International Actuarial Association
Association Actuarielle Internationale

25 September 2019

International Accounting Standards Board
Columbus Building
7 Westferry Circus
Canary Wharf
London
E14 4HD
UK

Dear Mr. Hans Hoogervorst
Chairman

Re: IAA comments on the Exposure Draft ED/2019/4 Amendments to IFRS 17

In response to the IASB's request for comments on the Exposure Draft ED/2019/4 Amendments to IFRS 17 (ED) published on 26 June 2019, I am pleased to transmit on behalf of the International Actuarial Association (IAA) our comments and recommendations.

Our comments are structured around the specific matters for comment in the ED.

These comments have been prepared by the IAA Insurance Accounting Committee. The IAA welcomes the opportunity to discuss these ideas further with you and to cooperate with IASB in the finalization of IFRS 17.

If you wish to discuss any of our feedback please do not hesitate to contact William Hines, Chair of the IAA Insurance Accounting Committee, via the IAA Secretariat.

Yours sincerely,

Gabor Hanak
President

Attachment: IAA Comments

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The International Actuarial Association and its Due Process

The International Actuarial Association (IAA) represents the international actuarial profession. Our seventy-three Full Member actuarial associations, listed in Appendix A, represent more than 95% of all actuaries practicing in over 115 countries around the world. The IAA promotes high standards of actuarial professionalism across the globe and serves as the voice of the actuarial profession when dealing with other international bodies on matters falling within or likely to have an impact upon the areas of expertise of actuaries.

We are pleased to be given the opportunity to provide input to the IASB on this important consultation. These comments have been prepared by the Insurance Accounting Committee of the IAA, whose current members are listed in Appendix B. These comments have been subject to the due process required for it to constitute a formal view of the IAA and will be posted to the IAA's official web site.

Our comments are as follows:
General Comments

We are broadly supportive of the proposed amendments to IFRS 17. We provide comments to the ED's specific questions below.

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)
No comment

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

We agree with the proposed amendment to require a portion of insurance acquisition cash flows that are directly attributable to a group to be allocated to groups outside the contract boundary that include expected renewals of the insurance contracts in that group. We believe this will improve the usefulness of information about the expected profitability of groups of newly issued contracts compared to groups of renewals of those contracts because this will better depict the underlying profitability of the contracts in line with the current practices of commissioning and patterns of acquisition cash flows.

Regarding the specific paragraphs, we offer the following comments:

Application of paragraph 28A to approaches other than PAA

We fear that IFRS 17.28A could be misinterpreted as applying in its entirety only when the premium allocation approach (PAA) is applied. We therefore suggest a revision to IFRS 17.28A such as:

"Unless insurance acquisition cash flows are recognized as expenses by the entity applying paragraph 59(a), the entity shall, irrespective of the valuation method, allocate insurance acquisition cash flows not recognized as expenses by applying paragraph 59(a) to a group of insurance contracts on a systematic and rational basis applying paragraph B35A."

We recommend a clarification to IFRS 17.28B so that the wording is made consistent with IFRS17.28C with regards to linking the acquisition costs to the underlying policies expected to be issued. The proposed wording is:

An entity shall recognize:

(a) insurance acquisition cash flows it expects to pay after the related insurance contracts are included in a group applying paragraph 28 as an expense within the fulfilment cash flows of the insurance contracts applying paragraph 32(a).

(b) insurance acquisition cash flows paid before the related insurance contract is included in the group applying paragraph 28 as an asset. An entity shall recognize such an asset for each existing or future group of insurance contracts to which insurance acquisition cash flows are allocated.

Linkage of Requirements for Allocation of Insurance Acquisition Costs to PAA

Paragraph 28C references paragraph 38(b), which is not relevant in the case of PAA. We therefore suggest adding references to paragraph 55(a)(iii) to clarify the approach under PAA. We also recommend including in the subparagraphs of IFRS 17.38 where costs would be recognized if they are not included in the measurement of the CSM.

Adjustment to Asset for Impairment

IFRS 17.28D: If facts and circumstances indicate that the asset may be impaired, the entity assesses the recoverability. Only if that assessment results in an impairment, the carrying amount is adjusted. The second sentence says that if facts and circumstances indicate that the asset MAY be impaired. It could be read as a choice or something less definitive than a determination of impairment could lead to adjusting the carrying amount. We recommend that the language be clear that the carrying amount is adjusted only when an impairment is deemed to take place.

Scope of Insurance Acquisition Costs

IFRS 17.B35A: Many insurance companies distribute their products using commission structures that pay higher commissions for writing certain volumes (e.g., 100) of insurance contracts. The higher commission is directly related to the contracts written. When applying IFRS 17 to the contracts written, they could be divided into several groups of insurance contracts for measurement purposes. The proposed amendment to IFRS 17.B35A appears to allow only those costs that are directly attributable to a particular IFRS 17 accounting group and not allow costs directly attributable to a collection of groups within a portfolio (such as the 100 contracts in our example) to be allocated to individual groups. This is inconsistent with IFRS 17.B65 (e) which requires that insurance acquisition cash flows, which are by definition directly attributable to the portfolio of insurance contracts, be considered in the measurement of the contracts in that portfolio. The current IFRS 17.27 uses the phrase "relating to a group" to express the apportioning of the total insurance acquisition cash flows to the individual groups. The proposed amendment to IFRS 17.28A uses already the phrase "systematic and rational basis" in referring to paragraph B35A and paragraph B35A should be consistent.

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In addition, 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.*

If the proposed wording of B35A is interpreted to mean that all directly attributable insurance acquisition costs are incorporated, irrespective of whether they are recovered through future renewals, then entities would require processes to split between new and renewing contracts to facilitate deferral and amortisation over different periods of expected renewals. This could result in significant process redesign and potentially unduly disrupt implementation projects as well as fundamentally change the principle in IFRS 17 relating to acquisition cash flows which go against the IASB staff's criteria for proposed changes.

We recommend rewording of IFRS 17.B35A to read as follows to address these issues:

To apply paragraph 28A, an entity allocates insurance acquisition cash flows related to a group of insurance contracts, on a systematic and rational basis:

- *(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.*

Impact on PAA eligibility

Allowing the recognition of an asset for insurance acquisition expenses paid before the group of insurance contracts (to which they are allocated) is recognized has an impact on the assessment of eligibility for the premium allocation approach. In particular, is the assessment required under IFRS 17.53(a) before or after the recognition of any insurance acquisition expenses, or can the decision as to whether to recognize such an asset be taken after making this assessment?

Transition and Acquisition Expenses

The requirement to recognize the asset proposed in 28B(b) is expected to add significant cost and complexity to implementation of IFRS 17 given that retrospective application is likely to be impracticable for many insurers.

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.

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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.

We suggest the following amendments 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 recognition of any asset relating to insurance acquisition cash flows paid before a group of insurance contracts is recognised</u> for insurance contracts with direct participation features.*

*<u>[Title before IFRS 17.C11] **Determining the contractual service margin, ~~or~~ loss component, or insurance cash flows for groups of insurance contracts without direct participation features**</u>*

<u>C16A To the extent permitted by paragraph C8, and if not applying the premium allocation approach by applying paragraph 59(a), 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</u>.

*<u>[Title before IFRS 17.C17] **Determining the contractual service margin, ~~or~~ loss component or insurance cash flows for groups of insurance contracts with direct participation features**</u>*

<u>C17A To the extent permitted by paragraph C8, and if not applying the premium allocation approach by applying paragraph 59(a), 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</u>.

<u>C20B To apply the fair value approach and if not applying the premium allocation approach by applying paragraph 59(a), 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</u>.

Recoverability Test

We agree that the recoverability of an asset set up for insurance acquisition cash flows paid before initial recognition of the group to which the cash flows are allocated should be assessed for each group as required by paragraph B35B(a). However, we do not agree with the additional test of the recoverability of the portion of each group's asset that arose from the insurance acquisition cash flows noted in 2(a). This additional impairment test would add significant complexity to implementation by adding an aspect of measurement within group – i.e., within the unit of account of measurement. Furthermore, in our view, this additional impairment test is unnecessary, as there is no reason to differentiate between recoverability of the portion of the DAC that arose from paragraph 35A cash flows and the portion that arose from other cash flows. Paragraph B35B(b) should be removed.

Furthermore, with respect to IFRS 17.B35C (reversal of impairment loss), it is our understanding from discussion with IASB Staff that the IASB did not intend to require such reversal at the time the DAC itself is derecognized because of initial recognition of its associated group of contracts (paragraph IFRS 17.38(b) or IFRS 17.55(a)(iii)). In other words, there is no requirement to write the DAC back up immediately before it is derecognized when initial recognition of the group indicates that the DAC was less impaired than the DAC balance at the end of the prior reporting period indicated, as this would require an arbitrary attribution of revenue to sources of loss. The amendments are unclear on this point, so we would suggest clarifying that the tests in paragraphs IFRS 17.35B and IFRS 17.B35C need only be undertaken at the end of each reporting period.

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)

We agree with the proposed amendment to require an investment service (under both the general model and variable fee approach) to be considered when allocating the contractual service margin using coverage units. This better reflects the services provided under insurance contracts than the current requirements in IFRS 17. However, we are concerned about how the amendment, coupled with the change in the definition of investment component, would work in practice. We believe that certain elements of the proposed amendments are likely to cause confusion and inconsistent application. In particular:

3(a)

We question whether the amount available to withdraw is the correct focus and whether it should instead be benefits whose value depends on the provision of an investment service. The amount of investment return service that is to be reflected is not clear in situations where the amount to which the policyholder has the "right to withdraw" in the current period is limited by the contract to a subset of the amount of investment return credited to the contract. We recommend deleting IFRS 17.B119B (a) and changing paragraph IFRS 17.B119B (b) to read:

"Insurance contracts may provide an investment-return service if the entity expects the investment component or underlying items related to rights to receive future services or withdraw amounts to include a positive investment return."

Positive Investment Return Definition

IFRS 17.B119B(b) – In identifying investment-return service, the meaning of "positive investment return" is unclear. Without the parentheses, "positive" clearly means "greater than zero". The parenthetical comment that a positive investment return could be below zero suggests that the word "positive" means "greater than something", in this context, but what is "something"? Risk-free rates? An example

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of a product for which the answer to this question is critical is permanent whole life insurance contracts with fixed guaranteed cash surrender values. The cash surrender values are investment components, but they may or may not provide investment-return service depending on the meaning of the word "positive" in IFRS 17.B119B(b). If "positive" means "greater than zero", then cash surrender values would provide investment-return services, but if "positive" means "greater than risk-free rates", then cash surrender values may or may not provide investment-return services (depending on the rate credited).

IFRS 17.B119B(c) – In identifying investment-return service, it is unclear what is meant by "investment activity to generate that positive investment return". In the cash surrender value example above, the entity undertakes investment activity by investing premiums received before claims are paid, but that activity would take place to the entire investment regardless of whether the entire or a part of the investment is not subject to a withdrawal right.

The ED proposes amendments to paragraph IFRS 17.34 to reflect the new term insurance contract services. We are concerned that the wording for defining a substantive obligation would not reflect all types of investment services without further adjustment. We recommend inserting a new clause (a) before the existing (a) which would read as follows:

(a) the entity has the practical ability to set a price for investment-return services or investment-related services that fully reflect the expected cost of providing those services AND

Cash Flows Within Contract Boundary

Paragraph IFRS 17.B65 is also relevant to the topics addressed in Question 3. The amendment to paragraph B65 brings into the cash flows to be considered within the contract boundary "costs the entity will incur in providing an investment-return service (for insurance contracts without direct participation features) or an investment-related service (for insurance contracts with direct participation features)." It is possible that some or all of these costs are subject to the accounting requirement of other IFRS standards and thus an entity will need to be careful not to double count these amounts in their financial statements. For example, in certain cases IFRS 9 requires that investment management costs be included in the measurement of a financial instrument.

We understand the changes in paragraph IFRS 17.B65 mean that investment management expenses are only included in the fulfilment cash flows when there is an investment service present. In those periods there is a potential double accounting in profit and loss where those expenses are recognised both when reducing the investment return and in the investment service result.

3(b)

We see no need to exclude direct participating contracts from the definition of investment-return services, as such contracts could include such in addition to investment-related services (e.g. a choice of policyholders between a unit fund and a fixed interest investment).

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3(c)

We understand that the additional disclosures will provide more information to users of financial statements.

The adjustments to the definition of liability for incurred claims and liability for remaining coverage create uncertainty as to what elements of a contract judgement will be applied when determining which liability category is appropriate. The discussion at the September 2018 IFRS 17 Transition Resource Group meeting appeared to have a consensus that certain liabilities could be considered part of a liability for remaining coverage or a liability for incurred claims. The meeting summary noted that "it is a matter of judgment for an entity to develop an accounting policy that reflects the insurance service provided by the entity to the policyholder under the contract in accordance with IFRS 17." We believe that the exercise of judgment should not be altered by the proposed amendments to include investment return or related services in the allocation of the CSM.

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

We agree with the goal of the proposed amendment to adjust the CSM of a group of reinsurance contracts held to offset the portion of a loss on initial recognition of onerous underlying contracts that will be recovered by reinsurance, as this will improve the usefulness of information about the profitability of the entity's insurance business. We believe that an entity should be able to recognise a gain from reinsurance contracts held when a 'day one loss' is initially recognised on underlying business, provided there is a direct link between the losses on the underlying contracts and the net gain on reinsurance contracts held. To this end we would recommend extending the scope of the amendments to all contracts with such a direct link.

We agree with defining the eligible loss recovery as the recovered portion of the initial loss on the underlying contracts. This is a simple, practical approach that achieves the objective of improving matching and therefore the usefulness of information about the profitability of the entity's insurance business

Definition of Proportionate

We understand the IASB may not want to apply the exemption to all reinsurance contracts held but limit it to those where a direct link between the losses on the underlying business and the gain from the reinsurance contract held is clearly present. In that case, we believe that the reference to "proportionate" reinsurance is too narrow and may result in many reinsurance contracts that provide such a direct link being excluded from recognizing the recovery of losses and thus the amendment being of limited use.

In paragraph IFRS 17.B119C (and Appendix A) the requirement for "a fixed percentage of all claims incurred on a group of underlying contracts" excludes common types of proportional reinsurance contract such as surplus reinsurance, catastrophe reinsurance, stop loss and excess of loss contracts.

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The restricted definition of proportionate excludes further groups that contain underlying contracts with different fixed percentages reinsured. For example, if some contracts were 50% reinsured and others 60% reinsured, the amendment would not apply. If the description of proportionate coverage is not changed, entities would be forced to refine their groups so that all contracts in the group share the same fixed percentage reinsured.

In addition, most quota share (generally thought of as proportional) arrangements will include some level of retention or limit of claims by the insurer which may not match exposure of the direct writer. As such they will therefore not meet the requirement of a reinsurance contract held that provides an entity with the right to recover from the issuer a percentage of all claims incurred on groups of underlying insurance contracts.

We believe that the reasoning given in IFRS 17.BC67-BC90 for the proposed amendment apply equally to each of the types of reinsurance arrangements noted above. Thus, we recommend that the description of proportionate coverage in paragraph IFRS 17.B119C be revised from

"…. fixed percentage of all claims incurred…." to *"…..known portion of each claim incurred…"*, with a corresponding change to Appendix A.

Consequently, paragraph B119D would be modified to

"An entity shall determine the adjustment to the contractual service margin and the resulting income recognised applying paragraph 66A as the portion of cash flows of the group of underlying insurance contracts that the entity has a right to recover from the group of reinsurance contracts held."

Recognition of Reinsurance Contracts

We do not believe that there is any need to differentiate in initial recognition between proportionate and non-proportionate reinsurance contracts held. The differentiation was introduced in 2011 to distinguish the contract boundary of reinsurance contracts held, not the initial recognition date. The tentative decision of 2011 regarding contract boundary was later reworded to refer to the initial recognition. Reinsurance contract coverage can, by definition, not commence before coverage of any underlying contract commences.

Some practitioners have found the reference to "or on addition of onerous underlying insurance contracts to that group," in paragraph 66A confusing. We believe that adding an example to the implementation guidance of such a case would be useful.

We are also of the view that the variable fee approach should be extended to apply to reinsurance contracts issued. For example, it is common in many markets for large-scale transfers of business to be initially effected through reinsurance treaties (covering both non-financial and financial risk) which can last for several years and the risk mitigation option would not apply. In other cases, there is a cooperation between two life insurers, the first issuing a direct contract to policyholders the second issuing a contract to the first life insurer transferring the mortality risk of the first contract to the second life insurer, i.e. being a reinsurance contract according to definition. However, the second contract is except the reference to the mortality of the first contract a normal participating contract in the collective pool of underlying item of the second life insurer. The first life insurer does not itself provide any investment service but the first contract refers to the participation granted under the second contract to be forwarded to the policyholder. The second insurer provides to the policyholders of the first insurer indirectly the same services as it provides to its direct policyholders. In addition, it is noted in paragraph IFRS 17.BC213 that the reason for excluding reinsurance issued from the variable fee approach was due to the fact that these contracts are insurance contracts and do not provide investment related services, but such contracts often do. The application of the variable fee approach to the direct contracts is not restricted to investment-related contracts. Thus, we recommend that reinsurance held and issued are permitted to be measured under the variable fee approach where the eligibility conditions in IFRS 17.B101 are met. In most common reinsurance contracts those conditions would not be met since reinsurers do not share their surplus with their cedants, they just provide certain claims-contingent premium refunds as many direct non-life insurance contracts do as well.

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

We agree with the proposed amendment to change the requirement for separate presentation of positive and negative insurance contract liabilities from the group level to the portfolio level as it provides significant implementation relief with no loss of useful information.

Further, we would support eliminating the need for separate presentation of the insurance liability in its entirety, as the separation does not provide useful information and could be confusing. The measurement of insurance contract liabilities includes all future inflows as well as all future outflows, and whether the total is positive or negative is usually a matter of the timing of inflows versus outflows rather than a reflection of expected profitability or of the status of rights or obligations (e.g., future non-enforceable premium that do not qualify as a stand-alone asset). Appropriate information about profitability will be in the disclosures – most importantly the separate disclosure of CSM and the new business disclosure requirements. Neither groups nor portfolios of insurance contracts represent insurer's off-setting rights since there are none between the legally independent contracts.

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

We agree with the proposed amendment to extend the risk mitigation option to circumstances when an entity uses reinsurance contracts held to mitigate financial risk arising from insurance contracts with direct participation features, as this solves the primary concern (mismatch) arising from the paragraph IFRS 17.B109 restriction that reinsurance contracts held cannot be insurance contracts with direct participation features for the purposes of IFRS 17. However, we think it would be helpful to point to IFRS 17.B128(c) to clarify that any risk in the underlying items is considered "financial" risk, because some stakeholders are (mistakenly) concerned that reinsurance of, say, mortality risk, in the underlying items would not be covered by the extension of the risk mitigation option.

Furthermore, in our view, the risk mitigation option should be extended to circumstances where financial risk is hedged with assets other than derivatives if those assets perform the same function as derivatives. For example, hedging a minimum guaranteed return can be accomplished by (a) purchasing a put option or (b) purchasing a combination of fixed income assets and derivatives that mimics the cash flows of the put option but less expensively. Since the risk mitigation option applies to (a), it should also apply to (b), provided the entity meets the requirements of paragraph IFRS 17.B116.

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)

We agree that the effective date of IFRS 17 should be deferred. We also agree with extending the temporary exemption from IFRS 9 to the effective date of IFRS 17.

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

We agree with the proposed amendment to permit the application of the fair value approach even if retrospective application is not impracticable if the group meets criteria relating to the risk mitigation.

However, we believe there are other circumstances in which the fair value approach should be permitted even if retrospective application is not impracticable. In particular, the fair value approach should be permitted whenever retrospective application would take <u>undue</u> cost and effort. This adds an element of judgement, but without it the Standard contains, by definition, the potential to create an undue burden on implementation. It appears that the accounting interpretation of the word "impracticable" in IAS 8 has evolved to ignore the cost and effort required to do the calculations, and though this might be reasonable for retrospective application of a Standard that affects only a small part of the business, we believe it is an unreasonable burden for insurance companies implementing IFRS 17. In our view, the extensive disclosures required for blocks using different transition approaches adequately addresses any concern that adding this element of judgement might reduce comparability.

We also welcome the extension of the risk mitigation option (question 8(b)) such that it can now apply prospectively from the date of transition rather from the date of initial application.

However, where an insurer has historically hedged financial risk in respect of business accounted for under the variable fee approach, past movements in the fair value of hedging instruments (prior to the date of transition) will have been taken through P&L into shareholder equity under IFRS 9 Financial Instruments whereas movements in the value of hedged items over that period will have been taken to CSM. As hedging is fundamental to how insurers manage and mitigate financial risk, this will result in a misstatement in shareholder equity at the date of transition and in profit emergence in future years.

The fair value transition option (question 8(c)) as an alternative to retrospective application of the hedge adjustment does not resolve the issue described above. The fair value approach is a different measurement basis to either the fully retrospective or the modified retrospective approach and, as such, it is to be expected that in many circumstances it will result in a different CSM at transition. For example:

- In an environment of decreasing interest rates where the predominant risk that is hedged is interest rate risk, the CSM at transition is likely to be higher on a fair value basis than on a retrospective basis.

- In an environment of equity growth where the predominant risk that is hedged is equity risk, the CSM at transition is likely to be lower on a fair value basis than on a retrospective basis.

This would result in a lack of comparability between portfolios that are or are not hedged, between portfolios subject to different types of risk, between business written before and after the transition date and, consequently, between entities.

Retrospective application of the risk mitigation option for periods prior to the date of transition would better reflect the actual economic performance of historic hedging relationships. We acknowledge the IASB's concerns regarding whether such retrospective application could be achieved without the use of hindsight and the risk of 'cherry-picking'. However, we believe that such concerns can be addressed by restricting the risk mitigation option to circumstances where the company can demonstrate, using reasonable and supportable information, that a documented and internally approved hedging strategy was in place.

Contracts Acquired in Claims Settlement

When an insurer acquires contracts in their claims settlement period they are typically classified as a liability for incurred claims unless the insurer acquires contracts whose nature is 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). 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 insurance business 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 would add significant operational complexity and cost with minimal information benefit from a user's standpoint. 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.

We contrast this treatment with the acquisition of financial instruments. IFRS 3 introduces requirements for re-measurement for financial instruments, but doesn't change the "classification" of the financial instrument itself. Whereas the application of IFRS 3 to insurance contracts accounted for under IFRS17 is potentially "reclassifying" the insurance contract. This change in classification will confuse users and drive up costs of IFRS 17 implementation on an ongoing and lasting basis.

In practice 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.

We 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. This is also consistent with the conclusions reached by the IFRS 17 Transition Resource Group (TRG) in its September 2018 meeting.

We suggest the following clarifications be made to IFRS 17.B5:

B5 Some insurance contracts <u>are issued to</u> cover events that have already occurred, but the financial effect of which is still uncertain. An example is an insurance contract <u>issued</u> that provides coverage against an adverse development of an event that has already occurred. In such contracts, the insured event is the determination of the ultimate cost of those claims. <u>Contracts acquired either fully or partially in their claims settlement period would also be accounted for as adverse development covers when, from the acquiring insurer's perspective, the character of the portion of the contract in its claims settlement period is in the nature of an adverse development cover.</u>

Question 9—Minor amendments (BC147–BC163)

B96(d), BC158 – The amendment to paragraph B96(d) introduces a measurement difference based on a presentation choice (whether to disaggregate the change in risk adjustment between financial and non-financial causes). However, in the past, when preparers argued that the discount rate used to unlock the CSM (B72(c)) should be the locked-in rates if the OCI option is elected but the current discount rates otherwise, the IASB refuted the argument by saying that measurement cannot be different because of a presentation choice. Now that B96(d) has been changed, we would ask the IASB to reconsider whether the discount rates in B72(c) should be chosen to match the impact on profit and loss.

Also, we observe that, due to differences in wording between the amended B96(d) and paragraph 81, it may not be entirely clear that there is a single disaggregation choice that applies to both paragraphs. We therefore suggest the use of consistent wording and a cross-reference between the paragraphs to clarify.

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B128(c), BC161 – Starting from the simplifying reference to an "investment-related service" and an "investment return" in IFRS 17.B101 the IASB concluded that changes in the fulfilment cash flows (and CSM) based on changes in the (fair value of) underlying items represent an effect from financial risk. Purpose of the simplification was to allow an easier access to the highly complex concept of participating contract but not to represent the reality. In reality, changes in the value of policyholder's rights from participation features may be driven in large part from changes in the policy's mortality experience, associated reinsurance results and cost experience all of which are required by IFRS 17 to be presented in the insurance service result since they are not subject to financial risk. In a low interest environment such as currently observed, changes in policyholders' rights might be predominantly caused by such sources. When the driver of the change in value of the underlying item is presented as non-financial risk, presenting the change in value of the underlying item as insurance finance expense would not be a faithful representation. We therefore recommend eliminating the amendment in paragraph B128 (c).

B107(b)(i) – The exposure draft paragraph B107 b (i) has been changed to say "over the duration of the insurance contract" , whereas previously it said "over the duration of the group of insurance contracts." Changing "group of insurance contracts" to "insurance contract" in this context could be misconstrued as a further restriction on the scope of contracts meeting the definition of insurance contracts with direct participation features. For example, in discussion at the February 2018 TRG meeting (item S26 of AP07), paragraph B107 was used to explain that contracts need not pay the fair value of underlying each year, but rather over time. However, this is done in pools, not contract-by-contract. An assessment at the contract level would require significant additional level of effort and cost and it is unclear that there is much benefit in term of useful financial reporting. We therefore suggest the IASB reverts to the previous wording.

Other topics

Annual Cohorts for mutualized participating contracts measured using VFA: We recommend an exception to the requirement to restrict the grouping of mutualized participating contracts using the annual cohort be added to IFRS 17 for contracts measured using the Variable Fee Approach as annual cohorts do not provide useful information for these products.

This point is of paramount importance for jurisdictions whose insurance market includes significant amounts of mutualized participating investment and insurance contracts with direct participation features.

These contracts share participating mechanisms based on the returns of an underlying pool of items that back all generations (i.e., multiple annual cohorts) and where the adjustments to the contractual service margins of cohorts depend on mutually each other. That dependence occurs only when the variable fee approach is applied; if the general measurement approach is applied those adjustments are recognized in the profit and loss and the mutual dependence doesn't occur. Moreover, appropriate asset-liability management requires that asset allocation is determined considering expectations and associated risks of all contracts.

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As a consequence, grouping by annual is burdensome and produces artificial cash-flow allocations to annual cohorts that do not reflect contractual and economic features of contracts.

We believe that under the Variable Free Approach group of contracts with cash-flows that affect or are affected by cash-flows of other group of contracts that would otherwise be in separate annual cohorts should be exempted from considering annual cohorts for grouping.

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Appendix A

Full Member Associations of the IAA (73 members)
25 September 2019

Asociación Centroamericana de Actuarios (ACEA)
Caribbean Actuarial Association
Consejo Profesional de Ciencias Económicas de la Ciudad Autónoma de Buenos Aires (Argentina)
Actuaries Institute Australia (Australia)
Aktuarvereinigung Österreichs (AVÖ) (Austria)
Institut des Actuaires en Belgique (Belgique)
Aktuarsko Drustvo U Bosni I Hercegovini (Bosnia and Herzegovina)
Instituto Brasileiro de Atuária (IBA) (Brazil)
Bulgarian Actuarial Society (Bulgaria)
Canadian Institute of Actuaries/Institut Canadien des Actuaires (Canada)
China Association of Actuaries (China)
Actuarial Institute of Chinese Taipei (Chinese Taipei)
Asociación Colombiana de Actuarios (Colombia)
Institut des Actuaires de Côte d'Ivoire (Côte D`Ivoire)
Hrvatsko Aktuarsko Drustvo (Croatia)
Cyprus Association of Actuaries (Cyprus)
Ceská Spolecnost Aktuárù (Czech Republic)
Den Danske Aktuarforening (Denmark)
Egyptian Society of Actuaries (Egypt)
Eesti Aktuaaride Liit (Estonia)
Suomen Aktuaariyhdistys (Finland)
Institut des Actuaires (France)
Deutsche Aktuarvereinigung e. V. (DAV) (Germany)
Actuarial Society of Ghana (Ghana)
Hellenic Actuarial Society (Greece)
Actuarial Society of Hong Kong (Hong Kong)
Magyar Aktuárius Társaság (Hungary)
Félag Islenskra Tryggingastærðfræðinga (Iceland)
Institute of Actuaries of India (India)
Persatuan Aktuaris Indonesia (Indonesia)
Society of Actuaries in Ireland (Ireland)
Israel Association of Actuaries (Israel)
Istituto Italiano degli Attuari and Ordine degli Attuari (Italy)
Institute of Actuaries of Japan (Japan)
Japanese Society of Certified Pension Actuaries (Japan)
Actuarial Society of Kazakhstan (Kazakhstan)
The Actuarial Society of Kenya (Kenya)
Latvijas Aktuaru Asociacija (Latvia)
Lebanese Association of Actuaries (Lebanon)

Full Member Associations of the IAA (73 members)
25 September 2019
Continued….

Lietuvos Aktuaru Draugija (Lithuania)
Macedonian Actuarial Association (Macedonia)
Persatuan Aktuari Malaysia (Malaysia)
Colegio Nacional de Actuarios A. C. (Mexico)
Association Marocaine des Actuaires (Morocco)
Het Koninklijk Actuarieel Genootschap (Netherlands)
New Zealand Society of Actuaries (New Zealand)
Nigeria Actuarial Society (Nigeria)
Den Norske Aktuarforening (Norway)
Pakistan Society of Actuaries (Pakistan)
Actuarial Society of the Philippines (Philippines)
Polskie Stowarzyszenie Aktuariuszy (Poland)
Instituto dos Actuários Portugueses (Portugal)
Asociatia Romana de Actuariat (Romania)
Russian Guild of Actuaries (Russia)
Udruzenje Aktuara Srbije (Serbia)
Singapore Actuarial Society (Singapore)
Slovenska Spolocnost Aktuarov (Slovakia)
Slovensko Aktuarsko Drustvo (Slovenia)
Actuarial Society of South Africa (South Africa)
Institute of Actuaries of Korea (South Korea)
Col.legi d'Actuaris de Catalunya (Spain)
Instituto de Actuarios Españoles (Spain)
Actuarial Association of Sri Lanka (Sri Lanka)
Svenska Aktuarieföreningen (Sweden)
Association Suisse des Actuaires (Switzerland)
Society of Actuaries of Thailand (Thailand)
Actuarial Society of Turkey (Turkey)
Association of Consulting Actuaries Limited (United Kingdom)
Institute and Faculty of Actuaries (United Kingdom)
ASPPA College of Pension Actuaries (United States)
Casualty Actuarial Society (United States)
Conference of Consulting Actuaries (United States)
Society of Actuaries (United States)

Appendix B

Members of the IAA Insurance Accounting Committee (25 September 2019)

William Hines	Chair
Maximilian Happacher	Co-Vice-Chair
Yoshio Nakamura	Co-Vice-Chair
Jacques Tremblay	Co-Vice-Chair
Gunn Albertsen	Den Norske Aktuarforening
Daniel Barron	Israel Association of Actuaries
Joaquin Benavides	Instituto de Actuarios Españoles
Robert F. Berendsen	Canadian Institute of Actuaries
Steve Cheung	Actuarial Society of Hong Kong
Antonella Chiricosta	Istituto Italiano degli Attuari and Ordine degli Attuari
Brendan Counsell	Actuaries Institute Australia
Leticia Doherty	Instituto Brasileiro de Atuária (IBA)
Alexander Dollhopf	Svenska Aktuarieföreningen
Ann Duchêne	Institut des Actuaires en Belgique
Stefan Engeländer	Deutsche Aktuarvereinigung e. V. (DAV)
Andrew David Gallacher	Association Suisse des Actuaires
Rokas Gylys	Lietuvos Aktuaru Draugija
Tara Hansen	Society of Actuaries
Judit Hauer	Magyar Aktuárius Társaság
Armand Maurice Ibo	Institut des Actuaires de Côte d'Ivoire
Changwon Im	Institute of Actuaries of Korea
Dragica Jankovic	Udruzenje aktuara Srbije
Gareth Kennedy	Casualty Actuarial Society
Tatsuhito Kondo	Institute of Actuaries of Japan
Christoph Krischanitz	Aktuarvereinigung Österreichs (AVÖ)
Mustapha Lebbar	Association Marocaine des Actuaires
Kristine Lomanovska	Latvijas Aktuaru Asociacija
Jesús Alfonso Zuñiga San Martin	Colegio Nacional de Actuarios A. C.
Brian Morrissey	Society of Actuaries in Ireland
Boatemaa Kakra Duffuor-Nyarko	Actuarial Society of Ghana
Ana Maria Martins Pereira	Instituto dos Actuários Portugueses
Andreja Radic	Hrvatsko Aktuarsko Drustvo
Jenny Maria Thers Rée	Den Danske Aktuarforening
Kyle Rudden	Caribbean Actuarial Association
Sunil Sharma	Institute of Actuaries of India
Jaanus Sibul	Eesti Aktuaaride Liit
Mateja Slapar	Slovensko Aktuarsko Drustvo
John Laurence Smith	New Zealand Society of Actuaries

Members of the IAA Insurance Accounting Committee (25 September 2019)
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Petr Sotona	Ceská Spolecnost Aktuárù
Pierre Therond	Institut des actuaires
Arseny Timakov	Russian Guild of Actuaries
Tatiana Tkácová	Slovenska Spolocnost Aktuarov
Ernst Visser	Het Koninklijk Actuarieel Genootschap
Andrew James Warren	Actuarial Society of South Africa
Derek Wright	Institute and Faculty of Actuaries
Jeng-Shiu Ye	Actuarial Institute of Chinese Taipei
Yuanhan Zhang	China Association of Actuaries

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