

**Association Suisse des Actuares  
Schweizerische Aktuarvereinigung  
Swiss Association of Actuaries**

**International Accounting Standards Board  
30 Cannon Street  
London EC4M 6XH  
United Kingdom**

**Exposure Draft ED/2015/11 Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts**

**Summary**

Overall, we support the IASB's proposal to address the effects of applying IFRS 9 before IFRS 4 Phase II becomes effective for the reasons mentioned in the ED. It is clear that we will have to have some inconsistency somewhere as we move from the current reporting basis to a future with both IFRS 9 and IFRS phase II. The important question here is which inconsistencies cause the least problem to users of the financial statements. Is it:

- a. Inconsistency between the treatment of assets and liabilities on the balance sheet of an insurer
- b. Inconsistency in the treatment of assets and liabilities of an entity over time
- c. Inconsistency in the treatment of assets between an insurer and an entity in another industry
- d. Inconsistency in the treatment of assets between different parts of an entity's business

The view of the Swiss Actuarial Association on the relative importance of these inconsistencies over time is as follows:

- a. The SAV believe that it is imperative to maintain consistency here. Any mismatch between the way assets are valued and their corresponding liabilities makes an insurer's financial statements essentially meaningless.
- b. While with the advent of IFRS 4 phase II this is inevitable, the SAV strongly believes that two significant changes in the way first assets and then liabilities are treated will make it much harder for users to pull relevant information over time from the financial statements. In particular, we believe that the user's interests are best served by avoiding mismatches in the treatment of assets and liabilities and also by avoiding having more than one significant change in the accounting basis for insurers over the next few years.
- c. While the SAV also believes that this should be avoided wherever possible, the fact that many users tend to look at the insurance industry as a whole in making investment decisions, we believe that for a temporary period, this inconsistency is less damaging than a) and b) above.
- d. Just to provide an example to illustrate our view here. Many insurers in Switzerland issue Group Pensions business. The SAV strongly believes that it is more important that these

insurers use a consistent method to report on that business, than achieving consistency between, say, this insurance business and a banking subsidiary within the same Group. Users already look at the insurance and banking business within the Group separately, disclosures already allow for a very different approach to understanding the results and drivers of those very different businesses. If two companies were forced to take very different approaches to reporting their Swiss Group Pensions business it would be very difficult for a user to make any sensible comparison.

Based on our view as set out above, that leads the SAV to the following recommendations:

- We agree with the IASB's decision to propose an amendment to the existing IFRS 4 to provide a solution for the different effective dates of IFRS 9 and the future IFRS 4 Phase II.
- The overlay approach ends up meaning there are three different ways that reporting entities could deal with IFRS 9 during the transition period which cannot be helpful to users. In addition the overlay approach would bear too much complexity and cost and therefore not be needed
- The deferral approach should be available to a larger population to allow for a reasonable comparison within the insurance industry for users and over time.

Our responses to the questions posed in the ED are set forth the Appendix to this letter.

Beat Müller

Chairman SAV Accounting Subcommittee

Holger Walz

Managing Director

### **Question 1 – Addressing the concerns raised**

*Paragraphs BC9–BC21 describe the following concerns raised by some interested parties about the different effective dates of IFRS 9 and the new insurance contracts Standard:*

*(a) Users of financial statements may find it difficult to understand the additional accounting mismatches and temporary volatility that could arise in profit or loss if IFRS 9 is applied before the new insurance contracts Standard (paragraphs BC10–BC16).*

*(b) Some entities that issue contracts within the scope of IFRS 4 have expressed concerns about having to apply the classification and measurement requirements in IFRS 9 before the effects of the new insurance contracts Standard can be fully evaluated (paragraph BC17–BC18).*

*(c) Two sets of major accounting changes in a short period of time could result in significant cost and effort for both preparers and users of financial statements (paragraphs BC19–BC21).*

*The proposals in this Exposure Draft are designed to address these concerns.*

**Do you agree that the IASB should seek to address these concerns? Why or why not?**

### **SAV's response to 1**

We agree that the IASB should address the concerns raised with regard to the accounting issues created by having different effective dates. We agree because users, as well as preparers, need to have a set of financial statements that provide relevant information. The additional accounting mismatches that are not expected to continue after IFRS 4 Phase II is implemented will create financial statements that will not be as valuable to the users as the current financial statements due to these additional accounting mismatches.

The SAV would like to stress its view that the financial statement users (in particular the analyst community) are generally less concerned about a limited lack of comparability across industries (e.g. banks and insurers) but keen to have as much comparability as possible within the industry (see also statement c) in our introductory summary). Therefore, even though there will be reduced comparability across industries (with regards to IFRS 9) for a number of years, the IASB's decision to address the consequences of having different effective dates for IFRS 4 Phase II and IFRS 9 makes sense.

As proposed by the IASB, the solution should be optional so companies can still apply IFRS 9 without any adjustment starting 1 January 2018.

It is also important that any solution should come from the IASB in order to retain a level-playing field.

**Question 2- Proposing both an overlay approach and a temporary exemption from applying IFRS 9**

*The IASB proposes to address the concerns described in paragraphs BC9–BC21 by amending IFRS 4:*

*(a) to permit entities that issue contracts within the scope of IFRS 4 to reclassify from profit or loss to other comprehensive income some of the income or expenses arising from designated financial assets that:*

*(i) are measured at fair value through profit or loss in their entirety applying IFRS 9 but*

*(ii) would not have been so measured applying IAS 39 (the 'overlay approach') (see paragraphs BC24–BC25);*

*(b) to provide an optional temporary exemption from applying IFRS 9 for entities whose predominant activity is issuing contracts within the scope of IFRS 4 (the 'temporary exemption from applying IFRS 9') (see paragraphs BC26–BC31).*

**Do you agree that there should be both an overlay approach and a temporary exemption from applying IFRS 9? Why or why not?**

**If you consider that only one of the proposed amendments is needed, please explain which and why.**

**SAV's response to 2**

The IASB proposes two alternatives for addressing the issue of different effective dates.

Whilst we believe that the temporary exemption (deferral approach) is needed to avoid two rounds of change in a relatively short period we believe that the overlay approach on one hand would mean the industry is offered with three different ways that reporting entities could deal with IFRS 9 during the transition period and on the other hand) would introduce too much additional cost and complexity by requiring the preparers to set up a parallel reporting (IFRS 9 and IAS 39 (e.g. parallel administration and accounting systems) and would therefore not be needed.

### Question 3 – The overlay approach

Paragraphs 35A–35F and BC32–BC53 describe the proposed overlay approach.

(a) Paragraphs 35B and BC35–BC43 describe the assets to which the overlay approach can be applied. **Do you agree that the assets described (and only those assets) should be eligible for the overlay approach? Why or why not? If not, what do you propose instead and why?**

(b) Paragraphs 35C and BC48–BC50 discuss presentation of amounts reclassified from profit or loss to other comprehensive income applying the overlay approach. **Do you agree with the proposed approach to presentation? Why or why not? If not, what do you propose instead and why?**

**(c) Do you have any further comments on the overlay approach?**

### SAV's response to 3

As stated above, we are concerned about the costs and complexity of the overlay approach in general and do not think it would be needed. However, if the ultimate amendment should still include this option, our comments would be the following.

The IASB proposes that the overlay approach only applies to financial assets which are both:

- Designated as relating to contracts in the scope of IFRS 4 and
- Measured at fair value through profit or loss (FVPL) in accordance with IFRS 9 but would not have been measured in their entirety as FVPL under IAS 39

The ED refers to financial assets that meet these two conditions as 'qualifying financial assets'.

On the first criterion, designation, we agree that, based on the objective of mitigating the effects of applying IFRS 9 before IFRS 4 Phase II is applied, the overlay should only apply to the portion of assets that relate to the insurance liabilities. In order to identify the portion that relates to the insurance liabilities, a designation is necessary, however, we identify some issues on how designation should be applied:

- The ED does not define 'related to' or explain how such relationship should be established other than that this is a designation determined by the insurer.
- The Board does explain entities cannot include assets "clearly held in respect of activities other than contracts within the scope of IFRS 4", such as financial assets held by a banking subsidiary that does not issue contracts within the scope of IFRS 4 or financial assets held in funds clearly related to investment contracts that are outside of the scope of IFRS 4. Although we can understand what the IASB is trying to achieve, the ED does not include any guidance on what 'clearly held in respect of activities other than contracts within the scope of IFRS 4' means. In order to support comparability, further guidance would be needed.
- The examples in BC 38 do not address financial assets held by an insurer that are in the shareholders' fund or assets not directly related to insurance liabilities. This raises the issue whether designated assets may, for example, also include additional assets an entity holds to meet regulatory requirements or its own (internal) capital requirements in respect of insured events being more frequent or more severe than expected.

The second criterion is a natural consequence of the IASB's objective to resolve additional accounting mismatches in profit or loss from the introduction of IFRS 9 before IFRS 4 Phase II. However, the ED does not provide clarity on whether instruments being measured at FVPL under IFRS 9 but not under IAS 39 would apply to mandatory FVPL measurement only or also includes financial instruments that are designated as at FVPL under the fair value option.

In order to prevent undue diversity, we believe that the Board should further clarify how to deal with the above issues in practice.

### **Disclosure**

To provide information about transfers within a group or re-designation of financial assets to achieve a particular accounting outcome, the Board proposes that entities disclose the effects on profit or loss and OCI of financial assets that move in and out of the overlay approach in the reporting period.

We share the IASB's concern for transactions taking place to achieve desired accounting outcomes. That said, these disclosures would be quite onerous and may therefore also prevent transactions based on an economic rationale.

### **Presentation**

A single line item for the amount of the overlay adjustment should be presented in either profit or loss or OCI, or both. To the extent an entity does not separately identify the effect of the overlay adjustment on line items in profit or loss on the face of the profit or loss account, this disaggregation should be shown in the note disclosures. This means entities can choose to disaggregate the adjustment amount in profit or loss or in the notes. Whilst this choice allows entities to provide information about profit or loss effects under both IFRS 9 and IAS 39 in the way they find most useful, it also has a potential for different ways of presentation by different entities. Therefore emphasis should be put on clarity and comprehension of disclosing the impact of the overlay adjustments for users.

### **Transition**

We agree with the Board that on the transition to IFRS 9, the overlay approach, if selected, must be applied consistently with the transition requirements of IFRS 9: retrospectively application of the overlay adjustment and restatement of comparatives if the entity also restates comparatives under IFRS 9.

#### **Question 4 – The temporary exemption from applying IFRS 9**

*As described in paragraphs 20A and BC58–BC60 the Exposure Draft proposes that only entities whose predominant activity is issuing contracts within the scope of IFRS 4 can qualify for the temporary exemption from applying IFRS 9.*

**(a) Do you agree that eligibility for the temporary exemption from applying IFRS 9 should be based on whether the entity’s predominant activity is issuing contracts within the scope of IFRS 4? Why or why not? If not, what do you propose instead and why?**

*As described in paragraphs 20C and BC62–BC66, the Exposure Draft proposes that an entity would determine whether its predominant activity is issuing contracts within the scope of IFRS 4 by comparing the carrying amount of its liabilities arising from contracts within the scope of IFRS 4 with the total carrying amount of its liabilities (including liabilities arising from contracts within the scope of IFRS 4).*

**(b) Do you agree that an entity should assess its predominant activity in this way? Why or why not? If you believe predominance should be assessed differently, please describe the approach you would propose and why?**

Paragraphs BC55–BC57 explain the IASB’s proposal that an entity would assess the predominant activity of the reporting entity as a whole (i.e. assessment at the reporting entity level).

**(c) Do you agree with the proposal that an entity would assess its predominant activity at the reporting entity level? Why or why not? If not, what do you propose instead and why?**

#### **SAV’s response to 4**

##### **Eligibility**

We agree with the IASB’s rationale for setting a test that needs to be met to be eligible for the deferral approach. However, we are of the opinion that the deferral approach should be available to a large enough population to allow for a reasonable comparison within the insurance industry for users over time.

The IASB proposes that only entities whose predominant activity is issuing contracts that are within the scope of IFRS 4 qualify for the deferral approach. This means the definition of ‘predominance’ is critical to the scope of the deferral approach. The ED proposes that predominance should be determined on the basis of an entity’s liabilities arising from contracts within the scope of in scope of IFRS 4 in proportion to the entity’s total liabilities. However, the ED does not contain any further definition of ‘predominance’ within the standard nor does it include application guidance as to its meaning within the ED. There is, for example, no discussion of any quantitative characteristics that would determine ‘predominance’ other than through the outcome of a single calculation. The only detailed guidance appears in BC 65 which is not part of the authoritative guidance in the proposed amendments. We believe that any guidance of the nature contained in BC 65 should be included within the body of the standard and not as part of the basis for conclusions. We further believe that BC 65 is contradictory since it states that a particular quantitative threshold for ‘predominance’ would be arbitrary but then provides an example with an ‘arbitrary’ figure of 75% of an entity’s liabilities which is stated to not meet the predominance condition for the purpose of the ED.

We believe that it is very likely the method proposed in the ED and interpretation of the associated example in the Basis for Conclusions will create an implied ‘bright line’ in practice based on the single quantitative factor mentioned in the BC, even though such an approach does not seem to be the IASB’s intent. We therefore believe that the IASB should decide on an unambiguous approach through either:

- i. Remove any reference to one particular quantitative threshold. Then a clear set of quantitative and/or qualitative characteristics must be provided together with a robust

definition of predominance – again, allowing for a large enough population to qualify for the approach for the reasons stated above.

- ii. Clearly specify a quantitative threshold as part of the ED and explicitly mention that this is the Board's intent. As part of this route, the IASB should carefully consider both the level of this threshold as well as the further definition of 'liabilities arising from contracts within the scope of this IFRS' in order to allow for a large enough population qualifying for the approach and thus allow for a reasonable comparison within the insurance industry - particularly in light of the fact that based on a preliminary assessment (with the implied 75% threshold) some of the "pure play" insurers seem to have serious doubts whether they would qualify for the deferral approach.

We note that (ii) will be the simplest approach but will continue to operate on the basis of bright-line. In contrast, (i) would allow for an approach that considers other specific circumstances but will be more complex and may require significant judgement – which is currently not the IASB's intent. Whatever route the IASB decides to follow, the design of predominance test and threshold(s) are matters that require appropriate consideration.

### **Reporting entity level**

The ED proposes that the entity evaluates whether its insurance activities are predominant at the reporting entity level. This could result in one entity reporting the same instruments on different basis for different financial statements (e.g. IAS 39 for consolidation purposes and IFRS 9 for individual financial statements). We would regard this situation as being analogous to a company that applies IFRS in its reporting package for consolidation purposes and local GAAP in its individual financial statements, however further increase complexity by introducing an additional accounting and reporting logic.

If the IASB wishes to consider application at any level other than the reporting entity level, careful evaluation of users' views will be critical.

### **Disclosure**

Although the deferral approach provides a temporary exemption from applying IFRS 9, the ED requires certain disclosures that would enable users to make comparisons between entities that deferred IFRS 9 and other entities which already fully implemented the new standard. These disclosures focus on contractual terms of the financial assets ('SPPI') and aggregated credit risk information.

We agree with the IASB's objective to provide some useful disclosures on some aspects of the impact of IFRS 9 to allow for limited comparability whilst not negating the full effect of deferral. However, we believe that the list of required disclosures should be reconsidered carefully in order to avoid too much complexity and by this diminish the value of the deferral option.

Furthermore, we would like to highlight, that from our perspective, we do not agree with the IASB's argument that a broader population of entities would always ask for a more detailed disclosures (including a full reconciliation to the IFRS 9 impact on the financial statements).

### **Transition**

The IASB proposes that predominance should be re-assessed if there is a demonstrable change in corporate structure (e.g., acquisitions or disposals) that could result in a change of the predominant activities.

We would expect the IASB to provide further clarity on what is a demonstrable change in corporate structure and when it would be on an extent that would result in a change to the predominance conclusion. Furthermore, we do believe that the cost benefit ratio of reassessing the predominance and earlier implementation of IFRS 9 might only be positive in rare circumstances (e.g. following an acquisition of a non-IFRS 4 portfolio by a preparer previously qualifying for the deferral approach, would a user / analyst post-acquisition really want to look at the financials accounted under a different model or still have a comparable basis?). This also in combination with the almost unrealistically short preparation time for full IFRS 9 implementation, in case a reassessment would result in an entity no longer qualifying for the deferral approach.

**Question 5 – Should the overlay approach and the temporary exemption from applying IFRS 9 be optional?**

*As explained in paragraphs BC78–BC81, the Exposure Draft proposes that both the overlay approach and the temporary exemption from applying IFRS 9 would be optional for entities that qualify. Consistently with this approach, paragraphs BC45 and BC76 explain that an entity would be permitted to stop applying those approaches before the new insurance contracts Standard is applied.*

**(a) Do you agree with the proposal that the overlay approach and the temporary exemption from applying IFRS 9 should be optional? Why or why not?**

**(b) Do you agree with the proposal to allow entities to stop applying the overlay approach or the temporary exemption from applying IFRS 9 from the beginning of any annual reporting period before the new insurance contracts Standards is applied? Why or why not?**

**SAV's response to 5**

We agree with the IASB that any alternative to the 'full' application of IFRS 9 should be optional.

Before IFRS 4 Phase II becomes effective, a company can voluntarily change:

- from deferral to overlay approach or full IFRS 9, or
- from overlay approach to full IFRS 9 but not to deferral

We agree with the proposal that a company can, and has the option to change only in the direction towards 'full' IFRS 9 application so retrograde steps that take a company further way from 'full' IFRS 9 application are prevented.

**Question 6 – Expiry date for the temporary exemption from applying IFRS 9**

*Paragraphs 20A and BC77 propose that the temporary exemption from applying IFRS 9 should expire at the start of annual reporting periods beginning on or after 1 January 2021.*

**Do you agree that the temporary exemption should have an expiry date? Why or why not?**

**Do you agree with the proposed expiry date of annual reporting periods beginning on or after 1 January 2021? If not, what expiry date would you propose and why?**

**SAV's response to 6**

The IASB proposes a 'sunset clause' to emphasise the temporary nature of IFRS 9 deferral in case the introduction of IFRS 4 Phase II would be subject to further delay. We understand how the IASB came up with this clause, however, would expect the IASB to re-evaluate the sunset clause once the final effective date for IFRS 4 Phase II is set.