Hong Kong Institute of
Certified Public Accountants
香港會計師公會

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Sent electronically through the IASB Website (www.ifrs.org)

27 September 2021

Dr Andreas Barckow
International Accounting Standards Board
Columbus Building
7 Westferry Circus
Canary Wharf
London E14 4HD
United Kingdom

Dear Andreas,

IASB Exposure Draft ED/2021/08
Initial Application of IFRS 17 and IFRS 9 – Comparative information

The Hong Kong Institute of Certified Public Accountants (HKICPA) is the only body authorised by law to set and promulgate standards relating to financial reporting, auditing, and ethics for professional accountants, in Hong Kong. We are grateful for the opportunity to provide you with our comments on this Exposure Draft (ED).

We welcome the proposed classification overlay as it will improve the usefulness of the comparative information in question and not unnecessarily disrupt the implementation of IFRS 9 and IFRS 17.

Additionally, we have some suggestions on the ED. Firstly, regarding the scope of the proposed classification overlay, we note that the scope is limited to financial assets that are connected with insurance contracts. This differs from the scope of the temporary exemption for IFRS 9 in IFRS 4, which applies to all financial assets and liabilities. During our outreach, many stakeholders suggested that the scope of the classification overlay be extended to cover all financial assets, while a small minority strongly objected to this suggestion for the reasons as stated in the Appendix. On balance, we consider that extending the scope of the overlay would ease the operational burden of identifying in scope assets and would better align with the current exemption from IFRS 9 in IFRS 4.

Secondly, we suggest that the IASB clarify the application of the expected credit loss (ECL) model in IFRS 9 in the context of the ED. In particular, to avoid confusion, the ED should explicitly specify whether the application of the IFRS 9 ECL model is optional or prohibited and whether it applies on an instrument-by-instrument basis, on an asset class basis, or for all assets subject to the classification overlay. We also suggest that the Board clarify whether the IAS 39 incurred loss model applies to assets subject to the overlay for which the entity has elected not to apply the IFRS 9 ECL model.

Our detailed comments are provided in the Appendix. If you have any questions regarding the matters raised in this letter, please contact me (ceciliakwei@hkicpa.org.hk) or Carmen Ho (carmenho@hkicpa.org.hk), Associate Director of the Standard Setting Department.

Sincerely,

Cecilia Kwei
Director, Standard Setting Department

Work undertaken by HKICPA in forming its views

The HKICPA:

(i) issued an Invitation to Comment on ED/2021/08 on 29 July 2021 to its members and other stakeholders;

(ii) sought input from its Hong Kong Insurance Implementation Support Group and Insurance Regulatory Advisory Panel, which are mainly comprised of technical and industry experts;

(iii) developed its views through its Financial Reporting Standards Committee, having reflected on its stakeholder views. The Committee comprises academics, preparer representatives from various industry sectors, regulators, as well as technical and industry experts from small, medium and large accounting firms.

Detailed comments on IASB ED/2021/08

Question: Do you agree with the proposed amendment in this Exposure Draft? Why or why not? If not, what alternative do you propose and why?

Overall

1. We generally agree with the overall objective of the ED and support the proposed amendments. The ED offers a practical solution to improve information usefulness and eliminate accounting mismatches in the comparative period upon the initial adoption of IFRS 17 and IFRS 9. The HKICPA thinks that the proposals will ease or otherwise not negatively impact the ongoing implementation activities for the two standards, and the implementation of the proposals would:

   (a) alleviate significant accounting mismatches between insurance contract liabilities (measured at current value) and related financial assets (if measured at amortized cost) under IAS 39; and

   (b) if the entity restates comparative information for IFRS 9, help resolve classification differences between financial assets derecognized in the comparative year (to which IAS 39 will apply) and other financial assets (to which IFRS 9 will apply).

2. The HKICPA considers the proposals will help entities to present comparative information in a clear and consistent manner. The proposals will also allow for greater alignment of the resulting information presented, enabling financial statement users to better identify and assess changes and trends between periods. The HKICPA is hopeful that the implementation of these proposals will also reduce the need for supplementary information necessary to explain mismatches that would otherwise arise if entities continued to apply IAS 39 in the comparative period.

3. The HKICPA supports finalizing the ED in a timely manner. Based on the feedback gathered from our stakeholders, we do not expect the amendments to negatively affect entities' ongoing implementation activities.

4. While we generally agree with the proposals in the ED, we have some suggestions on how the proposals may be improved:

   (a) *Extend the scope to cover all financial assets rather than only those connected with insurance activities*

   The scope of the classification overlay proposed in the ED is different from the scope of the temporary exemption to IFRS 9 in IFRS 4. In particular, paragraph C28E(a) of the ED prevents an entity from applying the classification overlay to financial assets that are not connected to insurance contracts. In contrast, paragraphs 20A and 20B in IFRS 4 allow an entity to apply the temporary exemption to IFRS 9 to all financial assets and liabilities, subject to an insurance entity's activities being predominately connected to insurance.

   Many of our stakeholders recommended that the IASB further explore expanding the perimeter of the application of the classification overlay in the ED to be the same as that in the IFRS 4 temporary exemption (i.e. at a reporting entity level). These stakeholders suggested that the operational burden would be minimized if insurers do not need to separately identify out-of-scope financial assets. In addition, the proposed scope could create inconsistencies in presentation for financial assets related to insignificant banking or asset management activities at the consolidated reporting entity level of an entity with predominantly insurance activities. These stakeholders also noted that the ED's proposals are developed in the context of providing relief to entities that are applying the temporary exemption from IFRS 9 in IFRS 4, and hence it makes sense to have a scope consistent with that temporary exemption.

   However, a small minority of our stakeholders agreed with the scope of the overlay as proposed in the ED, which is to avoid accounting mismatches between only insurance contract liabilities and related financial assets. These respondents are of the view that the overlay should not be made available to, for example, an insurer with a banking business to restate comparatives for the banking business's financial assets under IFRS 9 without having to apply the IFRS 9 impairment model as the ECL model is considered to be optional for assets subject to the overlay approach based on the ED's current drafting (see below). These stakeholders also considered that it should not be operationally challenging for entities to identify in-scope assets. As noted in BC19 of the ED, entities should be familiar with identifying assets connected with insurance contracts as this is already a requirement in paragraph C29(a) of IFRS 17. Moreover, it is likely that only assets that arise under a different business model (i.e., a banking business) will be ineligible under the ED's proposals, and these should already be segregated.

   We broadly agree with many of our stakeholders and think that the IASB should further explore aligning the scope of the classification overlay in the ED to be the same as that in the IFRS 4 temporary exemption (i.e., at a reporting entity level, hence for entities whose activities are predominately connected with insurance), as we think that this may ease the operational difficulty of identifying in-scope financial assets and promote comparable and consistent presentation of all financial assets. Nevertheless, we acknowledge the concerns raised by a small majority of our stakeholders above. Therefore, we suggest that the IASB consider these when taking into account cost-benefit considerations and determining what is most useful for financial statement users.

(b) *Clarify the application of the IFRS 9 impairment model*

We welcome the proposal in the ED that entities can, but are not required to, apply the ECL requirements in IFRS 9 to financial assets subject to the overlay model given that this could disrupt implementation activities.

Nevertheless, we suggest that the ED explicitly clarify the application of the IFRS 9 impairment requirements in two respects:

(1) *Whether it is optional or prohibited*

ED paragraphs BC15, BC23, and C28C state that an entity is not or would not be required to apply the impairment requirements in IFRS 9, as entities may not be prepared to do so and it would cause a significant burden to entities. However, the requirements in ED are somewhat confusing when compared to the text in the May IASB agenda paper 2. For instance, paragraphs 23-25 of the May IASB paper explain the challenges of applying the IFRS 9 impairment model in this situation and paragraph 37 and the table in Appendix C also indicate that entities would continue to apply the incurred loss model under IAS 39 even if the classification overlay has been applied.

Given the above, we recommend that the IASB clarifies whether the IFRS 9 impairment model is optional or prohibited.

It may also be worth clarifying whether the IAS 39 incurred loss model must be applied to assets subject to the overlay approach if the IFRS 9 ECL model is indeed optional under this approach. This will have an impact to interim financial statements (as the assets subject to the overlay approach will have been derecognised at the date of initial application of IFRS 17). For example, if a debt instrument measured at FVTPL under IAS 39 would be classified as FVTOCI under IFRS 9 in terms of the overlay approach, is the entity required to determine impairment loss for the debt instrument in the comparative period? Bearing in mind that such an assessment would have no impact on the date of initial application of IFRS 9/17, we would suggest the Board consider the cost-benefits of such an application.

(2) *Whether it is on an instrument-by-instrument basis or entity-level accounting policy choice*

We noted that it is currently unclear as to whether the application of the IFRS 9 impairment test would be applied on an instrument-by-instrument basis or whether it is an entity-wide accounting policy choice. Some of our stakeholders suggested that the ECL model be applied as an entity-wide accounting policy choice to ensure consistency. Others suggested an instrument-by-instrument election as an entity-wide policy choice might discourage entities from applying the ECL requirements at all due to complexity in applying the ECL model to some assets subject to the overlay when ECL information is readily available for the majority of the other assets subject to the overlay.

Other suggestions from stakeholders

5. Some of our stakeholders raised other suggestions on the ED. We have included these suggestions below.

   (a) Providing additional disclosures

   (1) Disclose whether IFRS 9 impairment requirements have been applied

   These stakeholders considered that application of IFRS 9 impairment is optional under the ED. Accordingly, these stakeholders suggest disclosures to help users of financial statements understand whether entities have selected this option and, if the option is on an instrument-by-instrument basis, to which assets it has been applied.

   (2) Disclose to which financial assets the classification overlay has been applied

   Some stakeholders believe that this would make the comparative period's information more understandable.

   However, we also note that a primary feature of the ED is that it is designed not to disrupt implementation, and some stakeholders stated that additional disclosures could disincentivize the use of the proposals, which could reduce their value. Hence, we suggest the IASB take due care in considering whether to add additional disclosure requirements.

   (b) Extending the scope of the classification overlay to entities that have adopted IFRS 9

   The proposals in the ED are not applicable to entities that have already applied IFRS 9 before the initial application of IFRS 17. A couple of stakeholders who are currently applying IFRS 9 considered that accounting mismatches may arise from assets derecognised during the comparative period in their case. This is because while IFRS 17 provides an option to redesignate financial assets on initial application (IFRS 17 paragraphs C29-C33) that option refers to IFRS 9's transition requirements with regard to the restatement of prior period information, and as a result, cannot be applied to financial assets derecognised during the comparative period. These entities noted that such mismatches would primarily relate to financial assets currently measured at amortised cost under IFRS 9 but which are expected to move to a fair value measurement, or to equity instruments currently measured at fair value through other comprehensive income which are expected to move to fair value through profit or loss measurement.

   The HKICPA acknowledges the stakeholders' concerns above; however, we note again that the proposals in the ED are narrow in scope and specifically designed around issues that arise when entities first apply IFRS 17 and IFRS 9 at the same time. We hence suggest that the IASB take care of introducing unintended consequences or disrupting timely publication and implementation of the ED's proposals when considering this suggestion.

~ End ~