STAFF PAPER

February 2020

IASB® meeting

Project	Amendments to IFRS 17		
Paper topic	Minor amendments		
CONTACT(S)	Roberta Ravelli	rravelli@ifrs.org	+44 (0)20 7246 6935
	Anne McGeachin	amcgeachin@ifrs.org	+44 (0) 20 7246 6486

Purpose of the paper

1. This paper provides staff analysis and recommendations about the feedback from respondents to the Exposure Draft *Amendments to IFRS 17* relating to proposed minor amendments. This paper follows the tentative decision of the International Accounting Standards Board (Board), at its November 2019 meeting, to consider further the feedback from outreach and comment letters on these minor amendments.

2. The Exposure Draft:

   (a) proposed minor amendments to the requirements in IFRS 17 *Insurance Contracts*—as well as some minor consequential amendments to other IFRS Standards—to address a number of cases in which the drafting did not achieve the Board's intended outcome; and

   (b) included a number of editorial corrections to IFRS 17 that the Board had identified after IFRS 17 was issued.

3. Overall, respondents expressed support for the proposed minor amendments. However, some respondents expressed concerns or asked for clarifications about some of the proposed minor amendments. This paper discusses those concerns and requests for clarifications.

Summary of staff recommendations

4. The staff recommend the Board finalise the minor amendments proposed in the Exposure Draft with the following changes:

   (a) the amendment to paragraph B128 of IFRS 17 should specify that changes in the measurement of a group of insurance contracts caused by changes in the *value* of underlying items (excluding additions and withdrawals) are changes arising from the effect of the time value of money and financial risk and changes therein (rather than changes in the *fair value* of underlying items as incorrectly referred to in the Exposure Draft). The last sentence of paragraph B134 of IFRS 17 should clarify that, applying paragraph B134 of IFRS 17, the amount included for the insurance contracts is determined by considering all income or expenses included in profit or loss for the underlying items, wherever in profit or loss the income or expenses are presented (see paragraphs 15–25 of this paper).

   (b) the amendment to paragraph B96(c) of IFRS 17 should also apply to loans to policyholders—ie for insurance contracts without direct participation features, the contractual service margin is not adjusted for changes in fulfilment cash flows arising from differences that relate to the time value of money and assumptions that relate to financial risk between:

      (i) any loan to a policyholder expected to become payable in the period; and

      (ii) the actual loan to the policyholder that becomes payable in the period (see paragraphs 33–37 of this paper).

   (c) the amendment to paragraphs 106(a) and B124 of IFRS 17 should specify that an entity should present experience adjustments for premium receipts *that relate to current or past service* as insurance revenue (see paragraphs 43–47 of this paper).

   (d) the consequential amendment to paragraph 2.1 of IFRS 9 *Financial Instruments* to clarify that insurance contracts held are not in the scope of IFRS 9 should refer to financial guarantee contracts *issued* as being in the scope of IFRS 9 (rather than to financial guarantee contracts—ie issued and held—as incorrectly referred to in the Exposure Draft) (see paragraphs 64–67 of this paper).

Structure of the paper

5. The following table:

   (a) lists the minor amendments in the Exposure Draft for which respondents expressed concerns or asked for clarifications; and

   (b) provides references to the paragraphs in this paper that provide, for each proposed minor amendment:

      (i) an overview of the proposals in the Exposure Draft;

      (ii) an overview of the feedback; and

      (iii) the staff analysis, recommendations and questions for Board members.

Proposed minor amendment	Paragraphs of this paper
1—Proposed amendment to paragraph 11 of IFRS 17	6–9
2—Proposed amendment to paragraph 28 of IFRS 17	10–14
3—Proposed amendment to paragraph B128 of IFRS 17	15–25
4—Proposed amendment to the definition of an investment component	26–32
5—Proposed amendment to paragraph B96(c) of IFRS 17	33–37
6—Proposed amendment to paragraph B123(a) of IFRS 17	38–42
7—Proposed amendment to paragraphs 106(a) and B124 of IFRS 17	43–47
8—Proposed amendment to paragraph B96(d) of IFRS 17	48–53
9—Editorial correction to paragraph B107 of IFRS 17	54–59
10—Proposed consequential amendment to IFRS 3 *Business Combinations*	60–63
11—Proposed consequential amendment to paragraph 2.1 of IFRS 9	64–67

1—Proposed amendment to paragraph 11 of IFRS 17

Proposals in the Exposure Draft

6. The Exposure Draft proposed amending paragraph 11 of IFRS 17 to clarify that, if an entity separates an investment component from a host insurance contract and the component meets the definition of an investment contract with discretionary participation features, the entity should account for that component applying IFRS 17.

Feedback

7. A small number of respondents asked the Board to clarify that an investment contract with discretionary participation features may contain a distinct investment component that should be separated and measured applying IFRS 9.

Staff analysis and recommendation

8. The staff note that:

   (a) a distinct investment component that has been separated from an insurance contract may, in itself, meet the definition of an investment contract with discretionary participation features. Hence, the proposed amendment to paragraph 11 of IFRS 17 aims to specify that such separated investment components are within the scope of IFRS 17.

   (b) applying paragraph 4 of IFRS 17, most of the requirements in IFRS 17 for insurance contracts also apply to investment contracts with discretionary participation features, provided that the entity issuing those investment contracts also issues insurance contracts. The requirements applicable to investment contracts with discretionary participation features include the requirements for separating components from an insurance contract (or from an investment contract with discretionary participation features).[1]

[1] Applying paragraphs 10–13 of IFRS 17, an entity should assess for separation embedded derivatives, investment components, goods and non-insurance services.

9. Therefore, the staff:

   (a) think that the Board does not need to clarify that an investment contract with discretionary participation features may contain components that should be separated applying the requirements in IFRS 17 (ie this is already required); and

   (b) recommend the Board finalise the proposed amendment to paragraph 11 of IFRS 17 as proposed in the Exposure Draft.

2—Proposed amendment to paragraph 28 of IFRS 17

Proposals in the Exposure Draft

10. The Exposure Draft proposed amending paragraph 28 of IFRS 17 to require an entity to include only contracts that meet the criteria for recognition in paragraph 25 of IFRS 17 (rather than contracts issued by the end of the reporting period) in recognising a group of insurance contracts in a reporting period. The proposed amendment aims to clarify that insurance contracts are added to a group when they meet the recognition criteria (which may or may not be when those contracts are issued).

Feedback

11. Respondents generally supported the proposed amendment to paragraph 28 of IFRS 17. However, some respondents disagreed with the Board's decision not to propose the same amendment to paragraph 22 of IFRS 17 (prohibition from including contracts issued more than one year apart in the same group). Those respondents continued to express concerns that:

   (a) tracking insurance contracts based on the issue date requires a database which is not currently available in most systems;

   (b) if two contracts issued more than a year apart meet the recognition criteria in IFRS 17 during the same reporting period, those contracts would need to be included in two different groups; and

(c) in their view, using the word ‘issued’ in paragraph 22 of IFRS 17 and the word ‘recognised’ in paragraph 28 of IFRS 17 creates inconsistencies within IFRS 17.

Staff analysis and recommendation

12. When developing the Exposure Draft, the Board considered whether paragraph 22 of IFRS 17 also needed an amendment to change the reference from ‘issued’ to ‘recognised’. As explained in paragraph BC150 of the Basis for Conclusions on the Exposure Draft, the intention of paragraph 22 of IFRS 17, in contrast to paragraph 28 of IFRS 17, is to refer to the time at which insurance contracts are issued, rather than recognised. Therefore, the Board did not propose amending paragraph 22 of IFRS 17.

13. The Board previously noted that, usually, the date of issue of a contract and the date of recognition will not be far apart. However, if an entity issues profitable contracts for coverage that does not start for several years and the premiums are not due until the coverage starts, the date of recognition will be several years after the date of issue. The objective of prohibiting an entity from including contracts issued more than one year apart in the same group is to provide timely recognition of profits, losses and trends in profitability. The profitability of contracts is initially set when they are issued, based on facts and circumstances (for example, interest rates and underwriting practices) that exist at the date the contracts are issued. Hence, determining annual cohorts based on the date of issue is necessary to provide useful information about trends in profitability.

14. The staff have not identified points the Board has not considered previously and, therefore, the staff recommend the Board finalise the amendment to paragraph 28 of IFRS 17 as proposed in the Exposure Draft and retain, unchanged, paragraph 22 of IFRS 17.

3—Proposed amendment to paragraph B128 of IFRS 17

Proposals in the Exposure Draft

15. The Exposure Draft proposed amending paragraph B128 of IFRS 17 to clarify that, for the purpose of applying IFRS 17, changes in the measurement of a group of insurance contracts caused by changes in the value of underlying items (excluding additions and withdrawals) should be treated as changes in investments—ie they are changes arising from:

    (a) the effect of the time value of money and changes in the time value of money; and

    (b) the effect of financial risk and changes in financial risk.

Feedback

16. Some respondents continued to express concerns that the proposed requirement to present all changes in underlying items as insurance finance income or expenses would distort the presentation of the different sources of profits from insurance contracts. Although more complex, some respondents suggested that the effects of changes in cash flows from participating in underlying items that are not financial in nature (for example, the effect of changes in mortality expectations when insurance contracts are part of underlying items) should be presented instead within the insurance service result. They said this would be consistent with how the changes in the underlying items are themselves presented applying other requirements in IFRS 17.[2]

17. A small number of respondents questioned whether the requirements in paragraph B128 of IFRS 17 apply to both insurance contracts with direct participation features and insurance contracts without direct participation features.

18. A small number of respondents commented on the application of paragraph B134 of IFRS 17 when an entity holds the underlying items of insurance contracts with direct participation features and chooses to present insurance finance income or expenses

[2] Appendix A of IFRS 17 and paragraph B106 of IFRS 17 state that underlying items can comprise any items, for example a reference portfolio of assets, the net assets of the entity, or a specified subset of the net assets of the entity.

partially in profit and loss and partially in other comprehensive income. Applying paragraph B134 of IFRS 17, the entity is required to include in profit or loss expenses or income that exactly match the income or expenses included in profit or loss for the underlying items. This results in the net of the two separately presented items being nil. Those respondents expressed the view that to apply this requirement an entity would be forced to recognise part of the changes in the underlying items in the insurance service result. They said this would not be possible applying the proposed amendment to paragraph B128 of IFRS 17.

Staff analysis and recommendation

Presentation

19. The staff note that the proposed amendment:

    (a) avoids a mismatch for insurance contracts without direct participation features that would otherwise arise when a change in underlying items held by an entity is recognised in the statement of comprehensive income but the effect of that change on the insurance contracts is recognised as an adjustment to the contractual service margin;

    (b) avoids potential double counting of the effect of the risk adjustment for non-financial risk of insurance contracts that have other insurance contracts as underlying items; and

    (c) results in a faithful representation of policyholders' participation in underlying items as participation in an investment.

20. Consider the example of insurance contracts for which the policyholders participate in the returns of non-participating insurance contracts (ie the underlying items are the non-participating insurance contracts). The presentation of the result of the underlying non-participating insurance contracts should not be affected by the fact that policyholders in participating contracts take a share of the result. Rather, the effect of that participation is shown as insurance finance income or expenses, representing the effect of the entity's sharing of its returns with the policyholders participating in the insurance contracts.

21. The staff think this approach is consistent with the requirements in IFRS 17 to group contracts and to account for the outcomes of those groups distinctly from the outcomes of other groups. It is also consistent with the requirements in IFRS 17 to present the result of the insurance activity separately from the result of any reinsurance activity.

22. The staff therefore think that stakeholders' suggestion to present the effect of some changes in underlying items of participating insurance contracts as part of the insurance service result would result in a loss of useful information.

Application to the general model

23. The proposed amendment to paragraph B128 of IFRS 17 applies to both insurance contracts without direct participation features (general model contracts) and insurance contracts with direct participation features (variable fee approach contracts). The staff acknowledge that the proposed wording 'changes in fair value of underlying items' in paragraph B128(c) of the Exposure Draft raises questions in the context of the measurement of general model contracts. For general model contracts, IFRS 17 requires an entity to measure amounts related to underlying items at the present value of the risk adjusted probability-weighted cash flows, using current market consistent assumptions, rather than at fair value.[3] The staff think that the reference to 'fair value' in paragraph B128(c) is a drafting error in the Exposure Draft that the staff will remove if the Board decides to finalise the amendment to paragraph B128 of IFRS 17.

Current period book yield

24. In relation to stakeholders' concerns about the application of paragraph B134 of IFRS 17 (sometimes referred to as 'current period book yield'), the staff observe that paragraph B134 of IFRS 17 applies to insurance contracts with direct participation features when the entity holds the underlying items of those contracts. If applied, it requires an entity to disaggregate the insurance finance income or expenses between profit or loss and other comprehensive income by including in profit or loss the amount that exactly matches the income or expense included in profit or loss for the underlying items. The staff note that some respondents read the words of

[3] For variable fee approach contracts, IFRS 17 requires an entity to measure the fulfilment cash flows based on the fair value of the underlying items.

paragraph B134 of IFRS 17 as reflecting the situation in which all the income or expenses on the underlying items are financing items. This is because it states that the result is ‘the net of the *two* separately presented items [investment income on underlying items and insurance finance income or expenses] being nil’. However, the requirement in paragraph B134 of IFRS 17 avoids an accounting mismatch *in profit or loss as a whole*, and the amount included for the insurance contracts is determined applying paragraph B134 of IFRS 17 by considering all income or expenses included in profit or loss for the underlying items, wherever in profit or loss the income or expenses are presented. The staff, therefore, do not think an amendment to paragraph B134 of IFRS 17 is needed because of the proposed change to paragraph B128 of IFRS 17, other than the following correction to the last sentence of paragraph B134 of IFRS 17:

> B134 … If an entity chooses to disaggregate insurance finance income or expenses applying paragraph 89(b), it shall include in profit or loss expenses or income that exactly match the income or expenses included in profit or loss for the underlying items, resulting in the net of the ~~two~~ separately presented items being nil.

Staff recommendation

25. The staff therefore recommend the Board:

    (a) finalise the amendment to paragraph B128 of IFRS 17 to specify that changes in the measurement of a group of insurance contracts caused by changes in the *value* of underlying items (excluding additions and withdrawals) are changes arising from the effect of the time value of money and financial risk and changes therein; and

    (b) reflect a correction to the last sentence of paragraph B134 of IFRS 17 by deleting the word ‘two’ as discussed in paragraph 24 of this paper.

4—Proposed amendment to the definition of an investment component

Proposals in the Exposure Draft

26. The Exposure Draft proposed amending the definition of an investment component in Appendix A of IFRS 17 to clarify the Board's intention that an investment component is the amount an insurance contract requires the entity to repay to a policyholder in all circumstances, regardless of whether an insured event occurs.

Feedback

27. Some respondents:

    (a) suggested alternative definitions of an investment component, such as limiting insurance contracts including an investment component to contracts with:

      (i) a right for the policyholder to withdraw a deposit;

      (ii) account or unit balances or surrender values; or

      (iii) cash flows for which repayment is certain and contingent only on the passage of time.

    (b) asked the Board to clarify whether policy loans meet the definition of an investment component, also in the light of the explanation in paragraph BC114 of the Basis for Conclusions on IFRS 17;[4]

    (c) asked the Board to clarify that an entity is required to identify whether an investment component exists at initial recognition of an insurance contract and to measure any non-distinct investment component when a claim occurs; and

    (d) asked the Board to define a premium refund in IFRS 17 to make it easier to distinguish repayments of investment components from refunds of premiums.

[4] Paragraph BC114 of the Basis for Conclusions on IFRS 17 explains that the Board considered whether to permit an entity to separate a non-insurance component when not required to do so by IFRS 17; for example, some investment components with interrelated cash flows, such as policy loans.

Staff analysis and recommendation

28. The staff observe that the alternative definitions of an investment component suggested by respondents indicate differences in perspective between the Board and some respondents about the cash flows in an insurance contract that an entity should exclude from both insurance revenue and insurance service expenses, rather than a disagreement with the proposed amendment to the definition of an investment component itself. The objective of the proposed amendment was to more clearly articulate what the Board has previously concluded is an investment component whereas these suggestions would introduce changes to the Board's previous conclusions.

29. The staff note that:

    (a) IFRS 17 does not include specific requirements for accounting for a policy loan. The term 'policy loan' is not defined in IFRS 17 and might be used to refer to various forms of cash flows related to an insurance contract. It typically refers to an amount lent by an entity to a policyholder as either an advance payment of an investment component embedded in an insurance contract or a loan to a policyholder. The requirements in IFRS 17 that identify the fulfilment cash flows will determine whether amount regarded by an entity as policy loans are cash flows within the contract boundary.

    (b) paragraph BC114 of the Basis for Conclusions on IFRS 17 does not state that 'policy loans' are investment components. Typically, a 'loan' does not meet the definition of an investment component because it is not the amount an insurance contract requires the entity to *repay* to a policyholder. The policyholder typically borrows an amount from future benefits payable under an insurance contract and either repays the loan subsequently or forfeits some of the future benefit in lieu of repayment. Applying paragraph B123(a)(iia) of the Exposure Draft that amount does not generate revenue for the entity (see paragraphs 38–42 of this paper).

30. The staff observe that, at its April 2019 meeting, the Transition Resource Group for IFRS 17 (TRG) discussed determining the amount of an investment component. TRG members observed that an entity identifies amounts of a non-distinct investment component only when insurance revenue and incurred claims are recognised.[5]

31. The staff think that, although introducing a definition of a premium refund in IFRS 17 as suggested by some respondents might be helpful in some circumstances, it might raise new questions about applying the definition in other circumstances. Therefore, it might unduly disrupt implementation for entities.

32. As explained in paragraph BC156 of the Basis for Conclusions on the Exposure Draft, paragraph BC34 of the Basis for Conclusions on IFRS 17 explains that an investment component is an amount that is paid to the policyholder in all circumstances. The purpose of the proposed amendment is only to capture that explanation in the wording of the definition. Accordingly, the staff recommend the Board finalise the amendment to the definition of an investment component as proposed in the Exposure Draft.

5—Proposed amendment to paragraph B96(c) of IFRS 17

Proposals in the Exposure Draft

33. The Exposure Draft proposed amending paragraph B96(c) of IFRS 17 to clarify that, for insurance contracts without direct participation features, the contractual service margin is not adjusted for changes in fulfilment cash flows arising from differences that relate to the time value of money and assumptions that relate to financial risk between:

    (a) any investment component expected to become payable in the period; and

    (b) the actual investment component that becomes payable in the period.

[5] As noted in Agenda Paper 1 of the April 2019 TRG meeting, for an insurance contract that includes an investment component, IFRS 17 requires an entity to: (a) separate from the insurance contract any distinct investment component and apply IFRS 9 to such a component; and (b) consider whether the remainder of the insurance contract requires the entity to pay any amounts to the policyholder in all circumstances (after separating the distinct investment component, if any). Paragraph 85 of IFRS 17 requires the entity to exclude those amounts from the insurance revenue and insurance service expenses presented in profit or loss.

Feedback

34. A small number of respondents:

(a) expressed concerns that the proposed amendment would add operational complexity because it would require segregation of any unexpected investment component payments into a part which is due to a change in financial variables (ie time value of money and financial risk) and a part which is due to a change in non-financial variables.

(b) questioned whether an entity should present the changes discussed in paragraph 33 of this paper as part of the insurance service result or insurance finance income or expenses.

(c) questioned whether requirements similar to those in paragraph B96(c) of IFRS 17 apply to loans to policyholders that do not meet the definition of an investment component. They indicated that paragraph B96 of IFRS 17 should also specify that the contractual service margin is not adjusted for changes in fulfilment cash flows arising from differences that relate to the time value of money and assumptions that relate to financial risk between:

(i) any loan to a policyholder expected to become payable in the period; and

(ii) the actual loan to the policyholder that becomes payable in the period.

(d) asked the Board clarify the interaction between the requirements in paragraph B96(c) of IFRS 17 and those in paragraph B123(a) of IFRS 17 for loans to policyholders (see paragraph 38–42 of this paper).

Staff analysis and recommendation

35. The recognition of changes relating to the time value of money and financial risk in the statement of comprehensive income as insurance finance income or expenses is a clear principle of the general model in IFRS 17. The proposed amendment to paragraph B96(c) of IFRS 17 only clarifies that that principle applies to the changes arising from investment components. The staff think that introducing an exception to this principle would add further complexity to the treatment of changes in the

measurement of a group of insurance contracts without direct participation features. The staff therefore recommend the Board finalise the amendment to paragraph B96(c) of IFRS 17 as proposed in the Exposure Draft.

36. The staff note that, for insurance contracts without direct participation features, paragraph 87 of IFRS 17 states that insurance finance income or expenses comprises the change in the carrying amount of the group of insurance contracts arising from the effect of the time value of money and changes in the time value of money and the effect of financial risk and changes in financial risk. Accordingly, the staff think that the Board does not need to clarify that, applying paragraph B96(c) of IFRS 17, an entity presents as insurance finance income or expenses changes in fulfilment cash flows relating to the time value of money and assumptions that relate to financial risk that arise from differences between any investment component expected to become payable in the period and the actual investment component that becomes payable in the period.

37. The staff agree with respondents that noted that the same requirements in paragraph B96(c) of IFRS 17 for investment components should apply to loans to policyholders—ie amounts in an insurance contract that the entity lends to the policyholder and expects the policyholder to repay at a later date. Accordingly, the staff recommend the Board amend IFRS 17 to clarify that, for insurance contracts without direct participation features, the contractual service margin is not adjusted for changes in fulfilment cash flows arising from differences that relate to the time value of money and assumptions that relate to financial risk between:

    (a) any loan to a policyholder expected to become payable in the period; and

    (b) the actual loan to the policyholder that becomes payable in the period.

6—Proposed amendment to paragraph B123(a) of IFRS 17

Proposals in the Exposure Draft

38. The Exposure Draft proposed amending paragraph B123(a) of IFRS 17 to clarify that changes in the liability for remaining coverage caused by cash flows from loans to policyholders do not give rise to insurance revenue because they do not relate to insurance contract services provided by the entity.

Feedback

39. A small number of respondents questioned whether this proposed amendment would apply to policy loans.

Staff analysis and recommendation

40. The staff note that, consistent with changes that relate to an investment component in the period (see paragraph B123(a)(ii) of IFRS 17), the proposed amendment to paragraph B123(a) of IFRS 17 aims to clarify that changes resulting from cash flows from loans to policyholders do not give rise to insurance revenue.

41. As discussed in paragraph 29 of this paper, although the term 'policy loan' is not defined in IFRS 17, it typically refers to an amount lent by an entity to a policyholder as either an advance payment of an investment component embedded in an insurance contract or a loan to a policyholder. Either way they will be covered by paragraph B123(a) of IFRS 17 and therefore those amounts (and changes in them) do not give rise to insurance revenue.

42. Therefore, the staff recommend the Board finalise the proposed amendment to paragraph B123(a) of IFRS 17.

7—Proposed amendment to paragraphs 106(a) and B124 of IFRS 17

Proposals in the Exposure Draft

43. The Exposure Draft proposed that an entity should present experience adjustments for premium receipts as insurance revenue (see paragraphs 106(a)(iv) and B124(d) of the Exposure Draft).

Feedback

44. A small number of respondents:

    (a) expressed concerns that this proposed amendment seems inconsistent with the requirement in paragraph B96(a) of IFRS 17, which states that experience adjustments arising from premium received in the period that relate to future service should adjust the contractual service margin; and

    (b) suggested specifying that the proposed amendment refers to experience adjustments for premium receipts that relate to current or past service.

Staff analysis and recommendation

45. The staff note that:

    (a) experience adjustments arising from premium received in the period that relate to future service adjust the contractual service margin; and

    (b) experience adjustments arising from premium received in the period that relate to current or past service are recognised immediately in the statement of comprehensive income.

46. The staff agree with some respondents who suggested that it would be helpful specifying that the proposed amendment refers to experience adjustments for premium receipts that relate to current or past service.

47. Accordingly, the staff recommend the Board confirm the proposed amendment to paragraphs 106(a) and B124 of IFRS 17 but specify that an entity should present experience adjustments for premium receipts *that relate to current or past service* as insurance revenue.

8—Proposed amendment to paragraph B96(d) of IFRS 17

Proposals in the Exposure Draft

48. The Exposure Draft proposed amending paragraph B96(d) of IFRS 17 to clarify that, for insurance contracts without direct participation features, if an entity disaggregates the change in the risk adjustment for non-financial risk between the insurance service result and insurance finance income or expenses, the entity adjusts the contractual service margin only for the changes related to non-financial risk, measured at the discount rates determined on initial recognition (locked-in discount rates).

Feedback

49. A small number of respondents disagreed with this proposed amendment, particularly with the reference to locked-in discount rates. Some of those respondents would prefer that an entity is required to measure the adjustment to the contractual service margin discussed in paragraph 48 of this paper using current discount rates.

50. A small number of respondents provided drafting suggestions to align the wording of paragraphs 81, 87 and B96(d) of IFRS 17 (for example, adding the effect of financial risk and changes in financial risk to the wording of paragraph B96(d) of IFRS 17).

Staff analysis and recommendation

51. The staff note that:

    (a) the requirement to use locked-in discount rates to measure changes to the contractual service margin is a fundamental principle of the measurement of insurance contracts without direct participation features.

    (b) applying paragraph 81 of IFRS 17, an entity can choose not to disaggregate the change in the risk adjustment for non-financial risk between the insurance service result and insurance finance income or expenses and to recognise the entire effect of the change as an adjustment to the contractual service margin. This means that an entity is not required to disaggregate the change in the risk adjustment for non-financial risk between:

(i) a change related to non-financial risk, which adjusts the contractual service margin and therefore is recognised as insurance service result over time; and

(ii) the effect of the time value of money and changes in the time value of money, which is recognised immediately in the statement of comprehensive income as insurance finance income or expenses.

52. Accordingly, the staff recommend the Board finalise the proposed amendment to paragraph B96(d) of IFRS 17 to clarify that, for insurance contracts without direct participation features, if an entity chooses to disaggregate the change in the risk adjustment for non-financial risk between the insurance service result and insurance finance income or expenses, the entity should adjust the contractual service margin only for the changes related to non-financial risk, measured at the discount rates determined on initial recognition (locked-in discount rates).

53. The staff plan to consider the drafting suggestions discussed in paragraph 50 of this paper when drafting the final amendments to IFRS 17.

9—Editorial correction to paragraph B107 of IFRS 17

Proposals in the Exposure Draft

54. The Exposure Draft proposed amending paragraph B107 of IFRS 17 to specify that, when assessing whether a contract meets the criteria for the scope of the variable fee approach, an entity should assess the variability of the amounts to be paid to the policyholder over the duration of the insurance contract (rather than over the duration of the group of insurance contracts as incorrectly specified by paragraph B107 of IFRS 17 as originally issued). The Board considered this to be an editorial correction.

Feedback

55. Some respondents view the proposed amendment to paragraph B107 of IFRS 17 as a major change to the requirements in IFRS 17 that would disrupt implementation, rather than as an editorial correction.

56. Some of those respondents had assumed that an entity is required to apply the criteria for the scope of the variable fee approach in paragraph B101 of IFRS 17 at the level of a group of insurance contracts for consistency with paragraph 24 of IFRS 17. That paragraph states that an entity should apply the recognition and measurement requirements of IFRS 17 to groups of insurance contracts. Those respondents expressed the view that it would be burdensome for entities to allocate all cash flows to individual insurance contracts in order to perform the eligibility test for the variable fee approach.

Staff analysis and recommendation

57. The staff note that IFRS 17 includes different requirements for insurance contracts with direct participation features (contracts to which the variable fee approach applies) and for insurance contracts without direct participation features (contracts to which the general model applies). Accordingly, an entity is required to:

    (a) distinguish between insurance contracts with direct participation features and insurance contracts without direct participation features; and

    (b) apply the variable fee approach measurement requirements to groups of insurance contracts with direct participation features and the general model measurement requirements to groups of insurance contracts without direct participation features—ie a group of insurance contracts cannot at inception include a mix of insurance contracts with direct participation features and insurance contracts without direct participation features.

58. Insurance contracts with direct participation features are defined in paragraph B101 of IFRS 17. This paragraph requires an entity to assess whether it expects to pay a substantial share of fair value returns to *the policyholder*, and whether a substantial proportion of changes in amounts paid to *the policyholder* are expected to vary with changes in the fair value of the underlying items. To apply paragraph B101 of IFRS 17:

(a) paragraph B102 of IFRS 17 specifies that an entity assesses whether the conditions in paragraph B101 of IFRS 17 are met using its expectations at inception of *the contract* and does not reassess the conditions afterwards, unless *the contract* is modified;

(b) paragraph B103 of IFRS 17 specifies that if a contract affects the cash flows to policyholders of other contracts an entity assesses whether the conditions in paragraph B101 of IFRS 17 are met by considering also those cash flows; and

(c) paragraph B107 of IFRS 17 specifies how to assess the variability of the amounts mentioned in paragraph B101 of IFRS 17.

59. In the light of the analysis in paragraphs 57–58 of this paper, the staff think that it is clear that an entity is required to apply the criteria for the scope of the variable fee approach at the level of an individual contract applying IFRS 17. Accordingly, the staff recommend the Board finalise the editorial correction to paragraph B107 of IFRS 17 to ensure consistency within IFRS 17.

10—Proposed consequential amendment to IFRS 3

Proposals in the Exposure Draft

60. The Exposure Draft proposed amending IFRS 3 to clarify that an entity can continue to classify insurance contracts acquired through a business combination that occurred *before* the date of initial application of IFRS 17 based on the contractual terms and other factors at the inception of the contract, rather than at the acquisition date.

Feedback

61. A small number of respondents commented to support the clarification. However, they continued to suggest the Board amend IFRS 17 to extend this exception to the principle in IFRS 3 (ie an acquirer classifies assets acquired and liabilities assumed based on the terms and conditions as they exist at the acquisition date) to contracts acquired through a business combination that occurred *after* the date of initial application of IFRS 17.

Staff analysis and recommendation

62. At its November 2019 meeting, the Board tentatively decided that it would not consider further the feedback on the classification of contracts acquired through a business combination because:

    (a) when developing the Exposure Draft the Board considered the concerns and suggestions from respondents regarding the requirement in paragraph 15 of IFRS 3 that an entity should classify assets acquired and liabilities assumed based on the terms and conditions as they exist at the acquisition date; and

    (b) the staff have not identified points the Board has not considered previously.

63. Accordingly, the staff recommend the Board finalise the proposed consequential amendment to IFRS 3 to clarify that an entity can continue to classify insurance contracts acquired through a business combination that occurred *before* the date of initial application of IFRS 17 (and only those business combinations) based on the contractual terms and other factors at the inception of the contract, rather than at the acquisition date.

11—Proposed consequential amendment to paragraph 2.1 of IFRS 9

Proposals in the Exposure Draft

64. The Exposure Draft proposed amending paragraph 2.1 IFRS 9 to clarify that, consistent with the scope of that Standard before IFRS 17 was issued, insurance contracts held are not in the scope of IFRS 9.

Feedback

65. Some respondents noted a mistake in the drafting of the proposed consequential amendment to paragraph 2.1 of IFRS 9 that would result in the unintended consequence of requiring entities to account for financial guarantee contracts held applying IFRS 9.

Staff analysis and recommendation

66. The staff acknowledge the Exposure Draft included a drafting error that inadvertently resulted in proposing that an entity is required to apply IFRS 9 to all financial guarantee contracts (whether issued or held).

67. The staff recommend the Board confirm the proposed consequential amendment to paragraph 2.1 of IFRS 9 to clarify that insurance contracts held are not in the scope of IFRS 9. To achieve that objective the consequential amendment should refer to financial guarantee contracts *issued* as being in the scope of IFRS 9 (rather than to financial guarantee contracts—ie issued and held—as incorrectly specified in the Exposure Draft). This would reinstate the scope of IFRS 9 as it was prior to the issue of IFRS 17, which was the intention of the amendment.

Question for Board members
Do you agree with the staff recommendations for finalising the minor amendments proposed in the Exposure Draft with the changes discussed in this paper?