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Chairman

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Paris, September 6th, 2019

Mr Jean-Paul Gauzes
Chairman EFRAG Board
35 Square de Meeùs
B-1000 Bruxelles

ED/2019/4 Amendments to IFRS 17

Dear Jean-Paul,

On behalf of the Autorité des Normes Comptables (ANC), I am writing to express our views on EFRAG's draft comment letter on the ED/2019/4 issued by the IASB and proposing to amend IFRS 17. This letter sets out some of the most critical comments raised by interested stakeholders involved in ANC's due process.

Objective of the proposed amendments

ANC welcomes the thorough and unprecedented work undertaken by EFRAG when analysing case studies in spring 2018, raising issues that have been communicated to IASB in a letter issued in September 2018. ANC also welcomes the IASB responsiveness in addressing the issues raised by stakeholders.

ANC has been contributing to the diagnosis and analysis of the application of IFRS 17, persistently supporting the implementation of that new genuine global standard in place of the previous IFRS 4 which has mainly been grandfathering local GAAP. ANC has consistently expressed the view that some amendments could dramatically improve the relevance and practicability of IFRS 17. We have summarised in seven papers our preliminary analyses on issues, developed examples in order to illustrate our understanding of the standard's provisions and eventually suggested amendments. These papers are available on our website and relate to: Acquisition cash-flows, Balance sheet presentation, CSM allocation related to investment services, Level of aggregation, Reinsurance, Transition and Interaction with IFRS 9.

In this letter, ANC is commenting on the answers provided by IASB to the concerns identified by ANC. The scope of these concerns slightly differs from the one retained by IASB (25 issues) or EFRAG (6 issues). Moreover, proposed amendments made in the ED have raised additional questions that are also addressed in this letter. Finally, this comment letter aims at suggesting technical

improvements in the amendments of the standard, neither providing any hierarchy among the concerns nor evaluating their impact on the future European endorsement process that will be considered later on.

Main ANC comments

By and large, ANC welcomes the amendments proposed by IASB that address some of the concerns raised by its stakeholders and its Board. We remain however concerned that further improvements are still required. We believe the following concerns still require/deserve amendments in the standard (and not in the basis for conclusions).

We concur with EFRAG and IASB on the objectives set to annual cohorts ensuring a timely recognition of onerous contracts, allocating the margin in a way properly reflecting services provided and informing on profitability trends. When applied to mutualised contracts, annual cohorts however lead to allocating and recombining the CSM within a portfolio on an artificial basis since it reflects neither the legally organised and contractually accepted mutualisation, nor the economics of such policies. We therefore concur with EFRAG's recommendation to introduce an exception to annual cohorts for intergenerational mutualised contracts. We hereafter outline that the three above-mentioned objectives can be achieved at mutualised level since no contract subject to the exception becomes onerous in a mutualised population unless the whole population becomes onerous and no generation has individual rights on any subset of the overall portfolio. Different types of mutualised contracts might exist but most of them in our jurisdiction would be eligible to the variable fee approach (VFA). Therefore an exception for mutualised VFA contracts would significantly ease the operational implementation by our constituents.

We concur with EFRAG that, bearing in mind the difficulties to implement a full retrospective approach for certain very significant portfolios of long duration, clarifying in the standard current transition requirements on estimates is necessary in order not to deter a retrospective application that from a financial information perspective provides the most useful and comparable information on the performance path of an entity. In addition, transitional requirements of the modified retrospective approach still need to be adjusted.

We also concur with EFRAG that reinsurance contracts' provisions deserve further amendments. The scope of the proposed amendments is too narrow when referring to "proportionate" reinsurance contracts. Moreover the requirement to include cash-flows from underlying reinsured contracts not written within the boundaries of reinsurance contracts held provide information of little relevance whereas inducing significantly high costs of implementation. Prohibition to apply the VFA to reinsurance contracts issued is not conceptually supported. Reinsurance contracts held are subject to the general standard's provisions with some adjustment that prove not literally applicable or ambiguous.

Finally several presentation requirements are still unsatisfactory. Not providing any definition of premiums to be received and not separately presenting main accruals in the face of the balance sheet leads to compensate cash-flows of different nature, terms and counterparts relegating useful information to the notes. In addition, suggested minor amendments will unduly present certain *non-financial* changes in assumption as insurance *financial* result. Finally, requirements on interim financial statement are not consistent with IAS 34.

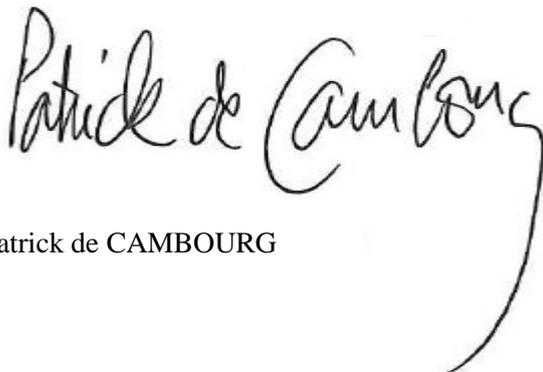
We also suggest EFRAG to comment on the interactions between IFRS 9 and IFRS 17 since the interrelation between assets (financial instruments) and liability (insurance commitments) management is a core feature of many insurance contracts. We are concerned that the proposed amendments do not address the specific concerns and mismatches that arise when dealing with risk mitigation, equity investments and locked-in rate. We highlight that the effective date / postponement of both standards should be aligned (and the European “top-up” be accordingly extended).

We believe that the feedback from the current public consultation will help IASB addressing all relevant concerns before finalising amendments that are needed notwithstanding the planned implementation date by 1st January 2022. We do not hear from our stakeholders that a further postponement (by 6-12 months) would actually be disruptive. As standard setter, our priority remains to improve a standard built to last.

The letter is structured in three parts: Appendix 1 addresses the questions raised by IASB in its ED; Appendix 2 deals with additional topics raised by EFRAG; Appendix 3 finally mentions (without developing them) several remaining concerns that have been addressed neither by IASB amendments nor in the EFRAG’s letter.

Please do not hesitate to contact us to further discuss that case,

Yours sincerely,

A handwritten signature in black ink that reads "Patrick de Cambourg". The signature is written in a cursive style with a long, sweeping underline that extends to the right.

Patrick de CAMBOURG

Appendix 1: Responses to questions raised in the ED

1 Q1: scope exclusions

1.1 Do amendments address all issues raised?

- 1 ANC agrees with EFRAG that the amendments proposed by IASB regarding loans that transfer significant insurance risk might ease the application of the standard.
- 2 In ANC's view, the amendments proposed by IASB regarding credit cards (in our view also including *payment* cards) that provide insurance coverage offer a practical solution to a very specific issue.

1.2 Additional EFRAG's questions

- 3 With regards to the EFRAG's additional question raised in Paragraph 10, there is no legal requirement in our jurisdiction to provide insurance services in addition to the financial services provided by credit cards. We have not been reported that the amendments would raise significant issues regarding IFRS 9 application of the SPPI test.

2 Q2: Expected recovery of insurance acquisition cash flows

2.1 Do amendments address all issues raised?

- 4 ANC concurs with EFRAG that amendments proposing the recognition of an asset for acquisition cash flows on new business expected to renew outside the contract boundary are improving the relevance of the standard in better reflecting the economic substance of these transactions.

2.2 Does the wording of the amendments raise additional concerns?

- 5 IFRS 17.79 has not been amended to require a separate presentation of the new created asset at portfolio level. As a consequence, an acquisition cash-flows asset will be presented as part of the carrying amount of the portfolio of insurance contracts, whereas presenting it separately in the balance sheet instead of disclosing that information in the notes (as required by amended IFRS 17.105A) is useful to users (see also presentation of accrual in the balance sheet in § 130).

2.3 Additional EFRAG's questions

- 6 With regards to the EFRAG's additional question raised in Paragraph 18, ANC is not aware of substantially different definitions of an "insurance contract renewal" so that an additional definition of that term is not required to prevent diversity in practice.

3 Q3: Contractual service margin attributable to investment-return service and investment-related service and disclosures about the profit recognition patterns

3.1 Do amendments address all issues raised?

- 7 ANC concurs with EFRAG that the amendments proposing to consider investment-related services in the CSM allocation of contracts that are not in the scope of the Variable Fee Approach (VFA) are improving the relevance of the standard in better reflecting the economic substance of the services provided.

3.2 Additional EFRAG's questions

- 8 Amended IFRS 17.109 requires providing quantitative information on the allocation of the CSM on future P&L in appropriate time bands. With regards to EFRAG's question raised in paragraph 36, no specific risk that this information is commercially sensitive has been reported to ANC.

4 Q4: Reinsurance contracts held – recovery of losses on underlying insurance contracts

4.1 Do amendments address all issues raised?

- 9 ANC concurs with EFRAG that the amendments proposing to recognise at inception a gain on reinsurance contracts are improving (i) the relevance of the standard by removing an accounting mismatch (acknowledged in BC 77 of the ED) and (ii) its consistency in aligning the accounting treatment at inception with the one after.
- 10 In a proportional reinsurance a reinsurer takes a part of the cash flows of the individual underlying insurance contracts. IASB has been proposing an accounting treatment for the net gain on a proportionate reinsurance treaty covering onerous underlying contracts. Conversely, IASB decided not to address “non-proportionate” reinsurance contracts (e.g. excess of loss such as reinsurance on catastrophic risks or where an insurance company takes the first 20% of the losses and the reinsurer anything above that benchmark) since they do not relate to one contract only but to several (possibly issued at different times or in different portfolios).
- 11 ANC's view is that proportional and non-proportional reinsurance treaties are conceptually similar for the ceding entity. For the primary insurer, they both are risk mitigation techniques that provide an effective hedge against the risks arising from underlying insurance contracts. Therefore, any timing difference between the recognition of gains on reinsurance held and the losses arising from the underlying reinsured contracts gives rise to an accounting mismatch. Accordingly, there is no reason for not addressing the accounting mismatch in both situations.
- 12 In practice, non-proportional reinsurance might require further estimates and thus raise more application difficulties than proportional reinsurance. This should however not preclude the amendments from providing a conceptual requirement based on a continuous symmetry in the accounting treatment of reinsurance contract held and the underlying insurance contracts issued, with no distinction between proportional and non-proportional reinsurance treaty.

4.2 Does the wording of the amendments raise additional concerns?

- 13 ANC concurs with EFRAG that using the term “proportionate” instead of “proportional” is uncommon and adds ambiguity.
- 14 Moreover, the definition of “proportionate” provided in the Appendix A of IFRS 17 would encompass *quota-share* reinsurance (e.g. the insurance company takes 60% of the losses and the reinsurer 40%) but would exclude *surplus-share* contracts (e.g. the reinsurer takes all losses above a benchmark on *each* insurance contract in a group); which is different from *excess of loss* (where the reinsurer takes all losses above a benchmark on *cumulative losses from a series of* insurance contracts). However, surplus-share contracts are commonly considered to pertain to proportional reinsurance.

4.3 Additional EFRAG’s questions

- 15 With regards to EFRAG’s question raised in paragraph 45, ANC is not aware of contracts that would meet the definition of a “*proportionate*” contract but would not be captured by the amendment. However, as mentioned above in § 14 surplus-share contracts are examples of *proportional* contracts that do not meet the IASB definition of *proportionate* and for which the solution proposed by the amendments would be relevant.
- 16 ANC also notes that the definition of proportionate reinsurance coverage proposed in the ED are limited to contracts that provide “the right to recover from the issuer a percentage of all claims incurred on a group of underlying insurance contracts”. This definition disregards all other contractual terms such as reinsurance commissions and may therefore not adequately capture the economic substance of the reinsurance arrangement.
- 17 With regards to EFRAG’s question raised in paragraph 47 on non-proportional contracts, ANC is of the view (see above in § 11) that there is no conceptual reason for having different accounting treatment for reinsurance contracts depending upon their proportionality or not.
- 18 Non-proportional contracts are very common in our jurisdiction. A typical situation is where an insurer provides coverage for risks within an accepted range and where extreme cases make that direct insurance onerous if not specifically reinsured. A common non-proportional reinsurance compensates for serious personal injury in motor insurance.
- 19 We agree with EFRAG’s analysis that addressing non-proportional reinsurance may additionally require assessing the existence of a “link” between the reinsured risk and the underlying contracts. Absent such a link it might not be possible to clearly identify which of many risks actually triggers the reinsurance gain (and to what extent). For instance, assuming the flood risk in a city is covered by different insurance policies (car, personal, public utility...), which one leads above the line?
- 20 An insurer accepting to issue onerous contracts would generally expect to recover a gain from the reinsurance contract. Accordingly, the entity should be in a situation to identify the link between the reinsured risk and the underlying contracts and even assess the expected losses as well as the expected gain. Finally the possible increased operational complexity (not necessarily more complex than others in the standard) shall not prevent from having a broader solution conceptually funded.

5 Q5: Presentation in the statement of financial position

5.1 Do amendments address all issues raised?

- 21 ANC concurs with BC 95-96 of the ED and welcomes the amendments proposing to aggregate assets and liability at portfolio level instead of at group level. At portfolio level, virtually all insurance contracts will then be presented as liabilities which would be very similar to presenting assets and liabilities at entity level.

5.2 Additional EFRAG's questions

- 22 With regards to EFRAG's question raised in paragraph 54 regarding the risk of significantly reducing the information available, ANC is not aware of any information getting lost.
- 23 Conversely, the presentation required by the standard does not distinguish accrual from non-accrual expected cash flows. Moreover the required presentation offsets assets and liabilities of different nature and with different counterparts. ANC is of the view that such distinctions in the existing presentation (under IFRS 4) are currently very helpful and informative. See also Topic 3 in Appendix 2 in the current letter § 115.

6 Q6: Applicability of the risk mitigation option

6.1 Issue

- 24 Risk mitigation provisions in the standard primarily provide a specific accounting treatment in order to prevent a mismatch with some financial instruments accounted for under IFRS 9.
- 25 The scope of the risk mitigation provisions has been expanded to also include reinsurance contracts held to mitigate financial risk. This extension helps circumventing an accounting mismatches arising from reinsured contracts accounted for under the VFA approach whereas IFRS 17.B109 prohibits applying the VFA to reinsurance contracts held.

6.2 Do amendments address all issues raised?

- 26 ANC's preferred solution to the issue relating to the prohibition of applying VFA to reinsurance contracts held was to simply remove the prohibition in IFRS 17.B109. In our view, reinsurance contracts should be subject to the same VFA criteria as insurance contracts or, to amended ones if it is necessary to not unduly encompass reinsurance contracts issued that would not be "in-substance" VFA (see also Topic 6 in Appendix 3).
- 27 ANC acknowledges that the extension of the risk mitigation also provides a workable solution to that issue. We therefore consider that the amendment is an improvement of the standard. We are however concerned that the current scope of the risk mitigation is too narrow since it excludes mitigating:
- risks other than financial: e.g. climate-related derivatives which are accounted for at fair value through profit and loss whereas changes in the fulfilment cash-flows of insurance contracts relating to future service adjust the contractual service margin (CSM);
 - risks relating to non-VFA underlying contracts (e.g. general model)

6.3 Does the wording of the amendments raise additional concerns?

- 28 Transition requirements IFRS 17.C3 (b) prohibit an entity from applying retrospectively the risk mitigation exception set out in IFRS 17.B115. This therefore also applies to reinsurance contract held. The reasons for extending this prohibition to reinsurance contract held are outlined in BC 128 of the ED. However, ANC is of the view that the risk of hindsight does not apply to the same extent to reinsurance contracts (see also transition issue in § 38).

6.4 Additional EFRAG's questions

- 29 EFRAG questions in paragraph 65 the prevalence of risk mitigation strategies in their interaction with IFRS 9 instruments. We have been reported several strategies (illustrating the issues above referred to in § 27) among which:
- Natural catastrophe risks mitigated with the help of climate derivatives;
 - Non-VFA participating contracts applying the OCI option, with minimum guarantees hedged with the help of financial derivatives;
 - Annuities resulting from PAA incurred claims applying the OCI option hedged with financial derivatives (e.g. interest rate swaps).

7 Q7: Effective date of IFRS 17 and the IFRS 9 temporary exemption in IFRS 4

- 30 ANC agrees with EFRAG welcoming the IASB's decision to defer the effective date of IFRS 17. We believe that IASB should thoroughly consider the feedback from the current public consultation and address all relevant concerns before finalising the amendments notwithstanding the planned implementation date by 1 January 2022. We do not hear from our stakeholder that a further postponement (by 6-12 months) would actually be disruptive. As standard setter, our priority remains to improve a standard built to last.
- 31 The effective date for IFRS 9 should continue to be aligned with the effective date of IFRS 17 (and accordingly the European "top-up" be extended).

8 Q8: Transition modifications and reliefs

8.1 Issue

- 32 The EFRAG case study has been the unprecedented opportunity to test on a large basis the practicability of the transition requirements.
- 33 It raised 5 issues of different natures:
- Operational difficulties:
 - in complying with the criteria for applying the three approaches offered (full retrospective FRA, modified retrospective MRA and fair value FVA). This issue has not been addressed by IASB amendments and is commented by EFRAG in Appendix 2 Topic 2 (see § 105);
 - in gathering data (Q8A: Business combination).
 - Possible accounting mismatches created by certain requirements:
 - Interaction with IFRS 9 - Risk mitigation (Q8B and Q8C);

- OCI set to nil for non-VFA contracts under the MRA. This issue has not been addressed by IASB amendments and is commented in Appendix 3 Topic 7 (see § 17.1)
- Interaction with IFRS 9 – comparative information. This issue has not been addressed by IASB amendments and is commented in Appendix 3 Topic 7 (see § 17.1)

8.2 Do amendments address all issues raised?

- 34 IASB amendments are addressing 2 of the 5 issues identified:
- by introducing (IFRS 17.C9A) a simplification to the treatment of business combinations under the modified retrospective approach (Q8A);
 - by allowing the prospective application of the risk mitigation option from the transition date (Q8B) and introducing an option to apply the FVA (Q8C).
- 35 ANC agrees with EFRAG that the option to classify as a liability for incurred claims a liability for settlement of claims incurred before a contract was acquired (Q8A) provides a workable solution to the issue raised.
- 36 On the other hand, ANC concurs with EFRAG that the solutions proposed by the amendments to the prohibition of applying the risk mitigation retrospectively are not adequate. In our view, this prohibition surely leads to misrepresenting the CSM upon transition that will last long after transition as well as deters from applying risk mitigation (supposed to be a good practice). Finally IASB uses here a behavioural argument (“risk of hindsight”) which is not consistent with the broad reference to “reasonable and supportable information” made otherwise.
- 37 The possibility to apply the FVA approach (Q8C) is not a solution to a preferable retrospective application, and the possibility to apply the risk mitigation on transition date is limited to the effect during the comparative period, but not addressing the opening effect on CSM and retained earnings (Q8B).
- 38 Moreover, the extension of the scope of the risk mitigation to some reinsurance contracts held has extended the impact of the prohibition set in IFRS 17.B119 to transactions that are not similarly exposed to the denounced “risk of hindsight” (see also § 28). Indeed the definition of a reinsurance contract held in appendix A of IFRS 17 secures the existence of an economic offset whereas the contractual terms allow identifying whether the reinsurance contract actually mitigates risks. As a consequence, the risk of hindsight arising from the absence of a documented risk management strategy does not apply. ANC therefore suggests that the retrospective application of risk mitigation relating to reinsurance be *mandatorily* applied (and IFRS 17.B115 requirements consequently amended).

8.3 Does the wording of the amendments raise additional concerns?

- 39 Based on a cost/benefit analysis, we believe that it would be worth considering offering that simplification also when the full retrospective approach (FRA) is applied, i.e. even when it is “practicable” for an entity to retrospectively apply the business combination (creating a new Paragraph C5B as an exception to C5).

8.4 Additional EFRAG’s questions

- 40 With regards to the EFRAG’s questions in Paragraph 94 and 95, ANC supports EFRAG’s view. Risk mitigation provisions in IFRS 17.B115 allows for recording in the P&L instead of in the CSM the financial risk’s component of changes in the CSM, in

order to match the corresponding changes in the derivatives. Retrospectively applying such risk mitigation on transition would accordingly impact the CSM and the retained earnings.

- 41 However IFRS 17.C3(b) specifically prohibits a retrospective application of risk mitigation that may “give rise to the risk of hindsight” (IFRS 17.BC 393). In our view, not reflecting it on transition could distort the historical CSM and significantly impact the insurance result for years.
- 42 In our view, the documentation on the risk-management objective and strategy for using derivatives to mitigate financial risk arising from the insurance contracts referred to in IFRS 17.B116 may already exist prior to the transition.
- 43 There is no conceptual reason for excluding the retrospective application of IFRS 17.B115 as long as the same documentation requirement applies. Risk mitigation is derived from a corporate strategy and does not result from a deliberate choice. An overall consistency with information provided in other parts of the previous reports could be additionally required: description of the hedging strategy and its major impact, clear distinction between instruments providing risk mitigation and the related contracts, and those that do not provide such risk mitigation.
- 44 Moreover, the reference made in IFRS 17.C6 to “reasonable and supportable information available without undue cost or effort” should be a general principle ensuring an adequate financial information in the very specific and temporary situation of a transition.

9 Q9: Minor amendments

- 45 ANC concurs with EFRAG that the minor amendments proposed improve the standard except for the two issues referred to by EFRAG in Paragraph 100 to 105.
- 46 We agree with the analysis performed by EFRAG on the amendments of IFRS 17.28 and IFRS 17.B128.
- 47 Amending IFRS 17.28 (as explained in IFRS 17.BC 150) also requires to replace “issued” by “recognised” in IFRS 17.22. The level of aggregation applies to the recognition and measurement of insurance contracts; disconnecting IFRS 17.22 from this purpose is, in our view neither properly justified in BC 150 of the ED nor relevant from a conceptual point of view.
- 48 Amending IFRS 17.B128 (as explained in IFRS 17.BC 161) provides a rules-based presentation of “changes in underlying items” as insurance financial result in the P&L. IFRS 17.B128 not solely applies to VFA contracts. Therefore, referring to “underlying items” without restricting to VFA creates an ambiguity on how to apply these requirements to non-VFA contracts. Moreover, underlying “items” do neither solely refer to “assets” nor to the sole “financial” component of an item. The proposed amendment would for instance lead to record as insurance financial result any change in actuarial assumption whereas the related changes in the underlying item would be presented as part of the insurance service result. We do not support this amendment that does not “clarify” but rather (i) adds confusion on the scope of “underlying items”, (ii) introduces a non-conceptually funded presentation of non-financial changes in insurance financial result and finally (iii) creates a mismatch in the P&L.

9.1 ANC additional suggestions

- 49 IFRS 17.B107(b) has been amended, replacing “group of insurance contracts” by “the insurance contract” when assessing the variability in the amounts as defined in

IFRS 17.B101(c). To our knowledge that amendment has not previously been discussed in IASB meetings addressing IFRS 17 issues. Since IFRS 17.B101 defines the criteria for applying the Variable Fee Approach (VFA), ANC is concerned that narrowing the application of the criteria might have unintended effects on the scope of the VFA and could disrupt the current implementation of the standard. We suggest that IASB removes that additional unsupported amendment.

10 Q10: Terminology

- 50 Terminology improvements are welcome even if non critical. As already commented in previous letters, we suggested several improvements in the wording of the standard that appear to us being more critical: for instance regarding the application of the level of aggregation provisions to reinsurance contracts.

Appendix 2: Other comments arising from topics in EFRAG's September 2018 letter to the IASB that have not been addressed by the ED

11 Topic 1: Annual cohorts

11.1 Objectives set to annual cohorts

- 51 Annual cohorts is a practical expedient designed to meet three qualitative objectives outlined in the bases for conclusions (mainly IFRS 17.BC 136):
- Objective 1: Ensuring that onerous contract are recognised in the P&L on a timely basis (e.g. IFRS 17.BC 119 and .BC 129);
 - Objective 2: (i) Ensuring a “correct” allocation of the margin (CSM) during the contract (IFRS 17.BC 120) and (ii) prohibiting open portfolios in order to ensure that the CSM is not allocated beyond the longest contract within the group (IFRS 17.BC 123(b));
 - Objective 3: Providing information on “trends in the profitability of a portfolio”.

The issue relates to contracts that affect or are affected by the cash flows to policyholders of other contracts

- 52 ANC agrees with EFRAG and IASB on the 3 reporting objectives set to the level of aggregation required by IFRS 17.
- 53 However, ANC disagrees with the IASB's view in IFRS 17.BC173 that, for contracts with cash-flows that affect or are affected by cash flows to policyholders of contracts in another group, the fulfilment cash flows (FCF) allocated to a group result in the CSM appropriately reflecting the future profit expected to be earned from the contracts in the group.
- 54 For such contracts, ANC notes that IFRS 17.B68 acknowledges that the requirement in IFRS 17.24 leads to a situation where the cash flows included for measurement purpose within a group may include payments to policyholders of other groups and to future policyholders while excluding some payments to policyholders within the group. This therefore confirms that the requirement leads to an arbitrary allocation of cash-flows that are contractually fungible across contracts.
- 55 This arbitrary allocation is exacerbated for contracts with cash-flows that affect or are affected by cash flows to policyholders of other groups that are accounted for under the Variable Fee Approach (VFA). Indeed IFRS 17.24 requires allocating the fair value of the underlying items (including the entity's share) to the existing cohorts. This disregards the fact that the changes in fair value of the underlying items generate future payments to both existing and future policyholders. Especially, an underlying asset may be held over a longer period of time than the lifetime of existing cohorts thus benefitting only to future policyholders. This leads to the situation where the entity's share in the fair value of the underlying items is spread over a shorter period than the period in which service is provided to the policyholders.
- 56 Another relevant consideration for such contracts accounted for under the VFA, is that as policyholders exercise their options to surrender their contracts, the fair value of the underlying items is realised so as to pay the surrender benefits. As the entity's share in the decrease in the value of the underlying item adjusts the CSM of VFA contracts, this ultimately secures that the CSM is exhausted over the period in which the policyholders benefits from the service i. e. until the point when they surrender the contract and receive their profit share.

- 57 Finally, within the context of VFA contracts, ANC disagrees with the assumption made in BC 178 of the ED that annual cohorts create the entity's share in the fair value of the underlying items. This statement assumes that the underlying items are managed separately on a cohort by cohort basis whereas in practice investments are managed on a portfolios basis.
- 58 In that regard, the most widespread French participating contracts primarily provide policyholders with discretionary benefits based on the returns from an underlying pool of items that backs all generations of contracts. In addition, the contractual terms provide that policyholders' participation is determined based on the realised gains and losses of the portfolio. This implies that (i) no generation of policyholders has a contractual right to any subset of the portfolio and that (ii) the fair value returns from the underlying pool of items are shared across generations of policyholders through management's allocation of discretionary benefits.
- 59 In that context, annual cohorts create a burdensome and artificial divide of future discretionary benefits between annual groups that does not reflect the contractual and economic features of contracts. Indeed, IFRS 17.22 leads to arbitrarily allocating the discretionary benefits to annual groups that afterwards need to be combined together for the purpose of determining the allocation of fulfilment cash-flows (FCF) to newly written contracts (IFRS 17.B68-B71). Accordingly, the initial allocation of benefits to a cohort needs to be reconsidered in all subsequent periods in order to reflect the allocation decisions made by the entity.
- 60 In the case of intergenerational mutualised insurance contracts it is therefore necessary to assess whether the 3 objectives sets to annual cohorts (i) are actually met *thanks to* annual cohorts and (ii) can be achieved through another (less burdensome) way.

Intergenerational mutualisation is a key feature of life-saving business in many European jurisdictions

- 61 The way insurers organise mutualised populations is a highly sensitive feature of insurance markets since it reflects and also shapes up a level of "social/societal" understanding of what is covered by insurance and what is left to the direct responsibility of the individual (natural or moral person). In this context the coherence and consistency of pricing and detailed coverage policies is a key element of stability and decision making for individuals and businesses in the development of their respective activities.
- 62 The perimeter of mutualised populations and the terms and conditions offered to them by insurers are the outcome of very long term evolutions and decisions reflecting fundamental choices made at the level of the society as a whole (explicitly via regulations, semi-explicitly when practices reflect or influence changes in behaviour). In many cases, the strategy of insurers is heavily influenced by a prevailing insurance environment (or culture) the evolution of which requires extensive debates.
- 63 Modifying the perimeter of mutualised populations for accounting purposes only may lead to unintended changes in the way insurers cover insurance risks. There is a significant difference between (i) reflecting, via accounting treatments, a slow and complex evolution of the insurance coverage system and (ii) introducing accounting treatments which may directly influence the way the insurance coverage system is organised and possibly reduce the current and accepted level of mutualisation.

11.2 Do EFRAG's proposals address the issue raised?

- 64 EFRAG raises the key question as to whether annual cohorts are *always an appropriate* "trade-off" between the individual level and the group level (managing similar risks) in order to achieve these objectives.
- 65 We fully support EFRAG's recommendation to introduce an exception to annual cohorts for certain contracts in particular intergenerational mutualised contracts. We have analysed in detailed below how the objectives set to cohorts actually apply. We come to the conclusion that with regard to intergenerational mutualised insurance contracts not only (i) annual cohorts do not help in achieving the 3 objectives but (ii) those objectives are more efficiently and relevantly achieved at the mutualised level (see below).
- 66 ANC therefore suggests introducing an exception to annual cohorts for intergenerational mutualised insurance (hereafter referred to as "mutualised contracts"). Such mutualised contracts are "contracts with cash flows that affect or are affected by cash-flows to policyholders of other contracts" as referred to in IFRS 17.B67-B71. Within "contracts with cash flows that affect or are affected by cash-flows to policyholders of other contracts", IFRS 17.BC138 acknowledges that situations exist where annual cohorts are not necessary. Examples provided by IASB of such situations however refer to a narrow understanding of "full risk sharing" (see also § 88) and require to "achieve the same outcome" as with annual cohorts.
- 67 We concur with EFRAG's recommendation to IASB reconsidering providing an exception to annual cohorts, starting from IFRS 17.BC138, for contracts in the scope of IFRS 17.B67-B71 but achieving the same accounting *objectives* rather than the same *outcome*. We acknowledge that setting the boundary for such an exception is quite challenging. We suggest the scope be defined as relating to "contracts with cash flows that *significantly* affect or are affected by cash flows to policyholders of other contracts". In other words mutualised contracts are those for which policyholders significantly share in the returns and risks of a pool of underlying items. In most cases such contracts also are eligible to the VFA.
- 68 We further suggest the scope of the exception be complemented by the principle-based requirement to comply with the 3 objectives set to annual cohorts. Hereafter, our analysis outlines that the above defined "mutualised contracts" comply with the objectives.
- **Objective 1:** No contract could become onerous in a mutualised population unless the whole population becomes onerous.
 - **Objective 2:** For mutualised contracts, an averaging effect is duly recognised during the average period of contracts: since a contractual or legal intergenerational mutualisation is accepted and organised, there is no reason to divide into annual cohorts a pooled CSM that will finally be reassembled through an allocation process. Moreover, in mutualised contracts, no generation has individual rights on any subset of the overall portfolio.
 - **Objective 3:** For intergenerational mutualised contracts the informative value of the CSM at annual cohort's level alone appears largely artificial (i.e. does not reflect the contractual terms or management's decisions) and the cumulative CSM for mutualised groups provides the most relevant information about profitability. In order to enhance transparency on profitability trends of intergenerational mutualised groups of contracts benefiting from the exception we suggest introducing:
 - (a) a qualitative disclosure describing the grouping criteria for contracts to which the annual cohort requirement is not applied;
 - (b) reconciliations for the CSM of those groups from the opening to the closing balances (according to paragraph 101 of the standard);

- (c) a disclosure on profitability trends by presenting the CSM effect of new business joining the groups, extracted from (b), as a series of historical data (in the last 3 years);
- (d) a disclosure on the actuarial technique applied for computing the CSM effect of new business joining the group as well as a disclosure on the method used for assessing the profitability referred to in (c).

11.3 ANC additional suggestions

- 69 ANC has been developing analyses and examples in order to assess whether, applied to intergenerational mutualised insurance contracts, the 3 objectives sets to annual cohorts (i) are actually met *thanks to* annual cohorts and (ii) can be achieved through another (less burdensome) way. These are summarised hereunder.

Objective 1: onerous contracts in mutualised groups

- 70 The occurrence of an expected risk in a contract does not make the individual contract “onerous”.
- 71 Within a population of mutualised contracts, a group of contracts does not become onerous (for the insurer) unless the cross-subsidisation among policyholders is not sufficient to cover the risks, so that the insurer is eventually exposed to a loss. There is no contract becoming “onerous” in a mutualised population unless the whole population becomes onerous.

Objective 2: allocation of the CSM

- 72 The second objective addresses how the CSM allocation (with the help of coverage/service units) best reflects services rendered by the entity. Basis for conclusions of the ED mainly focus on that objective when justifying why IASB eventually decided not to amend the standard for providing an exception to the level of aggregation.
- 73 In the following sections, we address the two sub-objectives set by IASB (“correctly” reflect the profitability of contracts and prohibit open portfolios) by (i) commenting on the basis for conclusions and (ii) assessing whether they apply the same way to intergenerational mutualised contracts.

Ensuring a “correct” allocation of the margin (CSM) during the contract

Useful information on performance requires grouping

- 74 According to the basis for conclusions of the ED, the adequate level of aggregation should “provide improved information about the profitability” (BC 165) / the periodic financial performance (BC 171) of insurance contracts while not requiring measurement of individual contracts because insurance activities often rely on groups of similar contracts in order for the entity to *reduce* risk (BC167). This aims at striking the best possible balance between contract-by-contract information supposed to result in more transparency and a need to aggregate that necessarily leads to “averaging profits and losses between contracts or averaging different levels of profit over time”.

Relevance of assessing profitability at annual cohort’s level

- 75 With regard to the objective of assessing the profitability at annual cohort’s level, we note that:

- 76 First, it is noteworthy that in some jurisdictions, the contractual minimum participation to policyholders is determined based on the “historical cost measurement” returns (i.e. measured based on historical costs in the statutory accounts) as required legally or contractually in the main European countries. Accordingly, when surrendering its insurance contract, a leaving policyholder waives its right to possibly benefit from the unrealised accumulated changes in fair value of the underlying assets. This does however not preclude that the entity has to pay 80% of the fair value returns to policyholders but the allocation among policyholders also depends on the discretionary assumptions / decisions made by management as well as on the policyholders’ behaviour (i.e. changes in the related assumptions).
- 77 Second, the relevance of information at the level of the annual cohort depends on whether contracts are mutualised or not:
- 78 As long as expected cash-flows can reasonably be allocated to a group of policyholders (e.g. an annual cohort) based on the contractual terms, profitability may be usefully assessed at that level. Within the context of participating contracts with discretionary benefits based on the realised returns of an underlying pool of items, this condition is met only when the contractual terms provide that each generation of contracts participates in the returns of separate pools of underlying items (i.e. when the premiums from newly written contracts are invested in ring-fenced assets so to ensure that their returns are kept separate from policyholders in other groups). In such a case the performance of the investment as well as the technical result (from changes in actuarial assumptions) is directly and solely attributable to the policyholders of the cohort. It makes sense for the related CSM/ profitability/ fair value return for the entity to be strictly linked to the performance and allocated according to the duration of that closed group of policyholders.
- 79 However, when different cohorts of participating contracts share the returns of a common underlying pool of items, the financial performance assessed at the mere annual cohort’s level may not prove relevant or reliable. In the context of participating contracts eligible to the VFA, IASB discussed an example dealing with the evolution of the initial CSM of a mutualised group of contracts exposed to the addition of further contracts (new business) as well as changes in assumptions (actuarial or discretionary). In a previous letter, we commented that example noting that:
- The reallocation process of FCF and CSM among groups/ annual cohorts (IFRS 17.B67-B71) is necessary to properly reflect the mutualisation mechanism; Notably to prevent a new cohort from being unduly considered onerous;
 - The entity’s share in the fair value of the mutualised pool of underlying items stems from the overall portfolio, which includes all the items acquired from investing the premiums collected from all policyholders. As a consequence, there is no contractual link between any subset of the portfolio of underlying items and a group of contracts. Those underlying items belong to the community of policyholders without any group having individual rights on any subset of the overall portfolio. This is illustrated by the possibility for an insurer to decide to use the premiums received from a new cohort to indemnify the lapse of policyholders instead of selling assets.
 - Applying the allocation provisions (IFRS 17.B 68-B 71), the CSM of a new cohort depends on *changes in discretionary assumptions made in periods before* issuing the new cohort.
 - Assuming a change in expectations takes place (e.g. market rate, crediting rate setting the returns to policyholders), the resulting change in fair from the pool of underlying items has to be allocated to the existing and newly written groups. Indeed, a common practice in managing participating contracts in France is to allocate to policyholders additional discretionary benefits that exceed the minimum contractual participation features of the contracts. For instance, the contract may entitle the policyholders to 80% of the realised returns from an underlying pool of

assets but for commercial reasons, insurers may anticipate future benefits above that threshold. Assuming that this expectation is reassessed in future periods, the change in the discretionary benefits also has to be allocated to the annual cohorts:

- this does however not mean that the changes in fair value are *created* by the existing groups and *belong* to them. In fact, should new policyholders join the mutualised group later on, a portion of that surplus might be allocated to them. This results from the discretion granted by law or contract to the entity (and accepted by the policyholders) in deciding when and how to allocate the FCF among the beneficiaries.
- the discretionary allocation is not necessarily related with the initial expected entity's share of the fair value returns of each group. Accordingly, even if the CSM determined upon the initial recognition of a new group of contract was deemed valuable, it quickly becomes obsolete because of the discretion left in the allocation of subsequent changes.

80 As a result, even if a minimum proportion of cash-flows is economically and legally due to policyholders (say 80%), the final allocation among policyholders of a mutualised group also largely depends on discretion and conditions in other groups.

81 CSM is the entity's compensation for managing the cash-flows of and among policyholders. By contrast with IFRS 15 services, it is therefore not a portion of the payment received (and therefore determined on an individual contract basis) but rather a margin i.e. a difference between cash-inflows and cash-outflows or a commission between parties contributing and receiving cash-flows. Such a margin/surplus might as well be considered a portion of the contributions received as a deduction from the insurance payments made. These two conceptual approaches can be described as follows:

- surplus *absorbed* by a contract, i.e. make estimates about actual allocations to policyholders;
- surplus *generated* by a contract, i.e. make estimates about the contribution of each contract to insurer's profit.

82 In our view, when analysing "profitability" i.e. creating a linkage between the CSM and the expected cash-flows, it is more relevant to consider the prospective final absorption of the cash outflows by the policyholders of groups (including upcoming new cohorts) than the evolution of cash-flows generated under initial conditions ignoring the other groups they are supposed to be mutualised with.

83 As a result, in the context of intergenerational mutualised contracts, we note that the informative value of the CSM at annual cohort's level *alone* appears largely artificial (i.e. does not reflect the contractual terms or management's decisions) and that the cumulative CSM for mutualised groups provides the most relevant information about profitability.

Prohibiting open portfolios

84 We concur with the objective to ensure that the allocation of the CSM in the P&L should not be indefinitely postponed; especially when contracts are not mutualised, there is no reason for having open portfolios.

Profitability is not necessarily indefinitely averaged in an open portfolio

85 According to BC 173 of the ED, in an open portfolio, the life of groups would last indefinitely and their CSM would average the profitability of all contracts over this indefinite life.

- 86 We however believe that adding new business to an existing group (in-Force) does not extend the portfolio duration indefinitely or make it “perpetual” since cash-flows attributable to the policyholders and the entity are permanently added and consumed. This mechanism is adequately reflected by the coverage units.
- 87 The averaging effect that results from grouping contracts is not an issue as long as it is contractually organised and accepted by the mutualisation. This effect is in fact already in the standard. ANC showed that thanks to the existing mechanism in the standard (IFRS 17.B68-B71) when allocating FCF from one cohort G 1 to another G 2, the entity *duly* postpones a portion of G 1 CSM in a period that exceeds the initial G 1 coverage period. We have evidenced that situation an example that shows the slight increase in the CSM due to the accretion effect by one year on that deferred part.

The reference to the TRG example is not helpful

- 88 BC 175 and BC 176 of the ED refer to an example discussed at the TRG. It is worth noting that this example is not sufficiently demonstrative since:
- A large majority of TRG members did not agree with the conclusions drawn by the staff;
 - This example is based on the non-realistic assumption that the insurer does not share any risk or return on the cash-flows (CSM is therefore nil);
 - The example is flawed since there is a critical confusion between expected and realised cash-flows. The standard instead requires that FCF be measured at inception considering estimates of future cash flows, not actual ones.
- 89 We commented further in our paper on this example. For the purpose of the ED, we suggest these BC be removed.

Phantom CSM

- 90 Situations have been illustrated where a “phantom CSM” haunts financial statements after the lapsing of the policyholders who initially paid an insurance fee. Such examples only take into consideration policyholders as *initial contributors* when the CSM has been generated, and not policyholders as *ultimate beneficiaries* of the allocation of that CSM, which might happen much later (as discussed previously in § 81).
- 91 These illustrating examples assume that:
- Changes in expectations may affect one cohort only and not the others: this could happen when cohorts are actually not mutualised (for instance because of ring-fenced assets dedicated to the cohort). However, within a portfolio of mutualised contracts, a change in expectations applies to the cash-flows of all mutualised contracts at the same time;
 - The CSM per coverage unit significantly differs from one cohort to another: this might happen when cohorts are actually not mutualised. However, within a portfolio of mutualised contracts, a change in the pricing for the same service from one year to another applies to the cash-flows of all mutualised contracts at the same time. We note that BC 178 of the ED assumes similarly that each annual cohort provides a specific profitability i.e. amount of the entity’s share in the returns from the underlying items. This assumes that the premiums paid by new policyholders are immediately invested according to current market conditions and that the underlying items are identifiable (managed separately) for each cohort. However, in practice within the context of participating contracts that share in the returns of a common pool of underlying items, premiums from new contracts may be used to pay the surrender value of an older contract and the underlying items are not managed separately by generations of contracts.

Conclusion on objective 2

92 We conclude that:

- An open portfolio does not mean that the profitability is indefinitely materially averaged as long as cash-flows attributable to the policyholders and the entity are permanently added and consumed;
- For non-mutualised contracts, annual cohorts prohibit new-business to be added to in-force so that there is in fact no “averaging effect” possible;
- For mutualised contract, an averaging effect is duly recognised (even with annual cohorts). In fact, since a contractual or legal intergenerational mutualisation is accepted and organised, there is no reason to divide into annual cohorts a pooled CSM that will finally be reassembled through an allocation process (B67-B71).

Objective 3: Providing information on “trends in the profitability of a portfolio”

Users’ expectations

93 According to IASB, investors expects from the Insurance standard to provide information on (i) specific risks taken in a year as well as on (ii) trends in the profitability (i.e. whether new business is less or more profitable than the old one).

Limits of annual cohorts in providing such information

94 We mentioned previously (§ 75-83) limits of providing information on the profitability of intergenerational mutualised contracts at the annual cohort’s level:

95 First, the standard does not require the CSM be presented at cohort’s level in the primary FS or in the disclosures. It is therefore unclear to us what useful information for users would get lost if it is not currently required.

96 Second, in some jurisdictions, the contractual minimum participation to policyholders is determined based on the “historical cost measurement” returns (i.e. measured based on historical costs in the statutory accounts) as required legally or contractually in the main European countries and not IFRS “fair value returns” (taken as a reference by IASB for measuring profitability). The allocation among policyholders / cohorts therefore also depends on the discretionary assumptions / decisions made by management.

97 Third, the relevance of information at the level of the annual cohort is limited in mutualised groups because:

- underlying items belong to the community of policyholders without any group having individual rights on any subset of the overall portfolio;
- even if a minimum proportion of cash-flows is economically and legally due to policyholders (say 80%), the final allocation among policyholders largely depends on discretion and conditions in other groups;

98 Fourth, CSM is a margin and when analysing “profitability” i.e. creating a linkage between the CSM and the expected cash-flows, it is more relevant to consider the prospective final absorption of the cash outflows by the policyholders of groups (including upcoming new cohorts) than the evolution of cash-flows generated under initial conditions ignoring the other groups they are supposed to be mutualised with.

99 As a result, in the context of intergenerational mutualised contracts, we note that the informative value of the CSM at annual cohort’s level *alone* appears largely artificial (i.e. does not reflect the contractual terms or management’s decisions) and that the

cumulative CSM for mutualised groups provides the most relevant information about profitability.

- 100 In addition, we have not collected evidence about the usefulness of the information provided by annual cohorts to users, as reported in an EFRAG's user outreach that rather refers to annual cohorts as a concern.

Alternative disclosures providing the expected information

- 101 Users are generally interested in analysing the effects of new business on in-force contracts.

- 102 An analysis of the impact (contribution or dilution) of newcomers (new business) on an existing mutualised portfolio (In-force) provides useful information since it indicates business profitability trends. By contrast, identifying which of the former generations of policyholders is actually "subsidising" a new coming one (through the "allocation process" in IFRS 17.B68-B71), or the other way around, is not usual and the information usefulness is questionable in particular if groups are numerous on the basis of a very granular approach to contracts grouping.

- 103 In order to enhance transparency, additional information could be provided on the intergenerational mutualised groups of contracts benefiting from an exception to the annual cohorts requirement:

- (a) qualitative disclosure describing the grouping criteria for contracts to which the annual cohort requirement is not applied;
- (b) reconciliations for the CSM of those groups from the opening to the closing balances (according to paragraph 101 of the standard);
- (c) disclosure on profitability trends by presenting the CSM effect of new business joining the groups, extracted from (b), as a series of historical data (in the last 3 years);
- (d) disclosure on the actuarial technique applied for computing the CSM effect of new business joining the group as well as disclosure on method used for assessing the profitability referred to in (c).

- 104 Among the existing actuarial techniques listed by EFRAG, we mention:

- (a) The stand-alone method: the CSM of new business is calculated without taking into account the wealth of the stock;
- (b) The adjusted stand-alone method: the CSM is calculated, regardless of the stock of contracts, by allocating some of the "wealth" of the underlying items to the new business;
- (c) The marginal approach: the CSM of the new business corresponds to the difference between the CSM of the book of business stock with and without new business. If it is intuitive enough, it does not meet the constraint of annual cohorts;
- (d) The value in force method by generation: the CSM is calculated including new business and the CSM of new business is identified separately;
- (e) The value in force method allocated to new business: in each period, the CSM of the book (including new business) is calculated and a portion of CSM is allocated to new business.

12 Topic 2: Transition: Modified retrospective approach and fair value approach

12.1 Issue

- 105 As mentioned above, the EFRAG case study has been the unprecedented opportunity to test on a large basis the practicability of the transition requirements. It raised several issues among which the most pervasive is an operational difficulty to apply the criteria for the three approaches offered (full retrospective FRA, modified retrospective MRA and fair value FVA).
- 106 ANC supports the application of retrospective approaches. In the insurance business, transactions are rarely performed on a quoted market so that fair value is difficult to gather and generally pertains to level 3 valuations that probably require as much judgment and assessments (and as few comparability) as applying a retrospective approach. We therefore do not consider that the fair value approach should take precedent on any retrospective approach.
- 107 Our understanding is that the FRA is very demanding. The concern has been raised that the simplifications introduced by the MRA may not result in much less efforts than the FRA. In order to facilitate a retrospective application rather than a prospective approach, the MRA should therefore be as flexible as possible.
- 108 We concur with the principle set in IFRS 17.C6 that the MRA aims at achieving “the closest outcome to retrospective application possible using reasonable and supportable information available without undue cost or effort”.
- 109 We expect the practice to develop in this area (and the reference to “supportable information” invites to such a development). However, we think that either in the FRA or in the MRA, it would be very useful that the standard more clearly states how estimates (which might relax a too strict application) may be used in FRA before being considered as a departure requiring applying the MRA or the FVA. Questions on how to use “reasonable and supportable” information under the FRA or MRA are key, for instance when determining the initial value or when applying annual cohort requirements.

12.2 Do EFRAG’s proposals address all issues raised?

- 110 ANC agrees with EFRAG’s analysis in Paragraph 153 recommending IASB to clarify the possibility within a chosen approach (among the three available) to make estimates, including those requiring to apply different methodologies depending on the available information in order to approximate missing information complying with the retained approach.
- 111 We welcome BC 139 and BC 143 of the ED confirming that the MRA provides solutions where missing data cannot be approximated with (reasonable and supportable) estimates. In other words, estimates can approximate missing past data. An estimate can rely on variable methodologies depending on the available information. We however believe such a clarification should be placed directly in the standard (e.g. amending IFRS 17.C8) instead of in a BC.
- 112 We also welcome BC 144 of the ED commenting on IFRS 17.C12 that estimates will often be needed as proxies for cash-flows that are known to have occurred. This clarification should however be placed directly in the standard (e.g. amending IFRS 17.C12) instead of in a BC.
- 113 IFRS 17.C8 could be amended as follows:
- To achieve the objective of the modified retrospective approach, an entity is permitted to use each modification in paragraphs C9–C19 only to the extent that an

entity does not have reasonable and supportable information to apply a retrospective approach. In addition, the existence of specified modifications in the modified retrospective approach does not prohibit an entity from:
(a) making estimates that are necessary in retrospectively applying an accounting policy as described in paragraph 51 of IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors; or
(b) similarly, making estimates when applying a specified modification in the modified retrospective approach.

114 IFRS 17.C12 could be amended as follows:

To the extent permitted by paragraph C8, an entity shall estimate the future cash flows at the date of initial recognition of a group of insurance contracts as the amount of the future cash flows at the transition date (or earlier date, if the future cash flows at that earlier date can be determined retrospectively, applying paragraph C4(a)), adjusted by the actual or estimated cash flows that ~~are known to~~ have occurred between the date of initial recognition of a group of insurance contracts and the transition date (or earlier date). The actual or estimated cash flows that ~~are known to have~~ occurred include cash flows resulting from contracts that ceased to exist before the transition date.

13 Topic 3: Balance sheet presentation: Non-separation of receivables and payables

13.1 Issue

115 IFRS 17 is based upon a cash basis approach for recognition and measurement. Without changing the recognition and measurement provisions, we believe that also applying such a cash basis approach to the presentation aggregates assets and liabilities of a different nature in a combined amount for each group of contracts. The decisions taken to elaborate IFRS 17 have the following consequences in terms of B/S presentation:

116 – **Premium receivables** (corresponding to a coverage period that has already started but for which payment has not yet been received) are not shown separately. This information is key for a proper understanding of the activity and risks involved. Generally, in case of non-payment, the coverage will remain in force for a period of time, i.e. until the contract is terminated following certain legally/contractually organised procedures. Following termination, the insurer is entitled to the payment of the premium up to that date and will have to cover any claim incurred during the coverage period.

117 Illustrative example 1: presentation of premium due in the general model

118 Assuming a one-year motor insurance policy is issued on 15 December N that covers third party liability. On 31 December N, the policyholder has still not paid the insurance premium of 240 CU. Under the local jurisdiction, not paying premium at the exact moment when due does not invalidate the insurance coverage. The estimates of future outflows relating to future claims and costs amount to 192.

119 As of 31 December N, applying IFRS 17.32-37, a liability for remaining coverage is recognised and measured as the difference between the premium due (240 CU), the other fulfilment cash flows relating to expected claims (192 CU) and the CSM ($48 \times 345 / 360 = 46$ CU). Finally, the amount presented for that insurance contract will be an asset amounting to 2 CU. The usefulness of information conveyed by the amount presented on the balance sheet and resulting from offsetting different components is questionable.

- 120 – **Liabilities for claims incurred and liabilities for remaining coverage** are not shown separately. This information is key for a proper understanding of the activity and risks involved. When an insured event occurs, there is a fundamental change in nature from liability for remaining coverage (LRC) to liability for incurred claim (LIC). The key factor for the former is the probability of occurrence in the future, the key factor for the latter is the quality of estimates (from very simple estimates to more complex ones and IBNR).
- 121 – **Collateral deposits related to reinsurance accepted and held** are not shown separately. This information is key for a proper understanding of the activity and risks of the reinsurer as well as of the cedant. The information on the liability for remaining coverage of the reinsurer does not depend on the nature of the guaranty provided by the reinsurer (deposit in cash, assets pledged or third party guarantee). This issue is the same for the insurer and the insurance contract held. Accordingly, deposits made or received are considered within the boundaries of the reinsurance contract.

Premium receivables

- 122 IFRS 17 does not require information on premium receivables in the balance sheet or in the notes. A definition of “premium receivables” should clarify whether they encompass “due and payable” (expected cash flows) or only “due and payable and enforceable” amounts (expected enforceable cash flows).
- 123 A common definition of a receivable shall not depend on the payment schedule i.e. be different when settled in one payment upfront compared with 12 instalments.
- 124 The impact of separately presenting premium receivables on the simplifications offered by the premium allocation approach has to be assessed in balance with the IT complexity raised by the current standard.

Measurement of premium receivables and liabilities for incurred claims

- 125 The nature of premium receivables and liabilities for incurred claims may put them under IFRS 9. It remains to be demonstrated that the risks covered under IFRS 9 (in particular related to premium receivables) are properly taken into account in the estimated FCF following IFRS 17.32 and IFRS 17.40.
- 126 We are of the view that there is no need for changing *measurement*, i.e. referring to IFRS 9 and therefore strongly suggest restricting the issue raised to the *presentation* of accruals in the balance sheet.

13.2 Do EFRAG’s proposals address all issues raised?

- 127 ANC does not agree with EFRAG and IASB not requiring a separate presentation of certain accrual in the balance sheet and not defining “premium receivables”.
- 128 Removing or offsetting current information commonly used by analysts on accruals would obscure relevant information. When possible, relevant information shall be presented in the balance sheet rather than being disclosed in the notes (IFRS 17.100 on liabilities for remaining coverage and for incurred claims; IFRS 17.101(c) on the CSM). In addition no information is currently required in the notes on premium receivables.
- 129 Amending the standard in order to require a separate presentation of the main accruals would significantly improve understandability and relevance. From an operational standpoint, implementation would be simplified and costs would be saved.
- 130 In addition to the modifications to the standard suggested below, amendments to IFRS 17.79 (especially regarding a separate presentation of assets for acquisition

cash-flows as mentioned above in § 5) and disclosure requirements (IFRS 17.98-109) have to be revised consequently. As mentioned in the IASB tentative decisions in March 2019, changes in the unit of account for presentation purpose also induce similar changes in the unit of account for disclosure requirements (amending IFRS 17.99).

- 131 It is also necessary that a non-ambiguous definition of certain accruals (such as premium receivables) is clarified in order to provide comparative and useful information on them.
- 132 We suggest supplementing Appendix A of IFRS 17 with a common definition of premium receivables that could be based on the IFRS15.105 definition of the “unconditional rights to consideration” taking into account the effective (not the theoretical) period before policyholder’s rights (to coverage) actually lapse.

13.3 ANC additional suggestions

- 133 We suggest amending the presentation requirement in order to introduce direct requirements to present the main accruals in the face of the balance sheet (instead of in the notes):
- 134 IFRS 17.78: An entity shall present separately in the statement of financial position the carrying amount of ~~groups of~~:
- ~~(a) insurance contracts issued that are assets~~ premium receivables related to insurance contracts,
 - (b) liabilities for remaining coverage (including contractual service margin) related to insurance contracts,
 - (c) liabilities for incurred claims related to insurance contracts,
 - (d) premium receivables (reinsurer) and payables (insurer) related to reinsurance contracts,
 - (e) liabilities for remaining coverage (reinsurer) and asset for reinsurance contracts held (insurer) for reinsurance contracts,
 - (f) liabilities for incurred claims (reinsurer) and assets for reinsurance contracts held (insurer) for reinsurance contracts,
 - (g) liabilities for deposits received (insurer) and assets for deposits made (reinsurer) related to reinsurance contracts.
- ~~(b) insurance contracts issued that are;~~
~~(c) reinsurance contracts held that are assets;~~
~~(d) reinsurance contracts held that are liabilities.~~
- 135 Appendix A: Premium receivable: represents the unconditional right of the entity to consideration for the coverage to be provided. It takes into account the effective, not the theoretical, period before policyholder’s rights to coverage actually lapse.

14 Topic 4: Reinsurance contracts: contract boundary

14.1 Do EFRAG's proposals address all issues raised?

- 136 ANC shares EFRAG's analysis of the issue and its possible impact. Both approaches (symmetry between reinsurance held and insurance issued, or between reinsurance held and reinsurance issued) are conceptually funded. IASB chose the latter in order to treat reinsurance contracts as a separate contract. It is however very unlikely that the assessment made by the primary insurer is comparable with the one made by the reinsurer who generally manages several reinsurance treaties together and thanks to this broader population as well as diversification probably calculates a lower risk adjustment. By contrast, from an economic point of view, reinsurance held by the primary insurer (being proportional or non-proportional, life or non-life) aims at mitigating the insurance risks recorded in the underlying liabilities. We note that the extension of the risk mitigation provision to reinsurance held reflects that approach.
- 137 Nevertheless, since both approaches lead to the same effects in the balance sheet and limited differences in the P&L and disclosures, we recommend considering a cost/benefit analysis rather than introducing a conceptual debate at this stage.
- 138 The information added to the P&L and disclosures by the boundaries retained for reinsurance contracts results from (i) changes between the initial assessment of future contracts and the assessment of future cash flows when contracts are eventually recognised; (ii) changes in estimates in key assumptions during that transitional period; (iii) the discount rate locked-in at inception whereas related future cash-flows may change during that transitional period.
- 139 We believe such additional information is of little relevance since it overemphasises discount rate changes that are one of the risks taken by the reinsurer when accepting the treaty. On the other hand, it creates volatility in the P&L and raises significant costs due to the operational complexity to deal with such temporary estimates in the IT systems and their possible discounting effect and subsequent changes.
- 140 Based on a cost/benefit analysis, we therefore suggest limiting the boundaries of reinsurance contracts held to the recognised underlying contracts and amending IFRS 17 consequently.

Appendix 3: Additional concerns neither addressed by IASB's proposed amendments nor by EFRAG's letter

15 Topic 5: relation with IFRS 9 other than hedge accounting (see § 29)

15.1 Scope: insurance components in financial instruments

- 141 Insurance components in financial instruments might raise concerns when applying IFRS 9: Insurance contracts that meet the definition of a financial guarantee *purchased* would henceforth be in the scope of IFRS 9 (because of IFRS 17 amending IFRS 9.2.1(c)(iii)).

15.2 Non-recycling OCI on Equity investment

- 142 Non-recycling OCI on equity investment and the accounting treatment of funds (UCITS, AIF) is an issue for all insurance contracts but those accounted for under the VFA. This remains also an issue for an entity investing on its own. It is finally a broader issue than IFRS 17 and may better be addressed at IFRS 9 level.

15.3 Measurement inconsistencies – IFRS 17 implies applying a fair value measurement to assets

- 143 Since insurance contracts are measured at current value, any corresponding asset is best matched when also measured at current value, leading to application issues (for instance by segregating assets into ring-fenced pools or accepting the created mismatch). We suggest targeted improvements facilitating the alignment of the measurement of underlying assets with the measurement of the insurance contract: e.g. by allowing measuring loans at FVOCI even if the IFRS 9 business model is held-to-collect; by splitting investment property providing returns to different types of contracts.

15.4 Measurement inconsistencies – locked-in Discount rate

- 144 Participating contracts not meeting the VFA criteria require to follow in the accounting IT-systems a “locked-in” discount rate in addition to the current rate for the purpose of CSM calculation. In addition, this accounting treatment might generate temporary OCI-volatility.

16 Topic 6: Reinsurance contracts: VFA and intelligibility of standard's provisions

16.1 Reinsurance contracts issued with direct participation features

- 145 Some reinsurance contracts issued in our jurisdiction provide an indirect compensation for the underlying insurance service rendered to policyholders. And for that service, the reinsurer does not only receive a fixed premium but rather a share of the returns in a pool of underlying items. The standard however prohibits applying VFA to reinsurance contracts *issued*.

16.2 Unclear provisions regarding reinsurance held

- 146 Reinsurance contracts held are subject to the general standard's provisions with some adjustment. We however noted that these specific provisions are not literally transposable.

17 Topic 7: mismatches created on transition (OCI set to nil and comparative period; see § 33)

17.1 OCI option for non VFA participating contracts under the MRA

- 147 For an entity that chooses to disaggregate insurance finance result between P&L and OCI to non-VFA contracts, the modified retrospective approach (MRA) requires the cumulative OCI be set to nil on transition under the assumption that the discount rate retained be the current rate on transition. We rather suggest the discount rate be approximated by the "crediting" rate i.e. the rate the entity is expecting to be committed to against its policyholders.

17.2 Interaction with IFRS 9 – Comparative information in 2021

- 148 Applying IFRS 9 provisions, an entity deciding to restate the comparative year 2021 will have to apply both standards (i) IAS 39 on financial instrument derecognised before transition and (ii) IFRS 9 on financial instrument that have *not* been derecognised before transition. We rather suggest offering the option to also retrospectively apply IFRS 9 to financial instrument that have been derecognised before transition.

18 Topic 8: Interim financial statements

- 149 IFRS 17.B137 requires the CSM be "locked-in" at interim reporting which is in contradiction with the "year to date" approach required otherwise by IAS 34. Moreover, the CSM measurement would then depend on the frequency of external financial reporting; reducing comparability.

19 Topic 9: Mutual entities

- 150 If IASB intends to clarify how IFRS 17 applies to certain mutual entities it should do it in the standard itself (and not in the BC) and also explicitly highlight the specific contractual/legal circumstances deserving such a treatment (neither CSM nor equity).