), which clarifies that costs incurred in providing investment-return or investment-related services are included within the fulfilment cashflows. We are concerned that it is unclear whether costs associated with tax payments attributable to the policyholder that arise from investment-return or investment-related services are also included in the fulfilment cash flows. Since such taxes represent a cost to the insurer incurred for or on behalf of the policyholder (i.e. asset management costs as part of the cost of fulfilling the contracts per paragraph BC63), we suggest clarifying that these taxes also represent a cost to the insurer.

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?

We support amending IFRS 17 to allow the recognition of reinsurance recovery income when the entity recognises losses on onerous underlying contracts. 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.

We understand a significant portion of reinsurance contracts in the market may not meet the proposed amendment based on proportionate coverage. Excluding them with a narrow ‘proportionate’ definition would not deliver meaningful reporting. The proposed approach is likely to result in the different accounting treatment of reinsurance transactions that have the same economic effect. This would lead to the inconsistent treatment of reinsurance contracts with the same nature and substance, where there is a direct link between the expected reinsurance recoveries and the losses on the underlying contracts. The term ‘proportionate’ may also be arbitrary and inconsistently applied.

To address the suggested extension of the proposed amendment to include non-proportionate reinsurance, the corresponding reinsurance recoveries in relation to non-proportionate reinsurance could be determined by applying the recovery percentage (the total expected reinsurance recoveries as a proportion of the total expected underlying claims) to the onerous loss recognised in profit or loss.

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?

We agree with the proposed amendment to require separate presentation of insurance assets and liabilities at the level of the ‘portfolio’ being a higher level of aggregation than ‘group.’ However, we strongly support using *entity* as the unit of account for presentation of insurance assets and liabilities on the balance sheet. Preparers cannot see any benefit for users in providing this information at portfolio level. Therefore, we encourage a higher level of aggregation further still - at the ‘entity’ level.

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?

We agree with the proposed amendment.

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?

We would like to see at least a further one year deferral of IFRS 17 to 1 January 2022 to allow for a more strategic implementation approach to be adopted by affected entities. Several constituents within Australia would specifically support a further one year deferral of IFRS 17 to 1 January 2023.

(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?

We 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. A consistent mandatory application date for IFRS 9 and IFRS 17 is not a prevalent issue locally, 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?

In relation to Question 8(a), we agree with the proposed amendments. We consider that a business model approach is the preferred approach to determine the appropriate presentation for all contracts acquired under IFRS 17, whether through a business combination or the acquisition of a portfolio of contracts.

With the proposed addition of paragraph C9A, paragraph BC120 could be inferred to imply that all contracts acquired in their claims settlement period (after transition) should be treated as adverse development covers. If so, this may create potentially inconsistent accounting treatments for identical contracts purely due to the timing of when the portfolio was purchased. To address this, we seek clarification whether an “adverse development” cover (as intended by paragraph B5) is:

- A contract relating to a specific type of cover underwritten to provide cover in the future for development of claims incurred in the past; and/or
- 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.

We offer no comments in response to Questions 8(b) and 8(c).

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?

We agree with the proposed minor amendments.

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?

We agree with the proposed changed in terminology.

Other amendments to consider proposing

Cash flows in the boundary of a reinsurance contract held (paragraphs 34 and B61-B66 of IFRS 17 and ED/2019/4 BC180 – BC185) and discount rate used to determine adjustments to the contractual service margin (paragraphs 44 and B72 of IFRS 17 and ED/2019/4 paragraphs BC193-BC199)

As set out in the AASB TRG's response to the IASB October 2018 Board Agenda ref 2D dated 27 November 2018,[1] we believe that the use of current discount rates should apply to all aspects of the insurance standard, including the Contractual Service Margin (CSM). We support a change to IFRS 17 that would reduce or eliminate the accounting mismatch impact of using locked-in discount rates, as it would improve the information reported to users.

Interim reporting (paragraphs BC214-BC216)

We agree that the exception from IAS 34 should not be extended to internal interim reports (as proposed in paragraph BC215 of the ED). As there are substantive reasons against overturning IAS 34 paragraph 28, we further recommend that paragraph B137 be removed. We do not support the override of another standard without due process relating to that standard.

---

[1] With regard to the use of locked-in discount rates to adjust the contractual service margin (Topic 4) and reinsurance contracts held: expected cash flows arising from underlying contracts not yet issued (Topic 14)