

IFRS 9 deferral ready to go, Phase II presentation confirmed and disclosures reassessed and amended

A quiet session but two main issues remain unresolved

Francesco Nagari
Deloitte Global IFRS Insurance Lead Partner
2 November 2015



Agenda

- **Highlights of the IASB meetings on 21 October 2015**
- **Detailed analysis of the IASB Staff analysis, discussion and IASB decisions**
- **Next steps**

Highlights

- The IASB took a series of minor decisions regarding their September decision to defer IFRS 9 for insurer including the **comment period** for the new ED (**60 days**) which is target for **publication in December**.
- IFRS 9 transition provisions were refreshed against the deferral decision. The **election to reassess the business model for assets designated as backing insurance liabilities** is given and it would be applied retrospectively on adoption of IFRS 4 Phase II. A set of **new disclosures** were approved.
- The **mirroring approach** from the 2013 ED has been **repealed** from the future IFRS and it will not be required or permitted. The issues on **indirect participating contracts** remain a final material unresolved matter together with the **unit of account**.
- **Presentation** and the new revenue requirements were **confirmed**, again.
- **Disclosures** were **amended to eliminate** the reconciliation of revenue to premium due and the reconciliation between P&L and OCI when the OCI solution is used. The latter will be replaced by new disclosures in line with the September decisions. **New disclosures** on the VFA “hedge accounting” were approved and the requirement to disclose the CSM future release pattern (quantum and timing – qualitative disclosure is possible)

Different effective dates of IFRS 9 and the new insurance contracts Standard

Overview

- In September the IASB decided, after the Chairman had exercised a casting vote, to propose a package of temporary measures in relation to the application of IFRS 9 before the new insurance contracts Standard come into force.
- These temporary measures would **amend IFRS 4** to:
 - Permit a reporting entity whose activities are predominantly insurance a **temporary exemption from applying IFRS 9 until the earliest of the entity's adoption of the new insurance contracts Standard or 1 January 2021** ((the 'Deferral Approach')
 - Give entities issuing insurance contracts that implement IFRS 9 the option to remove from profit or loss some of the accounting mismatches and temporary volatility that could occur before the new insurance contracts Standard is implemented (**the 'Overlay Approach'**).
- At the October meeting the IASB discussed how those measures would apply to first-time adopters and set the comment period.

Different effective dates of IFRS 9 and the new insurance contracts Standard

Comment period for an ED to amend IFRS 4

Staff recommendation

- The IASB should expose the proposed temporary measures for 60 days, on the grounds that it is urgent and narrow in scope because they are optional.
- The Staff expect to be able to publish the exposure draft in December 2015, with the intention of finalising the package in the third quarter of 2016.

IASB discussion and decision

- The Staff noted that the predominance threshold example in the ED will state that it is not passed if only 75% of an entity's liabilities are within the scope of IFRS 4.
- The Board unanimously agreed with the Staff recommendation to have a comment period of 60 days.

Different effective dates of IFRS 9 and the new insurance contracts Standard

Use of the deferral and overlay approaches by first-time IFRS adopters

Staff recommendation

- First-time IFRS adopters should be prohibited from using either the deferral or the overlay approaches, as it is unlikely to be relevant to first-time adopters and the arguments about comparability being undermined are not relevant.

IASB discussion and decision

- Both of these approaches require information resulting from applying IAS 39 in part or in full, which in itself would be a new requirement for first-time adopters .
- Both approaches are intended to address concerns regarding transition and are considered not to be relevant to first-time adopters.
- The recommendation is consistent with the principles of IFRS 1 of applying the current versions of IFRS and enhancing comparability within the entity over time.
- The IASB unanimously agreed with the staff recommendation to prohibit either of the approaches in the temporary package by first-time adopters.

Different effective dates of IFRS 9 and the new insurance contracts Standard

Next steps and timing for amendment of IFRS 4

Next steps	Expected timetable
ED is published to amend IFRS 4	December 2015
60 day comment period ends	February 2016
Re-deliberations on the ED proposals	Second quarter of 2016
Amendments to IFRS4 issued	Third quarter of 2016

Insurance contracts – Classification and measurement of financial assets on transition

Summary

- For entities that decide or need to adopt IFRS 9 prior to the new insurance contracts Standard, with or without the overlay approach, the Board considered whether to permit insurers to reassess their business models for IFRS 9 purposes upon transition to the new insurance contracts Standard.
- For example, entities that:
 1. fail the predominance test on 1/1/2018 and have to adopt IFRS 9
 2. decide to adopt IFRS 9 in 2018 even if they pass the predominance test
 3. have already early adopted IFRS 9

Insurance contracts – Classification and measurement of financial assets on transition

Staff recommendations

Recommendation 1

- Permit entities to reassess the business model for financial assets *designated as related* to contracts within the scope of the new insurance contracts Standard.
- Would apply to assets held to fund insurance contracts based on expected levels of claims and expenses and surplus assets held in case of unexpected increases in insurance liabilities. They would not apply to other financial assets held by an entity for a purpose clearly other than backing insurance contracts.
- On transition entities would be permitted to designate and de-designate equity investments with regards to the equity presentation.
- On transition both mandatory and elective use of the Fair Value Option can be reassessed and changed

Insurance contracts – Classification and measurement of financial assets on transition

Staff recommendations

Recommendation 2

- The reassessment would be based on the facts and circumstances existing on initial application of the new insurance contracts Standard (i.e. the beginning of the latest period presented) with new classifications/designations applying retrospectively. Any resulting changes would adjust opening retained earnings (retrospective restatement).

Insurance contracts – Classification and measurement of financial assets on transition

IASB discussion and decisions

IASB discussion

- There was some discussion about whether reassessment was similar to a change of business model.
- The Board asked the Staff to clarify in the drafting of the new Standard that reassessment of the business model does not imply that the model itself has changed, but that in the light of the new Standard and new circumstances an entity would have arrived at different classifications/designations.
- It was highlighted that the reassessment or re-designations are optional.
- Some Board members wanted to emphasise the need to explain the reasons for re-assessments and re-designations, whereas others argued that this information implied some necessary conditions which were not explicitly stated.

Board tentative decisions

- The Board approved both of the Staff recommendations

Insurance contracts – Restatement of comparative information on initial application of the new insurance contracts Standard

Summary

- IFRS 9 does not require restatement of comparative information for the initial application of the classification and measurement requirements, but permits it if it is possible to do so without the use of hindsight.
- By comparison, the June 2013 insurance contracts ED proposed that retrospective restatement of comparative information should be required, but permitted a simplified approach where full retrospective application was impractical.
- This was tentatively confirmed at the October 2014 meeting with proposals to allow a fair value approach if also the simplified approach was impractical.

Insurance contracts – Restatement of comparative information on initial application of the new insurance contracts Standard

IASB discussion and decisions

- A Board member noted that the use of hindsight could be avoided if insurers are given sufficient advance notice of the requirements, and could therefore collect the necessary information before transition to the new insurance contracts Standard.
- After a brief discussion, the Board agreed to reconfirm the intention to require all entities to restate the comparative information about insurance contracts.
- However, the Board tentatively decided that entities already applying IFRS 9 on initial application of the new insurance contracts Standard and that take advantage of the transition reliefs (see previous decision), they should restate comparatives for financial assets.

Insurance contracts – The “mirroring approach”

Summary and Staff recommendation

- The June 2013 ED proposed a “mirroring approach” for the measurement and presentation of contracts that require an entity to hold underlying items and that specify a link to the returns on such items. The Staff asked the IASB to decide whether that approach should be retained.
- Although there had been sympathy for removing accounting mismatches, this specific proposal had been widely criticised as it was too complex and potentially inconsistent for some participating contracts. The variable fee approach was developed in response to these concerns.

Staff recommendation

- The mirroring approach should not be permitted or required in the new insurance contracts Standard. The Staff noted that some mutual insurers might be concerned about this recommendation.

Insurance contracts – The “mirroring approach”

IASB discussion and decision

IASB discussion and tentative decision

- Entities with potentially no equity (including mutual insurers) and the possible presentation of financial statements available to them were discussed.
- It was noted that there may be circumstances in which the residual assets of a mutual may not be attributable to policyholders, and that a mutual may have some surplus as it may have a future but not a present obligation to current and future policyholders.
- The Board noted that liability versus equity issues were outside the scope of the insurance project.
- The Board unanimously decided that the mirroring approach should not be permitted or required.
- Although this decision clarifies entirely the recognition and measurement for direct participating contracts the issues surrounding the indirect participating contracts remain unresolved. The staff papers to date suggest that they would remain under the general model (building blocks approach)

Insurance contracts – Presentation and disclosure

Summary

- The Staff paper summarised the impacts on disclosure of all the re-deliberations and developments since the June 2013 ED was published, particularly the ‘variable fee approach’ for contracts with direct participating features, the modification of the presentation of interest expense in OCI and the impact of the publication of IFRS 15.

Insurance contracts – Presentation and disclosure

IASB discussion

- There was a lively discussion on the various disclosure requirements, their usefulness to users, the comparability across and within entities and the difficulty of producing them.
- **Disclosures for the OCI solution**
- The Staff clarified that an entity would need to keep track and disclose the movements in the financial assets designated as related to insurance contracts at the date of transition when the entity had made an election to disaggregate between profit or loss and OCI their interest expense and it also uses the simplified approach to transition.

Insurance contracts – Presentation and disclosure

IASB discussion (continued)

- **Disclosures on different methods to measure insurance contracts**
- Board members considered the need to present separately insurance contracts measured using different methods (e.g. the PAA and the VFA).
- Some felt that the measurement simply reflects different features of the contracts and therefore presenting them in one line would still give comparable information.
- Others considered that the contracts profitability may emerge differently over time.
- Overall the Board members felt that the reference to the IAS 1 requirements to present separately items different in nature or with different features should be emphasised more strongly.
- It is worth remembering that the PAA is available because it approximates the general measurement model. However the VFA produces materially different profit recognition patterns (see the issue around indirect participating contracts).

Insurance contracts – Presentation and disclosure

IASB discussion (continued)

➤ **Disclosures for the VFA**

- There was a lively debate on the onerousness and the usefulness of the Staff proposal to provide two CSM roll-forward calculations with and without a guarantee for entities using the VFA.
- This resulted in the Staff proposing a re-worded disclosure.

➤ **Disclosures on the interest expense for the OCI solution**

- In response to questions raised by some Board members during the discussion of the interest expense analysis, the staff reconfirmed that there was no default position as between the use of a current rate or a locked-in rate.
- Some Board members questioned whether for entities choosing to present the effect of all changes in profit or loss there should be some way to distinguish investing from underwriting activities. However, this proposal was considered to be unnecessary as the OCI presentation did not fully achieve that split.

Insurance contracts – Presentation and disclosure

IASB decisions

➤ **Presentation**

- The Board confirmed the June 2013 ED proposals for the presentation of insurance contract line items in the financial statements.

➤ **Disclosures for the VFA**

- For entities applying the VFA and recognising changes in the measurement of guarantees in profit or loss (the new “VFA hedge accounting” decided in September 2015), the amount of the CSM plus the amount of guarantees recognised in profit or loss for the reporting period would be required to be disclosed.

Insurance contracts – Presentation and disclosure

IASB decisions (continued)

➤ Disclosures for the time value of money – OCI solution

- If an entity chooses to disaggregate interest expense between profit or loss and OCI, it must disclose an explanation of the method used to calculate the cost-based interest expense presented in profit or loss
- Entities using the simplified restatement approach on the accumulated OCI required by the OCI solution at transition shall:
 - Designate financial assets relating to contracts within the scope of the new insurance contracts Standard at the date of transition; and
 - Disclose, at the date of transition and in each subsequent reporting period, a reconciliation from the opening to the closing balance of the accumulated balance of OCI for those financial assets.
 - Effectively an asset run off disclosure requirement for those assets at transition given that after transition the entity will account for the OCI entries on both insurance contracts and financial assets without the simplification used at transition

Insurance contracts – Presentation and disclosure

IASB decisions (continued)

➤ **Disclosures on the CSM**

➤ An entity would be required to disclose:

- For insurance contracts that do not use the VFA changes in the fulfilment cash flows that adjust the CSM
- For all insurance contracts
 - An explanation of when the remaining CSM is expected to be recognised in profit or loss either on a quantitative basis using the appropriate time bands or by using qualitative information
 - The amounts in the financial statements determined at transition using simplified approaches, both on transition and in subsequent periods. Effectively the impracticability that could justify the use of one or both the simplified approaches for CSM restatement results in a disclosure requirement to report how those CSM balances run off subsequently
 - Any practical expedients used in developing the simplified restatement approaches

Insurance contracts – Presentation and disclosure

IASB decisions (continued)

Deletion of earlier disclosure requirements

- An entity would **not** be required to:
 - Reconcile revenue recognised in profit or loss in the period to premiums received in the period (paragraph 79 of the June 2013 ED) – this requirement is already covered by the disclosure of the balance sheet movement for the period and it was deemed a duplicative disclosure; and
 - Disclose an analysis of the total interest expense between profit or loss and OCI (tentative decision from March 2015) given the new disclosure requirements developed in this session covering the interest expense disclosure when the OCI solution is used.

Insurance contracts - The next steps

Remaining technical decisions and publication date

- At future meetings the IASB plans to discuss **the differences between the building block approach (general model) and the variable fee approach.**
- In that context there remain two material issues to be debated:
 - The measurement of **indirect participating contracts** – currently the IASB seems to restrict the application of the VFA to direct participating contracts and several constituents have appealed for that decision to be reconsidered; and
 - The use of the concept of **unit of account** – the protracted discussion on different components of the standard has left several constituents unclear on the effective direction the new IFRS will take on this central recognition and measurement requirement
- The **mandatory effective date** of the new insurance contracts Standard will not be considered until after the IASB has concluded its deliberations. The IASB expects to complete its deliberations on insurance contracts in 2015 and publish the Standard in 2016.

Contact details

Francesco Nagari

Deloitte Global IFRS Insurance Lead Partner

+852 2852 1977 fnagari@deloitte.co.uk

Keep IFRS Insurance Connected by:

[Follow](#) my latest **LinkedIn**® posts

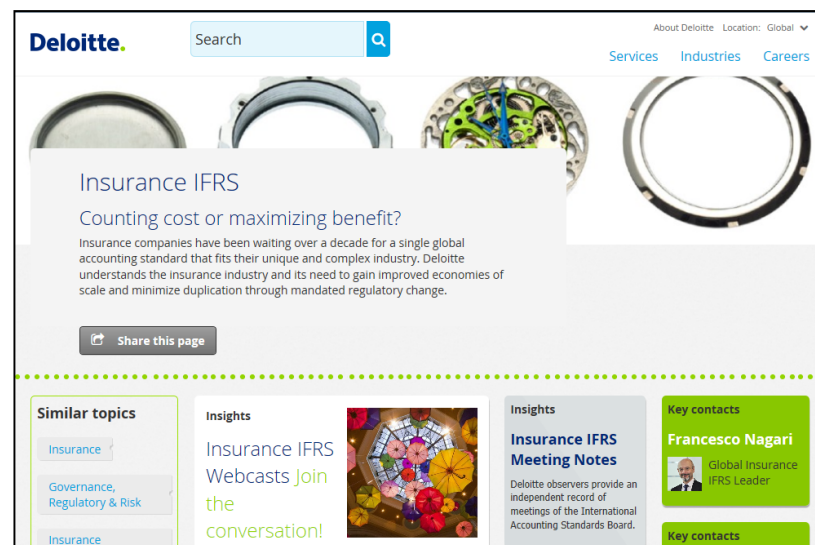
Follow me on  @Nagarif

[Subscribe](#) to Insights into IFRS Insurance Channel on



[Connect](#) to IFRS Insurance **LinkedIn**® Group for all the latest IFRS news

Add Deloitte Insights into IFRS Insurance (i2ii) www.deloitte.com/i2ii to your favourites





Deloitte refers to one or more of Deloitte Touche Tohmatsu Limited (“DTTL”), a UK private company limited by guarantee, and its network of member firms, each of which is a legally separate and independent entity. Please see www.deloitte.co.uk/about for a detailed description of the legal structure of DTTL and its member firms.

Deloitte LLP is the United Kingdom member firm of DTTL.

This publication has been written in general terms and therefore cannot be relied on to cover specific situations; application of the principles set out will depend upon the particular circumstances involved and we recommend that you obtain professional advice before acting or refraining from acting on any of the contents of this publication. Deloitte LLP would be pleased to advise readers on how to apply the principles set out in this publication to their specific circumstances. Deloitte LLP accepts no duty of care or liability for any loss occasioned to any person acting or refraining from action as a result of any material in this publication.

Deloitte LLP is a limited liability partnership registered in England and Wales with registered number OC303675 and its registered office at 2 New Street Square, London EC4A 3BZ, United Kingdom. Tel: +44 (0) 20 7936 3000 Fax: +44 (0) 20 7583 1198.