IFRS 17 – Important amendments in the pipeline

24 January 2019

“Overall, these proposed amendments will help reduce accounting mismatches and complexity. The proposals also mean that insurers would need to exercise judgement in new areas when applying the standard – they need to give early and careful consideration to these matters.”

Joachim Kölschbach,
KPMG’s global IFRS insurance leader

New proposals to amend the insurance contracts standard in four areas

Highlights

- Four further potential amendments to the requirements in IFRS 17
- The proposals address certain aspects of accounting for reinsurance contracts held, insurance acquisition cash flows and the recognition of the CSM in profit or loss
- Implications for insurers – Fewer accounting mismatches, new judgement areas
- Next steps – Remaining topics to be discussed early in the next few months

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The proposed amendments aim to provide better information about the economic substance of certain transactions.

Responding to the concerns and implementation challenges raised by insurers and other stakeholders, the International Accounting Standards Board (‘the Board’) has proposed several amendments to IFRS 17 *Insurance Contracts* at its first meeting in 2019.

At its January meeting, the Board has tentatively decided to make amendments covering four topics.

- Accounting for reinsurance of onerous insurance contracts.
- Accounting for direct participating contracts when reinsurance contracts held are used to mitigate financial risk.
- Accounting for insurance acquisition cash flows that relate to future contract renewals.
- Allocating the contractual service margin (CSM) in the general measurement model to investment return services.

What has the Board proposed?

Accounting for reinsurance of onerous insurance contracts

The Board proposes that if an insurer recognises losses on underlying insurance contracts assessed as onerous at initial recognition, it would also recognise a gain at the same time in profit or loss on reinsurance contracts held, to the extent that the reinsurance contracts cover the losses of the underlying contracts on a proportionate basis.

"While the proposed amendments are narrow in scope, they provide meaningful change and address concerns put forward by insurers. Although the amendments will be considered together and are subject to exposure, we recommend that insurers start to evaluate now and consider how they will respond."

Mary Trussell,
KPMG's Global Lead, Insurance Accounting Change

Accounting for direct participating contracts when reinsurance contracts held are used to mitigate financial risk

The Board proposes allowing insurers to reduce accounting mismatches by expanding the risk mitigation exception in IFRS 17 for direct participating contracts so that it may be applied when an insurer uses reinsurance contracts held to mitigate financial risks. Currently, the risk mitigation exception is available only when an entity uses derivatives for this purpose.

Accounting for insurance acquisition cash flows that relate to future contract renewals

The Board proposes amending IFRS 17 so that insurers would allocate part of the insurance acquisition cash flows directly attributable to newly issued contracts – e.g. initial commissions paid – to expected contract renewals that are outside the contract boundary.

Allocating the contractual service margin in the general measurement model to investment return services

The Board proposes that the contractual service margin of certain contracts without direct participation features should be allocated based on coverage units that are determined by considering both insurance coverage and a newly defined investment return service.

What are the implications?

These proposals are in line with the Board's **criteria** for proposed amendments to IFRS 17 and, in general, aim to reduce accounting mismatches and improve the alignment of insurers' profits with their economic substance. Better alignment of profit recognition with the economic substance of transactions should deliver a better performance reporting experience for users of financial statements.

If the proposed amendments are approved, insurers will need to make new decisions and apply new judgements to address them in their implementation process. Although the amendments will be considered together and are subject to exposure, we recommend that insurers start to evaluate them now and consider how they will respond.

Next steps

These proposed amendments complement the Board's tentative decisions:

- to **defer the effective date** of IFRS 17 to January 2022 together with an extension of the temporary exemption from applying IFRS 9 *Financial Instruments*, and
- to **propose an amendment** to balance sheet presentation requirements.

Any further actions will be subject to the Board's normal due process, which requires that an exposure draft be published followed by a public comment period.

The Board has now covered the majority of the 25 areas of IFRS 17 in which it decided to explore making amendments to address stakeholders' concerns and implementation challenges. The Board is expected to discuss the remaining topics in the coming months, while an exposure draft of the amendments to IFRS 17 is expected in mid-2019.

Stay tuned for our next web article, which will keep you up to date on the outcome of these important discussions.

Find out more

Check out our **Insurance – Transition to IFRS 17** page for more detail on the four amendments proposed by the Board. Visit **home.kpmg/ifrs17** to read all of our insights on the new insurance contracts standard. Also, our insights on insurers' progress with IFRS 17 and IFRS 9 implementation can be found on our **In it to win it** web page.

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