IFRS 17 *Insurance Contracts* – Narrow-scope amendment

Executive Summary

Project Type	Influencing
Project Scope	Limited (Narrow-scope amendment)

Purpose of the paper

This paper provides the Board with a draft Project Initiation Plan (PIP) for the expected IASB Exposure Draft (ED) *IFRS 17 Insurance Contracts – Narrow-scope amendment* for discussion and approval.

Summary of the Issue

The IASB is shortly expected to publish an ED to propose a narrow-scope amendment to IFRS 17. The proposed amendment would permit an entity within the scope of IFRS 17 to apply an optional classification overlay to financial assets that are related to insurance contract liabilities in the comparative period(s) on initial application of IFRS 17 and IFRS 9.

The ED is expected to be published by the end of July 2021 with a short, 60-day comment period. The IASB aims to finalise the amendment by the end of 2021.

Information on the proposed activities to ascertain UK views on the IASB's ED and a project timeline are set out in the PIP.

Decisions for the Board

The Board is asked:

- Whether it agrees with the preliminary views for the draft comment letter included at Appendix 1?
- Whether it agrees with the recommended option for approval of the draft comment letter?
- To approve the draft PIP.

Recommendation

We recommend the Board approves the draft PIP.

Appendices

Appendix 1 Tentative High-level Position for the UKEB Draft Comment Letter

Project Initiation Plan: IFRS 17 Insurance Contracts – Narrow-scope amendment

Overview

1. At its June 2021 meeting, the International Accounting Standards Board (IASB) agreed to propose a narrow-scope amendment to IFRS 17 *Insurance Contracts*. The proposed amendment would permit an entity within the scope of IFRS 17 to apply an optional classification overlay to financial assets that are related to insurance contract liabilities in the comparative period(s) on initial application of IFRS 17 and IFRS 9 *Financial Instruments*. No amendments were proposed to IFRS 9.

2. An Exposure Draft (ED) is expected to be published by the end of July with a 60-day comment period. The IASB aims to finalise the proposed amendment by the end of 2021.

3. In accordance with its statutory functions[1] [2], the UKEB will develop a response to the proposed narrow-scope amendment. This Project Initiation Plan (PIP) provides some background information and sets out how the UKEB response will be developed. It also considers whether the proposed narrow-scope amendment should be assessed for endorsement as part of the ongoing IFRS 17 endorsement process or as a separate endorsement project.

Background

4. The IASB's ED setting out these proposals is not expected to be published until after the UKEB's meeting on 20 July 2021. The following summary of the accounting issue and the proposed narrow-scope amendment is based on the IASB staff paper[3] discussed at the IASB's June 2021 meeting, together with key points from the discussion at the meeting.

Accounting issue

5. Many insurers will first apply IFRS 17 and IFRS 9 at the same time on or after 1 January 2023. The transition requirements in the two Standards apply at different dates:

   a) The IFRS 9 transition requirements apply on the date of initial application (ie 1 January 2023 for many insurers); whilst

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1 The International Accounting Standards and European Public Limited-Liability Company (Amendment etc.) (EU Exit) Regulations 2019 No 685: https://www.legislation.gov.uk/uksi/2019/685/made

2 The International Accounting Standards (Delegation of Functions (EU Exit) Regulations 2021 No 609: https://www.legislation.gov.uk/uksi/2021/609/contents/made

3 June 2021 IASB staff paper 'IFRS 17 Insurance Contracts – Initial application of IFRS 17 and IFRS 9 – comparative information' can be accessed here: AP2: Initial application of IFRS 17 and IFRS 9—comparative information

b) The IFRS 17 transition requirements apply on the transition date – the beginning of the comparative annual reporting period (ie 1 January 2022 for many insurers), or earlier if the entity voluntarily restates more than one year of comparative information.

6. IFRS 17 requires entities to restate comparative information. IFRS 9 does not require restatement but allows entities to restate prior periods if, and only if, it is possible without the use of hindsight.

7. For some insurers, the difference in the transition requirements for the two standards will result in one-time measurement differences in the comparative information presented on initial application of IFRS 17 and IFRS 9. This can be summarised as follows:

   a) Accounting mismatches between insurance contract liabilities measured at current value under IFRS 17 and some related4 financial assets measured at amortised cost.

   b) If the entity chooses to restate comparative information for IFRS 9, classification differences may occur between financial assets derecognised in 2022 (to which IFRS 9 will not apply) and other financial assets (to which IFRS 9 will apply).

Proposed narrow-scope amendment to IFRS 17 requirements

8. An entity would be permitted (but not required) to apply a classification overlay (the 'classification overlay') in the comparative period(s) presented on initial application of IFRS 17 and IFRS 9. The optional classification overlay would:

   a) Apply to financial assets that are related to insurance contract liabilities and to which IFRS 9 has not been applied in the comparative period(s);

   b) Allow an entity to classify those financial assets in the comparative period(s) in a way that aligns with how the entity expects those assets would be classified on initial application of IFRS 9;

   c) Apply for comparative periods that have been restated for IFRS 17 (that is, from the transition date to the date of initial application of IFRS 17); and

   d) Apply on an instrument by instrument basis.

9. The proposed classification overlay would apply only to financial assets that are related to insurance contract liabilities. It is expected that the description of 'related to insurance contract liabilities' would be consistent with paragraph C29(a) of IFRS 17, ensuring that unrelated financial assets, e.g. those held in respect of banking activities or financial

[4] 'Related' is the word used in the IASB staff paper. It is expected to be amended in the Exposure Draft to make it consistent with paragraph C29(a) of IFRS 17. Therefore, financial assets held in respect of banking activities or financial assets held in funds relating to investment contracts will be outside the scope of IFRS 17.

assets held in funds relating to investment contracts, will be outside the scope of the proposed narrow-scope amendment.

10. The classification overlay would be available for both:

    a) Entities that restate comparative information for IFRS 9 (applicable only for financial assets derecognised in the comparative period(s) because IFRS 9 does not apply to those assets); and

    b) Entities that do not restate comparative information for IFRS 9 (available for any financial assets related to insurance contract liabilities).

11. An entity would classify financial assets in a way that aligns with how it expects those financial assets to be classified on initial application of IFRS 9, without having to undertake the assessments required by IFRS 9[5] or to apply the expected credit losses model.

12. An entity would recognise in the opening retained earnings (or other component of equity, where applicable) the difference between:

    a) The carrying amount of the financial asset at the transition date to IFRS 17 applying the classification overlay; and

    b) The previous carrying amount at that date.

13. The classification overlay would be available only for comparative periods that are restated for IFRS 17 purposes. An entity could choose to restate more than one comparative period on initial application of IFRS 17, but must avoid the use of hindsight.

14. The classification overlay would apply on an instrument-by-instrument basis. This would allow entities to identify which financial assets are related to insurance contract liabilities and are the subject of classification differences, and then decide whether to apply the classification overlay.

15. The classification overlay approach would not require entities to separately identify financial assets in the comparative period(s) to which the classification overlay is applied.

5 This refers to the requirement to consider the business model or contractual cash flow characteristics (ie. solely payments of principal and interest – the 'SPPI test') for classification of financial assets.

Key planning assumptions, outreach and timeline

Assumptions

16. We have made the following assumptions in developing this project plan:

  a) The amendments are narrow in scope as they meet the IASB's criteria for narrow scope amendments.

  b) Few stakeholders in the UK are likely to be materially impacted by them.

  c) An Exposure Draft is expected by the end of July with a 60-day comment period, likely to be to the end of September.

  d) Due to the short-time line, mainly falling over the summer break, there will be limited opportunity for the UKEB to engage on the development of its draft comment letter. As a result, it will approve the Secretariat's recommendations in relation to the development of the draft comment letter (see paragraph 24 below).

  e) Secretariat's proposed final comment letter will be presented to the Board meeting on 17 September for approval. Once approved, the final comment letter will be submitted to the IASB in time for its end of September comment paper deadline.

  f) If the IASB finalises the proposed narrow-scope amendment before the end of 2021, it would be considered as part of the ongoing IFRS 17 endorsement process (so consideration for this amendment will be included in the DECA for that project) and not as a separate endorsement project. However, if there was a delay in IASB issuing the final amendment we will devise a separate endorsement and adoption plan for this narrow scope amendment to help ensure it is available for UK companies' use at the earliest opportunity.

17. A preliminary analysis for a draft comment letter is presented to the Board today (see Appendix 1 to this paper).

Questions for the Board	
18	Do Board members agree with the preliminary views for the draft comment letter included at Appendix 1?

Outreach

19 Due to the time constraint and the limited number of UK stakeholders expected to be impacted materially by the proposed amendment, we will conduct only limited outreach activities with those likely to be impacted by this narrow-scope amendment.

20 In anticipation of the short comment deadline, we discussed the proposed narrow-scope amendment with the Insurance Technical Advisory Group (Insurance TAG) at the meeting on 8 July and ascertained the TAG members' preliminary views.

21 Once the Exposure Draft is published, we will perform the following outreach activities before issuing the draft comment letter:

a) Obtain further comments (if any) from the Insurance TAG by email.

b) Contact the Association of British Insurers ABI to request their support in canvassing views from their members.

c) Contact a small number of insurers, as identified by our desktop research, who are not already members of the Insurance TAG and are likely to be impacted by the proposed amendment.

22 The Draft Comment Letter will be published on the UKEB website for wider stakeholder input and advertised via the usual channels.

23 During the public consultation period for the draft comment letter we will contact a small number of specialist users of insurers' accounts to ascertain their views.

24 Due to the short-time line, mainly falling over the summer break, there will be limited opportunity for the UKEB to engage on the development of its draft comment letter. Options for developing the UKEB's draft comment letter are:

a) Presenting to the Board a draft comment letter for approval at the September meeting. Electing this option would mean submitting a final comment letter after the IASB's consultation deadline.

b) Submitting a draft comment letter for approval to designated members of the Board. We believe this option would be acceptable given the limited number of stakeholders expected to be impacted by the proposed narrow-scope amendment. The approval process could be performed by either:

(i) Designating a sub-committee to approve on behalf of the Board. This option would allow us to publish our draft comment letter for stakeholder views in August, or

(ii) Obtaining approval of the draft comment letter from the Chair of the Board. This option would allow more time for stakeholders to consider and provide input on the UKEB's draft comment letter while still meeting the IASB's consultation deadline.

The UKEB's Secretariat recommends obtaining approval of the draft comment letter from the Chair of the Board and this is reflected in the proposed project timeline below.

Questions for the Board
25 Do Board members agree with the recommended option for approval of the draft comment letter (as per paragraph 24)?

Project closure

26 We intend to present drafts of the Feedback Statement and the Statement on Compliance with Due Process Steps for Board review at the 17 September meeting.

Project timeline

27 Given the short 60-day IASB comment period, that mainly falls over the summer break, and the expected narrow-scope of the amendment we are proposing a curtailed project plan, proportionate to the size of the project. The proposed project timeline will lead to a very short window for stakeholders to consider and provide input on the UKEB's draft comment letter.

28 The proposed high-level project timeline that assumes that the IASB will finalise the narrow scope amendment by the end of 2021 is as follows:

Date	Milestones
20 July **Board meeting**	Approve PIP. Approve preliminary views for draft comment letter.
30 July	IASB publishes Exposure Draft.
9 August	Publish draft comment letter.
30 August	Deadline for responses to draft comment letter (21 days from publishing).
17 September **Board meeting**	Approve final comment letter. Review draft Feedback Statement and draft Statement on Compliance with Due Process Steps.
30 September	Submit final comment letter to IASB.
31 December 2021	IASB finalises amendments to IFRS 17.
Q1 2022	Amendment to IFRS 17 subject to endorsement process.

29 The above timeline will be revised if there are any delays in the IASB's issuance of its ED or the final amendment.

Questions for the Board
30 Do Board members approve the draft PIP?
31 Do Board members have any additional comments?

IFRS 17 *Insurance Contracts* – Narrow-scope amendment

Appendix 1: Tentative High-level Position for the UKEB Draft Comment Letter

A1 The following represent some preliminary views for the UKEB draft comment letter, based on comments made by the Insurance TAG and on our own preliminary analysis. We intend to refine this analysis further once the IASB's ED is published and then incorporate it in the UKEB's draft comment letter to be issued for wider stakeholder consultation.

A2 Most UK insurers account for the majority of their financial assets under IAS 39 at fair value through profit or loss and are expected to proceed to the same model under IFRS 9. Therefore, the current expectation is that the classification overlay may not be significant for most UK insurers. As a result, we expect our commentary to the IASB to focus on the technical merits of the narrow scope amendment.

A3 Overall, we support the proposals in the ED. The classification overlay will increase the understandability of comparative information as it will enable entities to avoid classification mismatches (arising purely from differences in transition requirements between IFRS9 and IFRS 17) that do not represent economic mismatches.

A4 As a result of the optional nature of the proposed amendment, the classification overlay may reduce comparability between insurers. However, for an insurer it will enhance the relevance and comparability of financial information between periods. We believe it represents an acceptable compromise but disclosures will be necessary to enable users understand which entities apply the classification overlay.

A5 We agree with the narrow scope of the classification overlay for entities that elect to restate comparative information for IFRS 9. It only applies for financial assets 'related' to insurance liabilities and only for the comparative information presented on transition to IFRS 17 (one-time application).

A6 Further clarity is needed on some of the proposed amendments. We need to analyse the Exposure Draft and Basis for Conclusions once they are published, for issues such as:

a) The classification overlay applies only for financial assets 'related' to insurance. It is our understanding that the word 'related' will be changed in the Exposure Draft to make it consistent with paragraph C29(a) of IFRS 17. It is important that the scope for the amendments is clearly defined.

b) The rationale for allowing the application of the classification overlay for entities that do not restate comparative information for IFRS 9 is not clear. Insurers presenting comparative information under IAS 39 could apply the classification overlay to any financial assets related to insurance contract liabilities (not only for financial assets derecognised in the comparative period). Insurers that were planning to restate comparatives for IFRS 9 might now be dissuaded from doing so.

c) The IASB tries not to create an additional burden for insurers by not requiring full application of IFRS 9 requirements, such as the expected credit losses model. However, it is not clear what assessments insurers would need to perform to classify financial assets in a way that aligns with how it expects those financial assets to be classified on initial application of IFRS 9.

d) Entities could potentially end up with different categories of financial assets (each accounted for differently), which could be confusing for users of accounts. For example:

- An entity that elects to restate IFRS 9 comparative information could end up with: a) Financial assets under IFRS 9 – for assets that exist as of the end of the comparative period. b) Financial assets under IFRS 9 – for assets that do not exist as of the end of the comparative period, but for which the classification overlay would apply and c) Financial assets under IAS 39 – for assets that do not exist as of the end of the comparative period and which are not eligible for the classification overlay.

- An entity that does not restate comparative information for IFRS 9 could end up with: a) Financial assets under IAS 39 for assets not related to insurance contract liabilities and also for those assets related to insurance contract liabilities for which the entity chooses not to apply the classification overlay and b) Financial assets for which the classification overlay has been applied.

Disclosure requirements on the application of the classification overlay could help users better understand the financial information.