ASA | SVV

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Swiss Insurance Association

IFRS Foundation
30 Cannon Street
London EC4M 6XH
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Exposure Draft ED/2015/11

Dear Sir or Madam

The Swiss Insurance Association (SIA) would like to take the opportunity to respond to the questionnaire on the Exposure Draft ED/2015/11 "Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts". The SIA represents Swiss insurance companies including subsidiaries and branches of foreign companies in Switzerland representing 95 % of the premium volume written by insurers based in this country. The SIA comments were prepared by the Commission for Accounting and Reporting which is made up of leading finance and accounting executives from various companies including all large and listed companies.

The IFRS Framework is extremely relevant in Switzerland as the Swiss Stock Exchange requires the application of either IFRS or US GAAP from all companies listed in the main segment. In this respect, content and discussions about IFRS 4 and 9 are of utmost importance to the Swiss insurance industry.

Hereinafter you will find our detailed responses to the questions raised in the ED/2015/11.

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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?

SIA Answer to Question 1

The SIA does agree that the IASB should seek to address the concerns listed above in Questions 1 (a) through 1 (c), as they are valid for insurance entities for the following reasons:

- For insurance entities IFRS 4 Phase II and IFRS 9 are heavily interrelated. It is a fact that different effective dates for IFRS 9 and IFRS 4 cause mismatches that from an economic point of view are not justified.
- In addition it is also important to note that due to this interrelation the requirements and concepts of IFRS 4 Phase II have to be final and evaluated for the preparer to be able to properly classify in accordance with IFRS 9 the asset side of the business. If this is not done on a sound and stable basis this may result in financial information to investors that is not meaningful or may even be misleading.
- The cost argument is also valid as a staged introduction of these interrelated standards will result in substantially higher cost than an aligned implementation. Triggers for extra costs may be system and process adjustments, communication, etc.

In SIA's opinion, the deferral of IFRS 9 addresses the concerns raised about the different effective dates of IFRS 9 and IFRS 4 Phase II appropriately, provided that the scope of eligible insurers is sufficiently broad to suit the intended purpose. In addition, the IASB should align the effective dates of the IFRS 9 deferral approach and IFRS 4 Phase II.

The SIA urges the IASB to expedite the process of finalising the exposure draft. It is paramount for insurers to have clarity on the accounting and reporting requirements for 2018, as soon as possible.

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.

SIA Answer to Question 2

The SIA does agree that there should be both an overlay approach and a temporary exemption from applying IFRS 9.

Only a temporary exemption from applying IFRS 9 (deferral approach) appropriately addresses all of the concerns raised about the different effective dates of IFRS 9 and 4, as outlined in Questions 1 (a) through (c), whereas the overlay approach only responds to the mismatch topic, as specified in Question 1 (a), and that solely in the income statement, but not in the balance sheet.

The application of the overlay approach still requires a full IFRS 9 implementation at a point in time when the new insurance standard is not yet effective. In particular, the IFRS 9 classification of financial instruments will be performed devoid of IFRS 4 Phase II implications, as the final insurance standard has not been issued. Accordingly, once IFRS 4 Phase II becomes effective, any former IFRS 9 classification of financial instruments will need to be reassessed for the new insurance standard's implications, which may result in a materially different financial instruments classification from the one presented under the overlay approach. Hence, the overlay approach may not address the concerns related to a twofold implementation of IFRS 9.

In addition, when applying the overlay approach preparers need to set up and maintain parallel systems and processes for both IAS 39 and IFRS 9 financial instruments accounting in order to meet the relevant presentation and disclosure requirements. This requires a disproportionate effort in terms of time and cost against the background of only a transitional solution.

Notwithstanding the added costs and complexity of the overlay approach, the SIA acknowledges that there may be circumstances when it makes sense to opt for the overlay approach. Therefore both approaches should be available.

The deferral approach should be the preferred approach, however, the SIA reiterates its position as outlined under Question 1, that the IASB should align the effective dates of the IFRS 9 deferral approach and IFRS 4 Phase II. The overlay approach should be available as a secondary alternative only, as it does not sufficiently address concerns over twofold implementation of IFRS 9, and cost benefit concerns.

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?

SIA Answer to Question 3

Even though the overlay approach does not address all concerns raised by the insurance industry, as outlined in the SIA answer to question 2, it does partially address the accounting mismatch, with the accounting mismatch being one of the insurance industry's primary concerns. The SIA is therefore of the opinion, that the IASB should keep the overlay approach in the final amendment as an option.

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 (ie 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?

SIA Answer to Question 4

The SIA agrees with the concept of defining eligible insurers according to the predominance of insurance activities at the reporting entity level. However, the current interpretation of "predominance" appears inappropriate as it could exclude many insurance entities that are commonly regarded as "pure" insurers.

The approach to measure predominance of the insurance business, as a ratio of total liabilities, as proposed in the ED, is inappropriate to capture pure insurance entities. For example, insurers who raise debt, as opposed to raising shareholder funds, may not be considered pure insurers, although the substance of insurance activities may be the same in both types of entities. It should therefore be noted that the financing structure of an insurer is insignificant for the predominance assessment of insurance activities, and that other liabilities, such as defined benefit liabilities, negative fair values of derivatives, and insurance payables, affect the proposed threshold significantly, without impacting the substance of insurance activities.

The SIA proposes the following alternatives:

- Refraining from prescribing any calculation method in IFRS 4. In the absence of any reference to a particular formula (and ratio), predominance of insurance activities has to be assessed by each preparer individually. The SIA believes this to be both feasible and reasonable. If an entity were to conclude that it is eligible for the deferral approach it would describe and disclose this in its financial statements. This approach is consistent with principle-based accounting under IFRS. The IASB may still provide some eligibility guidance.

- If the IASB decides to retain a formula as proposed in ED IFRS 4.20C it should at least consider to lower the threshold currently set at 75% (IFRS 4 BC65) to well below 70% and / or to refine the formula to take into account, for example, different financing structures (debt vs. equity) and liabilities with no significance for a predominance assessment, such as defined benefit liabilities, deferred taxes related to insurance activities, negative fair values of derivatives and insurance payables, currently affecting the threshold significantly without impacting the predominance of insurance activities.

- Explore other criteria, or a combination of criteria to define a suitable scope that includes “pure” insurers. Such criteria could encompass income sources (e.g. comparison of premium volume in relation to total income over a certain number of years), regulated status of an entity, etc.

- Explore principle-based and qualitative criteria to avoid short-term changes in respect of meeting deferral requirements (e.g. the deferral assessment as of the financial reporting date, results in the entity having to implement IFRS 9 for the immediately following financial reporting period).

In addition, in the SIA’s opinion, the eligibility assessment should normally be performed at reporting entity level. Any assessment below the reporting entity level, might not address the concerns of pure insurers appropriately. However, financial conglomerates that are not pure insurers should be given the possibility to assess predominance below the reporting entity level, in order to determine if the insurance part of the conglomerate qualifies as pure insurer and is eligible for the deferral approach, while the other part of the conglomerate would apply IFRS 9 in full. In the SIA’s opinion, such a differentiation in assessment is more important than avoiding non-uniform accounting policies within the reporting entity, and would make financial conglomerates more comparable with both, pure insurers and other financial institutions.

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?

SIA Answer to Question 5

The SIA agrees that both approaches should be optional.

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?

SIA Answer to Question 6

The SIA does not agree with any expiry date for the temporary exemption from applying IFRS 9. In the SIA's understanding, this temporary exemption from applying IFRS 9 was introduced to address concerns raised, related to the different effective dates of the new insurance standard (IFRS 4 Phase II) and IFRS 9. If the IASB wishes to address these concerns, it should allow preparers to implement both standards at the same time, and align the effective date of the new insurance standard with the expiry date of the temporary exemption from applying IFRS 9. Such an alignment of effective dates should be described as the expiry date being dependent on the effective date of the new insurance standard.

Furthermore, the SIA suggests that clarification is given as to whether the disclosures proposed under IFRS 4.37A apply to interim financial statements.

Kind regards

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