STAFF PAPER

March 2016

IASB Meeting

Project	**Amendment to IFRS 4: Applying IFRS 9 *Financial Instruments* with IFRS 4 *Insurance Contracts***
Paper topic	Project direction and plan

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Objective

1. The objective of this paper is to:

   (a) ask for key decisions that will set the direction for the International Accounting Standards Board's (the Board's) redeliberations of the proposed amendments to IFRS 4 *Insurance Contracts* (IFRS 4). Those proposals are designed to address the concerns of some interested parties about the different effective dates of IFRS 9 *Financial Instruments* (IFRS 9) and the forthcoming insurance contracts Standard; and

   (b) describes the project plan for those proposed amendments to IFRS 4.

2. This paper:

   (a) summarises the background to the proposals in the Exposure Draft *Applying IFRS 9* Financial Instruments *with IFRS 4* Insurance Contracts (the ED) and the feedback received in paragraphs 6-8;

   (b) considers whether the Board should proceed with the temporary exemption from applying IFRS 9 (the temporary exemption) (sometimes called the deferral approach) in paragraphs 9-16. In addition, this paper:

      (i) considers (in paragraphs 18-22) whether the eligibility for the temporary exemption should be assessed at:

1. ‘the reporting entity level’ (ie the assessment is done considering all of activities of the reporting entity, and the reporting entity applies only one Standard, either IFRS 9 or IAS 39 *Financial Instruments: Recognition and Measurement*, to all of its financial instruments in its financial statements); or
2. ‘below the reporting entity level’ (ie the assessment is conducted on the activities conducted by differing parts of the reporting entity, and the reporting entity applies both IFRS 9 and IAS 39 to its financial instruments within a single set of financial statements);

(ii) considers whether there should be a fixed expiry date for the temporary exemption in paragraphs 29-31;

(c) considers whether the Board should proceed with the overlay approach in paragraphs 33-35;

(d) considers whether the temporary exemption and the overlay approach should be optional in paragraphs 36-38; and

(e) sets out the project plan for the Board’s redeliberations of those proposed amendments to IFRS 4 in paragraphs 42-43.

Staff recommendation

3. The staff is asking the Board to decide on key issues that will determine the direction of the project's redeliberations in future months. The analysis in future Agenda Papers will be predicated on the decisions made at this meeting.

4. The staff recommends that the Board confirm the ED proposals that:

   (a) there should be a temporary exemption and an overlay approach; and

   (b) that both the temporary exemption and the overlay approach should be optional.

5. The staff also recommends:

   (a) that the eligibility assessment for the temporary exemption is performed at 'the reporting entity level' only (ie the assessment is done considering all of the activities of the reporting entity and the reporting entity applies only one Standard, either IFRS 9 or IAS 39, to all of its financial instruments in its financial statements); and

   (b) that the temporary exemption has a fixed expiry date.

Background

Proposals in the ED

6. The ED proposed two approaches, which are designed to address the concerns about the different effective dates of IFRS 9 and the forthcoming insurance contracts Standard, the overlay approach and the temporary exemption (sometimes called the deferral approach). The Board believed that the overlay approach would result in better and more useful information about financial instruments than the temporary exemption. Consequently, the Board proposed that the overlay approach would be applicable to all entities that issue contracts within the scope of IFRS 4 because:

   (a) under the overlay approach entities would apply IFRS 9, which is a significant improvement in the reporting of financial instruments, on a timely basis. In contrast, entities that apply the temporary exemption would delay the application of IFRS 9 and instead continue to apply IAS 39*;*

   (b) the overlay approach addresses the primary issue the Board sought to address, which is the additional volatility and accounting mismatches in profit or loss that may arise if IFRS 9 is applied before the forthcoming insurance contracts Standard; and

   (c) the overlay approach provides additional and transparent information to users of financial statements that would assist them in understanding some of the effects of moving from IAS 39 to IFRS 9 whereas the temporary exemption would result in less information being provided.

7. Nevertheless, the Board proposed a temporary exemption for a narrow population of entities with a high proportion of liabilities arising from contracts within the scope of IFRS 4 (compared to total liabilities) because the Board believed that such entities engage primarily in insurance activities (with limited other activities); and thus would be most affected by the different effective dates. The Board noted that:

   (a) the temporary exemption could address the concerns about additional volatility and accounting mismatches in profit or loss that may arise if

IFRS 9 is applied before the forthcoming insurance contracts Standard and, *in addition*, would address concerns about applying the classification and measurement requirements in IFRS 9 before the forthcoming insurance contracts Standard is applied.

(b) the temporary exemption would reduce comparability for users of financial statements; to minimise that effect the population of entities that would be eligible should be limited. Under the proposals, the temporary exemption would be available to the entities most affected by the different effective dates (ie when the effect of the additional accounting mismatches and volatility would be the most significant).

Feedback received on the proposals in the ED

8. The paragraphs below summarise the feedback received from **all** types of constituents (That is, it combines in one place the high level feedback outlined in both Agenda Paper 14A *Summary of comment letters and outreach*, which did not include feedback from users and Agenda Paper 14B *Summary of feedback from users of financial statements.*):

(a) Most preparers, auditors, accounting and actuarial professional bodies, national standard-setters and regulators agreed that the Board should address the three concerns raised by some interested parties about the different effective dates of IFRS 9 and the new forthcoming insurance contracts Standard (discussed in Agenda Paper 14A). This is in contrast to the feedback from most users of financial statements who placed less weight on those concerns (discussed in Agenda Paper 14B).

(b) Most users of financial statements, some preparers that engage in both banking and insurance activities (sometimes termed ‘bancassurers’) and a few other respondents (eg from South America) preferred the overlay approach to the temporary exemption. In comparison, most preparers (especially those from Europe, North America and Asia) think that the temporary exemption is the only approach that addresses their concerns about applying IFRS 9 before the forthcoming insurance contracts Standard. Their view was shared by auditors, accounting bodies and national standard-setters. Finally, some preparers are unconcerned with applying IFRS 9 in 2018 because either all of their financial assets are measured at fair value through profit or loss (FVPL) today (eg South African insurers) or because they intend to apply IFRS 9 as they are the subsidiaries of banks.

(c) Most respondents, including users of financial statements, believed that the population of entities that qualify for the temporary exemption is too narrow because some entities that they regard as insurers would not qualify. Respondents had mixed views on whether the eligibility assessment for the temporary exemption should be conducted at the reporting entity level only or whether an assessment should also be permitted below the reporting entity level. For example, most users and most regulators (both prudential and security regulators) supported an assessment only at the reporting entity level. In contrast, most preparers, auditors and accounting bodies, and some national standard-setters would also support an approach that allowed an assessment below the reporting entity level so that insurance subsidiaries in a group with other activities (eg banking activities) could apply IAS 39 in the consolidated financial statements of the group whereas the rest of the non-insurance entities in the group would apply IFRS 9.

(d) Most users of financial statements are concerned that the proposals in the ED includes three options—an option to apply the temporary exemption (and continue to apply IAS 39), IFRS 9 with the overlay approach, or ‘pure’ IFRS 9. In contrast, all other types of respondents supported these options and some strongly believed that these options are necessary because different entities have differing facts and circumstances.

(e) Respondents had mixed views on whether there should be a fixed expiry date on the temporary exemption. Almost all users of financial statements and most regulators, and some standard-setters and auditors, support the proposed fixed expiry date (ie 2021). In particular, most users and regulators support that expiry date, regardless of the effective date of the forthcoming insurance contracts Standard. In contrast, most preparers believe that the insurers should be required to apply IFRS 9 only when they apply the forthcoming insurance contract Standard. Accordingly, they do not support a fixed expiry date but instead believe that the temporary exemption should expire on the mandatory effective date of the forthcoming insurance contracts Standard.

Whether to confirm the temporary exemption?

Feedback received

9. Many users did not support the temporary exemption because they believed that the temporary exemption reduces comparability, creates accounting arbitrage and diminishes information content. Most preferred the overlay approach over the temporary exemption.

10. In contrast, the majority of preparers, accounting and actuarial professional bodies, auditors, and standard-setters said:

    (a) that the temporary exemption was their preferred approach to address the concerns raised by the different effective dates of IFRS 9 and the forthcoming insurance contracts Standard; and

    (b) that the temporary exemption should apply to a wider population. Some respondents argued strongly for an eligibility assessment that is performed below the reporting entity level.

11. These respondents argued that the overlay approach would not address all their concerns. This is because most stated that a significant concern is the costs that would result from applying IFRS 9 before the forthcoming insurance contracts Standard and from applying the overlay approach. Some respondents argue that insurers that were not eligible to apply the temporary exemption would be at a competitive disadvantage relative to insurers that were eligible.

12. Respondents noted the following costs of applying IFRS 9 before the forthcoming insurance contracts Standard.

    (a) Most are concerned that insurers that are not eligible for the temporary exemption would have to apply IFRS 9 in 2018 and then reassess particular aspects of that Standard (for example, the business model or fair value option (FVO) for some financial assets) when they apply the forthcoming insurance contracts Standard.

    (b) Some did not think that it was feasible to apply IFRS 9 in 2018, because they did not think there will be enough time between the issuance of any amendments to IFRS 4 arising from this project and 2018.

(c) Most also noted the significant additional costs necessary to apply the overlay approach, such as the need to have systems to prepare information under both IAS 39 and IFRS 9 and the complexities that may arise to determine second-order effects (eg when shadow accounting is applied).

Staff analysis

13. While there are likely to be some additional implementation costs if an entity applies IFRS 9 before the forthcoming insurance contracts Standard, the staff remains unconvinced that they are significant:

(a) The staff notes that all entities with financial instruments will eventually have to apply IFRS 9 and incur the costs necessary to do so. So, in large part, the difference is the timing of when such expenditure is incurred. Many respondents commented on the need for ‘reworking’ IFRS 9 or being required to ‘apply IFRS 9 twice’. The staff notes that the Board has tentatively provided transition relief in the insurance contracts project to, for example, allow entities to reassess the business model for particular financial assets to reflect the current facts and circumstances on initial application of the forthcoming insurance contracts Standard. However, the staff makes the following observations about the additional work that could be required:

(i) The classification of assets that do not have contractual cash flows that are solely principal and interest (ie do not meet the SPPI test) will be unaffected as the SPPI test is based on the contractual terms on initial recognition of the assets.

(ii) Business model need not be reassessed (it is permitted not required) and even when it is, classifications will not change for those assets where the business model remains unchanged from when IFRS 9 was first applied.

(iii) An entity is permitted to change its designations under the FVO when it initially applies the forthcoming insurance contracts Standard to address accounting mismatches. As a result, entities may choose to measure more assets at

FVPL under this option as a result of using current measurement for their insurance contracts liabilities and choosing to remeasure those liabilities through profit or loss. Staff believes that, for most entities, this is likely to be the primary cause of changes in classification when IFRS 9 is reassessed when the forthcoming insurance contract Standard is applied.
However, staff does not think it is costly to apply the FVO when the forthcoming insurance contracts standard is first applied because the entity need not reassess the contractual terms of the financial assets or the business model – they can simply make a FVO election based on the outcome of the original assessment of the asset's classification.

(iv) In relation to increased use of the FVO when the forthcoming insurance contracts standard is applied some also raise concerns about needing to determine expected credit losses (ECL) temporarily. For example, if financial assets are measured at amortised cost or fair value through other comprehensive income (FVOCI) when IFRS 9 is initially applied and subsequently are measured at FVPL (under the FVO) when the forthcoming insurance contracts Standard is initially applied, the ECL model would be applied to those assets for a short period and then would no longer be required.
However, the staff thinks that most entities will need systems to measure ECLs because at least some financial assets will continue to be measured at amortised cost and FVOCI – so this is not wasted effort. This view is based on the following:

1. Most of those entities have actively supported the FVOCI measurement category in IFRS 9 and the use of OCI in the forthcoming insurance contracts Standard – this combination of accounting would still result in a need for measuring ECLs. The staff thinks that it is unlikely that those entities will elect the FVO for *all* their financial assets backing insurance contracts when they initially

apply the forthcoming insurance contracts Standard, except where the entity has a substantial amount of assets already at FVPL.

2. some entities have a mix of businesses (such as an insurance business and a banking business) so even if the ECL measurement is not needed for insurance related assets, entities would still need to develop systems to prepare their IFRS financial statements.

(b) The staff notes that the completed version of IFRS 9 was issued in mid-2014 to allow for a sufficient implementation period. At the time, the Board carefully considered what the mandatory effective date of IFRS 9 should be to ensure that entities had enough time to implement it. At that time, the Board also considered the interaction with the timing of the forthcoming insurance contract Standard.

14. The staff thinks that it is important to note that those entities applying IFRS 9 in 2018 (including those that do not qualify for the temporary exemption) could address the temporary volatility and accounting mismatches by:

(a) applying the overlay approach; and/or

(b) expanding the information that is currently being produced to explain any accounting mismatches when applying IFRS 9 in a similar way that some entities explain the accounting mismatches that already exist when they apply IAS 39 in conjunction with their existing accounting policies for insurance contracts.

In addition, the feedback from most users of financial statements has indicated that they would prefer the information provided by applying IFRS 9 to financial assets instead of applying IAS 39. We spoke with many users who expressed concerns about the existing complexity of insurance contract accounting. In addition, they were also concerned that further complexity and lack of comparability would arise as a result of the temporary exemption, which would introduce additional inconsistency in the accounting for financial assets within the insurance sector and in the market more generally.

15. The staff is unconvinced that the costs of applying IFRS 9 before the forthcoming insurance contracts Standard will result in a competitive disadvantage for entities that will apply IFRS 9 in 2018 compared to those that qualify for and apply the temporary exemption (see paragraph 11). Nevertheless, staff acknowledges that there are additional costs of applying the overlay approach compared to applying solely either IAS 39 or IFRS 9 (discussed in paragraph 12(c)).

16. To balance the different constituent views that we heard, the staff recommends that the Board should continue to develop a temporary exemption that would be available for some, but not all, entities that issue contracts within the scope of IFRS 4. The staff continues to believe that the main reason for the temporary exemption is to address the potential accounting mismatches and volatility that could arise as a result of the different effective dates rather than seeking to provide relief for all entities that may be affected by having to apply IFRS 9 before applying the forthcoming insurance contract standard. For that subset of entities, the temporary exemption could address the issue of additional volatility and accounting mismatches in a way that would be cost-effective.

17. The following paragraphs discuss:

    (a) which entities should qualify for the temporary exemption:

        (i) whether the eligibility assessment should be conducted at the reporting entity level or below the reporting entity level (in paragraphs 18-22); and

    (b) the criteria for qualification (in paragraphs 23-28); and

    (c) whether there should be a fixed expiry date for the temporary exemption (in paragraphs 29-32).

Assessment level of the temporary exemption

Below the reporting entity level

18. Some (eg preparers, national standard-setters, auditors) strongly recommended that the Board develop an approach that allows an assessment ‘below the

reporting entity level[1]'. For example, for a financial conglomerate that conducts both banking and insurance activities, some believe that IFRS 9 should apply to the banking activities and IAS 39 should apply to the insurance activities and that that accounting treatment should 'roll up' to the consolidated financial statements.

19. Proponents of this view make the following arguments:

(a) Many users do not rely on the information in a group's consolidated primary financial statements for the purposes of sector comparisons of conglomerates and instead focus on other types of information (eg segmental information). Therefore, it is not necessarily problematic that the consolidated financial statements would include both IFRS 9 and IAS 39 information.

(b) Under the proposals in the ED, a reporting entity qualifies for the temporary exemption if its predominant activity is issuing contracts within the scope of IFRS 4. A few entities with minor banking activities would qualify for the temporary exemption (if their predominant activity is issuing insurance contracts). Some are concerned that IAS 39 would be applied to those banking activities in the group's financial statements.

(c) Most think that concerns about how to account for transfers of financial instruments, between a part of the group applying IFRS 9 and a part applying IAS 39, should not be regarded as a critical issue because they believe such transfers occur only rarely. Additionally, some suggest potential accounting treatments for such transfers, including:

(i) transferring the instrument at fair value and recognising the resulting gains and losses in the statement of comprehensive income.

(ii) retaining the accounting that is applicable to the transferor. For example, if the financial instrument is transferred from a part of the group applying IAS 39 to a part of the group

[1] Some suggest a variation of this approach, a 'waterfall' approach, where a reporting entity assesses qualification at the reporting entity level first (ie considering all of its activities). If it qualifies, IAS 39 can be used in the consolidated financial statements. If it fails, it assesses below the reporting entity level and in that case apply IAS 39 to only part of the reporting entity that qualifies.

applying IFRS 9, the transferred asset would continue to apply IAS 39.

(d) The temporary exemption avoids the costs of applying IFRS 9 before the forthcoming insurance contracts Standard as discussed in paragraph 12; and the additional costs in applying the overlay approach as discussed in paragraph 12(c). Some regard this issue as just as important for the insurance activities within a group as it is for a group in its entirety. Under the proposals in the ED, the insurance activities in the group could qualify for the temporary exemption in their stand-alone (separate) financial statements but the group may not qualify for the temporary exemption in the consolidated financial statements because of substantial non-insurance activities (eg banking). Accordingly, IFRS 9 would need to be applied to the insurance activities for the purposes of the group's consolidated financial statements resulting in additional costs.

(e) Some think that applying both IFRS 9 and IAS 39 in the same financial statements, while not a good technical solution, is a pragmatic way of addressing the concerns raised on applying IFRS 9 before the forthcoming insurance contracts Standard, particularly as it is temporary. They note that doing so would be similar to the exemption in IFRS 4 that allows an entity to apply dissimilar accounting policies to its insurance liabilities.

(f) Some note that applying both IFRS 9 and IAS 39 in a single set of financial statements is acceptable because both standards are similar in that they have (for example) three measurement categories for debt instruments.

(g) Some raised particular concerns about the effect of a reporting entity level approach in circumstances when the reporting entity (ie the investor) would not qualify for the temporary exemption but its (insurance) associates or joint ventures would (and vice versa). That is, the investor would need to apply IFRS 9, instead of IAS 39, to the investee when the investor prepares its consolidated financial statements. This is because of the requirement in IAS 28 *Investments in*

Associates and Joint Ventures (IAS 28) paragraph 35, the investor has to apply consistent accounting policies. Some questioned the necessity of doing this and whether doing so was practical especially when the temporary exemption would be in place in a short period of time. (The issue is also applicable to the overlay approach).[2]

At the reporting entity level

20. In contrast, some strongly support the proposals in the ED, which would have the result that a reporting entity would assess its eligibility for the temporary exemption at the reporting entity level and thus apply only one Standard, either IFRS 9 or IAS 39, in its financial statements (see paragraph 8(c)); as follows:

    (a) Many users of financial statements and regulators believe it is more useful for a reporting entity to have consistent accounting policies (ie applying only one Standard, either IFRS 9 or IAS 39) than to have financial statements with non consistent accounting policies (ie applying both IFRS 9 and IAS 39). This is because some users note that financial statements with only IAS 39 information is acceptable because this is a continuation of previous information, or only IFRS 9 information because this is viewed as better information to IAS 39. Financial statements that contain a mix of both IFRS 9 and IAS 39 information is not considered a continuation of previous information. Moreover, while some users analyse disaggregated information of a reporting entity; nevertheless, they also rely on the information in the consolidated financial statements. IFRS Standards require reporting entities to use consistent accounting policies because this enables the reporting entity (eg the group producing the consolidated financial statements) as a whole to be compared with other reporting entities (and reduces accounting complexities arising from intragroup transactions).

    (b) Supporters of assessing 'at the reporting entity level' accept that a drawback of this approach is that an eligible entity applying the temporary exemption will apply IAS 39 to non-significant banking

[2] The staff intends to consider this issue in the future (see paragraphs 42-43).

activities. The extent of this issue, of course, depends on how the temporary exemption is ultimately scoped. However, banking regulators argue, and most users of financial statements agree, that this would be better (or at least a lesser evil) than allowing a reporting entity to apply both IAS 39 and IFRS 9 in its financial statements.

(c) Many users of financial statements and regulators support assessing eligibility for the temporary exemption at the reporting entity level because it avoids accounting arbitrage that may arise by transferring financial assets between a part of the group that applies IFRS 9 and a part of the group that applies IAS 39.

21. Staff agrees with the arguments for the assessment to be at the reporting entity level discussed above in paragraph 20. In addition, staff disagrees with the remaining arguments for assessing below the reporting entity as discussed in paragraphs 19(d)-19(f) as follows:

(d) As discussed in paragraph 12, staff thinks that the avoidance of costs arising from applying IFRS 9 before the forthcoming insurance contracts Standard is not an adequate basis for extending the temporary exemption to all entities that issue insurance contracts.

(e) The staff notes that the exemption in IFRS 4 that permits an entity to apply dissimilar accounting policies to its insurance liabilities is one of the most significant weakness of the current accounting for insurance contracts. We think that the existence of that problematic accounting should not be used to justify widening the use of dissimilar accounting policies in a single reporting entity.

(f) The staff disagrees with the argument that applying both IFRS 9 and IAS 39 in a single set of financial statements is acceptable because both standards have (for example) three measurement categories for debt instruments. The staff observes that the *basis* for the classification in those standards is different as are the impairment requirements; for example, available for sale (AFS) debt is not a direct equivalent of FVOCI debt due to both the different basis for the classification and the differences in measurement (for example FVOCI debt has ECL impairment recognised). Accordingly, the staff thinks that there are significant difference in applying a 'three category classification model' based solely on applying IFRS 9 or IAS 39 compared to allowing an entity to apply both IAS 39 and IFRS 9 in its financial statements.

22. Staff recommends that the Board confirm that the eligibility assessment for the temporary exemption is at the reporting entity level only. The staff notes the views of many of users of financial statements and regulators that believe it is more useful for a reporting entity to have consistent accounting policies. In addition, staff supports the arguments discussed in paragraph 20 and note that applying the eligibility assessment at the reporting entity level, instead of below the reporting entity level, addresses the concerns about different effective dates of IFRS 9 and the forthcoming insurance contracts Standard in a pragmatic way considering that the staff thinks the temporary exemption will be in place for only a short time. Staff intends to consider whether the criteria for qualification need to be amended to better capture the appropriate entities to qualify (discussed in paragraphs 23-28 below).

Qualifying criteria

23. Many respondents, from all respondent types, noted that the eligibility condition proposed in the ED (ie that the entity's predominant activity is issuing contracts within the scope of IFRS 4) may be unduly restrictive, and thus may have captured too narrow a population of entities.

24. There is an interaction between the consideration of whether the assessment should be at or below the reporting entity level and the qualification criteria. By confirming the ED proposal to assess at the reporting entity level, increasing the population of qualifying entities is possible only by examining the qualifying criteria.

25. Staff agrees that the ED proposals may not have captured the appropriate population of entities considered 'insurers'. Staff will consider how the eligibility condition could be changed to better capture the appropriate entities (ie those considered 'pure insurers') which will likely result in more entities qualifying than under the ED proposal. In particular, rather than focussing so much on the likely

extent of mismatches that may result from applying IFRS 9 before the forthcoming insurance contracts standard the staff will also consider how to allow better comparability between reporting entities that are compared as peer entities. This will include an analysis on whether the eligibility condition should consider the impact of investment contracts accounted for at fair value through profit and loss.

26. Also, the staff is mindful that any changes to the eligibility condition for the temporary exemption made during the Board's redeliberations should not result in more banking activities being eligible for the temporary exemption than would result from the proposals in the ED.

27. The staff is aware that any changes to the eligibility condition are unlikely to result in perfect comparability among all entities who issue insurance contracts, because perfect comparability can be achieved only by requiring all entities to apply IFRS 9 by 2018 (or by providing an exemption for all entities, which the IASB believes is unacceptable). However, the staff believes a number of comparability concerns could be reduced and also that changes can be made to increase the range of eligible entities while still ensuring that the temporary exemption still only captures those entities that are commonly regarded as 'insurers', while not capturing entities with significant non-insurance activities (eg banking).

28. The staff will bring the analysis on the qualifying criteria to a future Board meeting (see paragraphs 42-43).

Fixed expiry date

29. Almost all preparers disagreed with the proposal in the ED for a fixed expiry date (ie 1 January 2021 in the ED) because they believe the concerns addressed by the temporary exemption would remain so long as entities apply IFRS 9 prior the forthcoming insurance contracts Standard. In contrast, most regulators and users of financial statements agreed with a fixed expiry date. In particular, some users emphasised that the fixed expiry date is a necessary condition for the temporary exemption.

30. The staff notes that the rationale supporting the temporary exemption can be predicated only on that exemption being available for a short period. The longer the period that the temporary exemption is available, the longer there will be a lack of comparability between entities that apply the temporary exemption and those that do not. Also, many requesting that a temporary exemption be considered by the Board, did so predicated on the fact the concerns were caused by a short gap between the effective dates of IFRS 9 and the forthcoming insurance contracts Standard.

31. Accordingly, staff recommends that the Board confirm a fixed expiry date. Staff will consider in a future meeting what that expiry date should be (ie 2021 or something else). At that future meeting, the staff also expects further information on the progress of the drafting of the forthcoming insurance contracts Standard and its likely effective date.

Other issues related to the temporary exemption

32. Paragraph 36-38 discusses whether the temporary exemption should be optional. The staff outlines in the project plan in paragraphs 42-43 the other issues on the temporary exemption that the staff plans to consider in the redeliberations.

Whether to confirm the overlay approach?

33. As noted above, the staff intends consider amending the eligibility condition for the temporary exemption. Nonetheless, there will be entities that issue contracts within the scope of IFRS 4 that will not qualify for the temporary exemption (eg because of their banking activities). Accordingly, the staff thinks the overlay approach should be available for such entities. Moreover, a few preparers have expressed a preference to apply the overlay approach (even if they are eligible for the temporary exemption) and most users preferred the overlay approach to the temporary exemption.

34. The staff notes that if the Board were to decide against the staff recommendation and instead direct the staff to pursue a temporary exemption that assesses eligibility based on parts of the reporting entity (in other words, the exemption would not apply to the entire reporting entity but would apply at a lower level), questions would arise on the need for also having an overlay approach. This is because the population caught by an approach that applies to parts of a reporting entity likely would be similar to the population that would apply the overlay approach under the proposals in the ED.

35. Paragraph 36-38 discusses whether the overlay approach should be optional. The staff outlines in the project plan in paragraphs 42-43 some of the issues on the overlay approach that we plan to consider in the redeliberations.

Should the temporary exemption and the overlay approach be optional?

36. Many users of financial statements have expressed concern about the number of alternative approaches in the ED and the fact that the approaches are proposed to be optional. However, while options, in general, reduce comparability between entities, the staff thinks that it is inappropriate to prohibit a reporting entity from applying IFRS 9 in full (ie by *requiring* it to apply the temporary exemption if it is eligible or by *requiring* it to apply the overlay approach) because IFRS 9 is a significant improvement compared to IAS 39. In addition, for the overlay approach, the optionality could address the concern raised about the additional costs of the overlay approach (discussed in paragraph12(c)).

37. The staff will however consider ways to alleviate the concerns raised by users of financial statements. For example, if changes are made to address the scope of entities eligible for the temporary exemption in a way that better preserves peer comparability within the insurance industry some concerns could be alleviated. In addition, the staff intends to consider whether further disclosures are necessary to assist the comparability between entities that elect the temporary exemption (and thus continue to apply IAS 39) and those entities that apply IFRS 9, with the onus on the entities applying the temporary exemption to produce information that users of financial statements believe is necessary and important to understand the entity's financial performance and position and to enable comparison to entities that apply IFRS 9. For example, staff notes that user feedback indicated that they think that ECL disclosures would be useful for those entities applying the temporary exemption.

38. In addition, based on the feedback received, the staff thinks that entities that qualify for the temporary exemption in a particular jurisdiction are highly likely to make the same choice (ie apply IFRS 9 (with and without the overlay approach), or IAS 39.

Conclusion

39. The staff is asking the Board to decide on key issues that will determine the direction of the project's redeliberations in future months. The analysis in future Agenda Papers will be predicated on the decisions made at this meeting.

40. Overall, the package of the staff recommendation is as follows:

    (a) the overlay approach would be an option available to address any additional volatility and accounting mismatches that may arise if IFRS 9 is applied before the forthcoming insurance contracts Standard;

    (b) the temporary exemption would be an option available for reporting entities that are most affected by the different effective dates (ie those entities that 'predominately issue contracts within the scope of IFRS 4'). For these entities, more accounting mismatches and volatility could arise because the financial assets held to back contracts arising under the scope of IFRS 4 represents a more significant proportion of those entities' assets. Nevertheless, staff thinks that the population of entities eligible for the temporary deferral should be amended to better capture the appropriate entities (ie those considered 'pure insurers'). This is likely to result in the population of qualifying entities being larger than that under the ED's proposals, while the new population would not capture reporting entities with more non-insurance activities (eg banking) compared to that proposed in the ED. This would have the effect of increasing comparability within the insurance sector, while at the same time ensuring that any reporting entities with significant non-insurance activities (eg banking) would not be able to apply the temporary exemption. A key issue that the Board needs to decide is how to regard investment contracts without significant insurance risk that are issued by many life insurers.

(c) the temporary exemption would be optional for qualifying entities and would have a fixed expiry date (instead of expiring when the forthcoming insurance contract Standard is effective).

41. While the package in paragraph 40 would likely result in more entities qualifying for the temporary exemption, not all entities with insurance activities would qualify. An example of a reporting entity that will not qualify for the temporary exemption is a conglomerate with insurance activities and significant banking activities:

(a) That conglomerate will be required to apply IFRS 9 to all of the financial instruments reported in its consolidated financial statements. Staff notes that the overlay approach would be available to such an entity and this approach would address the additional volatility and accounting mismatches arising from the different effective dates for the conglomerate's insurance activities.

(b) In addition, if the insurance activities were undertaken in a separate reporting entity, such as a subsidiary, and separate financial statements are prepared; then the temporary exemption could be applicable for those separate financial statements. Accordingly, that insurance subsidiary could choose to apply IAS 39 to all the financial instruments reported in its separate financial statements. However, the subsidiary would still need to produce IFRS 9 information for the consolidated financial statements. In some cases, an entity may decide that the cost of applying the temporary exemption (ie IAS 39) in its separate financial statements is justified in order to facilitate comparison with other insurers applying IAS 39.

Questions to the Board—project direction

1. Does the Board agree to confirm the ED proposal to provide a temporary exemption from applying IFRS 9 for qualifying entities?

2. Does the Board agree to confirm the ED proposal that the eligibility for the temporary exemption should be determined at the reporting entity level only (ie the assessment is done considering all of the activities of the reporting entity, and the reporting entity applies only one Standard, either IFRS 9 or IAS 39, to all of its financial instruments in its financial statements)?

3. Does the Board agree to confirm that there should be a fixed expiry date for the temporary exemption?

4. Does the Board agree to confirm the ED proposal to provide an overlay approach?

5. Does the Board agree to confirm the ED proposal that the temporary exemption from applying IFRS 9 and the overlay approach should be optional?

Project plan

42. The following table outlines the project plan assuming that the Board agrees with the project direction outlined in Questions 1-5 above. (For completeness, the staff has included in the Appendix the additional considerations that would arise if the Board decides instead to explore a temporary exemption approach that assesses eligibility at a level below the reporting entity.)

43. If the Board is able to make decisions on the technical issues listed in the table below in April and May, the staff thinks that the Board will be in a position to issue final amendments to IFRS 4 in September 2016.

Main topics	Issues to be considered
Temporary exemption Target for Board discussion: April 2016	(a) amendments to the eligibility condition; (b) disclosures required; (c) timing of the eligibility assessment (ie when would the entity determine if it qualifies); (d) whether the entity should reassess its eligibility for the temporary exemption and if so, in what circumstances; (e) whether the entity can stop applying the temporary exemption before the fixed expiry date;
Overlay approach Target for Board discussion:	(f) clarify to which assets the approach applies; (g) the circumstances in which an entity is required or permitted to cease applying the overlay approach and the mechanics that it should apply; (h) presentation in the statement of comprehensive income (eg whether the option proposed in the ED should be restricted); (i) disclosures required; (j) whether the entity can stop applying the overlay

Main topics	Issues to be considered
	approach before applying the forthcoming insurance contracts Standard;
Other issues	(k) the fixed expiry date for the temporary exemption and whether it should also apply to the overlay approach; (l) whether to provide an exemption to IFRS 1 *First-time Adoption of International Financial Reporting Standards* so that specified first-time adopters of IFRS Standards would be permitted to apply the overlay approach and/or temporary exemption; (m) whether an exemption should be provided from requiring the entity's financial statements to be prepared using uniform accounting policies for financial instruments on application of the equity method when accounting for investments in associates and joint ventures under IAS 28 for affected entities (see paragraph 35 of IAS 28);
Due process and permission to ballot	(n) whether the due process steps have been completed; (o) permission to begin the balloting process for the amendments to IFRS 4; and (p) whether any Board member(s) intends to dissent at that stage.

Question to the Board—project timetable
6. Do Board members have any questions and comments of the project timetable?

Appendix: Additional issues if the Board wishes to consider an eligibility assessment below the reporting entity level for the temporary exemption

A1. Additional issues that would need to be considered if the assessment of eligibility for the temporary exemption is made below the reporting entity level include the following:

(a) What should be assessed? Suggestions received: legal entity, combination of several legal entities, approaches that consider different groups of assets of a legal entity (eg at segmental level).

(b) How the assessment should be conducted? Suggestions received: according to the entity determination, top down or bottom-up assessment;

(c) The requirements needed for financial instruments transferred between a part of the group that applies IFRS 9 and a part of the group that applies IAS 39;

(d) presentation and disclosure requirements in the financial statements; and

(e) whether to allow both a reporting entity level and below the reporting entity level assessment, and whether to maintain the overlay approach.