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The IASB takes decisions on “IFRS 9 decoupling”

Strategic deliberations on the interaction between assets and liabilities accounting before IFRS 4 Phase II is mandatory

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Agenda

- **Highlights of the IASB meeting on 15 March 2016**
- **IASB Staff analysis, IASB discussion, tentative decisions and comparison with Deloitte comment letter**
- **Next steps**

Highlights of March IASB meeting on the “IFRS 9 decoupling” ED

On 15 March 2016 the IASB **voted in favour** of the following matters:

- Provide a **temporary exemption from applying IFRS 9 for qualifying entities**
- The **eligibility for the temporary exemption should be determined at the reporting entity level only**
- There should be a **fixed expiry date for the temporary exemption**
- Provide an **overlay approach** as an additional solution
- The **temporary exemption from applying IFRS 9 and the overlay approach should be optional**

Amendments to IFRS 4: Applying IFRS *9 Financial Instruments* with IFRS 4 *Insurance Contracts*

Introduction to the meeting on 15 March 2016

- The comment letter deadline closed on 8 February, with 96 letters received.
- The proposed amendments to IFRS 4 are designed to address the concerns about the different effective dates of IFRS 9 and the forthcoming insurance contracts Standard.
- The Board gave the Staff permission to commence the ballot and drafting of the forthcoming insurance contracts Standard at its February meeting.
- The Board is expected to set the effective date of the Standard when drafting has sufficiently progressed.

Comment letters and outreach

Summary of feedback received from all respondents (except users)

- Most commentators wrote to the IASB to address the concerns that the ED highlighted
- Most preparers viewed the deferral approach as the only approach that addresses all of their concerns
- Their view is shared also by most auditors, accounting and actuarial bodies, and national standard-setters
- A few preparers were not convinced of the need for a decoupling solution or preferred the overlay approach. These preparers were mainly bancassurers
- Most respondents believe that the population of entities that would qualify for the deferral approach is too narrow because entities that regard themselves as insurers would not qualify under the proposed test

Comment letters and outreach

Summary of feedback received from all respondents (except users) (continued)

- There were mixed views on whether the eligibility assessment for the deferral approach should be conducted at 'the reporting entity level' only, or should be permitted 'below the reporting entity level'
- Most regulators supported an assessment at the reporting entity level, whereas most preparers, national standard-setters, auditors, and accounting and actuarial bodies supported an approach that allowed an assessment below the reporting entity level
- Respondents had mixed views on whether there should be a fixed expiry date for the deferral approach
- Most regulators, and some standard-setters and auditors supported the fixed expiry date, whereas many preparers believe that insurers should be required to apply IFRS 9 only when they apply the forthcoming insurance contracts Standard

Comment letters and outreach

IASB discussion

- Not convinced that the incremental costs would arise to the extent suggested. In particular because IFRS 9 will provide useful information, which would not be a wasted cost
- Many different classifications of financial assets are possible if both IAS 39 and IFRS 9 applied by the reporting entity. This represent a problem for the IASB
- Investors compare bancassurers to other banks, not to insurers, therefore applying IFRS 9 at the reporting entity level is important to preserve comparability
- Important to have a fixed expiry date the for the deferral approach. A further deferral may be allowed if and only if there are significant delays in publishing the insurance contracts Standard
- Staff noted the recommendations on avoiding that first-time adopters are prohibited from applying the overlay approach and the temporary exemption, and an entity may be required to apply different accounting to its investment in associates and joint ventures

Feedback from users of financial statements

Summary of feedback

Concerns raised

- Mixed views on whether the “decoupling” issue really makes the financial statements less understandable and create disruption for users
- Many users from different jurisdictions stated that any increased volatility that may arise in profit or loss when IFRS 9 is applied in conjunction with IFRS 4 would not make their analysis more difficult because they do not focus only on profit or loss but use other metrics, and they do not expect increased volatility to change their analysis significantly
- Other users (particularly from Europe and Asia) said that increased volatility would be unhelpful and would make the earnings reported in the insurance industry appear more uncertain and less attractive for investment
- In general, users who expressed concerns about potential increased volatility also tended to have concerns about two consecutive changes in accounting in a short period of time

Feedback from users of financial statements

Summary of feedback (continued)

Approaches proposed

- Many users noted that IFRS 9 is an improvement over IAS 39 and therefore should be applied by everyone without suspending it for a segment of the market because of the alleged interaction with the forthcoming insurance contracts Standard
- Most users thought that providing two approaches, especially if optional, would decrease comparability and would be confusing
- Most users preferred the overlay approach for its comparability and transparency
- Many users did not support the deferral of IFRS 9 as it introduces lack of comparability, creates accounting arbitrage and reduces information content
- The users who supported the deferral approach were mainly insurance analysts from Europe, Canada and Asia

Feedback from users of financial statements

Summary of feedback (continued)

Approaches proposed

- If the Board was to proceed with the deferral approach, most users commented as follows:
  - Support using IFRS 9 at the reporting entity level, mainly because it avoids applying two Standards for financial assets in a single set of financial statements
  - Want comparability within the insurance sector and therefore the proposed eligibility criteria to capture entities they consider to be within the insurance sector need to be improved/refined
  - Preparers should not be able to defer IFRS 9 after 2020. Some strongly emphasised that the deferral approach should be temporary and available only for a short period of time
- Some users urged the Board to complete the Insurance Contracts project as soon as possible. The current lack of transparency and comparability of insurance contract liabilities is a competitive disadvantage for the industry

Feedback from users of financial statements

IASB discussion

- The expected loss model (ELM) will provide useful information, and investors agreed that the benefits would exceed the costs
- Most insurers have a credit function, therefore the required information should be available to calculate impairment under the ELM
- Differing views about the extent to which it would be necessary to maintain two systems to produce both IAS 39 and IFRS 9 information.

Project direction and plan

IASB discussion

- Several members of the IASB continued to display lack of support for the deferral approach, but the large number of respondents in favour of it was duly acknowledged
- Potential for accounting mismatches to arise appeared to be more important than the cost considerations
- The costs to introduce the overlay approach were not deemed to be prohibitive and the choice of assets designated would be subjective
- The deferral approach would solve the accounting mismatch and cost issues, but should only be available in limited circumstances, which would be facilitated by rejecting the proposals for a waterfall application of the qualifying condition
- Expected credit losses information would not be obtained with that approach, therefore disclosures would need to be considered further

Project direction and plan

IASB discussion (continued)

- Having consistent accounting policies was a compelling reason not to move to a waterfall application of the deferral approach with a mix of IAS 39 and IFRS 9 accounting and lack of transparency
- The two extenuating circumstances to accept the deferral approach are that staying with IAS 39 was simpler, and there would be no change to existing accounting for a limited period
- These benefits would be reduced if there was a waterfall application of the deferral approach. This would add cost and complexity for users
- Added complexity would also arise if financial assets were transferred within a reporting entity where different accounting policies applied
- Preparers should be encouraged to adopt IFRS 9 before the expiry date

Project direction and plan

Questions to the Board

1. *Provide a temporary exemption from applying IFRS 9 for qualifying entities*

   Board approved Staff recommendation with 11 members voting for and 3 against

2. *The eligibility for the temporary exemption should be determined at the reporting entity level only*

   Board approved Staff recommendation with 13 members voting for and 1 against

3. *There should be a fixed expiry date for the temporary exemption*

   Board approved Staff recommendation with 13 members voting for and 1 against

4. *Provide an overlay approach*

   Board approved Staff recommendation with 13 members voting for and 1 against

5. *The temporary exemption from applying IFRS 9 and the overlay approach should be optional*

   Board unanimously approved Staff recommendation

Project direction and plan

Comparison of Board decisions with Deloitte response letter

Issue	Deloitte response letter
Temporary exemption (deferral approach) and overlay approach	The deferral approach is likely to prove a more effective solution than the overlay approach. However it should be allowed at "below reporting entity level". We do not support the "all or nothing" approach in the ED. The overlay approach should be retained only if constituents demand it. With an improved deferral approach it may prove redundant.
Eligibility at reporting entity level only	Application of the predominance test be permitted either at reporting entity level or a lower level to capture more predominantly insurance activities and draw a more precise boundary around financial assets related to insurance activities
Fixed expiry date	Agree with proposed expiry date for the reasons stated in the Basis of Conclusions Strongly recommend that the IASB concludes on its deliberations on the new insurance contracts Standard so that the effective date is within the timeline set by the deferral approach
Exemption optional	Agree that the temporary exemption should be optional

Project direction and plan

Project Plan

Main topics	Issues to be considered
Temporary exemption	• Amendments to the qualifying criterion • Disclosures required • Timing of the assessment to qualify for deferral • Whether the entity should reassess its qualifying condition • Whether the entity can stop applying the temporary exemption before the fixed expiry date
Overlay approach	• Clarify designation basis for the approach • Presentation in the SOCI • Disclosures required • The circumstances when the entity is required or permitted to cease applying the overlay approach on a by-asset basis • Whether the entity can stop applying the overlay approach before applying the new insurance contracts Standard

Project direction and plan

Project Plan (continued)

Main topics	Issues to be considered
Other issues	• The fixed expiry date for the temporary exemption and whether it should apply to the overlay approach • Whether specified first-time adopters of IFRS would be permitted to apply the overlay approach and/or temporary exemption • Whether an exemption should be provided from requiring the entity’s financial statements to be prepared using uniform accounting policies on application of the equity method when accounting for investments in associates and joint ventures
Due process and permission to ballot	• Whether the due process steps have been completed • Permission to begin the balloting process for the amendments to IFRS 4 • Whether any Board member intends to dissent at that stage

Next steps

Balloting process and possible need for future IASB discussion

- The remaining technical issues will be discussed in April and May
- If the decisions on these issues are completed by the May meeting, the Staff believes the Board will be in a position to issue final amendments to IFRS 4 in September 2016
- This work will take place in parallel with the balloting of the new IFRS for insurance contracts
- It is plausible that the Board will consider its choice on the mandatory effective date of the new IFRS for insurance contract as they finalise their choice on the expiry date for the deferral approach

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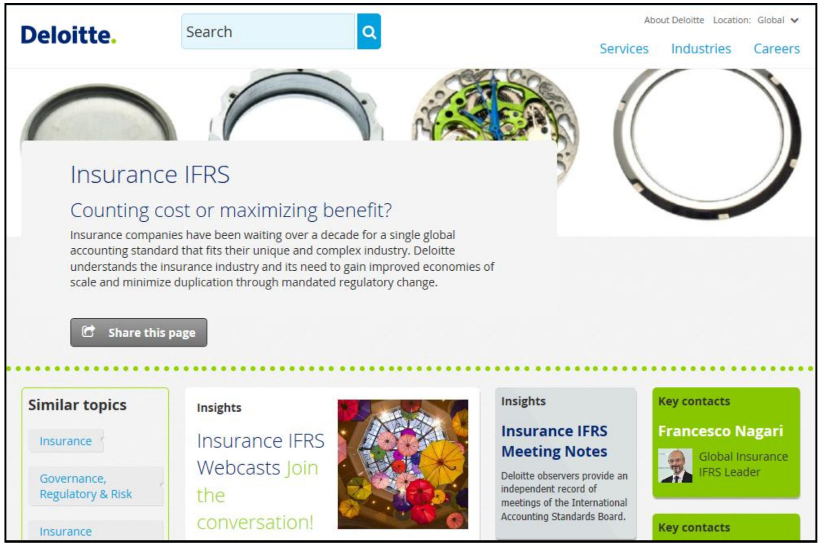

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