Ania

Associazione Nazionale fra le Imprese Assicuratrici

2021 Edition

ANIA Exploring IFRS

Focus on IFRS 17 and IFRS 9

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Contacts:
Angelo Doni, Alessandra Diotallevi, Giorgia Esposito, Martina Bisoffi
exploringifrs@ania.it

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*In light of the forthcoming "revolution" of the accounting framework of the insurance sector, brought forward by the adoption of IFRS 17 "Insurance Contracts" principle, ANIA has decided to launch a new series of newsletter: "**ANIA Exploring IFRS**".*

The aim of "ANIA Exploring IFRS" is to provide useful insights on the International Financial Reporting Standards world, with an initial focus on IFRS 17.

The series will then continue by addressing other standards relevant for the insurance industry, such as - but not limited to - IFRS 9 "Financial Instruments" principle.

The newsletters will be issued on a regular basis, in a one-page format, and each issue will focus on specific features of the IFRS principle in question.

The newsletters will be collected in a single volume to form a practical - and easy to use - reference guide.

Angelo Doni
ANIA Co-Director General

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IFRS 17: Endorsement Process

1 MARCH, 31 2021

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Entry-into-force

The entry into force of IFRS 17 "Insurance Contracts" was originally set as of 1 January 2021.

In March 2020, however, the International Accounting Standards Board (IASB) decided to postpone the effective date to annual reporting periods beginning on - or after - 1 January 2023, with the aim of allowing sufficient time for an orderly introduction of the new principle.

In order to align the dates of implementation of IFRS 9 and IFRS 17, the IASB decided at the same time to extend the exemption in place for the application of IFRS 9 "Financial Instruments" by insurers.

In June 2020, the IASB issued the amended version of IFRS 17, containing the new effective date of 1 January 2023.

European endorsement process

In order to become applicable in the European Union, IFRS principles have to be endorsed at European level following a specific procedure, as set out in Regulation (EC) No 1606/2002 (IAS Regulation).

The endorsement process is carried out by the European Commission (EC), that avails itself of two advisory organisations: the European Financial Reporting Advisory Group (EFRAG) and the Accounting Regulatory Committee (ARC).

The process starts with EFRAG, which is required to render an opinion to the EC on the compliance of the standard with the requirements set forth by EU regulation. The three endorsement criteria to be met are: i) the standard should not be contrary to the true and fair view principle; ii) the standard should be conducive to the European public good; iii) the standard should meet the criteria of understandability, relevance, reliability, and comparability.

After EFRAG has submitted its advice, the EC prepares and presents a draft regulation to ARC, a committee composed of representatives of EU countries and chaired by the EC. The ARC subsequently gives its opinion - voting on the basis of the qualified majority rule - on the endorsement of the standard.

If the ARC's opinion is positive, the EC submits the draft regulation to the European Parliament and the Council for a three-month scrutiny period. If there are no objections from the European Parliament or the Council, the Commission adopts the endorsing regulation.

The new regulation is then published in the Official Journal of the European Union and enters into force on the day laid down in the regulation itself.

As for IFRS 17, on 29 March 2021 the EFRAG Board approved its final endorsement advice.

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exploringifrs@ania.it

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IFRS 17: Main objectives

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The new standard for insurance contracts, **IFRS 17**, aims to increase transparency and to reduce differences in the accounting for insurance contracts. If IFRS 4 allows insurers to use their local accounting standards, IFRS 17 defines rules that will increase financial statements' comparability.

The new standard will replace the current IFRS 4 and, therefore, key financial metrics and key performance indicators will change.

Premium volumes will no longer drive the 'top line' in the income statement because investment components (many insurance premiums include an investment, i.e. deposit, component) and cash received can no longer be considered as revenues.

The 'top line' will be driven by a different way to represent revenues, and consequently, the new measurement model may result in profits being released over significantly different patterns for some insurance contracts with respect to the current IFRS 4 representation.

The impact that financial risks and investment income have on an insurer's results will be presented separately from insurance performance, with the aim to provide a clearer picture of profit drivers and to give a separate presentation of underwriting and financial results.

In addition, IFRS 17 contains detailed qualitative and quantitative disclosure requirements. The objective is to disclose information that - together with information presented in the primary financial statements - provides a basis for users of the financial statements to assess the effects that insurance contracts have on the financial position, the financial performance and the cash flows of the entity.

To achieve this objective, IFRS 17 requires specific disclosures about:

- **Amounts recognized in the financial statements;**
- **Significant judgments made when applying IFRS 17**; and
- **The nature and extent of risks from insurance contracts**.

If these specific disclosures are deemed insufficient, an entity has to disclose additional information necessary to meet the objective.

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exploringifrs@ania.it

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IFRS 17: Scope

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In line with **IFRS 4**, an entity applies **IFRS 17** to contracts that meet the insurance contract's definition. IFRS 17 focuses on types of contracts, rather than types of entities. Therefore, it applies to all entities, whether they are regulated as insurance entities or not.

An insurance contract is "*a contract under which one party - the issuer - accepts 'significant insurance risk' from another party - the policyholder.*" If a *"specified uncertain future event - the insured event - adversely affects the policyholder*", then the policyholder has a right to obtain compensation from the issuer under the contract.

'*Insurance risk*' is a risk, other than financial risk, that is transferred from the policyholder to the issuer of a contract.

Insurance risk is "*significant*" only if there is a scenario that has commercial substance in which, on a present value basis, there is a possibility that an issuer could:

- suffer a loss caused by the insured event; and
- pay significant additional amounts beyond what would be paid if the insured event had not occurred.

To have commercial substance, it must have a discernible effect on the economics of the transaction.A contract is not an insurance contract if it exposes the issuer only to financial risk but not to significant insurance risk. However, contracts that expose the issuer to both financial risk and significant insurance risk could be insurance contracts.

Reinsurance contracts need to meet the definition of an insurance contract to be in the scope of IFRS 17.

Investment contracts with Discretionary Participation Features (DPF) are in the scope of IFRS 17 if they are issued by an entity that issues also insurance contracts even if they do not transfer significant insurance risk. A DPF contract is a financial instrument that provides an investor with a contractual right to receive, as a supplement to an amount not subject to the discretion of the issuer, additional amounts that are:

- expected to be a significant portion of the total contractual benefits;
- contractually paid at the discretion of the issuer (regarding timing or amount); and
- contractually based on returns from a specified pool of contracts/ assets.

Insurers are subject to the requirements of other applicable standards for products (or components of products) that are not in the scope of IFRS 17.

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ANIA, the Italian Insurance Association,
founded in 1944, is a voluntary non-profit association.
Its main purpose is to develop and spread the culture of safety
and prevention in our country, so as to protect both people
and companies, and society as a whole, more and better.

Moreover, ANIA represents its members and the Italian insurance market
vis-à-vis the main political and administrative institutions, including the
Government and Parliament,
trade unions and other social bodies.

The Association studies and cooperates in the resolution
of technical, economic, financial, administrative, fiscal, social, juridical and
legislative issues concerning the insurance industry.
It supports and provides technical assistance to members,
promotes the education and professional training of those
working in the insurance sector.

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Via di S. Nicola da Tolentino, 72 | 00187 Roma | Tel. 06.326881

www.ania.it

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