Alert: Amendments to IFRS 17 *Insurance Contracts*

May 2020

Background

In June 2020, the International Accounting Standards Board (IASB) amended IFRS 17 *Insurance Contracts* in response to concerns and challenges raised by stakeholders on the implementation of IFRS 17. The main objective of the proposed amendments are to ease the IFRS 17 implementation by addressing, and providing support, on several issues encountered by insurers as they started their implementation process. The targeted amendments will also make it easier for insurers to explain the results of applying IFRS 17 to investors.

Scope

Additional scope exclusions have been approved for IFRS 17.

The first relates to credit card contracts, and other similar contracts that provide credit or payment arrangements, that meet the definition of an insurance contract. Such contracts can be excluded from the scope of IFRS 17 if the fee charged to the customer on those contracts does not reflect an assessment of the insurance risk associated with the individual customer. If the entity provides the insurance coverage to the customer as part of the contractual terms of such a contract, the entity is required to apply IFRS 17 to the insurance coverage component and other applicable IFRS standards (e.g. IFRS 9) to the other components of the contract.

The second new scope exclusion permits an entity to apply either IFRS 17 or IFRS 9 to insurance contracts that limit compensation for insured events to the amount required to settle the policyholder’s obligations created by the contract. This option would be made at a portfolio level and would be irrevocable.

Recognition & Measurement

A number of changes to the recognition and measurement requirements of IFRS 17 have been approved by the IASB as follows:

- For the expected recovery of insurance acquisition cash flows:
    - Part of the insurance acquisition cash flows are allocated to expected contract renewals.
    - The insurance acquisition cash flows are to be recognized as an asset when paid until the entity recognizes contract renewals.
    - The insurance acquisition cash flows recognized as an asset must be assessed for recoverability at each reporting period if facts and circumstances indicate the asset may be impaired.
    - For insurance contracts acquired in a business combination or asset acquisition, an asset is recognized for insurance acquisition cash flows and is measured at fair value as at the date of acquisition.
- For insurance contracts with direct participation features, the contractual service margin should be recognized in profit or loss considering both insurance coverage and investment-related service.
- The use of the risk mitigation option has been extended for insurance contracts with direct participation features when the entity uses reinsurance contracts or non-derivative financial instruments measured at fair value through profit or loss to mitigate financial risks.
- For all reinsurance contracts held, a gain should be recognized when the underlying contracts are onerous and only if the reinsurance contracts are entered into before or at the same time the onerous underlying contracts are issued. The gain is recognized based on a fixed percentage of claims that the entity expects to recover from holding the reinsurance contracts.

Presentation & Disclosure

The amendments to IFRS 17 includes a simplified balance sheet presentation for insurance contract assets and liabilities to require that they be aggregated at a portfolio level rather than at a group level.

Further, new required disclosures include:

- A reconciliation from the opening to closing balance of any asset for insurance acquisition cash flows, showing separately impairment losses or reversals of impairment.
- Quantitative information (i.e., time bands) for when the entity expects to derecognize an asset for insurance acquisition cash flows.
- Quantitative information about when the entity expects to recognize in profit or loss the contractual service margins remaining as at the reporting date.
- The entity's judgement applied to assess the relative weighting of the benefits from insurance coverage and investment-related services or investment-return services.

Interim Financial Statements

A new accounting policy choice has been introduced to permit entities to decide whether to change the treatment of accounting estimates made in prior interim financial statements when IFRS 17 is subsequently adopted.

Transitional Relief

The following transitional reliefs are included as part of the amendments to IFRS 17:

- A requirement to recognize an asset for acquisition cash flows retrospectively as at the date of transition, unless impracticable. If impracticable, the modified retrospective or fair value approach would be applied.
- At the transition date, there is no requirement for an entity to determine whether facts or circumstances existed prior to that date that could indicate impairment of assets recognized.
- Permission to apply the risk mitigation option from the IFRS 17 transition date if the entity designates the risk mitigation relationships to which it will apply the option no later than that date.
- Permission to use the fair value approach to transition, if the entity chooses to apply the risk mitigation option prospectively from the transition date, has used derivatives or reinsurance to mitigate financial risk before the date of transition and can apply IFRS 17 retrospectively.
- For entities applying the modified retrospective approach, liabilities for claims settlement acquired in a business combination or portfolio transfer are required to be recognized as a liability for incurred claims if the entity does not have reasonable and supportable information to apply a retrospective approach.
- Extensions of the modification in the modified retrospective approach and relief in the fair value approach to permit an entity to determine whether a contract meets the definition of an investment contract with discretionary participation features using information available at the date of transition to IFRS rather than at inception or initial recognition. This extension is only available when the entity does not have reasonable and supportable information to apply the retrospective method.
- An amendment to the modification in the modified retrospective approach to specify that if an entity does not have reasonable and supportable information to identify whether the reinsurance contract held was acquired before or at the same time that the underlying onerous insurance contracts were issued, the entity must assume it was acquired after.
  - Therefore, the reinsurance contract would not have a loss-recovery component at the date of transition.
- The addition of a modification for entities that do not have reasonable and supportable information to apply their accounting policy relating to the treatment of accounting estimates in previous interim financial statements retrospectively. Under this modification, the entity determines the contractual service margin, loss component and amounts related to insurance finance income/expenses at the date of transition as if interim financial statements had not been prepared prior to that date.

Effective Date

IFRS 17 was initially effective for annual periods beginning on or after January 1, 2021, with earlier application permitted if IFRS 9 *Financial Instruments* and IFRS 15 *Revenue from Contracts with Customers* are applied at, or earlier than, the adoption date.

In October 2020 the IASB deferred the effective date of the initial application of IFRS 17, including the above-noted amendments, by two years to annual reporting periods beginning on or after January 1, 2023 and changed the fixed expiry date for the temporary exemption in IFRS 4, *Insurance Contracts* from applying IFRS 9, *Financial Instruments* so that entities would also be required to apply IFRS 9 for annual periods beginning on or after January 1, 2023.

Resources

The full history of this IASB project, including related supporting materials, can be accessed here.

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