



What constituents are saying...

Feedback on the 2013 Exposure Draft

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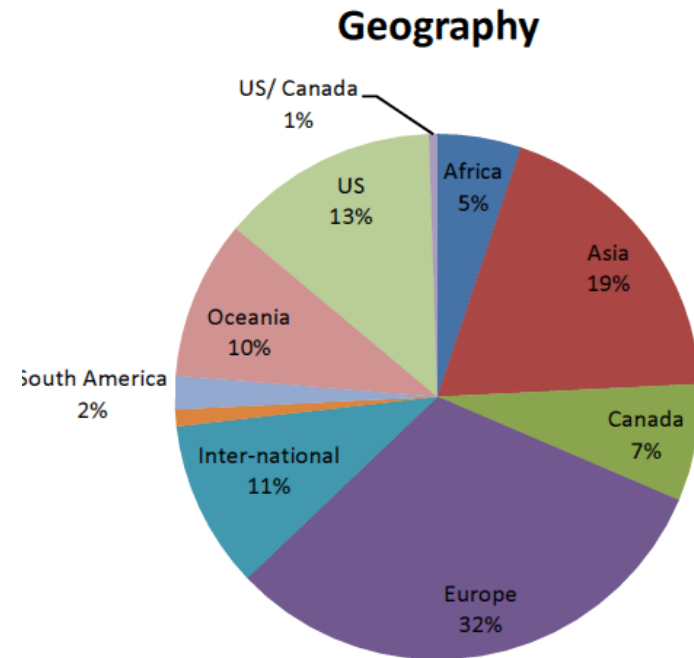
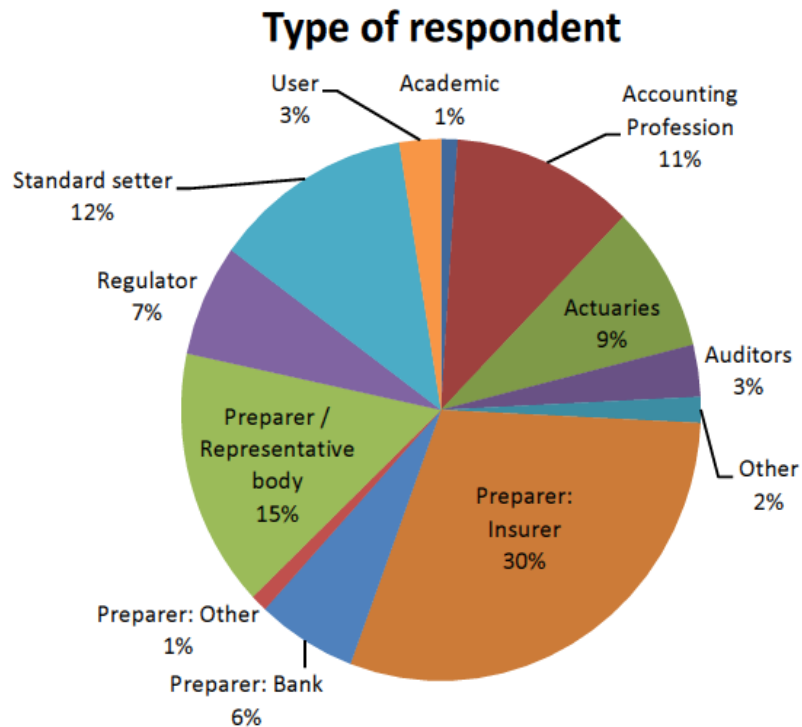


Agenda

- Main themes raised in comment letters and outreach activities
- Feedback from users of financial statements
- Results and observations arising from the fieldwork
- Significant comments made by IASB and FASB members – 22 January joint meeting
- Discussion on the interaction between IFRS 9 and insurance contracts
- Timetable and next steps

Summary of comments received

194 comment letters received from various respondents in different geographical locations



Source: IASB Staff Paper 2A, January 2014

Main themes in comment letters and outreach activities

General comments

- Majority of respondents believe that the 2013 ED proposals are an improvement over those in the 2010 ED
- Many respondents welcomed the current value measurement of the insurance contract liability
- Key concerns that need to be addressed further:
 - Operational complexity of some specific proposals, e.g.
 - need to bifurcate cash flows under mirroring approach,
 - use of information that is currently not used by management for insurance revenue
 - Extent of accounting mismatches resulting from mandatory OCI solution

Unlocking the contractual service margin

General support with some concerns

- Wide support on the proposal to unlock contractual service margin (“CSM”) for changes in estimates of future cash flows relating to future service
 - Better representation of the CSM as the unearned profit in a contract
 - Consistency between initial recognition and subsequent measurement
 - Consistency in measurement under building block model and premium allocation approach
- Some respondents did not agree on the CSM unlocking proposals
 - Financial statements do not reflect changes in estimates as soon as insurers are aware of the changes
 - Will result in decreased transparency and smoothing in underwriting results

Unlocking the contractual service margin (cont.)

Proposed changes and Deloitte position

- **Proposed changes:**

- Unlock CSM for changes in risk adjustment relating to future service
- Reversal of losses previously recognised in profit or loss before CSM is rebuilt
- Unlock for additional changes in estimates, i.e. changes in reinvestment assumptions relating to future service, changes in underlying asset returns to the extent of their impact on unearned profit

Deloitte position:

- Welcome unlocking proposal
- Propose to modify:
 - To extend the CSM earning period beyond coverage
 - To adjust CSM for prospective changes in risk adjustment
 - To not restrict CSM unlocking for changes in future cash flows

Mirroring Approach

Mixed views with many concerns

- Many respondents support the Board's intention to eliminate accounting mismatches for some participating contracts through mirroring approach
- Mixed views depending on jurisdictions – respondents in Canada and Asia support mirroring approach. However, most constituents expressed significant concerns about the mirroring proposals
- Concerns were raised over the complexity of the proposals to decompose the cash flows
- Other concerns included:
 - Lack of scope clarity
 - Concerns over comparability of results
 - Participating contracts vs. other insurance contracts
 - Contracts to which mirroring applies vs. contracts to which it does not
 - Mirroring could result in misleading results if underlying items are not at FV

Mirroring Approach (cont.)

Proposed changes and Deloitte position

- **Proposed changes**

Differing views received from respondents

- All insurance liabilities be measured using the BBA with accounting mismatches addressed by modifying asset accounting
 - An optional OCI solution, rather than a mandatory requirement
 - Alternative approaches were proposed by some respondents
- Comments also received on participating contracts to which mirroring approach does not apply, although no explicit question was raised by IASB on this area
 - Operationally complex as it requires different discount rates for different cash flows
 - Lack of clarity over which cash flows should be discounted at the current market rate and those discounted at locked-in rate

Deloitte position:

- Agree that economic match of asset-liability cash flows should be faithfully represented
- Propose to abandon the mirroring approach decomposition and replace with a modified BBA

Insurance Revenue

Mixed views

- Mixed views from respondents
 - Supporters' view: increased comparability with other industries
 - Opposition's view: will not provide useful information; analysts will compare insurance companies with other insurance companies
- The requirement to exclude investment component from insurance contract revenue underpins the opposition raised over the proposals
 - Deposit component is an integral part of an insurance contract
 - Separating the investment component will be operationally complex; information required not available within existing accounting systems
- General agreement on the need for IASB to educate preparers and users about the proposals and the impact on key performance indicators

Insurance Revenue (cont.)

Proposed changes and Deloitte position

- **Proposed changes:**
 - Certain jurisdictions supported a premium due presentation, including deposit component, as it provides more relevant information about cash flows and is more consistent with how management assess performance
 - Small minority support presentation of gross written premiums as this will provide comparability and information about performance
 - Some respondents proposed the summarised margin approach
 - Provide most direct link to the measurement model and information about key drivers of insurance contract performance
 - Eliminate cash receipts and payments from income statement
 - Easier to apply

Deloitte position:

- New revenue metric not the most faithful representation of long duration contracts
- New metric does not provide the volume information requested by investors
- Recommend the presentation of the summarised margin as in the 2010 ED

Presentation of interest expense

- Many support the proposal for an amortised cost view of insurance contracts in profit or loss and a current value view in the balance sheet.
- Limited support over mandatory recognition of changes in discount rate in other comprehensive income ('OCI solution')
 - General concerns over significant accounting mismatches that would result from applying the proposals where assets backing the insurance liabilities are measured under different bases
- Non-life insurers were less supportive than life insurers on the OCI solution. Most non-life insurers would prefer presenting the impact of discount rate changes in profit or loss

Presentation of interest expense (cont.)

Proposed alternatives and Deloitte position

- **Proposed alternatives**

- Many suggest an option of where to reflect changes in discount rate
 - Default presentation in OCI, with an option to present in profit or loss
 - Default presentation in profit or loss, with an option to present in OCI
 - No default position, allow insurers to choose whether to present changes in discount rate in either OCI or profit or loss
- Most respondents suggested that election of an option should be applied at portfolio level while some suggested it should be applied at entity level.
- Most respondents suggest that the election be made irrevocably at inception.

Deloitte position:

- Support development in conjunction with IFRS 9
- Permit designation of insurance contracts – no mandatory OCI
- Failing this, allow presenting in profit or loss changes in insurance contracts accumulated OCI reserve to the extent that they represent gains/losses attributable to the hedged risk
- Unconstrained ability to adopt FV options on assets

Approach to transition

Wide support but some concerns

- Wide support over retrospective approach to transition, with specified simplifications provided where this is deemed impracticable
- Most respondents welcome the proposal to recognise CSM on transition even though this would result in increased implementation costs
- Concerns raised over:
 - Availability of information required to determine cash flows
 - Impracticable to determine historical discount rates
 - Proposed simplifications could overstate CSM at the date of transition
 - Subjective nature of estimates and the extent that these would be auditable
- Most believe that the effective dates of the new insurance contracts standard and IFRS 9 should be aligned, with varying proposals if this is not possible
- Most agree with the proposed three-year implementation period

Approach to transition (cont.)

Deloitte position

Deloitte position:

- Full retrospective approach is the most appropriate and accurate method
- A period of 3 years is sufficient to allow implementation
- Consider FASB proposal to measure CSM by aggregating contracts at the portfolio level
- Encourage effective dates of insurance contracts standard and IFRS 9 to be aligned
- Failing this, an option to reclassify financial assets
- An unconstrained ability for an irrevocable option to adopt fair value on assets

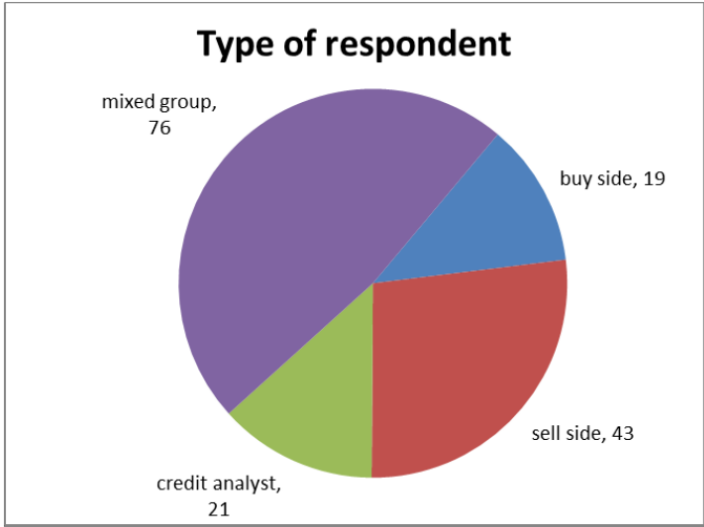
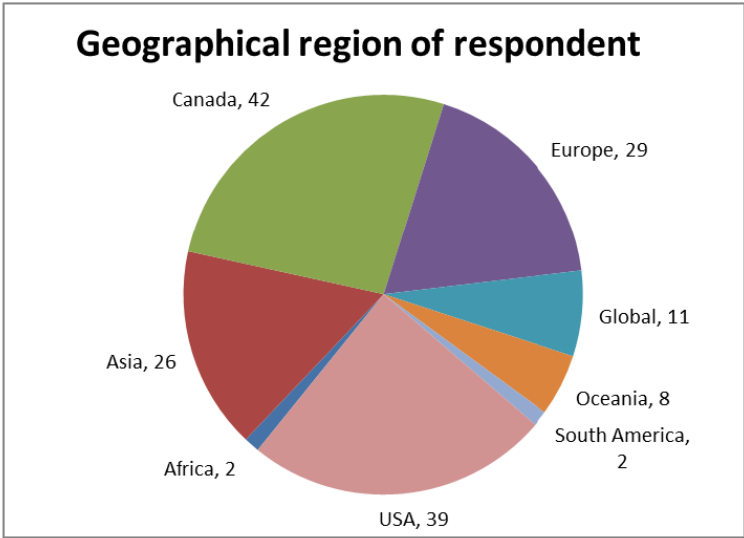
Effects of the Standard as a whole

Wide support with some concerns

- Wide support over the proposal for a single accounting model that would apply to all types of insurance contracts
- However, concerns remain about the impact of changing from existing accounting practices (depending on jurisdictions)
- Varying views on how IASB should proceed given that full convergence between IFRS and US GAAP is unlikely
- Most acknowledge that implementation costs would be significant
- However, many believe that the benefits will outweigh the costs if key issues such as accounting mismatches and participating contracts are resolved

Summary of feedback from financial statement users

44 discussions between June and December 2013 with 159 users of financials statements



Source: IASB Staff Paper 2B, January 2014

Feedback from users of financial statements

Overall comments

- Need for change
 - Most users recognise the need for change, particularly where operations are in different jurisdictions or where different types of business are compared
 - There is a lack of comparability and transparency
 - Users in USA and Australia, and where entities issue primarily non-life insurance contracts, think that significant change is not required
- Current, market-consistent information
 - Most users support the model as this would result in more timely delivery of more objective information
 - Some believe that an accounting model based on market-consistent information would not faithfully represent the insurance business model
 - Some think that the separate measurement of financial assets and insurance liabilities will result in unintended accounting mismatches and volatility
 - A few US analysts doubt the benefits of discounting short-duration contracts
 - Depends on subjective estimates and assumptions

Feedback from users of financial statements

Support for disclosures

- Disclosures
 - Most users emphasise the importance of disclosures
 - Support for disclosure of reconciliation of balance sheet movements, amounts recognised in the statement of comprehensive income, assumptions and sensitivity to changes in those assumptions and disclosures at a granular level
 - Some concerns that additional information would be provided in order to comply with US GAAP or Solvency II, in which case reconciliations between such information and IFRS should be disclosed

Topics on which IASB was seeking feedback

Support for some proposals but not others

- Unlocking CSM
 - Most users agree with proposals
 - Most noted the importance of disclosing the amounts of changes in estimates in the period that are adjusted in the CSM
 - Some preferred that the effect of any changes in assumptions should be recognised immediately in profit or loss
- Mirroring
 - This topic was only discussed with users who analyse participating contracts
 - Many agreed with the proposal because they think it reflects better the economics of those contracts
 - Some disagreed because they think that any exceptions to the measurement for some insurance contracts would impair comparability, and some disagree with measuring components in different ways i.e. amortised cost and current value
 - Most agreed that options and guarantees should be measured using a current value approach

Topics on which IASB was seeking feedback

Mixed views on presentation of revenue and expenses

- Presentation of revenue and expenses
 - Buy-side analysts generally agreed with the conceptual merits of the proposal
 - Sell-side analysts and those that analyse mostly long-term contracts and other financial institutions generally disagreed with the proposals. They think that different presentation approaches for different types of contract reflects the different economics of those contracts. They prefer the summarised margin presentation
 - All are concerned about the understandability and usefulness of the proposed insurance contract revenue, which would require the IASB to educate users
 - Many emphasised the need for information provided by the summarised margin presentation and activity measures
 - All emphasised that deposits included in the premium should not be presented as revenue

Topics on which IASB was seeking feedback

Support for some proposals but not others

- Presentation of some of the investment result in OCI
 - Many agreed with the proposal.
 - Some disagreed where they already receive current value information and are used to understanding its effects. These would prefer all changes to be recognised immediately in profit or loss
 - Many are concerned about the mismatches that would be created by the proposed mandatory use of OCI if assets are measured at other than FVOCI
- Transition
 - All users agreed with the proposed approach
 - Many supported disclosures that explain the assumptions and simplifications used and disclose the amounts determined using simplifications
 - Some expressed concerns about operational complexity, possible lack of data, and possible non-alignment of the effective dates of IFRS 9 and IFRS 4-Phase II

Summary of observations from the fieldwork

Overall observations

- The fundamental proposals can be applied
- The proposals will result in significant implementation costs, which will differ between entities
- The amounts reported are affected by the assumptions used to estimate them. Some believe that the costs of applying the proposals outweighed the benefits because differences in the assumptions may lead to a lack of comparability.

Summary of observations from the fieldwork

Targeted proposals

- Mixed responses on whether the benefits outweighed the costs on the five targeted proposals
- Generally the five proposals could be made operational with differing levels of complexity
- However, the majority of participants from the EU did not believe that the presentation of revenue and expenses for long-term contracts and for the mirroring approach were operational
- Some participants requested further simplification or a suggested alternative approaches for all five proposals due to their complexity

Significant comments made by IASB and FASB members

IASB and FASB joint meeting on 22 January 2014

- Unlocking the CSM – Two FASB members who had previously supported a locked margin expressed a willingness to unlock the CSM in order to make the profit and loss more current and more comparable with the profit or loss of non-insurers, and that this was worth exploring in order to achieve convergence with the IASB
- Mirroring approach – The IASB members were surprised at the adverse comments received on its mirroring proposals
- Presentation of revenue and expenses – A few IASB and FASB members expressed the view that it might be better to revert back to the summarised margin approach, with volume disclosures in the notes
- Presentation of the effect of changes in discount rate in OCI – The FASB members mentioned that it would be important to ensure that the IASB and FASB definition of the discount rate converged

Significant comments on the interaction with IFRS 9

IASB meeting on 22 January 2014

- The view of the IASB staff was that the introduction of FVOCI was sufficient to address the concerns of Insurance companies
- Although some IASB members felt that it was not appropriate to finalise IFRS 9 without a complete understanding of the interaction with the insurance contracts standard, the majority considered that it was important to finalise IFRS 9 irrespective of the completion status of IFRS 4-Phase II

Timetable and next steps

Likely course of action

- The IASB will not be re-deliberating its proposals for an insurance contracts standard until the March joint meeting with the FASB
- The Staff plan to provide a project plan to address priorities for the insurance contracts project
 - To address significant concerns relating to OCI solution and participating contracts
 - To consider further simplifications, clarification and refinements for transition and unlocking of the CSM
 - To assess benefits over costs in relation to insurance revenue proposals
 - To determine other issues that require re-deliberation
- The interaction of IFRS 9 with the insurance contracts standard will be discussed during the re-deliberations of the insurance contracts standard rather than being separately addressed during the finalisation of IFRS 9
- The IASB re-deliberations are expected to continue until the end of the summer of 2014, following which the IASB staff will commence drafting the IFRS.
- If this timetable is achieved, the most likely date for the publication of the final insurance contracts standard is during the first quarter of 2015.

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