How we responded to feedback on the 2013 Exposure Draft

In the redeliberation phase of the 2013 Exposure Draft *Insurance Contracts* (the 2013 ED), the IASB responded to the feedback on the proposals in the 2013 ED as summarised in the table below.

- Issues 1-5 describe the five targeted areas on which the IASB sought specific input in the 2013 ED.
- Issues 6-12 describe the additional issues which the IASB decided to consider that were not specifically targeted for the feedback.

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<tr><th>Proposal in 2013 Exposure Draft</th><th>Feedback received</th><th>How the IASB responded</th></tr>
<tr><td colspan="3">1. Measurement proposal: unlocking of the contractual service margin (CSM)</td></tr>
<tr><td>• The changes in present value of expected cash flows related to future service should be recognised over the period during which the future service is provided, rather than when the change becomes known.

• Accordingly, the CSM should be adjusted for the difference between the current and previous estimates of the present value of future cash flows, if those differences relate to future coverage and other future services, provided that the CSM would not be negative.

• Because changes in estimates are offset within the insurance contract, the total carrying value of the insurance contract before and after the change in estimates would remain the same. To explain</td><td>• There was a general agreement with the proposals for unlocking the CSM from all types of constituents and jurisdictions. However, some users of financial statements and regulators believe that unlocking decreases transparency because the amounts are offset within the insurance liability. Some also believe that unlocking inappropriately smoothens the underwriting result. Many noted the consequent importance of the reconciliation of the insurance contract balance.

• Some propose refining the proposals as follows:
○ the CSM should be unlocked for the changes in risk adjustment; and
○ losses previously recognised in profit or</td><td>Consistently with the feedback received, the Board tentatively decided to confirm that, after inception, the CSM would be adjusted for changes between the current and previous periods' estimates of the present value of future cash flows relating to future service.

After considering the feedback to the 2013 ED, the Board tentatively decided that:

• an entity should unlock the CSM for the changes in risk relating to future service, consistently with the changes in estimates of cash flows to which the risk adjustment relates. Changes in discretionary cash flows, as specified by the entity, should be regarded as relating to future service.

• favourable changes in estimates that arise after losses were previously recognised in profit or</td></tr>
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Proposal in 2013 Exposure Draft	Feedback received	How the IASB responded
changes in the assumptions in the period, the IASB proposed that an entity should provide a reconciliation of the insurance contract balances (including changes in the CSM). • To decrease the operational burden an entity should adjust the CSM prospectively. Therefore, the entity does not need to adjust previously recognised gains and losses.	loss should be reversed before the CSM is rebuilt. • Some preparers (especially smaller preparers and those from emerging economies) had operational concerns about: ○ whether it is possible to distinguish estimates of cash flows relating to past service from estimates of cash flows relating to future service. ○ the need to track information and unit of account for unlocking the CSM. • Some suggested that additional changes in estimates for contracts with participation features should be offset in the CSM.	loss should be recognised in profit or loss to the extent that they reverse losses that relate to coverage and other services in the future. • the guidance on changes in the fulfilment cash flows that relate to future service and those that relate to current and past service should be clarified. The Board noted the concerns about operational complexity but concluded that these concerns were outweighed by the depiction of unearned profit resulting from unlocking the CSM. Contracts with participation features are discussed in Item 2.
2. Measurement proposal: mirroring exception for some contracts with participation features		
• The 2013 ED proposed that an entity should measure and present cash flows that vary directly with underlying items on the basis used to measure and present the cash flows of the underlying items (the mirroring exception). Cash flows that vary directly with underlying items arise when an insurance contract promises both insurance protection and a return on	• Respondents criticised the mirroring exception for being unduly complex, questioning whether entities would be able to identify the cash flows that the mirroring would apply to. • In addition, some respondents noted that the scope of the mirroring exception would be unduly narrow. As a result, the mirroring exception would avoid accounting	The Board tentatively decided that the mirroring approach proposed in paragraphs 33-34 of the 2013 ED should not be permitted or required. The Board reconsidered its proposals for all contracts with participation features, defined as those for which cash flows varied with returns on underlying items. As a result, the Board tentatively decided:

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underlying items (for example financial assets). When cash flows vary directly with underlying items, there is no risk to the insurer arising from economic mismatches between the cash flows promised to the policyholders and the cash flows of the underlying items. • In addition, the ED proposed that, when mirroring applies, an entity should recognise changes in options and guarantees immediately in profit or loss.	mismatches for only some participating contracts. Many constituents questioned whether the mirroring exception was worthwhile, given its narrow scope, and suggested that the IASB should consider developing different solutions to accounting mismatches that could be applied more generally. • Many constituents thought that there should be consistent treatment of the options and guarantees embedded in insurance contracts, though there was a diverse range of views about what that treatment should be.	• that for insurance contracts with direct participation features, changes in the estimate of the fee (equal to the entity's expected share of the returns on underlying items, less any expected cash flows that do not vary directly with the underlying items) that the entity expects to earn from the contract are adjusted in the CSM. • that contracts with direct participation features should be defined as contracts for which: i. the contractual terms specify that the policyholder participates in a share of a clearly identified pool of underlying items; ii. the entity expects to pay to the policyholder an amount equal to a substantial share of the returns from the underlying items; and iii. a substantial proportion of the cash flows that the entity expects to pay to the policyholder should be expected to vary with the cash flows from the underlying items. • in some specific situations when an entity uses a derivative to mitigate the financial market risk from the guarantee embedded in insurance contracts with direct participation features, the entity should be permitted to recognise in profit

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		or loss (rather than CSM) the changes in the value of the guarantee embedded in an insurance contract.
3. Presentation proposal: revenue consistent with revenue for non-insurance services		
• An entity should present revenue and expense for all insurance contracts consistently with revenue for other types of contracts with customers. Consequently: ○ revenue should be reported as the entity provides services under the contract. The services that an entity provides in each period are measured by reference to the change in the measurement of the insurance contract liability. ○ expenses should be reported as incurred. ○ both revenue and expense should exclude investment components. • An entity should disclose: ○ reconciliations for the amounts recognised in the reporting period that explain how the premiums received relates to insurance contract revenue, and the inputs used to determine	• Some respondents supported the objective of consistent reporting of revenue and expense for entities that issue insurance contracts compared with those that do not, thereby assisting non-specialist investors in making decisions. • Some preparers opposed the revenue proposals, stating that coexistence of two different presentation requirements for life and non-life insurance contracts respectively better reflects the different nature of those contracts. They proposed that entities should instead present as revenue existing measures such as premiums due or premiums written. • All users agreed that the repayment of an investment component should not be presented as part of the revenue and claims. The main reason was comparability and consistency with revenue presented for other service contracts. However, there was strong disagreement from life	The Board tentatively decided: • to confirm the proposal in 2013 ED that insurance contract revenue and expense should be presented in the statement of comprehensive income. Revenue should be recognised as earned and exclude investment components. • to prohibit the presentation of premium information in the statement of comprehensive income if that information is not consistent with commonly understood notions of revenue. • to confirm most of the disclosures relating to revenue proposed in the 2013 ED.

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<tr><td>insurance contracts revenue.
o the effect of the insurance contracts that are initially recognised in the period on the amounts that are recognised in the statement of financial position.</td><td>insurance preparers, on grounds of complexity.</td><td></td></tr>
<tr><td colspan="3">4. Presentation proposal: effect of changes in the discount rate presented in Other Comprehensive Income (OCI)</td></tr>
<tr><td>• An entity should be required to present an amortised cost view of the changes in the insurance contract that separates market fluctuations resulting from the discount rate changes from other changes in the performance of the entity.

• Consequently,
o the effect of the changes in the discount rate on the insurance contract liability should be excluded from the profit or loss statement and presented in OCI.
o the interest expense in the profit or loss statement should be presented on an amortised cost basis.</td><td>• Many users of financial statements agreed that both the amortised cost and current value view provide useful information.

• Some preparers, in particular non-life insurers that intended to use the simplified model for measuring insurance contracts) were concerned about the complexity and operational burden that requiring this disaggregation would impose.

• Many preparers and users were concerned about the possible accounting mismatches that could occur between insurance contracts measured using OCI and assets that are measured other than at fair value through OCI. Those mismatches would arise, for example, because IFRS 9 Financial Instruments requires a mixed measurement attribute approach for measuring financial assets.</td><td>The Board tentatively decided that:
• an entity should make an accounting policy choice between:
o including insurance finance income or expenses for the period in the statement of profit or loss; or
o disaggregating insurance finance income or expenses for the period into an amount recognised in profit or loss and an amount recognised in OCI.

• an entity should apply the same accounting policy to all similar insurance contracts, and apply IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors to changes in the accounting policy.

• if an entity disaggregates insurance finance income or expenses into an amount recognised in profit or loss and an amount recognised in</td></tr>
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	• Some suggested that, for contracts with participation features, the interest expense presented in profit or loss should be based on the presentation of the underlying assets that the entity holds.	OCI: ○ in most circumstances, the amount included in the statement of profit or loss is determined by a systematic allocation of the total expected insurance finance income or expenses over the life of the contract. ○ when the contract is an insurance contract with direct participation features and the entity holds the underlying items whether by choice or by requirement (ie there is no economic mismatch between the contract and related underlying items), the amount included in the statement of profit or loss is determined so as to eliminate accounting mismatches with the finance income or expenses arising on the underlying items held.
5.a. Transition: measurement		
At transition, an entity should measure: • The fulfilment cash flows using current information at transition date; and • the CSM and cumulative OCI retrospectively if practicable. If it is not practicable, the CSM and OCI should be determined using specified simplifications.	• The proposals for transition were widely supported, though there were concerns about the operational complexity in some jurisdictions. Consequently, some suggested further refinements to the simplifications provided.	The Board tentatively decided: • to confirm the 2013 ED proposals that at the beginning of the earliest period presented, an entity should apply the Standard retrospectively in accordance with IAS 8 unless impracticable. • if retrospective application of the Standard is impracticable, an entity should apply a simplified approach. The Board tentatively decided to

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		further simplify the approach proposed in paragraphs C5 and C6 of the 2013 ED for insurance contracts that do not have direct participation features, and to add a simplification for insurance contracts with direct participation features. • if it is impracticable to determine the CSM using the simplified approach described above, an entity should apply a 'fair value approach' in which the entity should determine the CSM at the beginning of the earliest period presented as the difference between the fair value of the insurance contract at that date and the fulfilment cash flows measured at that date. • if it is impracticable to determine the insurance finance income or expense in profit or loss, and the related amount of OCI accumulated in equity using the simplified approach described above, an entity should apply one of the following: ○ when the insurance finance income or expense is determined using the effective yield approach, by assuming that the earliest financial assumptions that should be considered for determining insurance finance expense are those that occur when the entity first applies the new Standard. Accordingly, on the date when the entity first applies the

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		new Standard, the accumulated balance in OCI for the insurance contract is zero. ○ when the insurance finance income or expense is determined using the current period book yield approach, by assuming that the insurance finance expense or income is equal and opposite in amount to the gain (or loss) presented in profit or loss for the items held by the entity. • that for each period presented for which there are contracts that were measured in accordance with the simplified approach or the fair value approach, an entity should disclose the information proposed in paragraph C8 of the 2013 ED (ie the disclosures for contracts for which retrospective application is impracticable) separately for: ○ contracts measured using the simplified approach; and ○ contracts measured using the fair value approach. The Board also tentatively decided that an entity should apply the option within the variable fee approach to recognise changes in the value of the guarantee embedded in the insurance contract with direct participation features in profit or loss in specified circumstances prospectively from the date of initial application of the Standard.

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5.b. Initial application of the new insurance contracts Standard after implementation of IFRS 9 *Financial Instruments*		
The 2013 ED proposed transition relief for the designation and redesignation of financial assets. That transition relief: • would apply when an entity initially applies the new insurance contracts Standard. • allows an entity to use options available in IAS 39 and IFRS 9 at initial recognition of financial assets (and at initial application of IFRS 9).	While many constituents would prefer alignment of effective dates (to avoid two rounds of substantial system changes and to allow for suboptimal asset designation), most constituents recognise that IFRS 9 should not be delayed only because of the new insurance contracts Standard. Therefore, the constituents suggested that if the two dates could not be aligned: • entities that apply the new insurance contracts Standard should be given an option to defer application of IFRS 9; • entities that apply IFRS 9 before applying the new insurance contracts Standard should be permitted a more wholesale opportunity to redesignate accounting treatments for financial assets and to reassess the business model in which the entity holds financial assets; and/or • if the IASB decides to finalise IFRS 9 before finalising the new insurance contracts Standard, that it should delay the mandatory effective date of the insurance contracts Standard so that it is at least	The Board decided that the mandatory effective date of IFRS 9 should be 1 January 2018. The Board is in the last stages of finalising an amendment to IFRS 4 *Insurance Contract*s that addresses the concerns of some interested parties about the different effective dates of IFRS 9 and the forthcoming insurance contracts Standard. The Board tentatively decided to confirm the transition relief proposals in the 2013 Exposure Draft that, on the initial application of the new insurance contracts Standard: • an entity is permitted to newly designate financial assets under the fair value option as measured at fair value through profit or loss to eliminate (or significantly reduce) an accounting mismatch according to paragraph 4.1.5 of IFRS 9; • an entity is required to revoke previous fair value option designations for financial assets if the accounting mismatch that led to the previous designation according to paragraph 4.1.5 of IFRS 9 no longer exists; and • an entity is permitted to newly designate an investment in an equity instrument as measured at fair value through OCI in accordance with

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	three years after the mandatory effective date of IFRS 9, to avoid entities having to make two fundamental changes in a short period.	paragraph 5.7.5 of IFRS 9 and is permitted to revoke previous designations. In addition, the Board tentatively decided that: • when an entity first applies the new insurance contracts Standard the entity should be permitted, but not required, to newly assess the business model for managing financial assets that are accounted for in accordance with IFRS 9 and that the entity designates as related to contracts within the scope of IFRS 4 or within the scope of the new insurance contracts Standard. • the entity should provide additional disclosures to assist users of financial statements understand those changes when the classification and measurement of financial assets change as a result of applying any of the transition reliefs in the new insurance contracts Standard.
5.c. Mandatory effective date		
The IASB intends to allow approximately three years between the date of publication of the final insurance contracts Standard and the mandatory effective date.	Many respondents agreed with the length of the implementation period while expressing concerns about the possibility that entities would not be able to apply the proposals at the same time as applying IFRS 9.	The Board expects to set the mandatory effective date in Q4 of 2016.

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6. Scope: Fixed-fee service contracts		
Fixed-fee service contracts are excluded from the scope of the insurance contract Standard.	Some entities objected to the cost and disruption from applying revenue contract accounting to fixed-fee service contracts even though they would use insurance contracts accounting for other contracts they issue. Consequently, they suggested having an option to permit them to apply insurance contracts accounting to fixed-fee service contracts that meet the definition of an insurance contract.	The Board tentatively decided that entities should be permitted, but not required, to apply IFRS 15 *Revenue from Contracts with Customers* to the fixed-fee service contracts that meet the definition of an insurance contract. This decision is consistent with the IASB's aim to provide relief to all entities that issue fixed-fee service contracts.
7. Discount rates		
The discount rates used to adjust the cash flows of an insurance contract for the time value of money should be consistent with observable current market prices for instruments with cash flows whose characteristics are consistent with those of the insurance contract.	Some constituents requested additional guidance on how to determine the rates used to discount long-term obligations over periods of time in which there are few or no observable market interest rates.	The Board tentatively decided: • to confirm the principle that the discount rates used to adjust the cash flows in insurance contracts should be consistent with observable current market prices for instruments with cash flows whose characteristics are consistent with those of the insurance contract. • to provide additional guidance that an entity should use judgement to ensure that appropriate adjustments are made to observable inputs to accommodate any differences between observed transactions and the insurance contracts being measured and to develop any unobservable inputs using the best information

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		available in the circumstances, while remaining consistent with the objective of reflecting how market participants assess those inputs.
8. CSM accretion, allocation pattern and period		
An entity shall recognise the remaining CSM in profit or loss over the coverage period in the systematic way that best reflects the remaining transfer of services that are provided under the contract.	Some respondents were concerned that, without further guidance, the subjectivity in determining the pattern of the underlying services will create significant diversity in the pattern of recognition of the CSM in profit or loss.	The Board tentatively decided to: • confirm the principle for recognition pattern proposed in the 2013 ED. • provide guidance that, for all insurance contracts, an entity should recognise the CSM in profit or loss on the basis of the passage of time. • not require or permit in the general model the remeasurement of the CSM using current discount rates.
9. Asymmetrical treatment of reinsurance contracts		
For a reinsurance contract that an entity holds any changes in fulfilment cash flows that relate to future service should adjust the remaining CSM (consistently with the unlocking decision—refer to issue 1). That remaining CSM will be recognised over the coverage period when the service is provided.	Some respondents were concerned that there is an accounting mismatch when (i) unfavourable changes in estimates on the underlying direct contract are recognised immediately in profit or loss (contract is onerous) and (ii) a corresponding favourable changes in estimates in the reinsurance contract are recognised over the coverage period.	The Board tentatively decided that an entity that holds a reinsurance contract should recognise immediately in profit or loss any changes in estimates of fulfilment cash flows that arise from changes in estimates of fulfilment cash flows for an underlying direct insurance contract that are recognised immediately in profit or loss. This decision would minimise the accounting mismatch that might otherwise occur when a change in

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		estimate affects both the underlying direct contract and the reinsurance contract.
10. Business combinations and portfolio transfers		
An entity should use the general requirements to account for contracts acquired in business combinations and portfolio transfers with the following clarifications: • The date of initial recognition is deemed to be the date of portfolio transfer or a business combination. • The expected cash inflow is deemed to be the fair value of the acquired contracts.	Respondents sought clarification for the accounting for the CSM that arises in its settlement period for an insurance contract that is acquired through a portfolio transfer or a business combination.	The Board tentatively decided to clarify that contracts acquired in their settlement period should be accounted for as if they had been issued by the entity at the date of the portfolio transfer or business combination.
11. Portfolio definition and unit of account		
• In general, an entity should measure insurance contracts on a portfolio basis unless a different level of aggregation is needed to meet the objectives of measuring different components of the insurance contracts. • A portfolio of insurance contracts is defined as a group of insurance contracts that: ○ provide coverage for similar risks and	• Most respondents were unclear as to the level of aggregation required for implementing the insurance contracts Standard. In addition, many were concerned that the level of aggregation would be lower than they currently use for measurement, resulting in higher operational costs. • Some respondents asked when an entity should recognise loss-making contracts and	The Board tentatively decided that: • an entity should aggregate contracts into groups to determine whether to recognise a loss for onerous contracts and to measure the CSM after initial recognition. Those groups comprise contracts that on initial recognition have: ○ future cash flows the entity expects will respond similarly in terms of amount and timing to changes in key assumptions; and ○ similar expected profitability, ie the CSM as a percentage of the total expected revenue is

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that are priced similarly relative to the risk taken on; and ○ are managed together as a single pool. • An entity should recognise immediately in profit or loss any losses related to onerous contracts.	how to test whether a contract is loss making.	similar. An entity can use as a practical expedient the expected return on premiums, ie the CSM as a percentage of expected premiums. • an entity should determine the amount of the CSM to recognise in the statement of profit or loss in a way that is consistent with the objective of allocating the CSM for a group of contracts remaining at the end of the reporting period over the coverage provided in the current period and expected remaining future coverage to be provided on the basis of the passage of time. The allocation should be based on coverage units, reflecting the expected duration and size of the contracts in the group.
12. Definition of significant insurance risk		
The 2013 ED defines an insurance contract as a contract with significant insurance risk. The 2013 ED also includes additional guidance, specifying that a contract does not transfer insurance risk if there is no scenario that has commercial substance in which the present value of the net cash outflows that is paid by the issuer can exceed the present value of the premiums.	Some respondents were concerned that a literal interpretation of the guidance would lead to a reclassification of some contracts that are widely accepted as containing significant insurance risk under the existing IFRS 4.	The Board tentatively decided to clarify the guidance in the principle of the 2013 ED that significant insurance risk only occurs when there is a possibility that an issuer will incur a loss on a present value basis.

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13. Determination of interest expense for the liability for incurred claims in the premium allocation approach		
For the premium allocation approach, the 2013 ED required that the interest expense presented in profit or loss in the premium allocation approach should be determined using the discount rate set when contract is initially recognised.	• The majority of constituents did not support the 2013 ED proposals for the discount rate to be locked-in at the inception of the contract. • The main reason for respondents' preference for the locked-in rate at the date of incurred claim over the locked-in rate at the contract inception date is the operational complexity and prohibitive costs associated with changes in systems required to collect and retain information on contract inception dates.	The Board tentatively decided that, when an entity applies the premium allocation approach to contracts for which the entity discounts the liability for incurred claims and chooses to present the effect of changes in discount rates in OCI, the interest expense in profit or loss for the liability for incurred claims should be determined using the discount rate locked-in at the date the liability for incurred claims is recognised.