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This paper provides the technical advice from EFRAG TEG to the EFRAG Board, following EFRAG TEG's public discussion. The paper does not represent the official views of EFRAG or any individual member of the EFRAG Board. This paper is made available to enable the public to follow the EFRAG's due process. Tentative decisions are reported in EFRAG Update. EFRAG positions as approved by the EFRAG Board are published as comment letters, discussion or position papers or in any other form considered appropriate in the circumstances.

Initial application of IFRS 17 and IFRS 9 – Comparative information - Cover Note

Objective

1 The objective of this session is to discuss and approve a draft final comment letter regarding the IASB ED on *Initial application of IFRS 17 and IFRS 9 – Comparative Information* (the 'Amendments').

Background and introduction

2 The IASB's ED on the topic was published on 28 July 2021 with the comment period closing on 27 September 2021. The issue of the comparatives is an urgent issue as insurers will apply the comparative information on IFRS 17 and IFRS 9 as from 2022 (and some insurers even as from 2021).

3 Many insurance entities will first apply IFRS 17 *Insurance Contracts* and IFRS 9 *Financial Instruments* for annual reporting periods beginning on or after 1 January 2023. The ED addresses concerns relating to the differences in the transition requirements between these two Standards and the resulting accounting mismatches which are expected to have a significant effect on the usefulness of the comparative information presented on initial application of IFRS 17 and IFRS 9.

4 The ED proposes a narrow-scope amendment to the IFRS 17 transition requirements for entities that first apply IFRS 17 and IFRS 9 at the same time. This proposed amendment relates to financial assets for which comparative information presented on initial application of IFRS 17 and IFRS 9 has not been restated for IFRS 9. Applying the proposed amendment, an entity would be permitted to present comparative information about such a financial asset as if the classification and measurement requirements of IFRS 9 had been applied to that financial asset.

5 EFRAG's draft comment letter was published on 5 August 2021, the comment period closed on 15 September 2021.

EFRAG's draft comment letter

6 In the Draft Comment Letter, EFRAG expresses its appreciation for the IASB's swift response and delivery of the ED. Also, EFRAG commends the IASB for addressing most of the comments raised by European constituents in this area. Overall, EFRAG agrees with the IASB proposals in the ED as they form a clear improvement over the current situation. In finalising the proposals, EFRAG recommends the IASB to align the scopes of the classification overlay and the temporary exemption from applying IFRS 9 (which is under IFRS 4 *Insurance Contracts*) due to inconsistencies in the consolidated financial statements and unnecessary operational complexity.

Comment letters received

7 Eight comment letters have been received (including one draft).

8 All respondents supported the classification overlay and provided the following main comments:

(a) All respondents agreed that the scope of the classification overlay approach should be aligned with the scope of the temporary exemption from applying IFRS 9. This for conceptual and operational reasons. One respondent noted that it was unclear whether surplus assets were in the scope;

(b) While supportive of the proposal that the IFRS 9 impairment approach is not required, respondents suggested that the wording is clarified;

(c) There was support for the IASB proposal not to require extensive disclosures. However, there were concerns that IFRS 7 disclosures[1] would be required at both the effective date of 1 January 2023 as by the standard as well as 1 January 2022 – for users to understand the transition. The former would create operational burden with no benefit for users;

(d) The classification overlay approach should also be applicable to those insurers that do not intend or are not in a position to directly restate IFRS 9 numbers for the preceding period when applying IFRS 17 for the first time.

9 Some respondents also provided suggestions to further improve the draft comment letter. One respondent added that EFRAG should include in its endorsement advice a reference to permit the classification overlay to roll-up into conglomerate groups.

Key changes from the EFRAG draft comment letter

10 The draft final comment letter has been updated for the following:

(a) Expanding the reasoning for aligning the classification overlay and the temporary exemption from applying IFRS 9;

(b) Adding a request for clarification on the application of the classification overlay pre-dating the publication of the ED or the final amendment;

(c) Indicating the concern from our constituents relating to entities having to prepare double transition disclosures: for 1 January 2022 for information purposes and for 1 January 2023 as required;

(d) Suggesting clarification on the wording relating to the impairment requirements - "are permitted but not required to apply"; would be available on an instrument-by-instrument basis; and that IAS 39 impairment requirements would apply in the absence of the IFRS 9 requirements;

(e) Removal of paragraphs 20 and 21 of the draft comment letter about concerns on the comparative period opening balance sheet; and

(f) Welcoming the proposal not to add detailed disclosure requirements. Also, suggesting that the IASB considers the need of users to understand potential material differences between 31 December 2022 (application of classification overlay) and 1 January 2023 (first time application of IFRS 9).

EFRAG TEG discussion and advice to the EFRAG Board

EFRAG TEG discussion

11 At its meeting on 28 September 2021, EFRAG TEG reviewed the feedback received in response to EFRAG's draft comment letter and considered the final comment letter to be recommended to the EFRAG Board.

12 EFRAG TEG also considered three issues that were raised by individual EFRAG TEG members prior to the publication of EFRAG's draft comment letter. The issues were:

(a) *Comparing the temporary exemption to the classification overlay*:

[1] The additional information as required by paragraphs 42I, 42L and 42M.

(i) *The issue* - The temporary exemption in IFRS 4 (IASB version) applies to an entity which has activities that are predominantly connected with insurance (i.e., whether the carrying amount of liabilities is within the in scope of IFRS 4), while the overlay approach looks at whether the financial asset side is connected with insurance contracts in scope of IFRS 17. Then the question is whether it is possible to use the wording of the temporary exemption in the context of the classification overlay since it would lack any reference to eligibility of financial assets.

(ii) *EFRAG TEG discussion* - All respondents from the comment letters received agreed with the scope alignment and EFRAG TEG agreed that the reasoning for requesting an alignment should be expanded.

(b) *The use of hindsight*:

(i) *The issue* - The ED does not address the use of hindsight in the proposed amendment, except in the Basis for Conclusions (BC21 and BC26), even though entities may elect to show 2 years of comparatives (i.e., 2021 and 2022) and the amendment will not be finalised until late 2021. A suggestion was made to include in the comment letter:

- Stating that the classification overlay may be applied from a date that pre-dates the publication of the ED or the final amendment; and
- To include a requirement to disclose how the entity have applied the optional overlay without the use of hindsight.

(ii) *EFRAG TEG discussion* - EFRAG TEG members were in agreement to include point (i) above and most of the EFRAG TEG members did not consider that there was an issue regarding the use of hindsight, therefore, point (ii) was not included in the comment letter (EFRAG IAWG agreed with this as well). One EFRAG TEG member indicated that standard-setting was required in order to avoid the use of hindsight.

(c) *Duplication of transition disclosures*:

(i) *The issue* – Insurers consider it essential to provide the IFRS 9 transition disclosures in IFRS 7 paragraphs 42I,42L and 42M at 1 January 2022. However, the requirement is to provide these disclosures at the effective date of 1 January 2023.

(ii) *EFRAG TEG discussion* – Members agreed not to put IFRS 9 disclosures into question at this stage and agreed with the EFRAG IAWG solution to highlight this as a concern without requesting a change. However, some members considered that there was a bridging issue for users of financial statements because the transition date of IFRS 9 is 2023 but it is 2022 for IFRS 17. Therefore, they proposed that the IASB considers relevant disclosures for users to understand any material differences between the application of the overlay (end of 2022) and first-time application of IFRS 9 (beginning of 2023).

(d) EFRAG TEG members agreed with the other changes as listed in paragraph 10 above.

EFRAG TEG advice to the EFRAG Board

13 EFRAG TEG advises the EFRAG Board to approve the comment letter on the Amendments.

Questions for EFRAG Board

14 Do EFRAG Board members have comments on the draft final comment letter?

15 Do EFRAG Board members approve the draft final comment letter?

Agenda Papers

16 In addition to this cover note, the following agenda papers have been provided for the session:

(a) Agenda paper 07-02 – draft final comment letter (compared to the draft comment letter); and

(b) Agenda paper 07-03 – draft final comment letter (clean version).