In depth
A look at current financial reporting issues

21 October 2016

No. INT2016-05

What's inside?

Amendment to IFRS 4 – relief for insurers regarding IFRS 9

At a glance

On 12 September 2016, the International Accounting Standards Board (IASB) published an amendment to IFRS 4, 'Insurance Contracts' (Applying IFRS 9 'Financial Instruments' with IFRS 4 'Insurance Contracts' (Amendments to IFRS 4)).

The amendment addresses the concerns that have been expressed about the **different effective dates** of **IFRS 9** (annual periods beginning on or after 1 January 2018) and the forthcoming **new insurance contracts standard** (not likely to be before 2021).

One main concern was that applying IFRS 9 before applying the new insurance contracts standard may result in a temporary accounting mismatch and volatility in profit or loss. The reason for this is that under IFRS 9 certain financial assets have to be measured at fair value through profit or loss, whereas under current IFRS 4 the related liabilities from insurance contracts are often measured on a cost basis. This accounting mismatch may be temporary, because the new insurance contracts standard is expected to require insurers to discount their insurance contracts using a current interest rate and to allow reporting of the effect of changes in the interest rate in profit or loss.

Furthermore, several insurers were worried about applying the classification and measurement requirements in IFRS 9 before being able to fully evaluate the new insurance contracts standard. Many considered two sets of major accounting changes within a short period of time as onerous.

The amendment offers insurers two possible solutions: a **temporary exemption from IFRS 9** for annual periods beginning before 1 January 2021 and the 'overlay approach'. Both of these approaches are optional.

The temporary exemption from IFRS 9 addresses most of the concerns raised. However, it is only available for a limited period of time and in limited circumstances. In particular, it has to be applied at the level of the reporting entity. Even if a subsidiary might be eligible for the temporary exemption, it will still have to prepare financial information applying IFRS 9 for consolidation purposes if the parent entity cannot apply the temporary exemption.

Under the **'overlay approach'** an insurer reclassifies from profit or loss to other comprehensive income any changes in the fair value of financial assets held in respect of an activity that is connected with contracts within the scope of IFRS 4, if these changes are recognised in profit or loss under IFRS 9, but not under IAS 39.

With respect to the temporary exemption from IFRS 9, the amendment is effective for annual periods beginning on or after 1 January 2018. The 'overlay approach' can be applied from the period in which the insurer first applies IFRS 9. If the insurer chooses to apply the 'overlay approach' it has to be applied retrospectively.

IFRS 4 (including the amendments that have now been issued) will be superseded by the forthcoming insurance contracts standard. Accordingly, both the temporary exemption and the 'overlay approach' are expected to cease to be applicable, at the latest, at the point in time the new insurance standard becomes effective.

Both solutions are also available to first-time adopters of IFRS.

Temporary exemption from applying IFRS 9

For annual periods beginning before 1 January 2021 the amendment to IFRS 4, 'Insurance Contracts', allows entities to continue to apply IAS 39, 'Financial Instruments: Recognition and Measurement', instead of adopting IFRS 9, 'Financial Instruments', if they meet the criteria explained below.

It is important to note that the exemption is optional. Even if the entity is eligible for the temporary exemption it can still decide to adopt IFRS 9. Furthermore, an entity that has previously elected to apply the temporary exemption from IFRS 9 may, at the beginning of any subsequent annual period, irrevocably elect to apply IFRS 9 rather than IAS 39.

PwC observation:

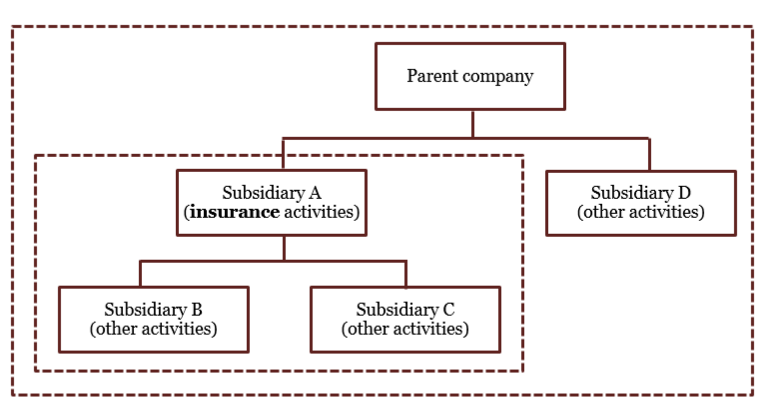
The temporary exemption is limited to annual periods beginning before 1 January 2021. Hence, insurers will have to adopt IFRS 9, 'Financial Instruments', for annual periods beginning on or after 1 January 2021 even if the new standard on insurance contracts is not effective at that point in time, unless there is a subsequent amendment to the standard.

Application at reporting entity level

Groups that contain insurance subsidiaries should be aware that the temporary exemption only applies at the **level of the reporting entity**. Unless the whole group is eligible for the temporary exemption, the insurance subsidiary can continue to apply IAS 39 only in its individual financial statements (provided the eligibility criteria are met), but the group has to prepare consolidated financial statements under IFRS 9.

Example

Take as an example the group structure as follows:



Scenario A: The group as a whole is **not eligible** for the temporary exemption

If the group as a whole is not eligible for the temporary exemption it has to adopt IFRS 9 in its consolidated financial statements. However, this does not affect the separate financial statements of subsidiaries A, B, C and D and the consolidated financial statements for the sub-group controlled by subsidiary A. For those financial statements it has to be assessed separately, whether or not the issuing reporting entity is eligible for the temporary exemption from IFRS 9.

If, for example, the sub-group controlled by subsidiary A is eligible for the temporary exemption, subsidiary A can continue to apply IAS 39 in its sub-group consolidated financial statements. However, on consolidation, the parent entity has to reverse the effect of applying IAS 39 by subsidiary A. In effect, subsidiary A has to prepare two sets of sub-group consolidated financial statements – one set applying IAS 39 (for its own consolidated financial statements, provided it chooses the temporary exemption) and one set applying IFRS 9 (to be included in its parent's consolidated financial statements).

Scenario B: The group as a whole is **eligible** for the temporary exemption

The group as a whole can decide to apply the temporary exemption from IFRS 9 and continue to apply IAS 39 in its consolidated financial statements. If the group decides to use the temporary exemption each subsidiary has to prepare financial information applying IAS 39, to be included in the group's consolidated financial statements.

If, for example, subsidiary D has a significant banking business without any insurance activities and is hence not eligible for the temporary exemption, it has to adopt IFRS 9 in its separate financial statements and prepare additional financial information applying IAS 39, to be included in the parent's consolidated financial statements.

PwC observation:

The requirement to make the assessment at the reporting entity level may result in IFRS 9 being applied in separate financial statements of a parent and IAS 39 being applied in the consolidated financial statements of a group. In some situations the parent entity of a group may not be eligible for the temporary exemption from applying IFRS 9. However, the group as a whole may be eligible. If the parent prepares separate financial statements, IFRS 9 should be applied in the separate financial statements, while in the consolidated financial statements the group may choose to apply IFRS 9 or IAS 39.

Eligibility criteria

The temporary exemption from IFRS 9 is available for an insurer that has **not previously applied any version of IFRS 9** and whose **activities are predominantly connected with insurance**. The amendment defines an 'insurer' as any entity that issues an insurance contract within the scope of IFRS 4, no matter whether the entity is regarded as an insurer for legal or supervisory purposes. Furthermore, the issuer of a financial instrument that contains a discretionary participation feature is also regarded as an insurer for the application of the amendment.

No previous application of IFRS 9

As a key principle the temporary exemption from IFRS 9 is not applicable if the insurer has already applied any version of IFRS 9.

However, the requirements in IFRS 9 for the presentation of gains and losses on financial liabilities designated as at fair value through profit or loss are excluded from this principle. Provided the other criteria are met, an insurer can continue to use IAS 39 even if it has already applied the requirements in IFRS 9 for financial liabilities designated as at fair value through profit or loss. Furthermore, a later adoption of this part of IFRS 9 does not affect the insurer's eligibility for the temporary exemption regarding the other parts of IFRS 9.

Activities are predominantly connected with insurance

An insurer can apply the temporary exemption only if its activities are predominantly connected with insurance. This criterion is assessed in a two-step approach; both tests have to be passed.

First, the insurer compares the carrying amount of its **liabilities arising from contracts within the scope of IFRS 4** (including deposit components or embedded derivatives unbundled from insurance contracts), with the total carrying amount of all its liabilities. If the carrying amount of liabilities arising from contracts within the scope of IFRS 4 is significant compared to the total carrying amount of all its liabilities, the insurer moves on to step two. Otherwise, the temporary exemption from IFRS 9 is not applicable.

PwC observation:

There is no guidance in the amendment on how the term 'significant' should be interpreted. In practice, this will be one of the key areas of judgment in applying the amendment.

In a **second** step, the total carrying amount of an insurer's **liabilities connected with insurance** is compared to the total carrying amount of all its liabilities. The total carrying amount of liabilities connected with insurance includes not only liabilities arising from contracts within the scope of IFRS 4 (including deposit components or embedded derivatives unbundled from insurance contracts), but also non-derivative investment contract liabilities measured at fair value through profit or loss applying IAS 39 (including those designated as at fair value through profit or loss to which the insurer has applied the requirements in IFRS 9 for the presentation of gains and losses) and liabilities that arise because the insurer issues, or fulfils obligations arising from, those insurance and non-derivative investment contracts. These non-derivative investment contract liabilities will include unit linked balances and separate account balances in many countries.

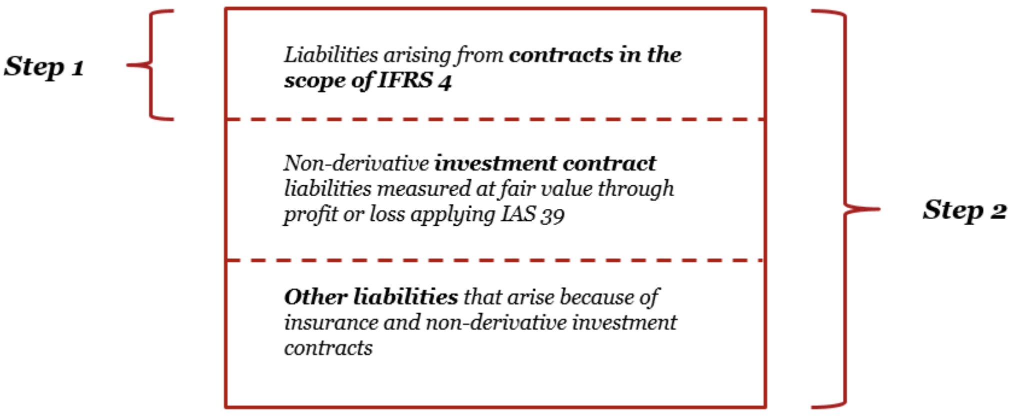
PwC observation:

Liabilities connected with insurance not only include liabilities arising from contracts in the scope of IFRS 4, but also non-derivative investment contract liabilities that are measured at fair value through profit or loss. Those contracts are often sold alongside similar products with a significant insurance risk and are in many jurisdictions regulated as insurance contracts.

This change to the eligibility criteria proposed in the Exposure Draft will allow more life insurers to benefit from the temporary exemption.

Consolidated financial statements including life insurers may also consolidate insurance funds, including collective investment funds, and show the puttable non-controlling interest in these funds as a liability and these will also be seen as connected with insurance.

Composition of liabilities connected with insurance



Examples of liabilities that arise because the insurer issues, or fulfils obligations arising from, insurance and non-derivative investment contracts, include derivatives used to mitigate risks arising from those contracts and from the assets backing those contracts, relevant tax liabilities such as the deferred tax liabilities for temporary taxable differences on liabilities arising from those contracts, and debt instruments issued that are included in the insurer's regulatory capital. In the Basis for Conclusions the Board also mentions that such liabilities include liabilities for salaries and other employment benefits for employees of the insurance activities.

For the **percentage** of the total carrying amount of an insurer's liabilities connected with insurance compared to total carrying amount of all its liabilities, the amendment distinguishes between three possible outcomes:

1) If the percentage is greater than 90 per cent the insurer's activities are predominantly connected with insurance.

2) If the percentage is less than or equal to 90 per cent, but greater than 80 per cent and the insurer does not engage in a significant activity unconnected with insurance, its activities are predominantly connected with insurance. Otherwise, the activities are not predominantly connected with insurance.

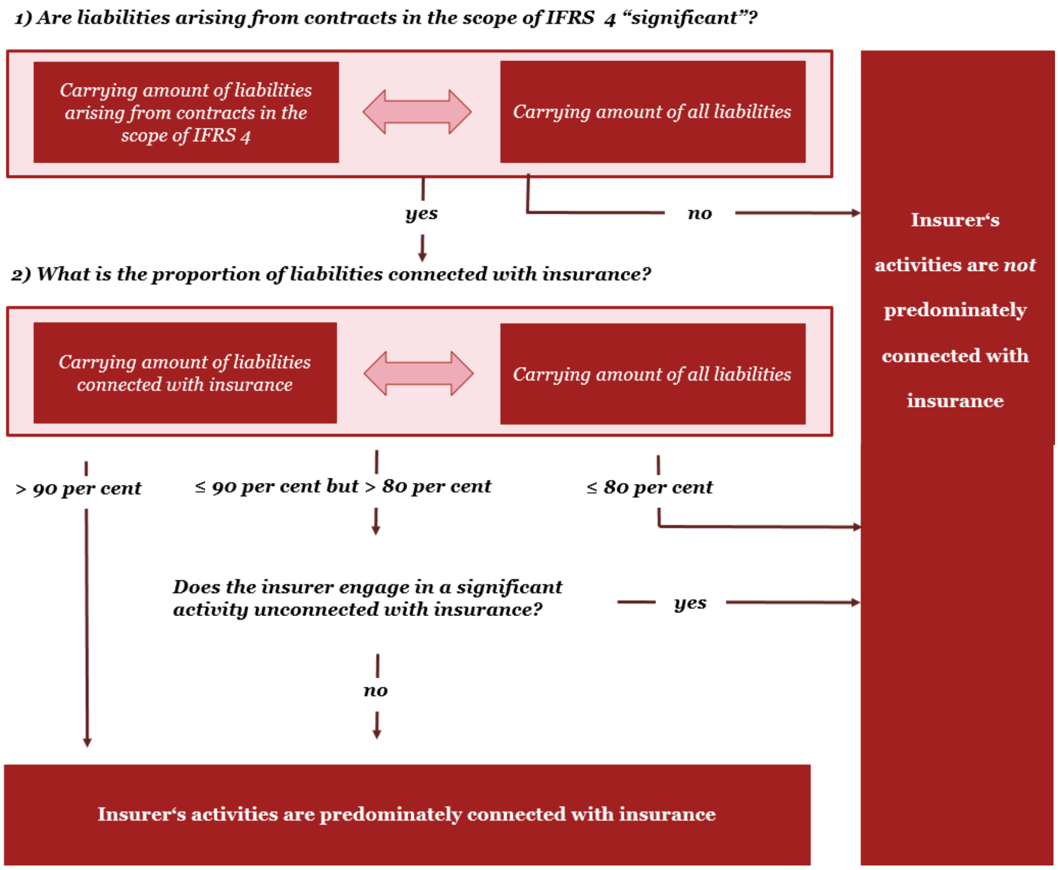
3) If the percentage is less than or equal to 80 per cent, the insurer's activities are not predominantly connected with insurance.

To assess whether an activity is unconnected with insurance, an insurer shall consider only those activities from which it may earn revenue and incur expenses. This will take into account qualitative and/or quantitative factors, including publicly-available information such as the industry classification that users of financial statements apply to the insurer.

PwC observation:

Liabilities that form a part of discontinued operations under IFRS 5 should still be included in the assessment, in accordance with the nature of the liabilities. However, the actual disposal of operations may later trigger the requirement to reassess entity's eligibility for the temporary exemption from applying IFRS 9.

The analysis of whether an insurer's activities are predominantly connected with insurance are illustrated in the **flowchart** below:



Date of assessment

The assessment of whether an insurer qualifies for the temporary exemption from IFRS 9 is made at the annual reporting date that immediately precedes 1 April 2016. After that date, a **reassessment** is made only in limited circumstances.

PwC observation:

In the Exposure Draft the IASB suggested an initial assessment on the date an entity would otherwise apply IFRS 9 (that is, the first day of the annual period beginning on or after 1 January 2018). This date changed in the final amendment to give entities that do not meet the eligibility criteria, (i.e. do not qualify for the temporary exemption), adequate time to implement IFRS 9.

An entity that **qualifies** for the temporary exemption from IFRS 9 ***shall*** reassess whether its activities are predominantly connected with insurance at a subsequent annual reporting date if, and only if, there is a change in the entity's activities during the annual period that ended on that date.

An entity that does **not qualify** for the temporary exemption from IFRS 9 is ***allowed*** to reassess whether its activities are predominantly connected with insurance if, and only if, there is a change in the insurer's activities during the annual period that ended on that date. However, the reassessment can only be made at an annual reporting date before 31 December 2018 (i.e. the date on which the entity otherwise would have to present financial statements prepared based on IFRS 9 for the first time).

A **change in an entity's activities** that may trigger a reassessment has to be determined by the entity's senior management as a result of external or internal changes. Furthermore, it must be significant to the entity's operations and demonstrable to external parties. It occurs only when the entity begins, or ceases to perform, an activity that is significant to its operations or significantly changes the magnitude of one of its activities. An example of a change in an entity's activities may be the acquisition or disposal/termination of a line of business.

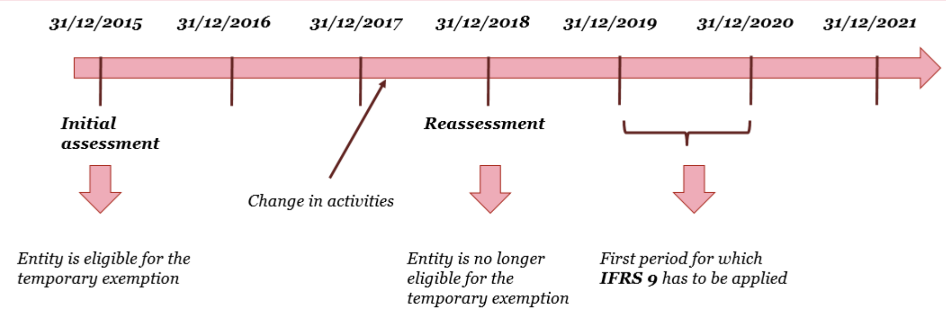
The IASB expects changes in an entity's activities that may result in a reassessment to be very infrequent. In particular, it is pointed out that a change in the entity's funding structure that in itself does not affect the activities from which the entity earns revenues and incurs expenses, is not a change in the entity's activities. A mere plan to sell a business line also does not yet establish a change in the entity's activities even if the assets and liabilities are already classified as held for sale in accordance with IFRS 5, 'Non-current Assets Held for Sale and Discontinued Operations'.

If a reassessment results in an entity no longer being eligible for the temporary exemption from IFRS 9 it is permitted to continue to apply the temporary exemption from IFRS 9 until the end of the annual period that began immediately after that reassessment. However, IFRS 9 must be applied for annual periods beginning on or after 1 January 2021.

Example

An insurer that is eligible for the temporary exemption from IFRS 9 based on the initial assessment later changes its activities. After a reassessment it is concluded that it is no longer eligible for the temporary exemption. The entity's annual reporting date is 31 December.

Scenario A: The change in activities took place in 2018.



The entity is permitted to continue applying IAS 39 only until the end of the period that immediately follows the reassessment. Hence, the first period in which it has to apply IFRS 9 is 2020.

First-time adopter

The temporary exemption from IFRS 9 is also available for a first-time adopter as defined in IFRS 1, 'First-time Adoption of International Financial Reporting Standards', provided it meets the eligibility criteria.

PwC observation:

The final amendment also permits first-time adopters to apply the temporary exemption if the eligibility criteria are met. This is a change compared to the Exposure Draft to acknowledge the fact that if national GAAP does not significantly differ from IFRS, a first-time adopter faces the same issues as a current IFRS reporter and should therefore be dealt with on a consistent basis.

Associates and joint ventures

When the equity method is used for associates and joint ventures IAS 28, 'Investment in Associates and Joint Ventures', requires that uniform accounting policies are used for like transactions and events in similar circumstances.

The temporary exemption from IFRS 9 is excluded from this general requirement. If the entity applies the temporary exemption but the associate or joint venture already applies IFRS 9, the entity is allowed to retain the relevant accounting policies applied by the associate or joint venture. The same is true if the entity applies IFRS 9 but the associate or joint venture applies the temporary exemption from IFRS 9. Retaining the accounting policy of the associate or joint venture is an option. The entity can still decide to adjust the accounting policies of the associate or joint venture when its financial statements are used in applying the equity method.

The entity can make this choice separately for each associate or joint venture for annual periods beginning before 1 January 2021.

PwC observation:

Extensive additional disclosure requirements apply if an entity applies the temporary exemption from IFRS 9 when accounting for its investment in an associate or joint venture using the equity method.

Disclosure requirements

Entities that apply the temporary exemption from IFRS 9 have to make extensive disclosures to help users to understand *why* they are allowed to apply the temporary exemption from IFRS 9 and *how* this affects their financial statements. The major new disclosures are listed below:

Application of the temporary exemption

- The **fact** that the insurer is applying the temporary exemption from IFRS 9
- Explanations about **how the insurer concluded that it qualifies for the temporary exemption** from IFRS 9, including:
    - o The nature and carrying amounts of the liabilities connected with insurance that are not liabilities arising from contracts in the scope of

IFRS 4 (only if the carrying amount of liabilities arising from contracts within the scope of IFRS 4 is less than, or equal to, 90 per cent of the total carrying amount of all the insurer's liabilities).
    - How the insurer determined that it has no significant activity that is unconnected with insurance, including what information it considered (only if the percentage of its liabilities connected with insurance to the total carrying amount of all its liabilities is less than or equal to 90 per cent but greater than 80 per cent).
    - If the insurer qualified for the temporary exemption from IFRS 9 on the basis of a reassessment it shall disclose the reason for the reassessment, the date on which the relevant change in activities occurred, and a detailed description of the change in activities and the effect of that change on its financial statements.
- If an insurer concludes that its activities are no longer predominantly connected with insurance, it shall disclose the fact that it no longer qualifies for the temporary exemption from IFRS 9, the date on which the relevant change in activities occurred, and a detailed description of the change in activities and the effect of that change on its financial statements in each reporting period before it begins to apply IFRS 9.

Effect of applying the temporary exemption

- The **fair value** at the end of the reporting period and the amount of change in the fair value during the period separately for financial assets with contractual terms that give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding (SPPI), (excluding any financial asset that meets the definition of held for trading in IFRS 9, or that is managed and whose performance is evaluated on a fair value basis) and all other financial assets.
- For financial assets that have cash flows that are SPPI (excluding any financial asset that meets the definition of held for trading in IFRS 9, or that is managed and whose performance is evaluated on a fair value basis), information about the **credit risk exposure**, including significant credit risk concentrations. This shall include at a minimum:
    - The gross carrying amounts applying IAS 39 by credit risk rating grades as defined in IFRS 7.
    - For financial assets that do not have a low credit risk (as defined in IFRS 9) the fair value and the gross carrying amount applying IAS 39.
- Information about where a user of financial statements can obtain any publicly-available IFRS 9 information that is not already provided in the consolidated financial statements for the relevant reporting period.

PwC observation:

In the Exposure Draft the IASB suggested that fair value disclosures should be made separately for financial assets with contractual terms that give rise on specified dates to cash flows that are SPPI and all other financial assets. To provide this disclosure entities would have been required to perform a SPPI-test for all financial assets, even if it is already clear from the business model test that the financial assets are measured at fair value through profit or loss.

In the final amendment financial assets that either meet the definition of held for trading in IFRS 9, or that are managed and whose performance is evaluated on a fair value basis (and therefore fail the business model test), are grouped together with financial assets that fail the SPPI test. Thus, for these financial assets a SPPI-test solely for the disclosure requirements in IFRS 4, is not necessary.

Information about associates and joint ventures

- If an entity decides not to adjust the accounting policies of an associate or a joint venture it shall disclose this fact.
- If an entity applied the temporary exemption from IFRS 9 when accounting for its investment in an associate or a joint venture using the equity method, the entity shall provide the disclosures outlined above for each of those associates or joint ventures that are individually material to the entity and in aggregate for all of those associates or joint ventures that are individually immaterial to the entity (separately for associates and joint ventures).

The overlay approach

The overlay approach addresses the concern of many insurers that applying IFRS 9 without applying the new insurance contracts standard will result in significant volatility in profit or loss. The reason for this is that under IFRS 9 certain financial assets have to be measured at fair value through profit or loss, whereas under current IFRS 4 the related liabilities from insurance contracts are often measured on a cost basis and hence changes in fair value do not affect profit or loss. This accounting mismatch is temporary because the new insurance contracts standard is expected to require insurers to discount their insurance contracts using a current interest rate and to allow reporting the effect of changes in the interest rate in profit or loss.

The overlay approach permits insurers (i.e. entities that issue an insurance contract within the scope of IFRS 4 or a financial instrument with a discretionary participation feature) to reclassify the profit or loss resulting from fair value changes of certain financial assets to other comprehensive income and thereby avoid volatility in profit or loss. Similar to the temporary exemption from IFRS 9, the overlay approach is optional. Even if the insurer is eligible for the overlay approach it can still decide not to apply it.

An insurer may choose to apply the overlay approach only when it first applies IFRS 9. This includes scenarios in which it first applies IFRS 9 after previously applying only the requirements for the presentation of gains and losses on financial liabilities designated as at fair value through profit or loss or the temporary exemption from IFRS 9.

PwC observation:

If the new insurance contracts standard is not effective for annual periods beginning on 1 January 2021 entities that have previously applied the temporary exemption will be required to adopt IFRS 9 but they may choose to apply the overlay approach from that date until the effective date of the new insurance contracts standard.

At the beginning of any annual period an insurer may decide to stop applying the overlay approach. The cessation of the overlay approach shall be accounted for as a change in accounting policy in accordance with IAS 8. Hence, the entity adjusts the opening balance of retained earnings for the balance accumulated in other comprehensive income. Once an entity has stopped using the overlay approach it is not allowed to apply it again in subsequent periods.

Mechanics

Under the overlay approach an insurer reclassifies between profit or loss and other comprehensive income the difference between:

- the amount that *is* reported in profit or loss for the designated financial assets applying IFRS 9; and
- the amount that *would have been* reported in profit or loss for the designated financial assets if the entity had applied IAS 39.

As a result the **profit or loss** for the designated financial assets at the end of the reporting period is the same as if the entity had applied **IAS 39** to the designated financial assets. The carrying amount of the designated financial assets presented on the **balance sheet** is still in line with the guidance in **IFRS 9**.

PwC observation:

When the amount of the overlay adjustment for the designated financial assets is calculated, the difference between profit or loss under IAS 39 and IFRS 9 will include items such as:

1. The amounts relating to impairment of financial assets.
2. Fair value adjustments for instruments that were included into available-for-sale, held to maturity and loans and receivables categories under IAS 39 but have to be measured at fair value through profit or loss because cash flows from such instruments do not represent solely payments of interest and principal.

In profit or loss the amount that is reclassified is presented as a separate line item. In other comprehensive income the amount is presented as a separate component of other comprehensive income.

An example of the presentation is set out below. The overlay adjustment will be grouped in other comprehensive income with other items that will be reclassified subsequently to profit or loss.

Statement of Comprehensive Income

Net underwriting income	1000
Investment income	100
Investment expense	(20)
IFRS 9 overlay approach adjustment	*(30)*
Profit or loss	1050
IFRS 9 overlay approach adjustment	*30*
Other comprehensive income	40
Total comprehensive income	1120

PwC observation:

An entity that applies the overlay approach can still apply 'shadow accounting' if the designated financial assets have a direct effect on the measurement of some or all of the insurance liabilities.

Applying both the overlay approach and shadow accounting will enable an insurer to show an income statement as if it had applied IAS 39 to the designated assets while the overall effect on total comprehensive income will be applying IFRS 9 to these assets.

Designation of financial assets

For a financial asset to be eligible for designation for the overlay approach two criteria have to be met:

1) The financial asset is measured at fair value through profit or loss applying IFRS 9 but would not have been measured at fair value through profit or loss in its entirety applying IAS 39.

PwC observation:

Provided the other criteria are met, a financial asset is eligible for the overlay approach if it would not have been measured at fair value through profit or loss under IAS 39 in its **entirety**. Accordingly, the fact that a financial asset contains an embedded derivative that would have been separated and measured at fair value through profit or loss under IAS 39, does not prevent the financial asset from being eligible for the overlay approach.

2) It is not held in respect of an activity that is unconnected with contracts within the scope of IFRS 4.

PwC observation:

The amendment does not define under which circumstances activities are connected with contracts in the scope of IFRS 4. It only points out that

- assets held in respect of banking activities; or
- financial assets held in funds relating to investment contracts that are outside the scope of IFRS 4;

are not eligible for the overlay approach. As an example of financial assets that may be eligible for the overlay approach, the Basis for Conclusions mentions financial assets held for insurance regulatory requirements or for meeting the internal capital objectives for the insurance business.

The guidance on liabilities connected with insurance (see above) may help to analyse when business activities are connected to contracts within the scope of IFRS 4.

PwC observation:

An entity may designate financial assets as eligible for the overlay approach if they are held in a separate legal entity from the legal entity that issues contracts in the scope of IFRS 4. Additional disclosures are required in this case to explain the basis for designation, including explaining why the entity considers that those assets are held in respect of an activity connected with contracts within the scope of IFRS 4.

An insurer is permitted to designate eligible financial assets for the overlay approach on an instrument-by-instrument basis. It designates a financial asset for the overlay approach either at the point in time it starts applying the overlay approach or when it subsequently first recognises the financial asset.

Aside from this, an entity is **allowed to newly designate** a previously recognised financial asset for the overlay approach if the asset has previously not met the eligibility criteria described above. If a previously recognised financial asset is newly recognised its fair value at the date of designation shall be its new amortised cost carrying amount. The effective interest rate shall be determined based on its fair value at the date of designation.

An entity **shall de-designate** a financial asset if the financial asset no longer meets the eligibility criteria (for example because it is transferred so that it is now held in respect of an insurer's banking activities or when an entity ceases to be an insurer). In that case the balance relating to that financial asset accumulated in other comprehensive income shall be reclassified to profit or loss as a reclassification adjustment (see IAS 1). An entity is not allowed to de-designate a financial asset voluntarily.

If an insurer initially has elected to apply the overlay approach but does not have any eligible financial assets it may subsequently apply the overlay approach as soon as it has eligible financial assets.

PwC observation:

An insurer may only elect to apply the overlay approach when it first applies IFRS 9. If an insurer does not have eligible financial assets when it first applies IFRS 9 it may still wish to choose the overlay approach in case its future financial assets meet the eligibility criteria. Without having chosen the overlay approach on adopting IFRS 9 the entity will not be able to apply it in subsequent periods.

Transition

The overlay approach is applied retrospectively. Accordingly, the difference between the fair value of the designated financial assets applying IFRS 9 and the carrying amount applying IAS 39 is recognised as an adjustment to the opening balance of accumulated other comprehensive income. Comparative information is restated only if the insurer restates comparative information when applying IFRS 9.

First-time adopter

The overlay approach is also available for a first-time adopter as defined in IFRS 1, 'First-time Adoption of International Financial Reporting Standards', provided it meets the eligibility criteria. A first-time adopter shall restate comparative information to reflect the overlay approach only if it restates comparative information to comply with IFRS 9.

Disclosure requirements

If an insurer applies the overlay approach it has to provide information that enables users of the financial statements to understand *how* the amount that is reclassified from profit or loss to other comprehensive income is calculated and *how* the reclassification affects its financial statements. Disclosures an insurer has to make include:

- The **fact** that the overlay approach is applied.
- The **carrying amount** at the end of the reporting period of financial assets to which the entity applies the overlay approach (by class of financial asset).
- The basis for designating the financial assets for the overlay approach.
- An **explanation** of the total **amount reclassified from profit or loss to other comprehensive income** in the reporting period (including the amounts that would be recognised in profit or loss for the designated financial assets if IAS 39 and if IFRS 9 were applied).
- The effect of the reclassification on **each affected line item in profit or loss.**
- If financial assets are **newly designated** the amount reclassified relating to these financial assets.
- If a financial asset is **de-designated** the amount that would have been reclassified if the financial asset had not been de-designated and the amount that has been reclassified to profit or loss from accumulated other comprehensive income.
- If an entity applied the overlay approach when accounting for its investment in an **associate or a joint venture** using the equity method, the entity shall provide the disclosures outlined above for each of those associates or joint ventures that is individually material to the entity and in aggregate for all of those associates or joint ventures that are individually immaterial to the entity (separately for associates and joint ventures).

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