Australian Government
Australian Accounting Standards Board

TRG Minutes

Meeting information

AASB 17 *Insurance Contracts* Transition Resource Group (TRG)
27 March 2019
9am-2pm

Objective: The AASB 17 TRG was asked to review the agenda papers released by the IASB for discussion at the April 2019 IASB TRG and provide their comments on the issues to be shared at the IASB TRG meeting. TRG members also discussed the outcomes of the 25 issues raised in AP2D of the IASB October 2018 Board meeting and provided updates on key topics being considered by Australian working groups.

ATTENDANCE	ORGANISATION
Anne Driver (Chair)	QBE
Patricia Au	AASB staff
Stephen Burton (via teleconference)	Suncorp
Cassandra Cope	HCF
Brendan Counsell	EY
Chris Maher (via teleconference)	AMP
Geoff Leemann (observer)	Swiss Re
Ian Moyser	KPMG
Rachel Poo	QBE
Rob Sharma	APRA
Richard Sheridan (on behalf of Peter Grant)	Insurance Australia Group (IAG)
Grant Robinson	AMP/ Institute of Actuaries IFRS 17 Implementation Task Force
Paul Ruiz	Non-executive director
David Rush (via teleconference)	Institute of Actuaries IFRS 17 Implementation Task Force
Warwick Spargo (via teleconference)	RSM
Angus Thomson (observer) (via teleconference)	QBE
Owen Tong (observer)	BT Financial Group
Tony Tong (via teleconference)	Pacific Life Re
Glenn Treadwell	NIB
Jeroen Van Koert	AIA
Richard Whiteoak (observer)	Swiss Re

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Topic	Agenda paper
Investment components within an insurance contract	**AP01**

- Some members thought there were helpful clarifications of principles in the paper.
- Some members considered that the paper provides more clarity around the definition of investment components. For example, it clarifies that premium refunds are not investment components (Example 5 of AP01).
- One member expressed concern that the clarification may result in unintended consequences for some types of life insurance products, specifically, whole of life and endowment contracts:
  - Some insurers are currently of the view that the surrender value is deemed to be the investment component. However, the views expressed in AP01 indicate that this may not always be the case. There will therefore, be operational implications for some life insurance contracts (e.g. endowment policies) where the surrender value is commonly nil in the first two years but subsequently increases over the remaining coverage period. Applying the views in AP01, an investment component would exist and would be valued at an amount that is not necessarily the same as the surrender value.
  - One member was concerned that the paper seemed to introduce the idea of creating a notional account balance (and surrender charges) purely to change line items but not total profit. This would add significant operational complexity.
  - One member asked about the pervasiveness of the impact in the Australian industry. Members responded that there is not expected to be a big impact in Australia as it will be contained to a small number of products.
  - A member agreed to draft a simple example(s) to illustrate circumstances in which a strict interpretation of the clarification may lead to unintended or inappropriate consequences.
- Members discussed the IASB staff's proposal to amend the definition of an investment component in Appendix A of IFRS 17 to clarify the IASB Board's intention that an investment component is an amount that the entity is required to repay to a policyholder in all circumstances, regardless of whether the insured event occurs (paragraph 9 of AP01):
  - Some members expressed concern that the amendment could result in the requirements being perceived to be more prescriptive. Other members pointed out that the amendment is a clarification of the IASB's intention which is already included in the Basis for Conclusions (IFRS 17.BC34) and questioned whether its inclusion in the body of IFRS 17 will make a difference to how the requirements should be applied.
  - Members agreed that the requirements in IFRS 17 should not be prescriptive to allow sensible outcomes to be achieved when applied to the wide variety of contracts available in the market globally.
- A member disagreed with Example 2 of AP01 and expressed the view that the non-cancellable whole of life contract described is equivalent to a term insurance contract, but with an indefinite term. The member considered that if a term insurance policy does not have an investment component, it should follow that the whole of life contract should also be considered not to have an investment component.
  - Other members disagreed and noted that given that the contract is non-cancellable and death of the policyholder is a certain event, the payment to the policyholder is guaranteed, i.e. payable in all circumstances. Only the timing of the payment is uncertain.

Reporting on other questions submitted	AP02

- Members discussed the topics and IASB staff responses in AP02. The following comments were made:

  S86 Definition of a portfolio when determining the boundary of a contract

  - A member noted that this may be a relevant consideration when applying IFRS 17.34(b)(i) to Yearly Renewable Term (YRT) contracts. Although repricing of YRT contracts is generally not performed at an individual contract level, insurers will need to consider whether the repricing is performed at the level of a 'portfolio' as defined in Appendix A of IFRS 17[1]. Another member commented that this is likely to be impacted by the way entities determine their IFRS 17 portfolios.

  S115 Definition of insurance contracts with direct participation features – applying paragraph B101(b) of IFRS 17

  - Members considered the IASB staff response to be helpful and will be relevant when considering whether investment-linked contracts can apply the variable fee approach (VFA).

  S116 Applying paragraph 66(c)(ii) of IFRS 17 for reinsurance contracts held

  - A member expressed the view that IFRS 17.66(c)(ii) may be subject to change as a result of the amendments being drafted by the IASB following the decision in the January 2019 IASB Board meeting. Members agreed that the implications of IFRS 17.66(c)(ii) should be reviewed when the Exposure Draft (ED) is released.
  - Another member pointed out that S116 acknowledges that the topic of reinsurance contracts held for onerous underlying insurance contracts is being considered by the IASB outside of the TRG.

  S118 Consideration of reinsurance in the risk adjustment for non-financial risk

  - Members considered the IASB staff response to be helpful as it confirms that the effect of reinsurance would be reflected in the risk adjustment for non-financial risk of the underlying insurance contracts if an entity considers reinsurance when determining the compensation it requires for bearing non-financial risk related to the underlying contracts. This is consistent with the views of the reinsurance working group on risk adjustment (see separate section below).
  - A member expressed the view that an implication of the IASB staff response[2] is that the risk adjustment of the reinsurance contract held can be nil in some circumstances.

  S122 Changes in fulfilment cash flows as a result of inflation

  - A member commented that this topic may be of particular interest to the general insurers. S122 appears to extend assumptions about inflation based on an index relate to financial risk and its effects are therefore, excluded from the insurance service result.

[1] "insurance contracts subject to similar risks and managed together" [Appendix A of IFRS 17]

[2] The IASB staff note in their response that the risk adjustment for non-financial risk of the reinsurance contract could not be nil, unless:

(a) the entity considers reinsurance when determining the compensation it requires for bearing non-financial risk related to underlying insurance contracts; and

(b) the cost of acquiring the reinsurance is equal or less than the expected recoveries.

- Another member asked if this will have an impact on products applying the simplified approach (PAA). A member responded that the liability for incurred claims (LIC) is measured based on fulfilment cash flows and will therefore, be impacted.
- A member considered that in practice, the effect of inflation may be offset by the effect of discounting.

S127 Fair value of insurance contracts

- Some members considered that the determination of fair value applying IFRS 13 may be subjective and could lead to a wide variety of outcomes across entities that apply the fair value approach on transition. Members agreed that the Accountants and Actuaries Liaison Committee (AALC) may be an appropriate forum to discuss the application of the fair value approach on transition. Members noted that the forum will not develop prescriptive guidance but could provide practical considerations or suggested approaches to determine the fair value of insurance contracts on transition.

Update on IASB's progress in addressing the 25 areas of concern	Update on 25 issues

- A member introduced the section and summarised the recent developments in relation to the 25 concerns and implementation challenges raised in the IASB October 2018 Board meeting AP2D. Note: The Australia industry response to each of the 25 issues submitted to the IASB in November 2018 is available here.

Top priority issues for the Australian industry

- The top 2 issues in Australia are Topic 15 Separate presentation of groups of assets and groups of liabilities on the balance sheet and Topic 12 Initial recognition of reinsurance contracts held when underlying insurance contracts are onerous.

Topics 9, 15 and 16

- The IASB agreed to amend Topic 15 to require aggregation on the balance sheet at the level of the portfolio. In response to the outreach conducted by the IASB staff in March 2018, Australian industry members had requested for aggregation at an entity level but were also supportive of aggregation at the portfolio level as a possible alternative.
- Members agreed that the implementation challenges arising from Topics 9 and 16 are expected to be significantly mitigated by the amendment to the balance sheet aggregation requirements (Topic 15).

Topic 12

- The issue on the treatment of reinsurance held has been partially addressed by the amendment proposed in the IASB January 2019 Board meeting. However, the amendment proposed is limited to 'proportionate' reinsurance only[3]. The reinsurance working group's feedback on the proposed amendment is discussed in a separate section below.

Issues raised where the Australian industry supported no change

- The Australian industry strongly supported no change in relation to Topics 6, 10, 17 and 19. The IASB decided to make no amendments for these topics. Members agreed that this was a good outcome.

Issues for which the Australian industry disagreed with the outcomes of the IASB decisions

[3] Where recoveries from reinsurance are proportionate to the underlying claims. Other ceded cash flows (e.g. ceded premiums, ceding commissions etc) do not need to be proportionate to the underlying cash flows in order to be in scope of the IASB's proposed amendment.

Topic 4 – use of locked in interest rates to adjust the CSM

- A member asked if other jurisdictions are requesting for an amendment to be made to address this issue. A member responded that there are other stakeholders who disagree with the IASB's decision not to amend for this issue but it is unclear the extent to which they will continue to request for an amendment to be made.

Topic 11- business combinations – contracts acquired in their settlement period

- This was one of the topics that the Australian industry responded to as part of the IASB staff outreach in March 2018. Members agreed that the current IFRS 17 requirements creates operational complexity and will have an impact on all entities that conduct acquisitions or portfolio transfers.
- A member pointed out that this topic is on the list of CFO forum issues discussed at the EFRAG Technical Expert Group (TEG) meeting on 21 March 2019.
- Members agreed that a working group will be set up to raise the issue with the IASB.

Topic 19 – interim financial statements

- A member stated that Australian insurers are required to perform quarterly APRA reporting and asked if the IAS 34 override will result in cumulative differences between APRA reporting and statutory reporting. A member noted that APRA reporting is not an interim report that is covered by IAS 34. Therefore, APRA reporting will not be subject to the IAS 34 override unless APRA requires the override to apply for the purposes of APRA reporting.
- A member expressed the view that assuming the override is not relevant for APRA reporting, the impact is likely to be focussed on entities which have overseas parent entities that perform interim reporting as those entities will have to maintain two sets of results.
- A member noted that this topic was discussed in the IASB September 2018 TRG and some TRG members disagreed with the IAS 34 override. The member stated that the IASB considered that the override was intended to reduce operational complexity and therefore, it may be beneficial to understand why the IASB held the view that the override would reduce operational complexity.
- Members agreed that the practical implications of the IAS 34 override should be discussed at the AALC.

Accounting Standards Advisory Forum (ASAF) request for feedback on the IASB's tentative decisions on 6 areas of concern	**ASAF agenda paper 3**

- The Accounting Standards Advisory Forum (ASAF) is a group of National Standard setters that meet four times a year with the IASB. The ASAF is an advisory panel to the IASB for some of the projects. The IASB have requested for feedback from ASAF on the IASB's tentative decisions on possible amendments to IFRS 17.
- Members agreed that the limitation of the amendment on reinsurance contracts covering onerous underlying contracts to 'proportionate' reinsurance is an issue that should be raised.
- Members agreed that two additional issues should also be raised with the IASB:
  - Treatment of contracts acquired during their settlement period – refer to discussion on Topic 11 above; and
  - IAS 34 override – refer to discussion on Topic 19 above.

Reinsurance and IASB's restriction to 'proportionate contracts'	

- A member of the reinsurance working group provided an update on the work performed by the group:
  - A working group of the AASB TRG was set up in 2018 to discuss and articulate the issue around the inability to reflect the reinsurance benefit on reinsurance held in the profit or loss at the same time as losses on underlying contracts where the reinsurance contracts held cover onerous underlying contracts – refer to July 2018 AASB TRG minutes for discussion of the issue.
  - A paper was drafted and shared with a number of national standard setters who agreed with the issue and proposals raised in the paper. The paper was submitted to the IASB in October 2018.
  - In January 2018, the IASB tentatively decided to amend IFRS 17 to require an entity to recognise a gain in profit or loss when the entity recognises losses on onerous underlying contracts to the extent that the reinsurance contract held covers the losses of each contract on a proportionate basis. The amendment therefore, would not apply to non-proportional reinsurance contracts.
  - Another paper was drafted by the working group to request for a principles-based approach which will apply to the extent the reinsurance recoveries are directly related to the claims on the underlying loss making contracts. The paper applies hedging principles to illustrate that proportional and non-proportional reinsurance contracts both have risk mitigation objectives and should not be accounted for differently based on their mechanics. This paper was discussed with the IASB in March 2019. In that discussion, the IASB expressed concerns around the determination of the reinsurance gain to be recognised in profit or loss for non-proportionate reinsurance, in particular, how much reinsurance premiums should be allocated in order to determine the gain that corresponds to the underlying losses recognised.
  - The reinsurance working group is currently drafting examples to respond to the IASB's concerns.

Risk adjustment applicable to insurance contracts – practical considerations in determining the risk adjustment	

- A member of the working group on risk adjustment provided an update on the work performed by the group:
  - The working group was set up to discuss how reinsurance can be reflected in the measurement of the risk adjustment of the underlying insurance contracts. Two possible approaches have been proposed so far but this is not considered exhaustive – only indicative approaches.
  - The output of the working group will be shared with the Institute of Actuaries Taskforce for possible incorporation into the Information Note, as well as the APRA working group on risk adjustment for life insurers.

Any other business

Update on Institute of Actuaries Taskforce

- A member of the Institute of Actuaries Taskforce provided an update on the activities of the group:
  - The Taskforce has issued an Information Note (IN) which is intended to provide useful guidance on the practical implementation of IFRS 17. The IN has been reissued based on

interpretations that emerge from the IASB TRG and amendments decided on by the IASB. An addendum to the IN includes tentative decisions made in January and February 2019.

- A similar document has been drafted by the International Actuarial Association (IAA) and a formal Exposure Draft (ED) has been issued for comment. Feedback on the ED is due at the end of April. Once issued, it will be an International Actuarial Note (IAN) which is intended to provide guidance and is not authoritative. So far, no major divergence from the Australian Actuaries Institute IN has been identified.

Any other business

- The IASB TRG meetings may potentially cease after the April TRG meeting. Membership and objectives of the AASB TRG will be reviewed after the completion of the IASB TRG meetings. The AASB TRG will continue to monitor the receipt of submissions from the industry.

End Meeting