Meeting Summary
Hong Kong Insurance Implementation Support Group (HKIISG)
9 June, 2021

Attendance
HKICPA representatives
Ernest Lee, Financial Reporting Standards Committee (FRSC)
Cecilia Kwei, Director, Standard Setting
Tiernan Ketchum, Deputy Director, Standard Setting
Carmen Ho, Associate Director, Standard Setting

HKIISG members and designees
Sam Ho, AIA Group Limited
Marcus Chung, AXA China Region Insurance Company Limited
Ronnie Ng, China Overseas Insurance
Sally Wang, Dajia Insurance Group
Kevin Wong, FWD Life Insurance Company (Bermuda) Limited
Alexander Wong, HSBC Life
Steven To (representing Tracey Polsgrove), Manulife Asia
Wenhao Zhao, Ping An Insurance (Group)
Matsuta Ng, Prudential Hong Kong Limited
Eric Chum, Prudential Hong Kong Limited
Joyce Lau, Target Insurance Company Limited
Francesco Nagari, Deloitte Hong Kong
Liza Gonzalo, Deloitte Hong Kong
Steve Cheung, EY Hong Kong
James Anderson (representing Erik Bleekrode), KPMG China
Ian Farrar (representing Chris Hancorn), PwC Hong Kong

Apologies
Sai-Cheong Foong, AIA Group Limited
Norman Yao, AXA China Region Insurance Company Limited
Tracey Polsgrove, Manulife Asia
Peter Telders, EY Hong Kong
Erik Bleekrode, KPMG China
Chris Hancorn, PwC Hong Kong

Discussion objectives:
Readers are reminded that the objective of the HKIISG is not to form a group consensus or decision on how to apply the requirements of HKFRS/IFRS 17 *Insurance Contracts*. The purpose of HKIISG is to share views on questions raised by stakeholders on the implementation of HKFRS 17. Refer to HKIISG terms of reference.

The meeting summaries of HKIISG discussions are solely to provide a forum for stakeholders to follow the discussion of questions raised. Stakeholders may reference HKIISG member views when reconsidering their own implementation questions—but should note that the meeting summaries do not form any interpretation or guidance of HKFRS/IFRS 17.

1. Local submission: Measurement of coverage units under IFRS 17:B119 and the determination of the relative weighting of the benefits provided by insurance coverage and investment-return service or by insurance coverage and investment-related service (subject to disclosure under IFRS 17:117(c)(v))

This summary should be read in conjunction with the local submission (Paper 2). Please refer to the full submission for the detailed fact pattern and analysis.

This paper considers whether the requirement to disclose the inputs, assumptions and estimation techniques used “top determine the relative weighting of the benefits provided by insurance coverage and investment-return service or by insurance coverage and investment-related service” in IFRS 17:117(c)(v) is a determination that needs to be current at the reporting date.

The submission presents the following views:

- View 1 – The determination of the relative weighting of the benefits provided by insurance coverage and investment-return service or by insurance coverage and investment-related service is a judgment (to be disclosed under IFRS 17:117(c)(v)) and **IFRS 17 does not require the entity to make such determination so that it is current at the reporting date**.
- View 2 – The determination of the relative weighting of the benefits provided by insurance coverage and investment-return service or by insurance coverage and investment-related service is a judgment (to be disclosed under IFRS 17:117(c)(v)) and **IFRS 17 requires the entity to make such determination so that it is current at the reporting date**.

Among the HKIISG members who commented on the submission, the following was noted:

Overall summary:

- Overall, a small majority of members who commented favored View 1; however, mixed views were expressed.
  - Those who supported View 1 did so largely on the basis that IFRS 17 does not explicitly require an entity to make such a determination so that it is current at the reporting date, nor does the Standard prohibit entities from locking-in the determination.
  - Some supporters of View 1 acknowledged that conceptually and in terms of the “spirit” of the Standard, View 2 could be reasonable. However, based on the actual wording of the Standard, View 1 is favored because the wording does not require a current determination. Hence, this may be a matter of accounting judgement.
  - Those who supported View 2 did so for the reasons in the submission. View 2 supporters also noted that the rest of IFRS 17 generally requires current measurement and there is no explicit exception to this. As far as paragraph 117(c)(v), this requirement was added through the Amendments to IFRS 17 and relates to disclosing judgements on current items making it internally inconsistent to assume that an item to be disclosed in that context is actually not current.

Detailed comments:

- Among members who supported View 1 it was commented that:
    - Although measurement of coverage units in general is current, there is no specific or detailed guidance on the weighting requirement in question. Given the lack of requirements, View 1 is supportable given that there is no prohibition to lock-in the determination of relative weighting at inception. Although there are conceptual arguments for View 2, the Standard is not clear enough for View 1 to be disallowed.
    - IFRS 17:117(c)(v) does not specifically require whether the weighting should be locked-in or refreshed at the current rate. The reason for the disclosure requirement is to help financial statement users interpret the results, which are based on complex calculations. Hence some companies may choose to reflect the refresh their assumptions and current weighting, but this is not a requirement in the Standard.
    - A few members commented that absent any explicit requirement that the determination be current, View 1 was acceptable. These members acknowledged that it may be reasonable to update the determination to be current (View 2), but that there is no clear requirement in the Standard that this be done. This may be a matter of accounting judgement.
- Among members who supported View 2 it was commented that:
    - As accounting for the CSM and calculation of coverage units in B119 is supposed to be a current measurement in its entirety, View 1 is incompatible with the spirit of IFRS 17. There should rather be explicit guidance that determination of relative weighting is not required to be current if View 1 were to be the intention of the IASB. Therefore, in the absence of any explicit requirements indicating either view, there is more circumstantial evidence that View 2 is the intention of the IASB.
    - While the Standard does not have explicit guidance, the disclosure is related to items that change due to the current nature of IFRS 17's measurement model. Therefore, these would be items that are expected to be updated regularly. Also, the additional paragraphs added in the Amendments to IFRS 17 in June 2020 specifically modified the definition of insurance services and introduced three types of services which then triggered this new disclosure requirement. This implies that this determination is, like the other judgements in the rest of paragraph 117, something that may change from period to period, and that the disclosures should be about such changes.
    - IFRS 17 generally uses current assumptions.
    - Although there is not explicit measurement guidance related to this disclosure requirement, the disclosure falls within a disclosure paragraph that deals with current estimates. Insurers should consider internal consistency (between weighting and inputs) if applying View 1.
- Other comments included:
    - An alternative view is that either View 1 or View 2 may be appropriate, but entities will need to apply judgement on how to perform the weighting and related updating of it. Coverage units clearly need to be current, but that weighting may or may not be required depending on the facts and circumstances. Entities will need to consider the services provided and apply judgement.
    - Paragraph B119 is clear that calculations need to be based on current conditions at the reporting date in terms of allocating coverage units, which are applied from the beginning of the reporting period, given that the value of coverage units used to release CSM to profit or loss and the value of the coverage units that makes up the CSM deferred for future periods has to be the same. Hence this has a current period impact and future period impact (not only prospective).
    - There may not be much difference between View 1 and View 2 in practice in cases where benefits considered for the coverage units' calculation are largely fixed. View

2 explicitly acknowledges there may be cases where benefits are fixed and coverage periods may be the same, in which case an insurer may not need to revise the weighting. However, the situation under View 2 would be different (and the weighting would need to be updated to be current) if there were variable benefits.

2. Local submission: Measurement of coverage units under IFRS 17:B119 and the use of the non-distinct investment component vs. the expected service expenses as a basis to determine the benefits provided by an investment-return service or by an investment-related service

This summary should be read in conjunction with the local submission [(Paper 3)](). Please refer to the full submission for the detailed fact pattern and analysis.

This paper considers whether an insurer can use the following:

- the non-distinct investment components (NDIC, sometimes referred to as "account balances"); or
- the expected service expenses that the insurer would include in the fulfilment cash flows of the group of contracts, adjusted to remove the effect of the probability of insured events occurring, if any,

as a basis to determine the quantity of benefits provided by an investment-return service (whenever the NDIC is present) or by an investment-related service in a group of contracts.

The submission presents the following views:

- View 1 – The NDIC represents the benefit provided by an investment-return service or by an investment-related service. The expected service expenses do not.
- View 2 – The expected service expenses represent the benefit provided by an investment return service or by an investment-related service. The NDIC does not, albeit it may act as a proxy for the benefit provided.
- View 3 – Both the NDIC and the expected service expenses represent the benefit provided by an investment-return service or by an investment-related service and it is an accounting judgement of the insurer to determine which amount to use for calculating the number of coverage units in a group of contracts having considered the specific facts and circumstances.

Among the HKIISG members who commented on the submission, the following was noted:

Overall summary:

- Overall, the members who commented expressed mixed views:
  - A majority of members who commented indicated that this may be a matter of accounting judgement, and that either or both approaches (NDIC and expected expenses) may be valid depending on the facts and circumstances (hence leaning more to View 3).
  - Some members commented that an approach based on cumulative premiums would also be acceptable.
  - Some members disagreed on whether expected expenses could be used as a principle. One of these members acknowledged it may be used under specific facts and circumstances regardless of whether it could be used on principle.

Detailed comments:

- Among members who disagreed on whether expected expenses (View 2) could be used as a principle it was commented that:

- A member considered the key consideration is what are the benefits provided, and considered that as a general principle, expected expenses are inputs whereas benefits are outputs, therefore expected expenses would not be a valid approach unless the insurer can demonstrate they represent a reasonable approximation of the benefits. Hence, expected expenses may only be a viable approach under specific facts and circumstances.
- One issue with expenses are that issues such as overruns could render that approach unworkable. However, another member (the submitter) suggested that View 2 is focused on expected service expenses, and overruns are a matter of actual expenses.
- The submitter suggested in support of View 2 that IFRS 17 was designed in consideration of IFRS 15, and that entities may analogize to how asset managers would apply IFRS 15 in measuring fulfilment of their performance obligations, which may be done by considering expected expenses as a basis. Insurers may consider whether they can apply a similar basis as a valid principle. Another member considered that using IFRS 15 and an input method as a point of principle in all circumstances may be dangerous because of the lack of guidance that is available in IFRS 17.
- The May 2018 TRG paper AP05 appears to reject using expenses as the proxy and as such questioned View 2. A member (the submitter) responded that View 2 acknowledges the staff view in May 2018 TRG AP05, but that this was prior to the Amendments to IFRS 17 and the introduction of its new concepts of service. Now that there are services not related to particular contractual benefits (generation of an investment return, management of underlying items), View 2 argues that if the IASB staff were writing that paper now they would not argue costs are not a representation of benefits for these new services.

- A member considered that that View 3 would be appropriate, depending on the fact pattern in question, and considered that there should be flexibility in determining coverage units.
- A member considered that the approach is a matter of accounting judgement, and that either View 1 or View 2 could be acceptable thus supporting View 3. View 1 is supported by the May 2018 TRG paper and the rationale in the submission. The approach used will depend on the fact pattern and product.
  - This member considered that in practice, the use of NDIC or expected expenses could generate a similar outcome as expected service expenses are often a percentage of NDIC.
  - A member (the submitter) responded that the outcomes from using NDIC or expected expenses could be similar when there is no volatility in the underlying items. However, when an account balance (NDIC) is used then there is exposure to financial variables' volatility and the NDIC is variable for that reason. This may not be a fair representation of the benefit the policyholder receives because the policyholder is receiving an asset management service that is not correlated to the volatility of the financial variables impacting the assets being managed. On the other hand, an expected expenses approach (View 2) would be more stable when such financial variables fluctuate and it would better represent the more stable activity being provided (asset management) versus the variability inherent in the changes in fair value of the underlying items impacting the NDIC. In this scenario, View 1 and View 2 would produce different patterns.
- A couple members (including the submitter) discussed the use of cumulative premium (in place of an account balance) as an approach to determine quantity of benefit. These members agreed they would allow cumulative premium payments as a basis under B119

because it would better reflect the policyholder benefit from the investment-related and the investment return services.
  - One member noted that in practice cumulative premiums have been found to provide a similar outcome to expected expenses, particularly in contracts with direct participation features and unit-linked contracts. This member (a supporter of View 2) considered expected expenses to have a stronger correlation to revenue.
  - One member noted that while cumulative premiums could be viable, entities should be able to demonstrate how this variable relates to services.
- One member considered that NDIC could be a basis for calculation (View 1), but that there are other possible approaches.
- One member considered that there is no single measure for investment-return or investment-related services that would be accepted as a point of principle in all cases. Rather, this member would look to see what is justifiable under the specific facts and circumstances. This member had however never encountered a case where the use of account balance was not acceptable. The member had noted a number of insurers using expenses as a fair approximation of services provided to the policyholder, but it would depend on what those expenses are and what the company's practices are. The member suggested insurers may look to the HKICPA's educational guidance on CSM for helpful information on relevant facts and circumstances. He also commented that expenses should have a relation to, and vary with changes in, the level of services provided to the policyholder for that approach to be viable.

3. Local submission: Impact of cash flow settlement arrangement in a reinsurance contract and presentation of insurance revenue and insurance service expenses in the profit or loss statement (Deloitte)

This summary should be read in conjunction with the local submission (Paper 4). Please refer to the full submission for the detailed fact pattern and analysis.

The purpose of Paper 4 is to discuss whether the cash flow settlement in a reinsurance contract issued is a relevant fact for determining the presentation of insurance revenue and insurance service expenses. Paper 4 is in two parts. The first part deals with the perspective of the issuer while the second part deals with the perspective of the cedant. The submitter believes that the conclusion of the discussion on Paper 4 is equally applicable to insurance contracts issued.

1. Impact of cash flow settlement arrangement (net vs. gross) in assessing insurance revenue and insurance service expense on an issued reinsurance contract

The first part of the paper asks what the amount of insurance revenue and insurance service expenses should be for the issuer of the reinsurance contract when the contractual amounts are based on scenario A in Paper 4. The submission presents the following views in part 1.

- View 1 – Insurance Revenue = CU 160; Insurance Service Expenses = nil; (Net = CU 160)
- View 2 – Insurance Revenue = CU 800; Insurance Service Expense = CU 640; (Net = CU 160)

Among the HKIISG members who commented on the submission, the following was noted:

Overall summary:

- Overall, the vast majority of members who commented supported View 2. The following reasons were noted:
  - View 2 is supported by the September 2018 TRG summary.
  - The mechanism by which consideration is settled should not affect the amount of insurance revenue (i.e. a net settlement method should not affect financial reporting or lead to View 1).
  - View 2 provides more useful information. In the event premiums were less than expected, View 1 would result in negative revenue, which would not be reasonable.
  - View 2 is more reasonable.

Detailed comments:

- One member also supported View 2 but noted that in Page 2 of the paper that the notional commission is varying because of the change in claims amount. This member therefore questioned whether this is defined as a claim dependent commission.
  - In response to the member above, the submitter noted that yes, View 2 supporters argued by analogy to IFRS 17:86 that there will be a claims contingent element.

2. Impact of cash flow settlement arrangement (net vs. gross) in assessing the presentation of reinsurance service expense on a reinsurance contract held based on IFRS 17:86. The submission presents the following views in part 2.

   - View 1 – Reinsurance Recoveries = nil; Cost of reinsurance = CU160 expense; (Net reinsurance service expense= CU160)
   - View 2 – Cost of reinsurance = CU 800; Reinsurance recoveries = CU 640; (Net reinsurance service expense = CU 160)

Overall summary:

- The majority of members did not object to the notion that View 2 is appropriate under part 2, symmetrical to part 1.

Detailed comments:

- A member (the submitter) supported View 2, which is analogous to View 2 of part 1 of the paper. The submitter noted that there is symmetry in the interpretation of this fact pattern to part 1 in that the netting or not of the cash flows should not impact the presentation of revenue or expenses. Equally, the cost of reinsurance and the recovery from reinsurance income element should not affect the profit and loss presentation even if the cash flows are net settled. The submitter shared that this paper was driven by the lack of clarity across a number of entities with regards to the requirements on funds withheld reinsurance arrangements. The submitter also noted that the second part of the paper also considers from a cedant's perspective how the presentation of insurance recoveries and the cost of reinsurance would be done as a result of the entity's choice to use a net amount or a gross amount.
  - Another member shared the same view as the submitter for the reasons outlined in Paper 4.
- A member (the submitter) noted that under View 2, entities still have the choice to present a single line item. Whereas under View 1 there would be a single number regardless of

choice. Neither View 1 nor View 2 would challenge the existence of an accounting policy choice for the cedant.

4. Local submission: How to determine the currency denomination of an insurance contract with cash flows denominated in multiple currencies (Deloitte)

This summary should be read in conjunction with the local submission (Paper 5). Please refer to the full submission for the detailed fact pattern and analysis.

Paper 5 asks which currency is the estimate of future cash flows from an insurance contract denominated when its cash flows are denominated in different currencies, and at which point is that determined. (E.g. a contract that has its premium in one currency, claims in another currency and expenses in a third currency, with all currencies different to the insurer's functional currency.)

The submission presents the following views:

- View 1 – The insurance contract is denominated in the currency of the premium inflows, with such assessment done at initial recognition of the contract and not subsequently reassessed.
- View 2 – The insurance contract is denominated in the currency of the "predominant" cash flows, with such assessment done at initial recognition of the contract and not subsequently reassessed.
- View 3 – The insurance contract is not denominated in any particular currency ("dual currency bonds issued" approach), with all foreign currency cash flows translated to the entity's functional currency.

Overall summary:

- Overall, the members had mixed views and considered that multiple approaches could be allowed. While some members expressed a preference for View 2, the majority of members generally considered that there is not a single view which would be required, and that different approaches are possible.

Detailed comments:

- A member (the submitter) preferred View 2 and considered the predominant cash flow is the correct interpretation of the Standard and correct application of IFRS 17:30.
- A few members noted that in practice, the outcome of View 1 and View 2 may be very similar or even identical.
- A member was accepting of all three views, but preferred View 2. Although View 3 could not be disallowed, there would need to be evidence on a case-by-case basis as to why it is appropriate.
- A member, supporting View 2, questioned the argument in View 3 concerning IFRS 17:44(d) and 45(d) given that under View 3 the CSM is already in the functional currency so there are no exchange differences.
    - A member (the submitter) explained that View 3 would argue that IFRS 17:44(d) and IFRS 17:45(d) are written for translation purposes for entities that choose to present the financial statements in a different currency other than their functional currency. In this scenario the CSM would need to reflect the difference between the presentation and functional currency in the currency translation adjustment to equity.
- A member supported View 2 but noted some entities may effectively apply View 1 by default due to how similar View 1 and 2 may be in outcomes. This member however had

some reservations regarding the practical challenges for applying View 2 due to the need to perform an initial assessment.

- A member considered that entities will tend to use View 1 or View 2. In practice, View 2 may potentially be operationally more demanding and require entities to provide auditors with more evidence on how the predominant cash flow was determined.
- A member was of none of the views in particular, but would not prohibit any of the views and any method for determining the currency based on and supported by principle would be acceptable. The member commented there is no guidance in IFRS 17 in particular on this. Potentially, IAS 21’s guidance on functional currency could be used by entities to establish a principle, and that if this principle were reasonable it would be acceptable. However, this member would not allow defaulting to functional currency because IFRS 17 does state that CSM is a monetary item rather than a non-monetary item.
- Other comments included:
    - The assessment should be done on a present value, probability-weighted basis of cash flows, as that is aligned with the measurement model. Were probabilities to be removed, there would be an entirely different measurement which may result in an inappropriate result.
    - It would not be the case that calculating the present value of the probability weighted cash flows would create a loop as to what discount rate to be used to determine the quantitative assessment. This is because the calculations would have to reflect the characteristics of the cash flows including currency regardless, and this is independent from how the contract will be eventually denominated. View 2 is a natural consequence of the fact that the measurement requirements provide all the necessary information to determine the predominant currency.
    - Entities would need to consider what initial qualitative and/or quantitative assessments would need to be performed to determine the currency of the predominant cash flows. Supporters of View 2 would look at the composition of the fulfillment cash flows' calculation on Day 1, i.e. in the context of the composition of the probability-weighted net present value of future cash flows, to determine the predominant currency. This may involve observing both qualitative and quantitative factors, given that entities would need to calculate fulfilment cash flows then determine what the dominant currency element was on a mathematical basis (looking at which subset of cash flows has the largest component percentage-wise after making all cash flows absolute amounts). As the measurement of fulfilment cash flows needs to be done regardless, View 2 would consider that it is reasonable and feasible to perform a qualitative and quantitative analysis.

5. Local submission: Consideration of foreign currency risk when identifying a portfolio of insurance contracts

This summary should be read in conjunction with the local submission (Paper 6). Please refer to the full submission for the detailed fact pattern and analysis.

Paper 6 considers whether foreign currency risk be taken into consideration when assessing “similar risks” for the purpose of determining portfolios of insurance contracts.

The submission presents the following views:

- View 1 – No, foreign currency risk is not considered a risk that is relevant when assessing whether contracts have similar risks in the identification of portfolios. Contracts with cash flows in different currencies can be included within one portfolio, and consequently, also within a group of contracts (subject to the criteria set out in IFRS 17:22).

- View 2 – Yes, currency risk is a relevant risk to consider when assessing whether contracts have similar risks. Depending on the facts and circumstances, the exposure to different currencies could require that insurance contracts within the same product line but with cash flows in different currencies be aggregated in different portfolios.

Among the HKIISG members who commented on the submission, the following was noted:

Overall summary:

- Overall, a majority of members who commented supported View 2, while a minority favored View 1.
  - Those who favored View 1 generally did so arguing that foreign currency risk is not transferred by the policyholder to the insurer or existent in the insurance contract.
  - Those who favored View 2 did so for the reasons in the paper and on the basis that foreign currency risk is part of a holistic assessment of 'similar risks'.

Detailed comments:

- Among members who supported View 1 it was commented that:
  - The February 2018 TRG summary is clear that policyholder risk includes both insurance risk and financial risk transferred form the policyholder to the entity, however excludes risks that are created by the contract. The examples in Paper 5 are not pre-existing risks, even in scenario 3, where one could argue foreign currency risk is part of price risk, it is hard to argue it is a pre-existing risk. Hence, it would not be a risk that is relevant in the assessment of what is a similar risk.
  - The policyholder is not always transferring foreign currency risk to the insurer, but rather only transferring insurance risk. Hence foreign currency risk does not necessarily need to be considered in portfolio determination.
- Among members who supported View 2 it was commented that:
  - The purpose of the paper is to consider whether insurers can define portfolios taking into account or ignoring foreign currency risk in the assessment of similar risk. This assessment is relevant for the application of IFRS 17:30 and other consequences of the translation of foreign currency risk. View 2 supporters would not agree that there is no transfer of risk as there is no persuasive argument that would differentiate why a particular element of financial risk (foreign currency risk) has not been transferred when the same contract transfers other types of financial risk (e.g. equity or interest rate risk).
  - The assessment of risk should be done from a broader perspective (i.e. from the entity's perspective versus the policyholder perspective), and how the entity manages the contracts in terms of similar risks. Policyholder risk could be limited to only insurance risk, but the scope of risk would be larger from an entity's perspective.
  - Those who support View 2 would consider "similar risks" as not being qualified in any way and hence not excluding foreign exchange risk. The distinction to View 1 is that View 1 is qualified by excluding foreign exchange risk.
  - For participating contract with liabilities with different currencies, but sharing the same pool of assets, the same basis may be considered so they may end up in the same pool. However, for non-participating insurance contracts a difference in currencies could have more of an effect. Foreign currency risk would need to be taken into account when determining grouping of contracts.

- Foreign currency risk should be considered when determining portfolios, but that it may not necessarily be a defining factor or result in the conclusions reached for the scenarios in Paper 5. Entities should be cautious of this when applying View 2.

- Other comments included:
    - A member stated that foreign currency is a risk and cannot be ignored. However, this member would not necessarily be in either view and considered that in the assessment of similar risks, there is no need to disaggregate portfolios to the point where every risk, including foreign currency risk, is taken into account in the separation of the different portfolios. Rather, this member considered that a holistic assessment should be done so a fair overall outcome could be achieved.
        - A member (the submitter) explained that View 2 supporters would assess similar risks holistically, and the point of View 2 is that foreign exchange risk would be included in that holistic assessment (unlike View 1 where it would be excluded entirely)
    - A couple members noted that insurers can choose to separate portfolios into groups based on foreign currency risk and manage them separately, and that there is nothing to stop insurers from creating groups of single currency contracts. View 1 supporters could achieve the same accounting as under View 2 by voluntarily adopting the consequences of the View 2 approach through the definition of groups.