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Submitted electronically

23 September 2019

Dear Board Members,

Exposure Draft ED/2019/4 *Amendments to IFRS 17*

I am writing on behalf of the UK Financial Reporting Council (FRC) to comment on the Exposure Draft ED/2019/4 *Amendments to IFRS 17* (ED).

Significant progress towards the implementation of IFRS 17 has been made since the standard's publication. Concerns around the use of the standard are not unexpected given the complexities of insurance accounting and the divergence between existing accounting practices around the world. We welcome these proposals to address some of the most pressing issues that were raised around the implementation of IFRS 17. We appreciate the IASB's efforts and flexibility to consider the concerns promptly and develop innovative solutions.

During our outreach we heard about other implementation problems. We reflected on these points and concluded that some would merit consideration by the IASB. We expand on these points at the end of the appendix to this letter.

A particular challenge is resolving the concerns over the annual cohort requirements, where we have not seen an alternative proposal that stakeholders agree on. If a change was to include an exemption from the use of annual cohorts for some contracts, a clear and robust boundary would need to be drawn for the application of the exemption. We are concerned about the time it may take to find a solution. Even if the IASB were to agree to postpone the effective date of IFRS 17 beyond 2022, we believe in order to address the uncertainty over timely endorsement of the standard in Europe, any amendments still need to be finalised by mid-2020.

We concur with the majority of the proposals in this ED. Where we believe a proposed solution could be improved, we have suggested alternatives. We wish to highlight our concerns with the IASB's proposal that addresses accounting mismatches between reinsurance contracts held and onerous underlying insurance contracts. We recommend an alternative approach that in our view would better reflect the economics of the transactions and is better aligned with gain and loss recognition principles in IFRS.

Our detailed responses to the questions and an explanation of the other issues that have been raised by our constituents are included in the Appendix to this letter.

If you would like to discuss these comments, please contact me or Susanne Pust Shah (s.pustshah@frc.org.uk) on 020 7492 2495.

Yours sincerely

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Appendix: Questions

Question 1—Scope exclusions—credit card contracts and loan contracts that meet the definition of an insurance contract (paragraphs 7(h), 8A, Appendix D and BC9–BC30)
(a) Paragraph 7(h) proposes that an entity would be required to exclude from the scope of IFRS 17 credit card contracts that meet the definition of an insurance contract if, and only if, the entity does not reflect an assessment of the insurance risk associated with an individual customer in setting the price of the contract with that customer. Do you agree with the proposed amendment? Why or why not? (b) If not excluded from the scope of IFRS 17 by paragraphs 7(a)–(h), paragraph 8A proposes that an entity would choose to apply IFRS 17 or IFRS 9 to contracts that meet the definition of an insurance contract but limit the compensation for insured events to the amount required to settle the policyholder's obligation created by the contract (for example, loans with death waivers). The entity would be required to make that choice for each portfolio of insurance contracts, and the choice for each portfolio would be irrevocable. Do you agree with the proposed amendment? Why or why not?

A1 We agree with the proposal in (a). It adequately addresses the concerns raised by stakeholders about credit card products with insurance components and the proposed accounting provides relevant information. We have heard calls that the exemption should be widened to other banking products that meet the definition of an insurance contract. We do not oppose the widening of the scope exemption to other banking products, provided the insurance risk associated with an individual customer is not reflected in the price of the insurance contract.

A2 We agree with the scope of the exemption in proposal (b), except that we believe a better solution would be to require the use of IFRS 9, instead of providing an option to apply IFRS 9 or IFRS 17. The use of the same accounting requirements for the same type of contracts supports consistency and comparability between entities and mandating the use of one standard is preferable. The contracts in scope of the exemption are financial assets and the accounting under IFRS 9 is well understood. The application of IFRS 17, however, is not as clear and the resulting information could be less useful. It seems reasonable to assume that IFRS 9 will be the preferred accounting standard by banks and many insurers for these financial assets.

A3 In addition to our suggestion to mandate the use of IFRS 9, we propose a drafting change to paragraph 8A of IFRS 17, to clarify that the contracts in scope of the exemption need to be financial instruments.

"~~Some contracts~~ Those financial instruments that meet the definition of an insurance contract but …"

A4 We concur with the proposed changes to the IFRS 9 transitional requirements for those entities that already apply IFRS 9.

Question 2—Expected recovery of insurance acquisition cash flows (paragraphs 28A–28D, 105A–105C, B35A–B35C and BC31–BC49)
Paragraphs 28A–28D and B35A–B35C propose that an entity: (a) allocate, on a systematic and rational basis, insurance acquisition cash flows that are directly attributable to a group of insurance contracts to that group and to any groups that include contracts that are expected to arise from renewals of the contracts in that group; (b) recognise as an asset insurance acquisition cash flows paid before the group of insurance contracts to which they are allocated is recognised; and (c) assess the recoverability of an asset for insurance acquisition cash flows if facts and circumstances indicate the asset may be impaired. Paragraphs 105A–105C propose disclosures about such assets. Do you agree with the proposed amendments? Why or why not?

A5 We agree with the proposals in (a), (b), and (c), although we note that the proposal increases complexity for preparers and arguably for users. However, we believe the additional complexity is justified because a deferral better reflects the economic substance of the transactions and hence provides more relevant information.

A6 We concur that a deferral should not be dependent on whether up-front commissions make the initial contracts onerous or not. In respect of the proposed impairment requirements, we note that they are inconsistent with the accounting for expected cash flows under IFRS 17. Changes in expectations about the recoverability of the deferred contract acquisition cash flows would usually affect the contractual service margin of those groups that the costs are directly attributable to. Nevertheless, we acknowledge the complexity of such a solution and therefore agree with the proposed impairment accounting model.

A7 We believe the proposed disclosures are appropriate. We note the flexibility around determination of appropriate time-bands for the disclosure of the expected derecognition of unallocated insurance acquisition cash flows. This disclosure will be useful if there is some consistency in presentation between entities to allow comparison. We believe the IASB should assess the disclosure requirement and its effectiveness as part of the IFRS 17 post-implementation review.

Question 3—Contractual service margin attributable to investment-return service and investment-related service (paragraphs 44–45, 109 and 117(c)(v), Appendix A, paragraphs B119–B119B and BC50–BC66)

(a) Paragraphs 44, B119–B119A and the definitions in Appendix A propose that an entity identify coverage units for insurance contracts without direct participation features considering the quantity of benefits and expected period of investment-return service, if any, in addition to insurance coverage. Paragraph B119B specifies criteria for when contracts may provide an investment-return service.

Do you agree with the proposed amendment? Why or why not?

(b) Paragraphs 45, B119–B119A and the definitions in Appendix A clarify that an entity is required to identify coverage units for insurance contracts with direct participation features considering the quantity of benefits and expected period of both insurance coverage and investment-related service.

Do you agree with the proposed amendment? Why or why not?

(c) Paragraph 109 proposes that an entity disclose quantitative information about when the entity expects to recognise in profit or loss the contractual service margin remaining at the end of a reporting period. Paragraph 117(c)(v) proposes an entity disclose the approach used to determine the relative weighting of the benefits provided by insurance coverage and investment-return service or investment-related service.

Do you agree with the proposed disclosure requirements? Why or why not?

A9 In respect of proposal (a), we concur that insurance contracts without direct participation features may provide insurance as well as investment return services. An allocation of the contractual service margin to both of these services will provide more relevant information, especially when the timing of insurance services and investment return services differ.

A10 Constituents from the insurance industry have suggested that the proposed conditions in B119B are too restrictive. They believe that any contract which is expected to provide a positive investment return to the policyholder should be included, regardless of whether this benefit can be accessed when the policy is surrendered or when the policyholder makes a claim.

A11 We agree with the IASB that the policyholder needs to have a right to the investment returns. We have heard the argument that a right to the investment returns may also exist if expected investment returns are priced into the contract. For example, in a deferred annuity contract positive expected returns from the investments may be shared with the policyholder through an enhanced annuity payout, which is reflected in the pricing of the contract at inception. We are not convinced that a pricing decision demonstrates a policyholder's right to the expected returns and a condition solely based on the notion of providing positive investment returns to policyholders does not seem a robust enough condition. The IASB's proposal that a withdrawal right and/or investment component must be present, provides a clear test for demonstrating the policyholder has a right to the returns. If the conditions were to be changed an alternative test that demonstrates the right of the policyholders would need to be found.

A12 Although we agree with the proposed conditions in B119B, we would welcome clarity around how the conditions should be applied. As drafted, meeting the conditions is necessary, but not sufficient to demonstrate that an investment return service exists. It is not clear to us what additional criteria would need to be assessed to conclude that an investment return service exists or does not exist. In our view the conditions are both necessary and sufficient. We therefore would suggest the requirement is redrafted as follows:

Insurance contracts without direct participation features ~~may~~ provide an investment-return service if, and only if: …

A13 We acknowledge that all insurance contracts without direct participation features would need to be assessed whether they contain an investment return service or not. This could have an effect on ongoing implementation and could increase cost and complexity. However, we do not believe it would be appropriate to provide an option, because it would unduly reduce consistency and comparability.

A14 We concur with proposal (b) and the IASB's clarification in respect of investment related services in contracts with direct participation features.

A15 We agree with the additional disclosures proposed in (c) because significant judgement is needed to determine the relative weighting of the benefits provided. We note that the IASB is also proposing to remove the choice for entities to qualitatively explain when the remaining contractual service margin will be recognised in the future. We are not aware users have called for this amendment and are not convinced it is necessary as part of this proposal. This disclosure requirement could be reassessed as part of the post-implementation review of IFRS 17.

Question 4—Reinsurance contracts held—recovery of losses on underlying insurance contracts (paragraphs 62, 66A–66B, B119C–B119F and BC67–BC90)

Paragraph 66A proposes that an entity adjust the contractual service margin of a group of reinsurance contracts held that provides proportionate coverage, and as a result recognise income, when the entity recognises a loss on initial recognition of an onerous group of underlying insurance contracts, or on addition of onerous contracts to that group. The amount of the adjustment and resulting income is determined by multiplying:

(a) the loss recognised on the group of underlying insurance contracts; and
(b) the fixed percentage of claims on the group of underlying contracts the entity has a right to recover from the group of reinsurance contracts held.

Do you agree with the proposed amendment? Why or why not?

A16 Insurance contracts and reinsurance contracts are related, but give rise to different rights and obligations. We therefore agree that despite that link between underlying insurance contracts and reinsurance contracts, they should be accounted for separately under IFRS 17. The separation of the two contracts is consistent with the accounting requirements for other non-insurance contracts.

A17 We agree that a solution which would remove the timing asymmetry between loss recognition on underlying insurance contracts and the recognition of a gain on a reinsurance contract, could provide more relevant information. However, we have reservations regarding the proposal.

A18 The proposal limits the off-set to reinsurance contracts that provide coverage for claims on a fixed percentage basis. These “plain vanilla” reinsurance arrangements appear to be rare in practice.Other forms of reinsurance are more prevalent and actively used by insurers to manage their risks. Since the scope is so narrow, the proposed exemption may be of very limited use in practice.

A19 We note the proposal disregards whether the reinsurance contract has a net gain or a net cost contractual service margin. However, we believe this is relevant for the assessment. A reinsurance contract with a net gain contractual service margin would reduce the overall loss on the insurance and reinsurance contract if added together. A reinsurance contract with a net cost contractual service margin would increase that overall loss, because the expected recoveries from the reinsurance are less than the net reinsurance premium paid. We believe recognising income on a reinsurance contract with a net cost contractual service margin is counterintuitive and could be misleading. It also offers the incentive to buy reinsurance to off-set a loss, with the cost of the reinsurance being deferred into the future.

A20 A formula that determines the income off-set amount by multiplying a claim recovery percentage with the loss on the onerous contracts disregards that other expenses or the risk adjustment could contribute to a loss on the group of underlying insurance contracts, although they are not recoverable from reinsurance. We therefore have reservations against the assumption underlying this proposal that all losses arise from claims (BC79 of the ED).

A21 We believe a better solution would be to limit the loss off-set to the lower of the loss on the underlying group of insurance contracts and any net gain on the reinsurance. We are also of the view that conceptually loss off-set should not be limited to reinsurance that operates on a proportional basis. However, we acknowledge the difficulties in developing a methodology or principle for all types of reinsurance arrangements that would avoid arbitrary allocation of reinsurance net gains or net costs to groups of underlying insurance contracts. Therefore, any solution would need to be limited to reinsurance arrangements where it is possible to match expected losses from claims on underlying insurance contracts with reinsurance recoveries and the net reinsurance premium paid. We understand that this would be possible for reinsurance arrangements that specify a recovery percentage for each contract in a group and insurance premiums are ceded on a proportional basis.

A22 We believe the IASB should explore alternative solutions that would provide wider practical relief, but also avoids the possible adverse consequences of the current proposal. However, we recognise that there is a limited time to develop a solution and there will inevitably be a trade-off between complexity and the relevance of any solution. Within these constraints we urge the IASB to find a solution.

A23 We note that any solution may not be consistent with the existing exception in paragraph 66(c)(ii) of IFRS 17. We believe it would be preferable to have the same requirements for onerous contracts at inception and those that become onerous subsequently. However, bringing in new restrictions to paragraph 66(c)(ii), would disrupt ongoing implementation and we therefore do not recommend alignment. Nevertheless, this should be an area of review during the post-implementation review of IFRS 17.

Question 5—Presentation in the statement of financial position (paragraphs 78–79, 99, 132 and BC91–BC100)
The proposed amendment to paragraph 78 would require an entity to present separately in the statement of financial position the carrying amount of portfolios of insurance contracts issued that are assets and those that are liabilities. Applying the existing requirements, an entity would present the carrying amount of groups of insurance contracts issued that are assets and those that are liabilities. The amendment would also apply to portfolios of reinsurance contracts held that are assets and those that are liabilities. Do you agree with the proposed amendment? Why or why not?

A24 We acknowledge the concerns the IASB seeks to address and agree with the proposed amendment, even though it is a departure from the unit of account in IFRS 17. Provided there is no need for a more granular allocation of cash flows for measurement purposes, allocation of cash flows at a portfolio level will provide relevant information.

Question 6—Applicability of the risk mitigation option (paragraphs B116 and BC101–BC109)
The proposed amendment to paragraph B116 would extend the risk mitigation option available when an entity uses derivatives to mitigate financial risk arising from insurance contracts with direct participation features. That option would apply in circumstances when an entity uses reinsurance contracts held to mitigate financial risk arising from insurance contracts with direct participation features. Do you agree with the proposed amendment? Why or why not?

A25 We concur with the IASB's proposal to include reinsurance contracts in the risk mitigation option.

A26 The IASB rejected the inclusion of financial instruments, other than derivatives, in the risk mitigation option. We believe the IASB could explore whether financial instruments measured at fair value through profit or loss could be included. The same accounting mismatch identified for derivatives arises for financial instruments measured at fair value through profit or loss.

A27 We also note the IASB's empirical view that reinsurance contracts held or issued cannot be contracts with participation features. However, it should be further explored whether such reinsurance contracts do in fact exist, as asserted by some stakeholders. We do not believe there is a conceptual argument against the inclusion of reinsurance contracts in the variable fee approach, if they meet the conditions of contracts with direct participation features.

Question 7—Effective date of IFRS 17 and the IFRS 9 temporary exemption in IFRS 4 (paragraphs C1, [Draft] Amendments to IFRS 4 and BC110–BC118)
IFRS 17 is effective for annual reporting periods beginning on or after 1 January 2021. The amendments proposed in this Exposure Draft are such that they should not unduly disrupt implementation already under way or risk undue delays in the effective date. (a) The proposed amendment to paragraph C1 would defer the effective date of IFRS 17 by one year from annual reporting periods beginning on or after 1 January 2021 to annual reporting periods beginning on or after 1 January 2022. Do you agree with the proposed amendment? Why or why not? (b) The proposed amendment to paragraph 20A of IFRS 4 would extend the temporary exemption from IFRS 9 by one year so that an entity applying the exemption would be required to apply IFRS 9 for annual reporting periods beginning on or after 1 January 2022. Do you agree with the proposed amendment? Why or why not?

A28 The implementation of IFRS 17 is a complex process and requires extensive resources. We therefore welcome the IASB's proposal to extend the effective date and allow more time for the implementation of IFRS 17, including these proposed amendments to the standard. Despite the practical challenges, we believe that there is an urgent need to replace IFRS 4 and the introduction of improved insurance accounting requirements should not be unnecessarily delayed.

A29 We have heard that an extension beyond one year would result in additional implementation costs for some insurers, whilst other insurers call for a deferral beyond 2022. These constituents are particularly concerned that the European endorsement process may not be completed in time for the adoption of the standard from 2022. For them the costliest outcome would be preparation for an adoption in 2022, if the effective date in the EU is later pushed back to 2023. Although this is largely an issue for entities subject to EU accounting legislation, it could also affect entities in other jurisdictions as they may prefer to adopt IFRS 17 at the same time as Europe.

A30 We believe all the views expressed by constituents regarding the deferral of IFRS 17 have merit. Nevertheless late European endorsement of IFRS 17 would be unhelpful for all constituents and that risk should be taken into consideration by the IASB in setting a revised effective date.

A31 We concur with the IASB that it is preferable for IFRS 9 and IFRS 17 to be adopted together. We therefore agree with the proposed extension of the IFRS 9 deferral in IFRS 4. However, we share concerns about a further delay to the adoption of IFRS 9 beyond 2022. Even if the IASB would decide to delay the effective date of IFRS 17 to 2023 or later, IFRS 9 should not be adopted later than 2022.

A32 We agree with the IASB that the option to adopt IFRS 9 without providing comparatives is not a reason for a similar exemption in IFRS 17. Accounting mismatches can be avoided by applying IFRS 9 in the comparative period. We believe a better solution would be to mandate the use of IFRS 9 in the comparative period, if the IASB could introduce such a change without delaying the finalisation of these amendments. We believe application of IFRS 9 in the comparative period would enhance comparability between insurers and non-insurers who already apply IFRS 9. Some changes would be needed to the transitional requirements of IFRS 9. For example, the relief from applying IFRS 9 to items that have been derecognised at the date of initial application instead to those de-recognised at the date of transition.

A33 We would request the IASB to finalise sooner than mid-2020 the proposals to defer the effective date of IFRS 17 and IFRS 9 for insurers. Earlier release of these amendments would provide greater certainty for implementation and should enable timely endorsement of the necessary amendments to IFRS 4 in the European Union.

Question 8—Transition modifications and reliefs (paragraphs C3(b), C5A, C9A, C22A and BC119–BC146)

(a) Paragraph C9A proposes an additional modification in the modified retrospective approach. The modification would require an entity, to the extent permitted by paragraph C8, to classify as a liability for incurred claims a liability for settlement of claims incurred before an insurance contract was acquired. Paragraph C22A proposes that an entity applying the fair value approach could choose to classify such a liability as a liability for incurred claims.

Do you agree with the proposed amendments? Why or why not?

(b) The proposed amendment to paragraph C3(b) would permit an entity to apply the option in paragraph B115 prospectively from the transition date, rather than the date of initial application. The amendment proposes that to apply the option in paragraph B115 prospectively on or after the transition date, an entity would be required to designate risk mitigation relationships at or before the date it applies the option.

Do you agree with the proposed amendment? Why or why not?

(c) Paragraph C5A proposes that an entity that can apply IFRS 17 retrospectively to a group of insurance contracts be permitted to instead apply the fair value approach to that group if it meets specified criteria relating to risk mitigation.

Do you agree with the proposed amendment? Why or why not?

A34 We agree with the proposal in (a). We believe this simplification should ease implementation challenges and should not result in a significant loss of useful information.

A35 The IASB rejected suggestions that the risk mitigation option should be applied retrospectively. We carefully considered the arguments for and against retrospective application and reflected on possible solutions around mandating retrospective application to limit the ability to “cherry pick”. We concluded that on balance optional retrospective application is our preferred approach.

A36 The use of the risk mitigation option under paragraph B116 of IFRS 17 is subject to some, but very limited conditions. The ability to stop and re-start the use of the risk mitigation option without many constrains means that mandating retrospective application would have virtually no effect. We further considered whether there should be restrictions to the amounts that can be off-set on retrospective application. We concluded that it would not be feasible to introduce restrictions for retrospective application beyond those in paragraph B116 of IFRS 17.

A37 We accept that there is a risk of “cherry picking”, but although it is a concern, we are less convinced that it would be the dominating consideration for entities when choosing the risk mitigation option. Disclosures around the use of the risk mitigation option and its effect on the contractual service margin, could give an indication of how profitability could be affected in the future. We therefore give greater weight to the argument that retrospective application would provide more relevant information because it makes pre- and post-transition reporting of the contractual service margin more consistent and comparable.

A38 If the IASB would develop a solution that allows for retrospective application of the risk mitigation option, the proposals in (b) and (c) would be redundant. Should the IASB retain its view that retrospective application should not be permitted, we concur that the proposals in (b) and (c) may limit the accounting mismatches and would be supportive.

A39 We concur with the IASB that the use of the modifications in the modified retrospective approach should be subject to reasonable and supportable information. Removal of this requirements could impair the reliability of the information. We belief BC143 of the ED is helpful, as it reaffirms our understanding of the application of IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*. In addition, we suggest a simple change to paragraphs C6 and C8 of IFRS 17 to clarify “reasonable and supportable information <u>and estimates</u>” should be used.

A40 We also note the Board’s explanations in BC144 of the ED regarding the requirements in paragraph C12 of IFRS 17. The Board confirms that estimates are expected to be used as proxies for known cash flows. If this is the Board’s intention, we believe it should be made clear in paragraph C12 and the word “known” deleted.

Question 9—Minor amendments (BC147–BC163)
This Exposure Draft also proposes minor amendments (see paragraphs BC147–BC163 of the Basis for Conclusions). Do you agree with the Board’s proposals for each of the minor amendments described in this Exposure Draft? Why or why not?

A41 We have two observations regarding the minor proposed amendments.

A42 We note that the proposed amendment to the definition of “investment component” is intended to clarify the IASB’s intention that an investment component includes amounts repayable in all circumstances and therefore could include payments for an insured event. The current definition includes only amounts repayable, even if an insured event does not occur and therefore scopes out payments related to an insured event. We agree the amendment is consistent with the Board’s view expressed in paragraph BC34 of IFRS 17. However, we are concerned about the impact of the amended definition on ongoing implementation. We would ask the IASB to consider whether the expected benefit of making this amendment outweighs the cost.

A43 The IASB is proposing an amendment to paragraph B96(d) to clarify that changes to the contractual service margin resulting from changes to the risk adjustment should be measured at locked-in rates, if the entity has chosen to disaggregate changes of the risk adjustment between changes relating to non-financial risk and changes relating to the time value of money. That option exists under paragraph 81 of IFRS 17. Currently, paragraph B96(d) is silent about whether changes in the risk adjustment related to future service are recorded at current or historical discount rates in the contractual service margin.

A44 We acknowledge that the proposed amendment seeks to align the accounting for changes in the risk adjustment, with the accounting for other changes to fulfilment cash flows under paragraph B96(b) of IFRS 17. However, it also introduces an inconsistency, because depending on whether an entity disaggregates the changes in the risk adjustment or not, the corresponding changes to the contractual service margin will be recorded at current or historical discount rates. We also note that the proposal would introduce operational complexities for entities that without the amendment would not have recalculated the adjustment to the contractual service margin at historical rates. We therefore request the IASB to consider the cost/ benefit trade-off for this amendment.

Question 10—Terminology
This Exposure Draft proposes to add to Appendix A of IFRS 17 the definition ‘insurance contract services’ to be consistent with other proposed amendments in this Exposure Draft. In the light of the proposed amendments in this Exposure Draft, the Board is considering whether to make a consequential change in terminology by amending the terms in IFRS 17 to replace ‘coverage’ with ‘service’ in the terms ‘coverage units’, ‘coverage period’ and ‘liability for remaining coverage’. If that change is made, those terms would become ‘service units’, ‘service period’ and ‘liability for remaining service’, respectively, throughout IFRS 17. Would you find this change in terminology helpful? Why or why not?

A45 Constituents have different views, some are supportive of changing the terminology, whilst others are concerned about unintended consequences. These changes are not a high priority for us, because they are not essential to the understanding of IFRS 17.

Appendix: Other issues

A46 During our outreach we heard concerns regarding the implementation of IFRS 17 which are not addressed in the specific questions. We highlight the key issues below.

Annual cohorts

A47 We have been informed of practical implementation challenges of the annual cohort requirement, especially for contracts that share risk. Allocating cash flows to annual cohorts may require significant judgement and may not necessarily be representative of how the contracts are managed. In the UK with-profit policies are particularly affected.

A48 We understand the concerns and are not opposed to an alternative solution. We are informed of proposals that define the scope of an exception along the lines of paragraph B67 of IFRS 17 which would include insurance contracts with cash flows that are significantly affected by cash flows to or from contracts with other policyholders. In our view a scope definition on this basis is not sufficiently robust to set an acceptable boundary for an exception. In addition, an alternative solution would need to define alternative aggregation requirements. We do not find arguments convincing that users are only interested in the performance of the entire portfolio. The implied open portfolio approach could in our view mask important profitability trends.

A49 Considering that the debates so far have not resulted in a proposal that seems acceptable to a wider range of stakeholders, we have doubts whether the IASB will be able to develop an alternative within the timetable for these amendments. A delay could make implementation of the standard in 2022 or even 2023 unachievable.

Guaranteed annuity options

A50 Some insurance products switch from contracts with direct participation to contracts without direct participation rights and vice versa. In the specific UK example, the contracts provide participation through a with-profit type policy during the initial savings phase. At the end of the savings phase the policyholder has the option to convert the contract to a guaranteed annuity. The annuity is purchased from the annuity provider at current market rates when the option is exercised and any additional costs are borne by the fund.

A51 The annuity rate in these products is guaranteed at inception and the annuity phase would fall within the contract boundary of the with-profit policy. IFRS 17 does not permit the reassessment of the conditions for the variable fee approach after inception. Both phases of the contract are therefore either accounted for under the variable fee approach or the general model. We have heard that it would be preferable to account for the savings phase separately from the annuity phase, but IFRS 17 does not provide that flexibility.

A52 We have sympathy with the concerns raised and in this specific example, it seems a better solution to separate the savings and annuity phase and account for them as two separate contracts. However, we have not been able to identify a suitable solution that would provide sufficient flexibility and aligns with the existing contract boundary requirements in IFRS 17. We would appreciate if the IASB could assess constituents' concerns and consider possible solutions because we do not believe this is a unique issue for the UK.

Policy holder tax

A53 UK tax legislation sets out specific tax rules for income and capital gains made by insurers from assets that are held in funds to support some long-term insurance liabilities. The taxation basis is referred to as "I-E" (income minus expenses). The insurer has the right to deduct from the policyholder funds an amount that reflects the policyholders' share of the tax paid by the company under the I-E regime. Policyholders also receive a tax credit for the tax paid by the company when they receive a payout from the insurer.

A54 We have heard mixed views on the accounting for the tax under IFRS 17. IFRS 17 requires that unless income tax is paid in a fiduciary capacity, it is in scope of IAS 12 *Income Taxes* and would be excluded from fulfilment cash flows (paragraphs B65(j) and B66(f) of IFRS 17). Others believe that the share of the tax which is deducted from policyholder funds is in effect paid on behalf of policyholders and therefore is a payment that should be included in fulfilment cash flows under paragraph B65(b) of IFRS 17.

A55 We are not convinced that this issue requires standard setting by the IASB. However, we believe this is not a unique issue to the UK and would appreciate if the IASB could assess possible ways to provide clarity.

Interim reporting

A56 The IASB redeliberated on the interim reporting of paragraph B137 of IFRS 17 as part of this ED. The Board rejected proposals to expand the application of these interim reporting requirements to interim reports that are not prepared in accordance with IAS 34. We concur with that decision. However, some of our constituents from the insurance industry have called for the deletion of paragraph B137, because the requirements would increase complexity and costs. This is a particularly pertinent issue for large groups with different reporting frequencies by individual subsidiaries and the group itself. We also heard a user view, who had no preference for interim accounting under paragraph B137 or IAS 34, however the user opposed a choice.

A57 Leaving the cost and complexity issue aside, we believe both methods for interim reporting in IFRS 17 and IAS 34 have merits and neither of the methods appear superior from an accounting technical perspective. It therefore comes down to a cost/benefit analysis and the conclusion will be different for different entities and groups. We concur with the investor view that a choice would impair comparability, although we assume that large groups may tend to favour on IAS 34 basis, whilst smaller insurers may prefer the IFRS 17 basis.

A58 We would request the IASB to reassess the cost/benefit trade-off between the current solution and IAS 34, based on the new information that has come to light. However, we recognise that there is no obvious solution which aligns the conflicting views.