

STAFF PAPER

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Project	Transition Resource Group for IFRS 17 <i>Insurance Contracts</i>		
Paper topic	Recovery of insurance acquisition cash flows		
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This paper has been prepared for discussion at a public meeting of the Transition Resource Group for IFRS 17 *Insurance Contracts* and does not represent the views of any individual member of the International Accounting Standards Board or staff. Comments on the application of IFRS® Standards do not purport to set out acceptable or unacceptable application of IFRS Standards.

Introduction

1. We have received a submission about whether insurance acquisition cash flows and the related revenue are recognised in the statement(s) of financial performance applying paragraph B125 of IFRS 17 if those cash flows cannot be recovered from the cash flows of the portfolio of contracts.
2. We have also received a submission about the accounting for changes in insurance acquisition cash flows applying paragraphs B123 and B125 of IFRS 17.
3. The objective of the paper is to provide background and an accounting analysis to support discussion at the Transition Resource Group for IFRS 17 *Insurance Contracts* (TRG).

Structure of the paper

4. This paper includes the following:
 - (a) background information;
 - (b) implementation question; and
 - (c) review of accounting requirements.
5. There are three appendices to this paper:
 - (a) Appendix A—Paragraphs explaining the requirements for insurance acquisition cash flows in the Basis for Conclusions on IFRS 17;
 - (b) Appendix B—Examples of applying the requirements in paragraphs B123 and B125 of IFRS 17 when insurance acquisition cash flows are not included in expected future cash flows; and
 - (c) Appendix C—Examples of applying the requirements in paragraphs B123 and B125 of IFRS 17 when insurance acquisition cash flows are included in expected future cash flows.

Background information

6. On measuring the contractual service margin at initial recognition, paragraph 38 of IFRS 17 states:

The contractual service margin is a component of the asset or liability for the group of insurance contracts that represents the unearned profit the entity will recognise as it provides services in the future. An entity shall measure the contractual service margin on initial recognition of a group of insurance contracts at an amount that, unless paragraph 47 (on onerous contracts) applies, results in no income or expenses arising from:

- (a) the initial recognition of an amount for the fulfilment cash flows, measured by applying paragraphs 32–37;

(b) the derecognition at the date of initial recognition of any asset or liability recognised for insurance acquisition cash flows applying paragraph 27; and

(c) any cash flows arising from the contracts in the group at that date.

7. On identifying insurance contracts that are onerous at initial recognition paragraph 47 of IFRS 17 states:

An insurance contract is onerous at the date of initial recognition if the fulfilment cash flows allocated to the contract, any previously recognised acquisition cash flows and any cash flows arising from the contract at the date of initial recognition in total are a net outflow. [...]

8. Appendix A of IFRS 17 defines insurance acquisition cash flows as:

Cash flows arising from the costs of selling, underwriting and starting a group of insurance contracts that are directly attributable to the portfolio of insurance contracts to which the group belongs. Such cash flows include cash flows that are not directly attributable to individual contracts or groups of insurance contracts within the portfolio.

9. On recognising insurance revenue, paragraphs B120–B125 of IFRS 17 state:

B120 The total insurance revenue for a group of insurance contracts is the consideration for the contracts, ie the amount of premiums paid to the entity:

- (a) adjusted for a financing effect; and
- (b) excluding any investment components.

B121 Paragraph 83 requires the amount of insurance revenue recognised in a period to depict the transfer of promised services at an amount that reflects the consideration to which the entity expects to be entitled in exchange for those services. The total consideration for a group of contracts covers the following amounts:

- (a) amounts related to the provision of services, comprising:

- (i) insurance service expenses, excluding any amounts allocated to the loss component of the liability for remaining coverage;
 - (ii) the risk adjustment for non-financial risk, excluding any amounts allocated to the loss component of the liability for remaining coverage; and
 - (iii) the contractual service margin.
- (b) amounts related to insurance acquisition cash flows.

B122 Insurance revenue for a period relating to the amounts described in paragraph B121(a) is determined as set out in paragraphs B123–B124. Insurance revenue for a period relating to amounts described in paragraph B121(b) is determined as set out in paragraph B125.

B123 Applying IFRS 15, when an entity provides services, it derecognises the performance obligation for those services and recognises revenue. Consistently, applying IFRS 17, when an entity provides services in a period, it reduces the liability for remaining coverage for the services provided and recognises insurance revenue. The reduction in the liability for remaining coverage that gives rise to insurance revenue excludes changes in the liability that do not relate to services expected to be covered by the consideration received by the entity. Those changes are:

- (a) changes that do not relate to services provided in the period, for example:

[...]

- (v) insurance acquisition cash flows (see paragraph B125); [...]

B124 [...]

B125 An entity shall determine insurance revenue related to insurance acquisition cash flows by allocating the portion of the premiums that relate to recovering those cash flows to each reporting period in a systematic

way on the basis of the passage of time. An entity shall recognise the same amount as insurance service expenses.

Implementation question

10. One of the submissions asks whether insurance acquisition cash flows and the related revenue are recognised in the statement(s) of financial performance applying paragraph B125 of IFRS 17 if those cash flows cannot be recovered from the cash flows of the portfolio of contracts.
11. The submission expresses two views. The first is that if insurance acquisition cash flows are not recoverable, the portion of the premiums that relate to recovering those cash flows is nil applying paragraph B125 of IFRS 17. The second is that amounts related to insurance acquisition cash flows are presented as insurance revenue and insurance service expenses applying paragraph B125 of IFRS 17 regardless of whether or not the group of insurance contracts is onerous.
12. The second submission is about the accounting for changes in insurance acquisition cash flows applying paragraphs B123 and B125 of IFRS 17.

Review of accounting requirements

13. Insurance acquisition cash flows are reflected in the contractual service margin or loss component for a group of insurance contracts on initial recognition. IFRS 17 achieves this by requiring that:
 - (a) insurance acquisition cash flows that occur on or before initial recognition are included in the measurement of the contractual service margin or loss component at initial recognition applying paragraphs 38(b)–(c) and 47 of IFRS 17; and
 - (b) insurance acquisition cash flows that are expected to occur after initial recognition are included in the fulfilment cash flows at initial recognition applying paragraphs 38(a) and 47 of IFRS 17.

14. This means that insurance acquisition cash flows are treated in the same way as other cash flows incurred in fulfilling insurance contracts. The way that the measurement model in IFRS 17 works means that an entity is not required to separately identify whether it will recover insurance acquisition cash flows at each reporting date. For example, if premiums are lower than the sum of insurance acquisition cash flows and other cash flows incurred in fulfilling the contracts, the entity is not required to determine how much of the premium relates to recovering the insurance acquisition cash flows and how much of the premium relates to recovering the other cash flows incurred in fulfilling the contracts. Paragraph BC180 of the Basis for Conclusions on IFRS 17 explains that this is because the measurement model captures any lack of recoverability automatically by remeasuring the fulfilment cash flows.
15. Insurance revenue is determined by applying both paragraphs B123 and B125 of IFRS 17. Because an entity is not required to separately identify whether it will recover insurance acquisition cash flows, any reduction in the contractual service margin or any loss component recognised because premiums are lower than expected cash outflows (consisting of both insurance acquisition cash flows and other cash flows incurred in fulfilling the contracts) affects insurance revenue recognised applying paragraph B123 of IFRS 17. The staff observe that paragraph B125 of IFRS 17 assumes that the portion of premiums relating to the recovery of insurance acquisition cash flows is equal to the current estimate of total expected insurance acquisition cash flows at each reporting period. Appendix B and Appendix C to this paper include seven examples to illustrate how paragraphs B123 and B125 of IFRS 17 work together.
16. In some cases, the premiums may be or may become less than the insurance acquisition cash flows. In those cases, it is clear that some or all of the insurance acquisition cash flows are not recoverable. Because an entity is not required to separately identify how much of the premium relates to recovering insurance acquisition cash flows, when looking at the amount of insurance revenue determined applying paragraph B125 of IFRS 17 in isolation, the insurance

revenue would appear to be an amount that is higher than the premiums. The staff observe that paragraphs B123 and B125 of IFRS 17 work together to achieve an insurance revenue that reflects the total premium (adjusted for a financing effect and excluding any investment component) as required by paragraph B120 of IFRS 17. Therefore, the insurance revenue determined applying paragraphs B123 and B125 of IFRS 17 should be considered together and not in isolation. Example 4 in Appendix B to this paper demonstrates how paragraphs B123 and B125 of IFRS 17 work together when premium becomes lower than insurance acquisition cash flows.

17. The staff observe that insurance acquisition cash flows may change over time, ie they may be settled or expected to be settled in an amount different than originally expected. Changes in the insurance acquisition cash flows should not impact the overall revenue recognised from a group of insurance contracts as they do not affect the total premiums (adjusted for a financing effect and excluding any investment components). However, the actual amount of insurance acquisition cash flows should be recognised as expenses. The staff observe that paragraph B125 of IFRS 17 assumes that the portion of premiums relating to the recovery of insurance acquisition cash flows is equal to the current estimate of total expected insurance acquisition cash flows at each reporting period.
18. Paragraph B96(b) of IFRS 17 requires changes in the expected future cash flows in the liability for remaining coverage to adjust the contractual service margin of a group of contracts. Therefore, changes in the expected future cash flows related to insurance acquisition cash flows would adjust the contractual service margin. In addition, the amount recognised applying paragraph B125 of IFRS 17 reflects the updated amount. Example 7 in Appendix C to this paper demonstrates how paragraphs B123 and B125 of IFRS 17 work together with a change in the expected future cash flow in the liability for remaining coverage.
19. Experience adjustments for insurance acquisition cash flows are defined as the difference between the estimate at the beginning of the period of the amounts expected in the period and the actual cash flows in the period.

20. Paragraph B96(a) of IFRS 17 requires that experience adjustments arising from premiums that relate to future service and related insurance acquisition cash flows adjust the contractual service margin. These experience adjustments would be accounted for similarly to changes in the expected future cash flows related to insurance acquisition cash flows, discussed in paragraph 18 of this paper.
21. Paragraph B97(c) of IFRS 17 requires that experience adjustments, except those described in paragraph B96(a) of IFRS 17, shall not adjust the contractual service margin because they do not relate to future service. Experience adjustments for insurance acquisition cash flows related to current or past service are therefore included in insurance revenue and insurance service expenses determined applying paragraph B125 of IFRS 17. Example 6 in Appendix C to this paper demonstrates how paragraphs B123 and B125 of IFRS 17 work together with an experience adjustment that relates to current or past service.
22. In summary:
 - (a) any reduction in the contractual service margin or any loss component recognised because premiums are lower than expected cash outflows (consisting of both insurance acquisition cash flows and other cash flows incurred in fulfilling the contracts) affects insurance revenue applying paragraph B123 of IFRS 17 (see paragraph 15 of this paper);
 - (b) changes in expectations for insurance acquisition cash flows adjust the contractual service margin, which is recognised as insurance revenue applying paragraph B123 of IFRS 17 and are also reflected in insurance revenue and insurance service expenses applying paragraph B125 of IFRS 17 (see paragraph 18 of this paper); and
 - (c) experience adjustments relating to insurance acquisition cash flows affect insurance revenue applying B123 of IFRS 17 and insurance revenue and insurance service expenses applying paragraph B125 of IFRS 17 (see paragraph 21 of this paper).

Additional points

23. One of the submissions refers to paragraph B65(h) of IFRS 17 which states that policy administration and maintenance costs include recurring commissions that are expected to be paid to intermediaries if a particular policyholder continues to pay premiums within the boundary of the insurance contract. The staff observe that paragraph B65(h) of IFRS 17 relates to commissions that do not meet the definition of insurance acquisition cash flows.

TRG Discussion**Question to TRG members**

What are your views on the implementation question presented above?

Appendix A—Paragraphs explaining the requirements for insurance acquisition cash flows in the Basis for Conclusions on IFRS 17

A1. Paragraphs BC175–BC180 of the Basis for Conclusions on IFRS 17 explain the measurement approach for insurance acquisition cash flows:

BC175 Entities often incur significant costs to sell, underwrite and start new insurance contracts. These costs are commonly referred to as ‘insurance acquisition cash flows’. Insurance contracts are generally priced to recover those costs through premiums or through surrender charges, or both.

BC176 The measurement approach required in IFRS 17 represents a change from many previous accounting models that measure insurance contract liabilities initially at the amount of the premiums received, with deferral of insurance acquisition cash flows. Such models treat insurance acquisition cash flows as a representation of the cost of a recognisable asset, which, depending on the model, might be described as a contract asset or a customer relationship intangible asset. The Board concluded that such an asset either does not exist, if the entity recovers insurance acquisition cash flows from premiums already received, or relates to future cash flows that are included in the measurement of the contract. The Board noted that an entity typically charges the policyholder a price the entity regards as sufficient to compensate it for undertaking the obligation to pay for insured losses and for the cost of originating the contracts. Thus, a faithful representation of the remaining obligation to pay for insured losses should not include the part of the premium intended to compensate for the cost of originating the contracts.

BC177 Consequently, the Board concluded that an entity should recognise insurance acquisition cash flows as an expense, and should recognise an amount of revenue equal to the portion of the premium that relates to recovering its insurance acquisition cash flows. IFRS 17 achieves this by requiring that the cash flows for a group of insurance contracts include the insurance acquisition cash outflows or inflows associated with the group of contracts (including amounts received or to

be received by the entity to acquire new insurance contracts). This approach reduces the contractual service margin on initial recognition of the group of insurance contracts and has the advantage that the insurance acquisition cash flows are treated the same as other cash flows incurred in fulfilling contracts.

BC178 In many cases, insurance acquisition cash flows occur at the beginning of the coverage period of a group of insurance contracts, before any coverage or other service has been provided. Because insurance revenue is recognised in the same pattern as changes in the liability for remaining coverage, this would mean that some of the insurance revenue would be recognised when the insurance acquisition cash flows are paid, often at the beginning of the coverage period.

BC179 The Board was concerned that recognising insurance revenue at the beginning of the coverage period would be inconsistent with the principles in IFRS 15 because, at the beginning of the coverage period, the entity has not satisfied any of the obligations to the policyholder under the contract. In contrast, IFRS 15 requires an entity to recognise as revenue the consideration received from the customer as it satisfies its performance obligations under the contract. Accordingly, the Board decided to include an exception in IFRS 17 for the treatment of insurance acquisition cash flows so that the premium related to insurance acquisition cash flows is not recognised as revenue when the insurance acquisition cash flows occur, but is separately identified and recognised over the coverage period. IFRS 17 also requires the insurance acquisition cash flows to be recognised as an expense over the same period.

BC180 The requirement to recognise insurance acquisition cash flows as an expense over the coverage period differs from recognising an asset or an explicit or implicit reduction in the carrying amount of the group of insurance contracts. At all times, the liability for the group is measured as the sum of the fulfilment cash flows, including any expected future insurance acquisition cash flows, and the contractual service margin. Because the contractual service margin cannot be less than zero, the

entity need not test separately whether it will recover the insurance acquisition cash flows that have occurred but have not yet been recognised as an expense. The measurement model captures any lack of recoverability automatically by remeasuring the fulfilment cash flows.

A2. On insurance acquisition cash flows included in the measurement of insurance contracts, paragraph BC184 of the Basis for Conclusions on IFRS 17 explains:

The Board also noted that the measurement approach in IFRS 17 automatically recognises as an immediate expense any insurance acquisition cash flows that cannot be recovered from the cash flows of the portfolio of contracts, because such cash flows reduce the contractual service margin below zero and must therefore be recognised as an expense. Hence, no amount can be recognised in the statement of financial position for insurance acquisition cash flows that are not recoverable.

Appendix B—Examples of applying the requirements in paragraphs B123 and B125 of IFRS 17 when insurance acquisition cash flows are not included in expected future cash flows

- B1. This appendix includes four examples demonstrating the treatment of insurance acquisition cash flows that are not included in expected future cash flows. In these four examples all insurance acquisition cash flows are paid on the date of initial recognition and are not adjusted subsequently. The examples are of groups of contracts that are:
- (a) Example 1—onerous at initial recognition;
 - (b) Example 2—profitable at initial recognition and onerous subsequently;
 - (c) Example 3—profitable at initial recognition and subsequently total premiums are less than the sum of expected cash flows and insurance acquisition cash flows paid; and
 - (d) Example 4—profitable at initial recognition and subsequently total premiums are less than insurance acquisition cash flows paid.
- B2. For simplicity, the following assumptions apply in all examples:
- (a) discount rates are 0%;
 - (b) the risk adjustment for non-financial risk (RA) is zero; and
 - (c) unless explicitly stated otherwise, services are provided evenly over the coverage period and claims are incurred evenly over the coverage period.

Example 1—onerous at initial recognition

- B3. On 1 January 2021 an entity issues a set of 100 insurance contracts with a coverage period of one year. At initial recognition, the entity receives premiums of 1,000 and pays insurance acquisition cash flows of 100. The entity expects future cash outflows of 1,000. Applying paragraph 47 of IFRS 17 the entity determines that the set of insurance contracts is onerous and treats them as an

onerous group of insurance contracts applying paragraph 16 of IFRS 17. The contractual service margin (CSM) is zero.

B4. Determining the loss component applying paragraph 47 of IFRS 17:

(a)	Expected future cash flows (CF)	1,000
(b)	Derecognition of any assets or liabilities recognised for insurance acquisition cash flows	0
(c)	Cash flows arising at that date:	
	Insurance acquisition cash flows paid	100
	Premium receipt	(1,000)
Loss recognised in profit or loss immediately		(100)¹

B5. At 31 December 2021, all events have occurred as expected and all claims have been paid. The change in the insurance contract liability following initial recognition can be analysed as follows:

	CF	RA	CSM	Total
1 January 2021	1,000	0	0	1,000
Cash outflows	(1,000)	0	0	(1,000)
31 December 2021	0	0	0	0

B6. The change in the insurance contract liability following initial recognition can also be analysed split between the liability for remaining coverage (LRC) and the liability for incurred claims (LIC) as follows:

¹ Applying IFRS 17 the entity is not required to identify how much of the loss component relates to insurance acquisition cash flows and how much relates to other future expected cash flows.

	LRC		LIC	Total
	Excluding loss component	Loss component		
1 January 2021	900	100	0	1,000
Insurance revenue	(1,000) ²	0	0	(1,000)
Insurance service expenses:				
Incurred claims	0	0	1,000	1,000
Reversal of losses	0	(100)	0	(100)
Amortisation of insurance acquisition cash flows	100	0	0	100
Cash outflows	0	0	(1,000)	(1,000)
31 December 2021	0	0	0	0

B7. Extract of the statement of profit or loss for the year ended 31 December 2021:

Insurance revenue (900 + 100)	1,000
Insurance service expenses (100 + 1,000 – 100 + 100)	(1,100)
Insurance service result	(100)

² Insurance revenue of 900 applying paragraph B123 of IFRS 17 (the total reduction in the liability for remaining coverage excluding the loss component is 900 which reflects insurance services provided in the period) and 100 applying paragraph B125 of IFRS 17.

Example 2—profitable at initial recognition and onerous subsequently

B8. On 1 January 2021 an entity issues a set of 100 insurance contracts with a coverage period of one year. At initial recognition, the entity receives premiums of 1,000 and pays insurance acquisition cash flows of 100. The entity expects future cash outflows of 800. The entity treats the set of contracts as a group of insurance contracts.

B9. Applying paragraph 38 of IFRS 17 the entity measures the contractual service margin at initial recognition:

(a)	Expected future cash flows	800
(b)	Derecognition of any assets or liabilities recognised for insurance acquisition cash flows	0
(c)	Cash flows arising at that date:	
	Insurance acquisition cash flows paid	100
	Premium receipt	(1,000)
Contractual service margin		100

B10. The entity prepares interim reporting for the six months ended 30 June 2021. At 30 June 2021, 600 of claims have been incurred and paid compared to an expected amount of 400 (800/2). The entity changes its expectation for the second half of the year to 600 compared to an expected amount of 400.

B11. The change in the insurance contract liability following initial recognition for the period of six months ended 30 June 2021 can be analysed as follows:

	CF	RA	CSM	Total
1 January 2021	800	0	100	900
Changes related to future service	200	0	(100)	100
Changes related to current service	200	0	0	200
Cash outflows	(600)	0	0	(600)
30 June 2021	600	0	0	600

B12. The change in the insurance contract liability following initial recognition can also be analysed split between the LRC and the LIC as follows:

	LRC		LIC	Total
	Excluding loss component	Loss component		
1 January 2021	900	0	0	900
Insurance revenue	(450) ³	0	0	(450)
Insurance service expenses:				
Incurred claims	0	0	600	600
Recognition of losses	0	100	0	100

³ Insurance revenue of 400 applying paragraph B123 of IFRS 17 (the total reduction in the liability for remaining coverage excluding the loss component is 400 which reflects insurance services provided in the period) and insurance revenue of 50 applying paragraph B125 of IFRS 17.

Amortisation of insurance acquisition cash flows	50	0	0	50
Cash outflows	0	0	(600)	(600)
30 June 2021	500	100	0	600

B13. At 31 December 2021 all events have occurred as expected at 30 June 2021 and all claims have been paid. The change in the insurance contract liability following initial recognition for the period of six months ending 31 December 2021 can be analysed as follows:

	CF	RA	CSM	Total
30 June 2021	600	0	0	600
Cash outflows	(600)	0	0	(600)
31 December 2021	0	0	0	0

B14. The change in the insurance contract liability following initial recognition can also be analysed split between the LRC and the LIC as follows:

	LRC		LIC	Total
	Excluding loss component	Loss component		
30 June 2021	500	100	0	600

Insurance revenue	(550) ⁴	0	0	(550)
Insurance service expenses				
Incurred claims	0	0	600	600
Reversal of losses	0	(100)	0	(100)
Amortisation of insurance acquisition cash flows	50	0	0	50
Cash outflows	0	0	(600)	(600)
31 December 2021	0	0	0	0

B15. Extract of the statement of profit or loss for the year ended 31 December 2021:

Insurance revenue (400 + 50 + 500 + 50)	1,000
Insurance service expenses (600 + 100 + 50 + 600 – 100 + 50)	(1,300)
Insurance service result	(300)

Example 3—profitable at initial recognition and subsequently total premiums are less than the sum of expected cash flows and insurance acquisition cash flows paid

B16. On 1 January 2021 an entity issues a set of 100 insurance contracts with a coverage period of one year. At initial recognition, the entity receives premiums of 1,000 which are contingent on the volume of the insurance coverage. The entity expects that the premium will be 1,000 (ie the entity expects there that will be no refund or extra payment of premium). The entity pays insurance acquisition cash

⁴ Insurance revenue of 500 applying paragraph B123 of IFRS 17 (the total reduction in the liability for remaining coverage excluding the loss component is 500 which reflects insurance services provided in the period) and insurance revenue of 50 applying paragraph B125 of IFRS 17.

flows of 100 which are non-refundable. The entity expects future cash outflows of 800. The entity treats the set of contracts as a group of insurance contracts.

B17. Applying paragraph 38 of IFRS 17 the entity measures the contractual service margin at initial recognition:

(a)	Expected future cash flows	800
(b)	Derecognition of any assets or liabilities recognised for insurance acquisition cash flows	0
(c)	Cash flows arising at that date:	
	Insurance acquisition cash flows paid	100
	Premium receipt	(1,000)
Contractual service margin		100

B18. At 31 December 2021, it is determined that the entity provided only 25% of the insurance coverage it had expected to provide and claims incurred are only 200. The entity pays 950 to the policyholders consisting of a 750 premium refund and 200 claims incurred.

B19. The change in the insurance contract liability following initial recognition can be analysed as follows:

	CF	RA	CSM	Total
1 January 2021	800	0	100	900
Changes related to current service	150	0	(100)	50
Cash outflows	(950)	0	0	(950)
31 December 2021	0	0	0	0

B20. The change in the insurance contract liability following initial recognition can also be analysed split between the LRC and the LIC as follows:

	LRC	LIC	Total
1 January 2021	900	0	900
Insurance revenue	(250) ⁵	0	(250)
Insurance service expenses:			
Incurred claims	0	200	200
Amortisation of insurance acquisition cash flows	100	0	100
Cash outflows	(750)	(200)	(950)
31 December 2021	0	0	0

B21. Extract of the statement of profit or loss for the year ended 31 December 2021:

Insurance revenue (150 + 100)	250
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⁵ Insurance revenue of 150 applying paragraph B123 of IFRS 17 and insurance revenue of 100 applying paragraph B125 of IFRS 17. The total reduction in the liability for remaining coverage is 900. Applying paragraph B123(a)(i) of IFRS 17, the reduction in the liability for remaining coverage that gives rise to insurance revenue excludes changes that result from cash inflows of premiums received. Therefore, the entity must exclude from the change of 900 the decrease of 750 from the refund of premiums. This means that the reduction in the liability for remaining coverage that gives rise to insurance revenue applying paragraph B123 of IFRS 17 is 150 (900 – 750 = 150).

Insurance service expenses (200 + 100)	(300)
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Insurance service result	(50)
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Example 4—profitable at initial recognition and subsequently total premiums are less than insurance acquisition cash flows paid

B22. On 1 January 2021 an entity issues a set of 100 insurance contracts with a coverage period of one year. At initial recognition, the entity receives premiums of 1,000 which are contingent on the volume of the insurance coverage. The entity expects that the premium will be 1,000 (ie the entity expects there that will be no refund or extra payment of premium). The entity pays insurance acquisition cash flows of 200 which are non-refundable. The entity expects future cash outflows of 700. The entity treats the set of contracts as a group of insurance contracts.

B23. Applying paragraph 38 of IFRS 17 the entity measures the contractual service margin at initial recognition:

(a) Expected future cash flows	700
(b) Derecognition of any assets or liabilities recognised for insurance acquisition cash flows	0
(c) Cash flows arising at that date:	
Insurance acquisition cash flows paid	200
Premium receipt	(1,000)
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Contractual service margin	100

B24. At 31 December 2021, it is determined that the entity provided only 10% of the insurance coverage it had expected to provide and incurred claims are only 70.

The entity pays 970 to the policyholders consisting of a 900 premium refund and 70 claims incurred.

B25. The change in the insurance contract liability following initial recognition can be analysed as follows:

	CF	RA	CSM	Total
1 January 2021	700	0	100	800
Changes related to current service	270	0	(100)	170
Cash outflows	(970)	0	0	(970)
31 December 2021	0	0	0	0

B26. The change in the insurance contract liability following initial recognition can also be analysed split between the LRC and the LIC as follows:

	LRC	LIC	Total
1 January 2021	800	0	800
Insurance revenue	(100) ⁶	0	(100)
Insurance service expenses:			
Incurred claims	0	70	70

⁶ Insurance revenue of (100) applying paragraph B123 of IFRS 17 and insurance revenue of 200 applying paragraph B125 of IFRS 17. The total reduction in the liability for remaining coverage is 800. Applying paragraph B123(a)(i) of IFRS 17, the reduction in the liability for remaining coverage that gives rise to insurance revenue excludes changes that result from cash inflows of premiums received. Therefore, the entity must exclude from the change of 800 the decrease of 900 from the refund of premiums. This means that the reduction in the liability for remaining coverage that gives rise to insurance revenue applying paragraph B123 of IFRS 17 is (100) (800 – 900 = -100).

Amortisation of insurance acquisition cash flows	200	0	200
Cash outflows	(900)	(70)	(970)
31 December 2021	0	0	0

B27. Extract of the statement of profit or loss for the year ended 31 December 2021:

Insurance revenue (-100 + 200)	100
Insurance service expenses (70 + 200)	(270)
Insurance service result	(170)

Appendix C—Examples of applying the requirements in paragraphs B123 and B125 of IFRS 17 when insurance acquisition cash flows are included in expected future cash flows

- C1. This appendix includes three examples demonstrating the treatment of insurance acquisition cash flows that are contingent (ie variable) and therefore may change over time. The examples are:
- (a) Example 5—onerous at initial recognition;
 - (b) Example 6—profitable with an experience adjustment relating to insurance acquisition cash flows; and
 - (c) Example 7—profitable with a change in expected future cash flows relating to insurance acquisition cash flows.
- C2. For simplicity, the following assumptions apply in all examples:
- (a) discount rates are 0%;
 - (b) the risk adjustment for non-financial risk (RA) is zero; and
 - (c) unless explicitly stated otherwise, services are provided evenly over the coverage period and claims are incurred evenly over the coverage period.

Example 5—Onerous at initial recognition

- C3. On 1 January 2021 an entity issues a set of 100 insurance contracts with a coverage period of one year. At initial recognition, the entity receives premiums of 1,000. The entity expects future cash outflows of 1,100 including 100 insurance acquisition cash flows. Applying paragraph 47 of IFRS 17 the entity determines that the set of insurance contracts is onerous and treats them as an onerous group of insurance contracts applying paragraph 16 of IFRS 17. The contractual service margin is zero.
- C4. Determining the loss component applying paragraph 47 of IFRS 17:
- (a) Expected future cash flows 1,100

(b) Derecognition of any assets or liabilities recognised for insurance acquisition cash flows 0

(c) Cash flows arising at that date:

Premium receipt (1,000)

Loss recognised in profit or loss immediately (100)

C5. At 31 December 2021, all events have occurred as expected and all claims have been paid. The change in the insurance contract liability following initial recognition can be analysed as follows:

	CF	RA	CSM	Total
1 January 2021	1,100	0	0	1,100
Cash outflows	(1,100)	0	0	(1,100)
31 December 2021	0	0	0	0

C6. The change in the insurance contract liability following initial recognition can also be analysed split between the LRC and the LIC as follows:

	LRC		LIC	Total
	Excluding loss component	Loss component		
1 January 2021	1,000	100	0	1,100
Insurance revenue	(1,000) ⁷	0	0	(1,000)

⁷ Insurance revenue of 900 applying paragraph B123 of IFRS 17 and insurance revenue of 100 applying paragraph B125 of IFRS 17. Applying paragraph B123(a)(v) of IFRS 17, the reduction in the liability for

Insurance service expenses:				
Incurred claims	0	0	1,000	1,000
Reversal of losses	0	(100)	0	(100)
Amortisation of insurance acquisition cash flows	100	0	0	100
Cash outflows	(100)	0	(1,000)	(1,100)
31 December 2021	0	0	0	0

C7. Extract of the statement of profit or loss for the year ended 31 December 2021:

Insurance revenue (900 + 100)	1,000
Insurance service expenses (100 + 1,000 – 100 + 100)	(1,100)
Insurance service result	(100)

Example 6—profitable with an experience adjustment relating to insurance acquisition cash flows

C8. On 1 January 2021 an entity issues a set of 100 insurance contracts with a coverage period of one year. At initial recognition, the entity receives premiums of 1,000. The entity expects future cash outflows of 800 consisting of 700 for expected claims and 100 relating to insurance acquisition cash flows to be paid at

remaining coverage excluding the loss component that gives rise to insurance revenue excludes changes that result from the payment of insurance acquisition cash flows. Therefore, the entity must exclude from the change of 1,000 the decrease of 100 because of the payment of insurance acquisition cash flows. This means that the reduction in the liability for remaining coverage that gives rise to insurance revenue applying paragraph B123 of IFRS 17 is 900 (1,000 – 100 = 900).

the end of the coverage period. The entity treats the set of contracts as a group of insurance contracts.

C9. Applying paragraph 38 of IFRS 17 the entity measures the contractual service margin at initial recognition:

(a)	Expected future cash flows	800
(b)	Derecognition of any assets or liabilities recognised for insurance acquisition cash flows	0
(c)	Cash flows arising at that date:	
	Insurance acquisition cash flows paid	0
	Premium receipt	(1,000)
Contractual service margin		200

C10. At 31 December 2021, all events have occurred as expected and all claims have been paid. However, insurance acquisition cash flows actually paid are 120 compared to the expectation of 100. The change in the insurance contract liability following initial recognition can be analysed as follows:

	CF	RA	CSM	Total
1 January 2021	800	0	200	1,000
Changes related to current service	20	0	(200)	(180)
Cash outflows	(820)	0	0	(820)
31 December 2021	0	0	0	0

C11. The change in the insurance contract liability following initial recognition can also be analysed split between the LRC and the LIC as follows:

	LRC	LIC	Total
1 January 2021	1,000	0	1,000
Insurance revenue	(1,000) ⁸	0	(1,000)
Insurance service expenses:			
Incurred claims	0	700	700
Amortisation of insurance acquisition cash flows	120	0	120
Cash outflows	(120)	(700)	(820)
31 December 2021	0	0	0

C12. Extract of the statement of profit or loss for the year ended 31 December 2021:

Insurance revenue (880 + 120)	1,000
Insurance service expenses (700 + 120)	(820)
Insurance service result	180

⁸ Insurance revenue of 880 applying paragraph B123 of IFRS 17 and insurance revenue of 120 applying paragraph B125 of IFRS 17. The total reduction in the liability for remaining coverage is 1,000. Applying paragraph B123(a)(v) of IFRS 17, the reduction in the liability for remaining coverage that gives rise to insurance revenue excludes changes that result from the payment of insurance acquisition cash flows. Therefore, the entity must exclude from the change of 1,000 the decrease of 120 from the payment of insurance acquisition cash flows. This means that the reduction in the liability that gives rise to insurance revenue applying paragraph B123 of IFRS 17 is 880 (1,000 – 120 = 880).

Example 7—profitable with change in expected future cash flows relating to insurance acquisition cash flows

C13. On 1 January 2021 an entity issues a set of 100 insurance contracts with a coverage period of one year. At initial recognition, the entity receives premiums of 1,000. The entity expects future cash outflows of 800 consisting of 700 for expected claims (paid as incurred) and 100 relating to insurance acquisition cash flows (to be paid at the end of the coverage period). The entity treats the set of contracts as a group of insurance contracts.

C14. Applying paragraph 38 of IFRS 17 the entity measures the contractual service margin at initial recognition:

(a)	Expected future cash flows	800
(b)	Derecognition of any assets or liabilities recognised for insurance acquisition cash flows	0
(c)	Cash flows arising at that date:	
	Insurance acquisition cash flows paid	0
	Premium receipt	(1,000)

	Contractual service margin	200
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C15. The entity prepares interim reporting for the six months ended 30 June 2021. At 30 June 2021, all claim events have occurred as expected and been paid and the entity makes no changes to its estimates of future cash flows relating to claims. However, the entity now expects to pay 120 for insurance acquisition cash flows at the end of the year compared to the original expectation of 100.

C16. The change in the insurance contract liability following initial recognition for the period of six months ending 30 June 2021 can be analysed as follows:

	CF	RA	CSM	Total
1 January 2021	800	0	200	1,000
Changes related to future service	20	0	(20)	0
Changes related to current service	0	0	(90)	(90)
Cash outflows	(350)	0	0	(350)
30 June 2021	470	0	90	560

C17. The change in the insurance contract liability following initial recognition can also be analysed split between the LRC and the LIC as follows:

	LRC	LIC	Total
1 January 2021	1,000	0	1,000
Insurance revenue	(500) ⁹	0	(500)
Insurance service expenses:			
Incurred claims	0	350	350
Amortisation of insurance acquisition cash flows	60	0	60
Cash outflows	0	(350)	(350)
30 June 2021	560	0	560

⁹ Insurance revenue of 440 applying paragraph B123 of IFRS 17 (the total reduction in the liability for remaining coverage is 440 which reflects insurance services provided in the period) and insurance revenue of 60 applying paragraph B125 of IFRS 17 (allocated in a systematic way on the basis of the passage of time).

C18. At 31 December 2021, all events have occurred as expected at 30 June 2021, all claims have been paid and insurance acquisition cash flows of 120 have been paid. The change in the insurance contract liability following initial recognition can be analysed as follows:

	CF	RA	CSM	Total
30 June 2021	470	0	90	560
Changes related to current service	0	0	(90)	(90)
Cash outflows	(470)	0	0	(470)
31 December 2021	0	0	0	0

C19. The change in the insurance contract liability following initial recognition can also be analysed split between the LRC and the LIC as follows:

	LRC	LIC	Total
30 June 2021	560	0	560
Insurance revenue	(500) ¹⁰	0	(500)
Insurance service expenses:			
Incurred claims	0	350	350

¹⁰ Insurance revenue of 440 applying paragraph B123 of IFRS 17 and insurance revenue of 60 applying paragraph B125 of IFRS 17 (allocated in a systematic way on the basis of the passage of time). The total reduction in the liability for remaining coverage is 560. Applying paragraph B123(a)(v) of IFRS 17, the reduction in the LRC that gives rise to insurance revenue excludes changes that result from the payment of insurance acquisition cash flows. Therefore, the entity must exclude from the change of 560 the decrease of 120 from the payment of insurance acquisition cash flows. This means that the reduction in the liability for remaining coverage that gives rise to insurance revenue applying paragraph B123 of IFRS 17 is 440 (560 – 120 = 440).

Amortisation of insurance acquisition cash flows	60	0	60
Cash outflows	(120)	(350)	(470)
31 December 2021	0	0	0

C20. Extract of the statement of profit or loss for the year ended 31 December 2021:

Insurance revenue (440 + 60 + 440 + 60)	1,000
Insurance service expenses (350 + 60 + 350 + 60)	(820)
Insurance service result	180

STAFF PAPER

September 2018

Project	Transition Resource Group for IFRS 17 <i>Insurance Contracts</i>		
Paper topic	Premium waivers		
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This paper has been prepared for discussion at a public meeting of the Transition Resource Group for IFRS 17 *Insurance Contracts* and does not represent the views of any individual member of the International Accounting Standards Board or staff. Comments on the application of IFRS[®] Standards do not purport to set out acceptable or unacceptable application of IFRS Standards.

Introduction

1. We have received a submission on whether terms in an insurance contract that waive premiums in specified circumstances create insurance risk. The identification of insurance risk is necessary to apply various aspects of IFRS 17 *Insurance Contracts*, including determining the coverage period.
2. The objective of this paper is to provide background and an accounting analysis to support discussion at the Transition Resource Group for IFRS 17 (TRG).

Structure of the paper

3. This paper includes the following:
 - (a) background information;
 - (b) implementation question; and
 - (c) review of accounting requirements.

Background information

4. Appendix A of IFRS 17 defines insurance risk as:

Risk, other than financial risk, transferred from the holder of a contract to the issuer.
5. Paragraph B11 of IFRS 17 states:

Insurance risk is the risk the entity accepts from the policyholder. This means the entity must accept, from the policyholder, a risk to which the policyholder was already exposed. Any new risk created by the contract for the entity or the policyholder is not insurance risk.
6. Paragraph B13 of IFRS 17 states:

Some contracts require a payment if a specified uncertain future event occurs, but do not require an adverse effect on the policyholder as a precondition for the payment. This type of contract is not an insurance contract even if the holder uses it to mitigate an underlying risk exposure. For example, if the holder uses a derivative to hedge an underlying financial or non-financial variable correlated with the cash flows from an asset of the entity, the derivative is not an insurance contract because the payment is not conditional on whether the holder is adversely affected by a reduction in the cash flows from the asset. The definition of an insurance contract refers to an uncertain future event for which an adverse effect on the policyholder is a contractual precondition for

payment. A contractual precondition does not require the entity to investigate whether the event actually caused an adverse effect, but it does permit the entity to deny the payment if it is not satisfied that the event did cause an adverse effect.

7. Paragraphs B21(a)–(b) of IFRS 17 state:

The additional amounts described in paragraph B18 refer to the present value of amounts that exceed those that would be payable if no insured event had occurred (excluding scenarios that lack commercial substance). Those additional amounts include claims handling and assessment costs, but exclude:

- (a) the loss of the ability to charge the policyholder for future service. For example, in an investment-linked life insurance contract, the death of the policyholder means that the entity can no longer perform investment management services and collect a fee for doing so. However, this economic loss for the entity does not result from insurance risk, just as a mutual fund manager does not take on insurance risk in relation to the possible death of a client. Consequently, the potential loss of future investment management fees is not relevant when assessing how much insurance risk is transferred by a contract.
- (b) a waiver, on death, of charges that would be made on cancellation or surrender. Because the contract brought those charges into existence, their waiver does not compensate the policyholder for a pre-existing risk. Consequently, they are not relevant when assessing how much insurance risk is transferred by a contract.

Implementation question

8. The submission discusses a term of an insurance contract that allows a policyholder to avoid paying premiums in specified circumstances, for example, if the policyholder has been disabled for six consecutive months. The policyholder continues to receive the benefits originally promised under the insurance contract. This term is referred to in this paper as a premium waiver.
9. The insured event covered under the contract (the primary coverage) differs from the event that entitles the policyholder to a premium waiver. For example, the primary coverage might be a term life contract that covers the mortality risk of a policyholder, with premiums waived if the policyholder becomes unable to work because of a disability.
10. The submission asks whether the risk related to the premium waiver is a pre-existing risk of the policyholder transferred to the entity by the contract and is therefore an insurance risk, or a new risk created by the contract applying paragraphs B11 and B21 of IFRS 17.

Review of accounting requirements

11. As a preliminary note, the staff observe that the definition of insurance risk in IFRS 17 has not changed from IFRS 4 *Insurance Contracts* and it is therefore not expected that the practice of determining whether a risk is an insurance risk would change.
12. The possible waiver of premiums is caused by an uncertain future event (for example, the policyholder being disabled for a period of six consecutive months). That uncertain future event results in an adverse effect on the policyholder such as the loss of income. To the extent of the premiums payable, that risk is transferred to the entity which has to provide benefits under the contract for the primary coverage without being paid premiums.

13. The examples given in the submission of events that would trigger a waiver of premiums are disability, critical illness and severe injury. The staff observe that the risk of these events occurring exists before the contract is issued. They are not created by the contract, and the contract does not increase their potential adverse effects. Further, the occurrence of the events that trigger a waiver of premiums are contractual preconditions without which the entity can deny the premium waiver.
14. The staff also observe that a waiver of premiums differs from the situations discussed in paragraphs B21(a)–(b) of IFRS 17:
- (a) in paragraph B21(a) of IFRS 17, the death of the policyholder means the entity does not receive future premiums. However, it also means the entity does not have to pay additional amounts or provide service in the future. The policyholder has not transferred risk to the entity.
 - (b) in paragraph B21(b) of IFRS 17, the death of the policyholder means the policyholder does not pay charges that would be made on cancellation or surrender. Those charges relate to ending the contract, not continuing the provision of benefits under the contract. Before entering the contract, the policyholder had pre-existing risk of death however had no risk corresponding to the charges (before the contract the policyholder does not have to pay charges to terminate the contract, after entering into the contract, the policyholder would have to pay such charges if they were not waived on death). In contrast, with the premium waiver, the policyholder had the pre-existing risk of the event that triggers the waiver of the premiums and no additional adverse consequence relating to that risk is created by the contract itself (before the contract the policyholder has to pay premiums to obtain insurance coverage, after entering into the contract, the policyholder would have to pay premiums to obtain coverage if they were not waived on death). Another way of explaining this difference is that the death of the policyholder is not a contractual precondition for the waiver of the

termination charges—they could also be waived if the policyholder does not terminate the contract early. Because the charges can be avoided if the policyholder does not die, they are an additional adverse effect created by the contract if they die.

15. In summary, the staff observe that a waiver of premiums if a specified event occurs creates insurance risk. The staff also observe that the consequences of this are:
- (a) the inclusion of such a waiver in an investment contract makes the investment contract an insurance contract; and
 - (b) the inclusion of such a waiver in a contract that would be an insurance contract without the waiver may affect the quantity of benefits provided by the contract and the coverage period, both of which could affect the recognition of the contractual service margin in profit or loss. The recognition of the contractual service margin was discussed in Agenda Paper 5 of the February 2018 TRG meeting and Agenda Paper 5 of the May 2018 TRG meeting.

TRG discussion

Question to TRG members

What are your views on the implementation question presented above?

STAFF PAPER

September 2018

Project	Transition Resource Group for IFRS 17 <i>Insurance Contracts</i>		
Paper topic	Group insurance policies		
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Introduction

1. We have received a submission about the boundary of a contract for an arrangement between an entity and an association or a bank under which the entity provides insurance coverage to members of an association or to customers of a bank.
2. The objective of the paper is to provide background and an accounting analysis to support discussion at the Transition Resource Group for IFRS 17 *Insurance Contracts* (TRG).

Structure of the paper

3. This paper includes the following:
 - (a) background information;
 - (b) implementation question; and
 - (c) review of accounting requirements.

Background information

4. Paragraph 2 of IFRS 17 states:

An entity shall consider its substantive rights and obligations, whether they arise from a contract, law or regulation, when applying IFRS 17. A contract is an agreement between two or more parties that creates enforceable rights and obligations. Enforceability of the rights and obligations in a contract is a matter of law. Contracts can be written, oral or implied by an entity's customary business practices. Contractual terms include all terms in a contract, explicit or implied, but an entity shall disregard terms that have no commercial substance (ie no discernible effect on the economics of the contract). Implied terms in a contract include those imposed by law or regulation. The practices and processes for establishing contracts with customers vary across legal jurisdictions, industries and entities. In addition, they may vary within an entity (for example, they may depend on the class of customer or the nature of the promised goods or services).

5. Paragraph 34 of IFRS 17 states:

Cash flows are within the boundary of an insurance contract if they arise from substantive rights and obligations that exist during the reporting period in which the entity can compel the policyholder to pay the premiums or in which the entity has a substantive obligation to provide the policyholder with services (see paragraphs B61–B71). A substantive obligation to provide services ends when:

- (a) the entity has the practical ability to reassess the risks of the particular policyholder and, as a result, can set a price or level of benefits that fully reflects those risks; or
- (b) both of the following criteria are satisfied:
 - (i) the entity has the practical ability to reassess the risks of the portfolio of insurance contracts that contains the contract and, as a result, can set a price or level of benefits that fully reflects the risk of that portfolio; and
 - (ii) the pricing of the premiums for coverage up to the date when the risks are reassessed does not take into account the risks that relate to periods after the reassessment date.

6. Appendix A of IFRS 17 defines an insurance contract as:

A contract under which one party (the issuer) accepts significant insurance risk from another party (the policyholder) by agreeing to compensate the policyholder if a specified uncertain future event (the insured event) adversely affects the policyholder.

7. Appendix A of IFRS 17 defines a policyholder as:

A party that has a right to compensation under an insurance contract if an insured event occurs.

Implementation question

8. The submission describes an arrangement between an entity and an association or a bank (referred to as the ‘group insurance policy’ in this paper). Under a group insurance policy an entity provides insurance coverage to members of an association or to customers of a bank (members or customers that purchase insurance coverage are referred to as ‘certificate holders’ in this paper).
9. The entity has a right to terminate the group insurance policy at any time with a notice period of 90 days which, in turn, terminates the insurance coverage for all certificate holders.
10. The submission asks whether cash flows related to periods after the notice period of 90 days are within the boundary of an insurance contract. As part of the analysis, the submission considers whether the policyholder of an insurance contract as defined in IFRS 17 is:
 - (a) the bank or association; or
 - (b) the certificate holder.
11. The submission describes two different types of group insurance policies:
 - (a) a group association policy; and
 - (b) a group creditor policy.
12. It is assumed that for the examples in the submission the entity cannot compel the certificate holders to pay premiums.

Group association policy

13. An entity has a group association policy with an association or bank that allows the entity to market and sell insurance coverage to individuals that are members of the association (for example, members of an automobile association) or customers of a bank. The facts and circumstances are as follows:

- (a) legally, the contract is between the entity and the association or bank; however, the insurance coverage for each certificate holder is priced as if it were an individual contract, considering all projected future cash flows (including claims, lapses and expenses);
- (b) the insurance coverage is optional for each individual (ie the association or bank does not require them to take out the coverage);
- (c) other than being a member of the association or customer of the bank, the individuals are not related to one another;
- (d) the group association policies charge step-rated premiums (for example, life insurance contracts premiums increase across periods of coverage with the age of the policyholder);
- (e) the entity and the association or bank each have the right to terminate the group association policy going forward at any time with a 90-day notice period, thus terminating the insurance coverage for all certificate holders;
- (f) certificate holders have an expectation that the group association policy will not be terminated earlier than the end of the contract term (for example, for life insurance contracts the full term of a contract would be the lifetime of the certificate holder or until the certificate holder reaches a specified age);
- (g) the entity cannot terminate coverage for a specific certificate holder (ie the entity has two options: to terminate coverage for all certificate holders or not to terminate coverage for any certificate holders);
- (h) the entity cannot reprice premiums; and
- (i) claims are payable directly to the certificate holder or their beneficiaries.

Group creditor policy

14. An entity has a group creditor policy with a bank that allows the entity to market and sell insurance coverage to individuals that are customers of the bank. The facts and circumstances of the group creditor policy are similar to the group association policy and the facts and circumstances described in paragraph 13(a)–(h) of this paper also apply to the group creditor policy. The differences between the group association policy and the group creditor policy are that for the group creditor policy:
- (a) the insurance coverage provided to the certificate holder is linked to the remaining outstanding balance of any loan or mortgage issued by the bank to the certificate holder (for example, the contract duration is limited to the earlier of the date that the loan is paid off or the certificate holder reaches a specified age); and
 - (b) if the certificate holder had not taken out the insurance coverage, the certificate holder or their beneficiaries would be liable to pay the outstanding balance of any loan or mortgage to the bank. However, with the insurance coverage provided to the certificate holder by the entity, the entity pays the remaining outstanding balance directly to the bank when an insured event occurs.

Review of accounting requirements

Identifying the policyholder

15. IFRS 17 defines an insurance contract as a contract under which one party (the issuer) accepts significant insurance risk from another party (the policyholder) by agreeing to compensate the policyholder if a specified uncertain future event (the insured event) adversely affects the policyholder. The policyholder is defined as a party that has a right to compensation under an insurance contract if an insured event occurs, ie the beneficiary.

16. IFRS 17 defines a policyholder by its right to compensation if it is adversely affected by an insured event. The staff observe that this is the case regardless of whether that compensation is received directly or indirectly by paying amounts on its behalf.¹ Therefore, for both group insurance policies described in the submission, the certificate holder is a policyholder for the purpose of applying IFRS 17.
17. For the group creditor policy, the submission questions whether the bank is the policyholder to an insurance contract because claims are paid directly to the bank. The staff observe that the fact that the bank is paid directly if a specified future event occurs does not mean that the bank is the policyholder for the purpose of applying IFRS 17. This is because the bank is being paid amounts due to it on behalf of its customer, rather than being compensated for a loss event. It is the customer that benefits from the coverage because the customer's debt is paid.

Identifying the insurance contract

18. The legal form of a group insurance policy as described in the submission is a single contract between an entity and an association or a bank. A contract with the legal form of a single contract would generally be considered to be a single contract for the purpose of applying IFRS 17. However, there might be circumstances in which the legal form of a single contract does not reflect the substance of its contractual rights and obligations.²
19. For group insurance policies, as described in the submission, an entity should consider whether the arrangement reflects a single insurance contract (with all certificate holders) or multiple insurance contracts (with each certificate holder).

¹ This is similar to, for example, death cover for which claim amounts are paid out to the beneficiaries of the policyholder.

² Agenda Paper 1 *Separation of insurance components of a single contract* was discussed at the February 2018 TRG meeting.

20. Consistent with previous TRG discussions, the staff observe that overriding the contract unit of account presumption by separating components of a single contract involves significant judgement and careful consideration of all facts and circumstances. The staff view is that, for both types of group insurance policy described in the submission, the following facts and circumstances are indicative that the arrangement reflects multiple insurance contracts (ie an insurance contract with each certificate holder) for the purpose of applying IFRS 17:
- (a) the insurance coverage is priced and sold separately;
 - (b) other than being members of the association or customers of the bank the individuals are not related to one another; and
 - (c) purchasing the insurance coverage is an option for each individual.
21. The staff view is that the rights of the entity and the association/bank to terminate the group insurance policy does not, in itself, indicate that the arrangement is a single contract for the purpose of applying IFRS 17.

Determining the boundary of an insurance contract

22. The submission asks whether, applying paragraph 34 of IFRS 17, the boundary of the contract reflects the entity's substantive right to terminate the group insurance policy at any time with a 90-day notice period which, in turn, terminates the insurance coverage for all certificate holders.
23. The staff observe that an entity should assess the boundary of each insurance contract with each certificate holder based on the outcome of the analysis discussed in paragraphs 18–21 of this paper. Paragraph BC160(a) of the Basis for Conclusions on IFRS 17 explains that the outer limit of an existing contract is the point at which the entity is no longer required to provide coverage. In accordance with paragraph 34 of IFRS 17, the staff view is that an entity's substantive obligation to provide services under a contract ends at the point that the entity can terminate the contract. Therefore, for the examples in the submission, the entity's substantive obligation ends after 90 days and cash flows within the contract

boundary are those related the obligation to provide service over the period of 90 days.³

24. The staff observe that the certificate holder's expectation that the group insurance policy will not be terminated earlier than the end of the contract term is not relevant to the assessment of the contract boundary applying paragraph 34 of IFRS 17.

TRG discussion

Question to TRG members

What are your views on the implementation question presented above?

³ The subsequent treatment for cash flows that are outside the contract boundaries is discussed in Agenda Paper 5 *Cash flows that are outside the contract boundary at initial recognition* of the September 2018 TRG meeting.

STAFF PAPER

September 2018

Project	Transition Resource Group for IFRS 17 <i>Insurance Contracts</i>		
Paper topic	Industry pools managed by an association		
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Introduction

1. We have received a submission about the level at which the risk adjustment for non-financial risk should be determined for insurance contracts that are within industry pools managed by an association.
2. The objective of the paper is to provide background and an accounting analysis to support discussion at the Transition Resource Group for IFRS 17 *Insurance Contracts* (TRG).

Structure of the paper

3. This paper includes the following:
 - (a) background information;
 - (b) implementation question; and
 - (c) review of accounting requirements.
4. There are two appendices to this paper:
 - (a) Appendix A—Extract: summary of the TRG meeting held on 2 May 2018 on determining the risk adjustment for non-financial risk in a group of entities; and
 - (b) Appendix B—Examples of industry pools described in the submission.

Background information

5. Paragraph 2 of IFRS 17 states:

An entity shall consider its substantive rights and obligations, whether they arise from a contract, law or regulation, when applying IFRS 17. A contract is an agreement between two or more parties that creates enforceable rights and obligations. Enforceability of the rights and obligations in a contract is a matter of law. Contracts can be written, oral or implied by an entity's customary business practices. Contractual terms include all terms in a contract, explicit or implied, but an entity shall disregard terms that have no commercial substance (ie no discernible effect on the economics of the contract). Implied terms in a contract include those imposed by law or regulation. The practices and processes for establishing contracts with customers vary across legal jurisdictions, industries and entities. In addition, they may vary within an entity (for example, they may depend on the class of customer or the nature of the promised goods or services).

6. Paragraph 37 of IFRS 17 states:

An entity shall adjust the estimate of the present value of the future cash flows to reflect the compensation that the entity requires for bearing the uncertainty about the amount and timing of the cash flows that arises from non-financial risk.

7. Appendix A of IFRS 17 defines an insurance contract as:

A contract under which one party (the issuer) accepts significant insurance risk from another party (the policyholder) by agreeing to compensate the policyholder if a specified uncertain future event (the insured event) adversely affects the policyholder.

8. Appendix A of IFRS 17 defines the risk adjustment for non-financial risk as:

The compensation an entity requires for bearing the uncertainty about the amount and timing of the cash flows that arises from non-financial risk as the entity fulfils insurance contracts.

9. Paragraph B87 of IFRS 17 states:

[...] the risk adjustment for non-financial risk conveys information to users of financial statements about the amount charged by the entity for the uncertainty arising from non-financial risk about the amount and timing of cash flows.

10. Paragraph B88 of IFRS 17 states:

Because the risk adjustment for non-financial risk reflects the compensation the entity would require for bearing non-financial risk arising from the uncertain amount and timing of the cash flows it also reflects:

- (a) the degree of diversification benefit the entity includes when determining the compensation it requires for bearing that risk; [...]

11. In May 2018 TRG members discussed a related topic in Agenda Paper 2

Determining the risk adjustment for non-financial risk in a group of entities. An

extract from the summary of the May 2018 TRG meeting is included in Appendix A to this paper.

Implementation question

12. In the submission, all entities issuing automobile insurance contracts in a specific jurisdiction are required by law to be a member of an association. The purpose of the association is to ensure that insurance coverage is provided to policyholders that cannot get that insurance in the voluntary market. The association manages two types of industry pools:
 - (a) Pool 1—in which some members are appointed to issue contracts on behalf of all of the members; and
 - (b) Pool 2—to which members can choose to transfer some insurance contracts they have issued.
13. The results of each industry pool are allocated to all the members of the association based on a specific sharing formula (generally based on market share). The submission notes that applying existing practice each member accounts for their share in the pool in their own financial statements as direct business. The full fact pattern described in the submission is included in Appendix B to this paper.
14. For insurance contracts that are within either of the two industry pools described, the submission asks whether the risk adjustment for non-financial risk should be determined at either:
 - (a) the association level; or
 - (b) the individual member entity level.
15. The submission also asks whether the risk adjustment for non-financial risk could be measured differently in the financial statements of the members when compared to the financial statements of the association.

Review of accounting requirements

Accounting by members for a share in the results of an industry pool

16. IFRS 17 applies to insurance contracts within its scope. IFRS 17 defines an insurance contract as:

A contract under which one party (the issuer) accepts significant insurance risk from another party (the policyholder) by agreeing to compensate the policyholder if a specified uncertain future event (the insured event) adversely affects the policyholder.

17. In some cases, the parties to the contract are clear from the legal form of the contract. In other cases, the terms of the contract require analysis to identify the substance of the rights and obligations—including who is the issuer of the contract. For example, for insurance contracts in an industry pool the issuer could be:

- (a) the individual member entity that writes the contracts;
- (b) each member entity for its respective share of each contract in the pool;
- or
- (c) the collective of all member entities.

18. The staff observe that if the individual member entity that writes the contract is the issuer, that entity shall account for the contract applying IFRS 17. IFRS 17 applies to insurance contracts issued by an entity and does not have specific requirements when an insurance contract is issued by more than one entity. Entities should assess whether the arrangement under which an insurance contract is issued by more than one entity would be considered a joint arrangement in the scope of IFRS 11 *Joint Arrangements*. If the arrangement is within the scope of IFRS 11, entities are required to determine, applying the requirements of IFRS 11, whether the arrangement would meet the definition of a joint venture or a joint operation. Applying IFRS 11:

- (a) if the arrangement meets the definition of a joint venture, each party that is a joint venturer is required by paragraph 24 of IFRS 11 to account for its interest using the equity method in accordance with IAS 28 *Investments in Associates and Joint Ventures*.¹
 - (b) if the arrangement meets the definition of a joint operation, each party that is a joint operator is required by paragraph 20 of IFRS 11 to recognise in relation to its interest in the joint operation:
 - (i) its assets, including its share of any assets held jointly;
 - (ii) its liabilities, including its share of any liabilities incurred jointly;
 - (iii) its revenue from the sale of its share of the output arising from the joint operation;
 - (iv) its share of the revenue from the sale of the output by the joint operation; and
 - (v) its expenses, including its share of any expenses incurred jointly.
19. The staff observe that an arrangement under which an insurance contract is issued by more than one entity may not meet the definition of joint control as required by paragraph 7 of IFRS 11 and therefore would not be within the scope of IFRS 11.
20. Applying IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*, in the absence of an IFRS Standard that specifically applies to a transaction, other event or condition, management shall use its judgement in developing and applying an accounting policy that results in information that is relevant to the economic decision-making needs of users and reliable. An entity first refers to and considers the applicability of other IFRS Standards dealing with similar and related issues. Arrangements under which a contract is issued by more than one entity may share similar characteristics to joint arrangements as

¹ Applying paragraph 18 of IAS 28, an entity that is a venture capital organisation, or a mutual fund, unit trust and similar entities including investment-linked insurance funds may elect to measure an investment in a joint venture at fair value through profit or loss in accordance with IFRS 9 *Financial Instruments*.

described in IFRS 11 and therefore it may be appropriate to consider the requirements in IFRS 11 in applying paragraph 11 of IAS 8.

21. In the absence of an IFRS Standard that specifically applies to a transaction, other event or condition or that deals with similar and related issues, an entity should consider the principles in the *Conceptual Framework for Financial Reporting*. Applying the *Conceptual Framework*, an entity is required to reflect the substance of its contractual rights and contractual obligations. The staff observe that this may result in an approach similar to that used applying existing practice as noted in the submission.
22. In some cases, an individual member entity may write the contract and then subsequently transfer the contract to the industry pool. If that member entity is the issuer of the contract applying IFRS 17, the entity should consider whether the transfer:
 - (a) is a contract that meets the definition of a reinsurance contract applying IFRS 17; or
 - (b) extinguishes the individual member's obligations to the policyholder applying paragraph 74 of IFRS 17.
23. The staff observe that the analysis of whether either (a) or (b) in paragraph 22 of this paper applies and the resulting accounting may differ depending on whether the party that is receiving the contract in the transfer is:
 - (a) each member entity for its respective share of each contract in the pool;
or
 - (b) the collective of all member entities.

At which level should the risk adjustment for non-financial risk be determined?

24. IFRS 17 is applied by an entity that is the issuer of insurance contracts as defined in Appendix A of IFRS 17. The issuer of the contract is the party that recognises

revenue from the contract, a component of which is the amounts related to the risk adjustment for non-financial risk. Therefore:

- (a) if the contracts are issued by the individual member entity that writes the contracts, revenue is recognised by that member entity applying IFRS 17, and that member entity determines the risk adjustment for non-financial risk. This may be the case when an individual member entity is identified as the issuer of a contract and then subsequently transfers the contract to an industry pool (see paragraphs 22–23 of this paper).
- (b) if the contracts are considered to be issued by more than one entity (ie issued by each member for its respective share or issued by the collective of all members as noted in paragraphs 17(b)–(c) of this paper) revenue is also shared. Therefore, the staff view is that the risk adjustment for non-financial risk is determined by all member entities together. This would apply to an entity's share in the results of an industry pool (see paragraphs 18–21 of this paper).

- 25. Applying paragraph B88 of IFRS 17, when determining the risk adjustment for non-financial risk, the entity (ie the issuer) is required to consider the degree of diversification benefit that it includes when determining the compensation it requires for bearing non-financial risk.
- 26. The submission asks if the risk adjustment for non-financial risk can be measured differently at different reporting levels for the same contracts. The staff view is that IFRS 17 requires that for one group of insurance contracts there is one risk adjustment for non-financial risk which reflects the degree of risk diversification that the issuer of the contract considers in determining the compensation required for bearing the non-financial risk. The staff note that some TRG members interpret the requirements in IFRS 17 differently (see Appendix A to this paper).

TRG Discussion

Question to TRG members

What are your views on the implementation question presented above?

Appendix A—Extract: summary of the TRG meeting held on 2 May 2018 on determining the risk adjustment for non-financial risk in a group of entities

Determining the risk adjustment for non-financial risk in a group of entities (Agenda Paper 2)

- A1. Agenda Paper 2 addresses a submission about the level at which the risk adjustment for non-financial risk is required to be determined.
- A2. The first question is whether, in the individual financial statements of the subsidiary, the risk adjustment for non-financial risk for groups of insurance contracts issued by the subsidiary should reflect the degree of risk diversification available only to the consolidated group as a whole.
- A3. The second question is whether, in the consolidated financial statements of the group of entities, the risk adjustment for non-financial risk for groups of insurance contracts issued by entities in the group should reflect the degree of risk diversification that is available only to the consolidated group as a whole.
- A4. TRG members discussed the analysis in Agenda Paper 2 and observed that:
- (a) IFRS 17 does not specify the level at which to determine the risk adjustment for non-financial risk.
 - (b) in the individual financial statements of the issuing entity, the degree of risk diversification that occurs at a level higher than the issuing entity level is required to be considered in the determination of the risk adjustment for non-financial risk if, and only if, it is considered when determining the compensation the issuing entity would require for bearing non-financial risk related to insurance contracts it issues. Equally, risk diversification that occurs at a level higher than the issuing entity level must not be considered when determining the risk adjustment for non-financial risk if it is not considered when determining the compensation, the issuing entity would require for bearing non-financial risk related to insurance contracts it issues.

- A5. Some TRG members agreed with the staff analysis that only the issuing entity that is party to the contract determines the compensation the entity would require for bearing non-financial risk related to insurance contracts that the entity issues. Therefore, for a group of insurance contracts issued by an entity that is party to the contracts, there is one risk adjustment for non-financial risk. This means that for a group of insurance contracts the risk adjustment for non-financial risk at the consolidated group level is the same as the risk adjustment for non-financial risk at the individual issuing entity level.
- A6. The analysis in paragraph A5 of this paper precludes different measurement of the risk adjustment for non-financial risk for a group of insurance contracts at different reporting levels. Some TRG members commented that they could read the requirements in IFRS 17 differently. Those TRG members read the requirements as requiring different measurement of the risk adjustment for non-financial risk for a group of insurance contracts at different reporting levels if the issuing entity would require different compensation for bearing non-financial risk than the consolidated group would require. TRG members observed that:
- (a) if the risk adjustment for non-financial risk is determined differently at different reporting levels in the group structure there could be multiple risk adjustments for non-financial risk for the same group of insurance contracts, depending on the reporting level;
 - (b) applying the requirements in IFRS 17 as analysed by the staff in paragraph A5 of this paper would be more practical to implement; and
 - (c) a group of entities must apply the requirements consistently across all groups of insurance contracts.
- A7. TRG members also observed that in some cases the compensation that an entity requires for bearing non-financial risk could be evidenced by capital allocation in a group of entities.

Appendix B—Examples of industry pools described in the submission

- B1. The submission describes two industry pools in a specific jurisdiction. In that specific jurisdiction, all entities issuing automobile insurance contracts are required by law to be a member of an association. The purpose of the association is to ensure that insurance coverage is provided to policyholders that cannot get that insurance in the voluntary market. The association manages two types of industry pools:
- (a) Pool 1—in which some members are appointed to issue contracts on behalf of all of the members; and
 - (b) Pool 2—to which members can choose to transfer some insurance contracts they have issued.
- B2. The operations of the association are determined by articles that are enforceable by law.
- B3. The association, itself, is not an entity that issues insurance contracts.
- B4. For both industry pools managed by the association:
- (a) all members share in the results of the industry pool based on specific sharing formulae (generally based on market share); and
 - (b) if a member is unable to meet their obligations to the industry pool, the remaining members are required to fulfil those obligations.

Pool 1—in which some members are appointed to issue contracts on behalf of all of the members

- B5. The association contracts with some members to write insurance contracts under their own name on behalf of the association as a whole. The association determines the rates that are charged to policyholders. In determining those rates, the association aims to achieve a specified return on equity that is set by the Board of Directors of the association. The member that writes the contract is responsible for managing the contract including any associated claims until all claims are

resolved. The member passes the premiums to the pool and claims paid by the member are reimbursed by the pool as they occur. The member also receives an administration fee for their services.

B6. Existing practice:

- (a) the association establishes an insurance contract liability and provides information to the members.
- (b) the member entities treat the insurance service result allocated to them as direct business (ie as if they had issued that portion of business themselves). Each member reports an insurance contract liability, premiums, claims and expenses incurred.
- (c) the member that writes the contracts on behalf of the association reflects the direct expenses incurred in providing services to the association and the revenue received from the association for providing those services (administration fee).

B7. The staff observe that the facts and circumstances presented in the submission are indicative that insurance contracts in this industry pool are issued by all members together. Therefore, the risk adjustment for non-financial risk is determined from the perspective of all members together. Practically, in this case, an association may determine the risk adjustment for non-financial risk on behalf of all members.

B8. The staff observe that members should consider the analysis provided in paragraphs 18–21 of this paper to determine how to reflect their share in the results of the industry pool in their financial statements.

Pool 2—to which members can choose to transfer some insurance contracts they have issued

B9. Insurance contracts are issued by each individual member and the prices are determined by the individual member. If a contract is eligible (ie it meets specified requirements set by the association), the member can choose to transfer the contract to an industry pool. In some cases, the transferring member may be

required to retain a percentage of the insurance risk of the contract or there may be restrictions on the level of coverage that is allowed to be transferred to the industry pool for the contract.

B10. If a member chooses to transfer the contract to the industry pool, the transferring member remains responsible for managing the contract including any associated claims until all claims are resolved. The member transfers the premiums to the pool (minus an expense allowance) and claims paid by the transferring member are reimbursed by the pool as they occur.

B11. Existing practice:

- (a) the transferring member treats the transferred insurance contracts as negative direct business.
- (b) the member entities treat the insurance service result allocated to them as direct business. Each member reports an insurance contract liability, premiums, claims and expenses incurred.

B12. Staff observations:

- (a) the facts and circumstances presented in the submission are indicative that the member that writes the contract is the issuer of the contract to the policyholder. Accordingly, that member shall account for the insurance contract it issues applying IFRS 17 and determine the risk adjustment for non-financial risk related to that contract.
- (b) the facts and circumstances presented in the submission are also indicative that the transfer of the contracts to the risk sharing pool might meet the definition of a reinsurance contract between the issuing member and all other members applying IFRS 17. Accordingly, the issuing entity should account for the reinsurance contract held applying IFRS 17.
- (c) the facts and circumstances presented in the submission are indicative that all members have issued together reinsurance contracts for each contract that has been transferred to the industry pool. Therefore, the

risk adjustment for non-financial risk related to these reinsurance contracts is determined from the perspective of all members together. Practically, in this case, an association may determine the risk adjustment for non-financial risk on behalf of all members.

- (d) the staff observe that members should consider the analysis provided in paragraphs 22–23 of this paper to determine how to reflect their share in the results of the industry pool in their financial statements.

STAFF PAPER

September 2018

Project	Transition Resource Group for IFRS 17 <i>Insurance Contracts</i>		
Paper topic	Annual cohorts for contracts that share in the return of a specified pool of underlying items		
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This paper has been prepared for discussion at a public meeting of the Transition Resource Group for IFRS 17 *Insurance Contracts* and does not represent the views of any individual member of the International Accounting Standards Board or staff. Comments on the application of IFRS® Standards do not purport to set out acceptable or unacceptable application of IFRS Standards.

Introduction

1. We have received a submission about annual groups of contracts with policyholders that all share in the return on a specified pool of underlying items, with some of the return contractually passing from one group of policyholders to another. For those contracts, the submission asks in what circumstances measuring the contractual service margin at a higher level than an annual cohort level, such as a portfolio level, would achieve the same accounting outcome as measuring the contractual service margin at an annual cohort level applying paragraph 22 of IFRS 17 *Insurance Contracts*.
2. The objective of this paper is to provide background and an accounting analysis to support discussion at the Transition Resource Group for IFRS 17 (TRG).

Structure of the paper

3. This paper includes the following:
 - (a) background information;
 - (b) implementation question; and
 - (c) review of accounting requirements.
4. Appendix A to this paper includes two examples provided in the submission.

Background information

5. Paragraph 14 of IFRS 17 states:

An entity shall identify portfolios of insurance contracts. A portfolio comprises contracts subject to similar risks and managed together. Contracts within a product line would be expected to have similar risks and hence would be expected to be in the same portfolio if they are managed together. Contracts in different product lines (for example single premium fixed annuities compared with regular term life assurance) would not be expected to have similar risks and hence would be expected to be in different portfolios.

6. Paragraph 16 of IFRS 17 states:

An entity shall divide a portfolio of insurance contracts issued into a minimum of:

- (a) a group of contracts that are onerous at initial recognition, if any;
- (b) a group of contracts that at initial recognition have no significant possibility of becoming onerous subsequently, if any; and
- (c) a group of the remaining contracts in the portfolio, if any.

7. Paragraph 22 of IFRS 17 states:

An entity shall not include contracts issued more than one year apart in the same group. To achieve this the entity shall, if necessary, further divide the groups described in paragraphs 16–21.

8. Paragraphs B67–B70 of IFRS 17 state:

B67 Some insurance contracts affect the cash flows to policyholders of other contracts by requiring:

- (a) the policyholder to share with policyholders of other contracts the returns on the same specified pool of underlying items; and
- (b) either:
 - (i) the policyholder to bear a reduction in their share of the returns on the underlying items because of payments to policyholders of other contracts that share in that pool, including payments arising under guarantees made to policyholders of those other contracts; or
 - (ii) policyholders of other contracts to bear a reduction in their share of returns on the underlying items because of payments to the policyholder, including payments arising from guarantees made to the policyholder.

B68 Sometimes, such contracts will affect the cash flows to policyholders of contracts in other groups. The fulfilment cash flows of each group reflect the extent to which the contracts in the group cause the entity to be affected by expected cash flows, whether to policyholders in that group or to policyholders in another group. Hence the fulfilment cash flows for a group:

- (a) include payments arising from the terms of existing contracts to policyholders of contracts in other groups, regardless of whether

those payments are expected to be made to current or future policyholders; and

- (b) exclude payments to policyholders in the group that, applying (a), have been included in the fulfilment cash flows of another group.

B69 For example, to the extent that payments to policyholders in one group are reduced from a share in the returns on underlying items of CU350 to CU250 because of payments of a guaranteed amount to policyholders in another group, the fulfilment cash flows of the first group would include the payments of CU100 (ie would be CU350) and the fulfilment cash flows of the second group would exclude CU100 of the guaranteed amount.

B70 Different practical approaches can be used to determine the fulfilment cash flows of groups of contracts that affect or are affected by cash flows to policyholders of contracts in other groups. In some cases, an entity might be able to identify the change in the underlying items and resulting change in the cash flows only at a higher level of aggregation than the groups. In such cases, the entity shall allocate the effect of the change in the underlying items to each group on a systematic and rational basis.

9. Paragraph BC138 of the Basis for Conclusions on IFRS 17 explains:

The Board considered whether prohibiting groups from including contracts issued more than one year apart would create an artificial divide for contracts with cash flows that affect or are affected by cash flows to policyholders of contracts in another group. Some stakeholders asserted that such a division would distort the reported result of those contracts and would be operationally burdensome. However, the Board concluded that applying the requirements of IFRS 17 to determine the fulfilment cash flows for groups of such contracts provides an appropriate depiction of the results of such contracts (see paragraphs BC171–BC174). The Board acknowledged that, for contracts that fully share risks, the groups together will give the same results as a single combined risk-sharing portfolio, and

therefore considered whether IFRS 17 should give an exception to the requirement to restrict groups to include only contracts issued within one year. However, the Board concluded that setting the boundary for such an exception would add complexity to IFRS 17 and create the risk that the boundary would not be robust or appropriate in all circumstances. Hence, IFRS 17 does not include such an exception. Nonetheless, the Board noted that the requirements specify the amounts to be reported, not the methodology to be used to arrive at those amounts. Therefore it may not be necessary for an entity to restrict groups in this way to achieve the same accounting outcome in some circumstances.

Implementation question

10. The submission is about annual groups of contracts that all share in the return of a specified pool of underlying items, with some of the return contractually passing from one group of policyholders to another. The submission observes that this could be because of guarantees, proportionate sharing in the returns of the pool or because some contracts have lapsed or expired and the return due to them was not paid out at the time and so instead is accumulated and passed to future annual groups of policyholders.
11. The submission notes that on the topic of applying the annual cohort requirements in paragraph 22 of IFRS 17 to contracts with cash flows that affect or are affected by cash flows to policyholders of contracts in another group, paragraph BC138 of the Basis for Conclusions on IFRS 17 explains:

[...] the requirements specify the amounts to be reported, not the methodology to be used to arrive at those amounts. Therefore it may not be necessary for an entity to restrict groups in this way to achieve the same accounting outcome in some circumstances.
12. For those contracts, the submission asks in what circumstances measuring the contractual service margin at a higher level than an annual cohort level, such as a

portfolio level, would achieve the same accounting outcome as measuring the contractual service margin at an annual cohort level applying paragraph 22 of IFRS 17. The submission expresses three views:

- (a) View A—An entity is only able to consider the contractual service margin at a level of a single combined risk-sharing portfolio when 100% of the returns of the specified pool of underlying items are allocated back to the policyholders of the portfolio, with all existing policyholders sharing in the returns pro-rata at the time of allocation. The submission provides an example of a portfolio of insurance contracts in which policyholders share equally in 100% of the returns of the insurance contracts in the portfolio to demonstrate this view (Example 1 in Appendix A to this paper).
- (b) View B—An entity is only able to consider the contractual service margin at a level of a single combined risk-sharing portfolio when a specified percentage of the returns of the specified pool of underlying items are allocated back to the policyholders of the portfolio, with all existing portfolio policyholders sharing in the returns pro-rata at the time of allocation. The submission provides an example of a portfolio of insurance contracts in which policyholders share equally in 90% of the returns of the insurance contracts in the portfolio with the remaining 10% belonging to the entity to demonstrate this view (Example 2 in Appendix A to this paper).
- (c) View C—An entity is only able to consider the contractual service margin at a level of a single combined risk-sharing portfolio when a significant portion of returns of the specified pool of underlying items are allocated back to the policyholders of the portfolio, with all existing policyholders sharing in the allocation, but the allocation can be made

on a non-proportional discretionary basis. The submission does not provide an example to demonstrate this view.

Review of accounting requirements

13. Paragraph B67 of IFRS 17 identifies insurance contracts that affect the cash flows to policyholders of other contracts by requiring the policyholder to share with policyholders of other contracts the returns on the same specified pool of underlying items, and requiring either:
 - (a) the policyholder to bear a reduction in their share of returns on the underlying items because of payments to policyholders of other contracts that share in that pool; or
 - (b) the policyholders of other contracts to bear a reduction in their share of returns on the underlying items because of payments to the policyholder.
14. The payments that cause a reduction in a policyholder's share of returns on the underlying items include payments arising from guarantees made to other policyholders.
15. The staff observe that when a specified pool of underlying items consists of the insurance contracts issued to the policyholders that share in the returns of that pool, the criteria in paragraph B67 of IFRS 17 are met. This is because the payments to policyholders (including those arising from guarantees) reduce the ultimate return on the pool of underlying items that is shared by the policyholders. The staff observe that this is regardless of whether the policyholders share in 100% of the return on the pool of underlying items or only part of the return on the pool of underlying items.
16. The staff observe that for some other types of contracts with policyholders that share in the return of a specified pool of underlying items, the underlying items do

not include the insurance contracts issued to those policyholders (for example, the underlying items are financial assets). Those insurance contracts also meet the criteria in paragraph B67 of IFRS 17, if the contracts require policyholders to bear a reduction in their share of the returns on the underlying items because of payments to policyholders of other contracts that share in that pool, applying paragraph B67(b) of IFRS 17.

17. Paragraph B68 of IFRS 17 requires that the fulfilment cash flows of each group of insurance contracts reflect the extent to which the contracts in that group cause the entity to be affected by the expected cash flows, whether to policyholders in that group or to policyholders in another group.

18. Contracts with policyholders that share in 100% of the returns on a pool of underlying items that includes the insurance contracts issued to those policyholders, ie that fully share all risks, do not cause the entity to be ultimately affected by the expected cash flows of each individual contract issued. For those contracts, applying paragraph B68 of IFRS 17, the contractual service margin will be nil. Therefore, for those contracts, an entity measuring the contractual service margin at a higher level than the annual cohort level, such as a portfolio level, would achieve the same accounting outcome as measuring the contractual service margin at an annual cohort level applying paragraph 22 of IFRS 17. This is demonstrated in Example 1 in Appendix A to this paper.

19. Contracts with policyholders that do not fully share risks could cause the entity to be affected by the expected cash flows of each contract issued. The staff observe that paragraph B68 of IFRS 17 results in the effect of risk-sharing between policyholders to be reflected in the fulfilment cash flows, and hence in the contractual service margin, of the groups of contracts to the extent that risk-sharing exists. However, after factoring in the risk-sharing, if the risks are not fully shared the entity is still affected by the expected cash flows of each contract issued. Therefore, the contractual service margin of the groups of contracts may

differ from a contractual service margin measured at a higher level, such as the portfolio level. This is demonstrated in Example 2 in Appendix A to this paper.¹

TRG discussion

Question to TRG members

What are your views on the implementation question presented above?

¹ Example 2 demonstrates the effect of less than 100% sharing by policyholders of the returns of underlying items that are the insurance contracts issued to the policyholders. The staff observe that less than full sharing of risk could also occur when the underlying items are financial assets rather than the insurance contracts issued and the policyholders do not share in the underwriting results.

Appendix A—Annual cohorts for contracts that share in the return of a specified pool of underlying items

- A1. This appendix includes two examples provided in the submission:
- (a) Example 1—policyholders participate in 100% of the returns on a specified pool of underlying items which are the insurance contracts issued to those policyholders; and
 - (b) Example 2—policyholders participate in 90% of the returns on a specified pool of underlying items which are the insurance contracts issued to those policyholders.
- A2. Assume, for simplicity that the discount rates are 0% and the risk adjustment for non-financial risk is zero.

Example 1—policyholders participate in 100% of the returns on a specified pool of underlying items which are the insurance contracts issued to those policyholders

- A3. An entity issues contracts to 10 groups² of policyholders, all forming a single portfolio of insurance contracts. Policyholders in each group pay a premium of 1,000 and each share equally in 100% of the overall returns on the portfolio of insurance contracts (ie the specified pool of underlying items). The returns on the pool are derived from the performance of the insurance contracts.
- A4. Claims incurred in group 1 amount to 4,000, resulting in a net loss to the entity of 3,000 on that group before allocating to the group its share of the return on the pool of underlying items. No claims are incurred in groups 2-10, resulting in a gain to the entity of 9,000 on those 9 groups before allocating to each group its share of the return on the pool of underlying items.

² This example assumes that the entity has chosen to identify 10 groups of insurance contracts, applying paragraph 21 of IFRS 17, to illustrate the accounting outcome of measuring groups of insurance contracts (for example, annual cohorts) and of measuring a portfolio of contracts.

- A5. The overall profit of the portfolio is 6,000. This profit belongs, in full, to the policyholders.
- A6. Each group shares equally in 100% of the return on the portfolio and is therefore due 600 (6,000 / 10). The cash flows to each group are demonstrated in the following table:

	Group 1	Each of groups 2-10	Groups 2-10	Groups 1-10 total
Premiums	1,000	1,000	9,000	10,000
Claims	(4,000)	-	-	(4,000)
Net cash flows	(3,000)	1,000	9,000	6,000
Share of return on pool	(600)	(600)	(5,400)	(6,000)
Net cash flows	(3,600)	400	3,600	0

A7. If the groups of insurance contracts were unconnected (ie each group share in the returns of the group only), the cash flows for each group would have been be as follows:

	Group 1	Each of groups 2-10	Groups 2-10	Groups 1-10 total
Premiums	1,000	1,000	9,000	10,000
Claims	(4,000)	-	-	(4,000)
Share of return on pool	3,000	(1,000)	(9,000)	(6,000)
Net cash flows	0	0	0	0

A8. Therefore, applying paragraph B68 of IFRS 17, the groups of insurance contracts are measured as follows:

	Group 1	Each of groups 2-10	Groups 2-10
Premiums	(1,000)	(1,000)	(9,000)
Claims	4,000	-	-
Share of return on pool	600	600	5,400
Paragraph B68 of IFRS 17	(3,600) ³	400	3,600 ⁴

³ Fulfilment cash flows in group 1 exclude payments to policyholders in the group that have been included in the fulfilment cash flows of group 2-10.

⁴ Fulfilment cash flows in group 2-10 include payments to policyholders of contracts in other groups.

Fulfilment cash flows	0	0	0
Contractual service margin	0	0	0

A9. The staff observe that for this example measuring the contractual service margin at a higher level than the annual cohort level, such as a portfolio level, would achieve the same accounting outcome as measuring the contractual service margin at an annual cohort level applying paragraph 22 of IFRS 17.

Example 2—policyholders participate in 90% of the returns on a specified pool of underlying items which are the insurance contracts issued to those policyholders

A10. An entity issues contracts to 10 groups of policyholders, all forming a single portfolio of insurance contracts. Policyholders in each group pay a premium of 1,000 and each share equally in 90% of the overall returns on the portfolio of insurance contracts (ie the specified pool of underlying items). The returns on the pool are derived from the performance of the insurance contracts. The remaining 10% goes to the entity.

A11. Claims incurred in group 1 amount to 4,000, resulting in a net loss to the entity of 3,000 on that group before allocating to the group its share of the return on the pool of underlying items. No claims are incurred in groups 2-10, resulting in a gain to the entity of 9,000 on those 9 groups before allocating to each group its share of the return on the pool of underlying items.

A12. The overall profit of the portfolio is 6,000. 5,400 belongs to the policyholders (6,000 x 90%) and 600 belongs to the entity (6,000 x 10%).

A13. Each group shares equally in 90% of the return on the portfolio and is therefore due 540 (5,400 / 10). The cash flows to each group are demonstrated in the following table:

	Group 1	Each of groups 2-10	Groups 2-10	Groups 1-10 total
Premiums	1,000	1,000	9,000	10,000
Claims	(4,000)	-	-	(4,000)
Net cash flows	(3,000)	1,000	9,000	6,000
Share of return on pool	(540)	(540)	(4,860)	(5,400)
Net cash flows	(3,540)	460	4,140	600

A14. If the groups of insurance contracts were unconnected (ie each group share in the returns of the group only), the cash flows for each group would have been be as follows:

	Group 1	Each of groups 2-10	Groups 2-10	Groups 1-10 total
Premiums	1,000	1,000	9,000	10,000
Claims	(4,000)	-	-	(4,000)
Share of return on pool	2,700	(900)	(8,100)	(5,400)
Net cash flows	(300)	100	900	600

A15. Therefore, applying paragraph B68 of IFRS 17, the groups of insurance contracts are measured as follows:

	Group 1	Each of groups 2-10	Groups 2-10
Premiums	1,000	1,000	9,000
Claims	(4,000)	-	-
Share of return on pool	(540)	(540)	(4,860)
Paragraph B68 of IFRS 17	3,240 ⁵	(360)	(3,240) ⁶
Fulfilment cash flows	(300)	100	900
Contractual service margin	0	(100)	(900)
Loss component	300	0	0

A16. The staff observe that for this example measuring the contractual service margin at a higher level than the annual cohort level, such as a portfolio level, would not achieve the same accounting outcome as measuring the contractual service margin at an annual cohort level applying paragraph 22 of IFRS 17.

⁵ Fulfilment cash flows in group 1 exclude payments to policyholders in the group that have been included in the fulfilment cash flows of group 2-10.

⁶ Fulfilment cash flows in group 2-10 include payments to policyholders of contracts in other groups (4,140-900).

STAFF PAPER

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Project	Transition Resource Group for IFRS 17 <i>Insurance Contracts</i>		
Paper topic	Reporting on other questions submitted		
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This paper has been prepared for discussion at a public meeting of the Transition Resource Group for IFRS 17 *Insurance Contracts* and does not represent the views of any individual member of the International Accounting Standards Board or staff. Comments on the application of IFRS® Standards do not purport to set out acceptable or unacceptable application of IFRS Standards.

Introduction

1. This paper summarises other questions submitted to the Transition Resource Group for IFRS 17 *Insurance Contracts* (TRG). These submissions have been categorised as questions that:
 - (a) can be answered applying only the words in IFRS 17;
 - (b) do not meet the submission criteria; or
 - (c) are being considered through a process other than a TRG discussion (such as a proposed annual improvement).
2. Submissions *not* summarised in this paper are those:
 - (a) that are discussed in a separate agenda paper;
 - (b) for which the staff have requested further information from the submitter; or
 - (c) that will be considered for discussion at a future TRG meeting.

(a) Questions that can be answered applying only the words in IFRS 17 *Insurance Contracts*

The staff will consider publishing educational materials on these topics in the future to further support implementation.

Log #	Topic	Question	Response
S33	Scope of IFRS 17— loan to buy a non-financial asset	The submission describes a specific fact pattern of a loan contract to buy a non-financial asset and asks whether it is in the scope of IFRS 17. The loan is repaid to the entity via low instalments over the period of the loan and a final higher ‘balloon’ payment at maturity. At the maturity of the loan, the customer can choose to return the non-financial asset to the entity instead of making the final ‘balloon’ payment. The submission states that the contract does not meet the definition of a lease in IFRS 16 <i>Leases</i> and that the entity granting the loan is not a manufacturer, dealer or retailer of the non-financial asset. Therefore, the scope exclusions for residual value guarantees in paragraph 7(d) of IFRS 17 do not apply.	A contract should be assessed against the definition of an insurance contract and the scope requirements of IFRS 17. When assessing whether the contract meets the definition of an insurance contract, an assessment is made as to whether the contract transfers significant insurance risk. The definition of an insurance contract in IFRS 17 is the same as the definition of an insurance contract in IFRS 4 <i>Insurance Contracts</i> , with clarifications to the related guidance in Appendix B of IFRS 4. ¹ Example 1.15 within paragraph IG2 of the Guidance on Implementing IFRS 4 includes factors to consider when assessing whether a contract with a residual value guarantee meets the definition of an insurance contract or, alternatively, meets the definition of a derivative in the scope of IFRS 9 <i>Financial Instruments</i> .

¹ The clarifications in IFRS 17 require that: (i) an entity should consider the time value of money in assessing whether the additional benefits payable in any scenario are significant; and (ii) a contract does not transfer significant insurance risk if there is no scenario with commercial substance in which the entity can suffer a loss on a present value basis.

Log #	Topic	Question	Response
S33	Scope of IFRS 17—loans that may waive some or all of the payments due under the contract on death	<p>The submission describes the features of three loan contracts and asks whether IFRS 17 would apply to those contracts.</p> <p>Although the three loan contracts have different features, all contracts combine a loan with an agreement from the entity to compensate the borrower—by waiving some or all the payments due under the contract (ie repayment of the loan balance and payment of interest)—if a specified uncertain future event adversely affects the borrower, ie death.</p>	<p>A contract should be assessed against the definition of an insurance contract and the scope requirements of IFRS 17. When assessing whether the contract meets the definition of an insurance contract, an assessment is made as to whether the contract transfers significant insurance risk. The definition of an insurance contract in IFRS 17 is the same as the definition of an insurance contract in IFRS 4, with clarifications to the related guidance in Appendix B of IFRS 4.¹ Example 1.24 within paragraph IG2 of the Guidance on Implementing IFRS 4 notes that a loan contract that waives repayment of the entire loan balance if the borrower dies contains an insurance component equivalent to a cash death benefit.</p>

(a) Questions that can be answered applying only the words in IFRS 17

Log #	Topic	Question	Response
S33	Scope of IFRS 17—credit cards providing its holder coverage for a supplier failure	<p>The submission describes a specific credit card contract and asks whether IFRS 17 would apply to that contract. The submission notes that local regulation requires the entity to provide coverage for some purchases made by the customer using the credit card. Under this coverage, the entity:</p> <ul style="list-style-type: none"> (a) must refund the customer for some claims against a supplier in respect of a misrepresentation or breach of the purchase agreement (for example, if the goods are defective or if the supplier fails to deliver the goods); and (b) is entitled to be indemnified by the supplier for any loss the entity suffers in satisfying its liability with its customer. <p>The submission also notes that the entity and the supplier are jointly and severally liable to the customer—ie the customer can choose whether to claim from the entity or from the supplier.</p>	<p>A contract should be assessed against the definition of an insurance contract and the scope requirements of IFRS 17. When assessing whether the contract meets the definition of an insurance contract, an assessment is made as to whether the contract transfers significant insurance risk. The definition of an insurance contract in IFRS 17 is the same as the definition of an insurance contract in IFRS 4, with clarifications to the related guidance in Appendix B of IFRS 4.¹</p> <p>Paragraph B26 of IFRS 17 provides examples of contracts that are insurance contracts if the transfer of insurance risk is significant. Those examples include contracts that compensate the holder if another party fails to perform a contractual obligation (paragraph B26(f) of IFRS 17).</p>

(a) Questions that can be answered applying only the words in IFRS 17

Log #	Topic	Question	Response
S33	Scope of IFRS 17—EBITDA guarantee	<p>The submission describes a specific fact pattern of an entity that provides hotel management services. The service fee that the entity charges is determined as a percentage of gross hotel revenue. The entity also guarantees the hotel owner a specified level of EBITDA. To the extent that the actual hotel EBITDA is below the specified level, the entity is obligated to make payments to the hotel owner. The amount payable under the guarantee may exceed the amount of the service fee receivable. The submission asks whether the guarantee provided by the entity is within the scope of IFRS 17.</p>	<p>A contract should be assessed against the definition of an insurance contract and the scope requirements of IFRS 17. The definition of an insurance contract in IFRS 17 is the same as the definition of an insurance contract in IFRS 4, with clarifications to the related guidance in Appendix B of IFRS 4.¹ When assessing whether the contract meets the definition of an insurance contract, an assessment is made as to whether the contract transfers significant insurance risk. When assessing whether an insurance contract is within the scope of IFRS 17, an assessment is made as to whether any of the scope exclusions of IFRS 17 are applicable. IFRS 17 includes a scope exclusion for warranties provided by a manufacturer, dealer or retailer in connection with the sale of its services to a customer and also excludes contractual obligations contingent on the future use of a non-financial item (for example, contingent payments), as stated in paragraph 7 of IFRS 17.</p>
S33	Separating components from an insurance contract	<p>The submission notes that, although the definition of an insurance contract in IFRS 17 is the same as the definition in IFRS 4 <i>Insurance Contracts</i>, the requirements in IFRS 17 for the separation of non-insurance components differ from the requirements in IFRS 4.</p> <p>The submission provides several views on whether non-insurance components embedded in an insurance contract could be accounted for separately applying IFRS 17.</p>	<p>Paragraphs 10–12 of IFRS 17 require an entity to account separately for non-insurance components only if specified criteria are met. If those specified criteria are not met IFRS 17 requires that the contract is accounted for as an insurance contract in its entirety.</p> <p>Therefore, when applying IFRS 17 an entity might be required to account for loans and other forms of credit that include a relatively small insurance component entirely as insurance contracts. The staff plan to bring this to the attention of the International Accounting Standards Board (Board).</p>

(a) Questions that can be answered applying only the words in IFRS 17

Log #	Topic	Question	Response
S56 & S67	Reporting frequency	S56 asks for the requirements in paragraph B137 of IFRS 17 to be extended to apply to monthly reporting that is prepared for internal management reporting and external regulatory reporting. The submission notes the operational issues and the complexity involved in developing systems considering the disparity in procedures between monthly closing and quarterly interim reporting. S67 asks, when the reporting frequency of an entity differs from the reporting frequency of its subsidiary, whether the measurement of contracts issued by the subsidiary should be the same in the entity's consolidated financial statements and the subsidiary's financial statements.	The requirements in paragraph B137 of IFRS 17 are an exception to the requirements in IAS 34 <i>Interim Financial Reporting</i> . The exception applies only to interim reports prepared applying IAS 34. If a subsidiary prepares annual IFRS financial statements but does not prepare interim reports applying IAS 34, paragraph B137 of IFRS 17 is not applicable to that subsidiary. Therefore, applying the requirements of IFRS 17, subject to materiality considerations, may result in different measurement of insurance contracts issued by the subsidiary in the subsidiary's financial statements and in the group's consolidated financial statements.
S57	Accounting for crediting rate changes	The submission considers whether a difference between the expected and the actual crediting rate applied to a policyholder's account balance is included in insurance finance income or expense or adjusts the contractual service margin applying paragraph B96(c) of IFRS 17. The submission is focused on insurance contracts without direct participation features for which the account balance is expected to become payable in the future and ignores the effect of any discretion.	Paragraph B96(c) of IFRS 17 is applicable for differences between any investment component expected to become payable in the period and the actual investment component that becomes payable in the period. In the fact pattern provided, the account balance is not expected to become payable in the period and does not become payable in the period, therefore paragraph B96(c) of IFRS 17 is not applicable.

(a) Questions that can be answered applying only the words in IFRS 17

TRG for IFRS 17 | Reporting on other questions submitted

Log #	Topic	Question	Response
S60	Presentation of separate accounts	<p>The submission asks, for insurance contracts that transfer most of the risks and benefits linked to asset-management to policyholders, whether the entity can disaggregate line items in the statement of financial position to present separately:</p> <p>(a) a single asset line item for all financial instruments that the premiums received from the policyholders have been invested in (for example, cash, loans and other securities); and</p> <p>(b) a separate liability line item for the portion of the insurance contract liability that is equal to the value of the single asset line item.</p>	<p>Paragraph 54 of IAS 1 <i>Presentation of financial statements</i> states which line items are required to be presented in the statement of financial position. This includes requirements for presenting insurance contracts and financial instruments. For example, IAS 1 requires cash to be presented separately from other financial instruments. For insurance contracts, the following line items are required to be presented in accordance with paragraph 78 of IFRS 17:</p> <p>(a) groups of insurance contracts that are assets; and</p> <p>(b) groups of insurance contracts that are liabilities.</p> <p>As well as presenting those required line items, applying IAS 1 an entity shall present additional line items (including by disaggregating the required line items), headings and subtotals in the statement of financial position when such presentation is relevant to an understanding of the entity’s financial position.</p>

Log #	Topic	Question	Response
S62	Coverage that an entity can cancel at any time	<p>The submission considers a specific type of entity in which parties become members by purchasing an insurance contract. Members of the entity are also provided with free additional insurance coverage. The entity can cancel the free additional insurance coverage at any time. The submission asks whether cash flows related to the free additional coverage are within the boundary of the insurance contracts purchased by policyholders.</p>	<p>An entity applies paragraph 2 of IFRS 17 to determine the rights and obligations arising from an insurance contract. The right of an entity to cancel coverage at any time means that the entity does not have a substantive obligation to provide future services related to the free additional insurance coverage. The expected cash flows related to future free additional insurance coverage are therefore not included in the boundary of the insurance contract and are not included in the liability for remaining coverage. If the entity has a substantive obligation for the free additional insurance coverage that has already been provided, such as unpaid claims, the cash flows related to that coverage are within the boundary of the contract and are included in the liability for incurred claims.</p>
S64	Discounting cash flows	<p>The submission notes that applying paragraph 59(b) of IFRS 17 for the premium allocation approach (PAA), an entity is not required to adjust future cash flows in the liability for incurred claims for the time value of money and the effect of financial risk if those cash flows are expected to be paid or received in one year or less from the date the claims are incurred. The submission asks why this option is limited to groups of contracts applying the PAA and notes that different interpretations may be applicable for discounting liabilities for incurred claims related to groups of contracts applying the general model.</p>	<p>The practical expedient in paragraph 59(b) of IFRS 17, as explained in paragraph BC294 of the Basis for Conclusions on IFRS 17, is a simplification that applies only to groups of insurance contracts accounted for applying the premium allocation approach which is a simplified approach. Applying the requirements of IFRS 17 to contracts applying the general model, subject to materiality considerations, an entity is required to adjust the estimates of future cash flows to reflect the time value of money and the effect of financial risk.</p>

(a) Questions that can be answered applying only the words in IFRS 17

TRG for IFRS 17 | Reporting on other questions submitted

Log #	Topic	Question	Response
S75	Boundary of a reinsurance contract issued	<p>The submission asks which cash flows are within the boundary of an annual reinsurance contract issued if the reinsurer has the right to compel the cedant to pay contractually agreed premiums for 12 months and has the option to reprice the contract at 90 days' notice. If the reinsurer exercises its right to reprice the contract, the cedant can accept the new terms or terminate the contract. The submission notes that a similar example was discussed in the May 2018 TRG meeting from the perspective of the cedant and asks whether there is an expectation of a symmetrical treatment of the contract boundary between the reinsurer and the cedant.</p>	<p>This example is similar to the example in Agenda Paper 4 <i>Boundary of reinsurance contracts held with repricing mechanisms</i> of the May 2018 TRG meeting. In that paper, the example was from the perspective of the cedant and in this example it is from the perspective of the reinsurer. The contract boundary is the same from each perspective because:</p> <ul style="list-style-type: none"> (a) when the cedant has a right to receive services, the reinsurer has an obligation to provide services; and (b) when the cedant has an obligation to pay premiums, the reinsurer has a right to compel premiums.

(a) Questions that can be answered applying only the words in IFRS 17

TRG for IFRS 17 | Reporting on other questions submitted

Log #	Topic	Question	Response
S79	Contract boundary and investment component	The submission considers insurance contracts with direct participation features and asks whether cash flows that relate to periods when insurance coverage is no longer provided and the policyholder bears all the risks related to the investment related services are within the boundary of the contract. The submission also asks, if the cash flows are within the boundary of the contract, whether this extends the coverage period of the contract to include the period in which the investment component exists but no insurance coverage is provided.	<p>The coverage period is defined in IFRS 17.² An entity is required to apply paragraph 34 of IFRS 17 to determine cash flows within the boundary of a contract.</p> <p>Cash flows within the boundary of a contract may relate to periods in which coverage is no longer provided, such as when claims are expected to be settled in the future that relate to premium within the boundary of a contract. Also, periods of coverage may be outside the boundary of a contract, for example, if an entity can fully reprice premiums.</p>

² At the June 2018 Board meeting, the Board tentatively decided to propose to clarify the definition of the coverage period for insurance contracts with direct participation features. The proposed amendment would clarify that the coverage period for such contracts includes periods in which the entity provides investment-related services.

(a) Questions that can be answered applying only the words in IFRS 17

(b) Questions that do not meet the submission criteria

The criteria established for the TRG state that implementation questions should meet the following criteria:

- (a) must be related to, or arise from, IFRS 17;
- (b) may result in possible diversity in practice; and
- (c) are expected to be pervasive, ie relevant to a wide group of stakeholders.

Any question submitted should include a detailed description of the possible ways in which IFRS 17 could be applied.

Log #	Topic	Question	Response
S51	Significant possibility of becoming onerous	The submission notes that the use of the term ‘no significant possibility’ in paragraph 16(b) of IFRS 17 is grammatically incorrect and may have meant to say ‘no significant probability’ instead.	The term ‘no significant possibility’ in paragraph 16(b) of IFRS 17 should be interpreted in the context of the objective of the requirement. The objective is identifying contracts with no significant possibility of becoming onerous at initial recognition to group such contracts separately from contracts that are onerous at initial recognition and any remaining contracts in the portfolio that are not onerous at initial recognition.
S69	Risk mitigation and reinsurance contracts held	The submission asks why reinsurance contracts held are not considered a valid risk mitigation strategy within the context of paragraphs B115–B116 of IFRS 17 for contracts with direct participation features and recommends amending paragraph B116 of IFRS 17 accordingly.	The requirements in paragraphs B115–B116 of IFRS 17 are limited to derivatives that an entity uses to mitigate the financial risk arising from insurance contracts. These requirements are consistent with the Board’s decision described in paragraphs BC250–BC256 of the Basis for Conclusions on IFRS 17.

Log #	Topic	Question	Response
S81	Determining the risk adjustment for non-financial risk in a group of entities	The submission is a follow up on the discussion of this topic at the May 2018 TRG meeting. The submission considers how entities should conceptually and practically apply the risk adjustment for non-financial risk requirements to a consolidated group of entities. The submission notes that in the event that the Board is requested to review the acceptability of the two views expressed at the May 2018 TRG meeting, it is critical to have both views fully explained.	The summary of the May 2018 TRG meeting was reported to the Board at the June 2018 Board meeting. The summary notes that some TRG members agreed with the staff analysis that only the issuing entity that is party to the contract determines the compensation the entity would require for bearing non-financial risk related to insurance contracts that the entity issues. Therefore, for a group of insurance contracts issued by an entity that is party to the contract there is one risk adjustment for non-financial risk. Some TRG members commented that they could read the requirements in IFRS 17 differently. Those TRG members read the requirements as requiring different measurement of the risk adjustment for non-financial risk for groups of insurance contracts at different reporting levels if the issuing entity would require different compensation for bearing non-financial risk than the consolidated group would require.

(c) Questions that are being considered through a process other than a TRG discussion

Log #	Topic	Question	Response
S21 and S45	Accounting for insurance contracts issued by mutual entities	S21 asks how paragraph BC265 of Basis for Conclusions on IFRS 17 should be applied when the residual interest of the mutual entity is due to policyholders through a vehicle other than the insurance contract they hold. S45 asks whether a contractual service margin should be recognised for participating insurance contracts and non-participating insurance contracts issued by a mutual entity	Educational materials on how IFRS 17 applies to insurance contracts issued by a mutual entity have been developed by staff to support the implementation of IFRS 17. The educational materials consider both: <ul style="list-style-type: none"> (a) insurance contracts that provide the policyholder with a residual interest in the mutual entity; and (b) conventional insurance contracts issued by a mutual entity.
S73	Coverage units for contracts with cash flows that vary based on returns on underlying items	The submission asks for further clarification on coverage units, discussed in Agenda Paper 5 of the May 2018 TRG meeting, specifically on determining the quantity of benefits for contracts with cash flows that vary based on the returns on underlying items that may be in the general model or the variable fee approach. The submission includes two examples: <ul style="list-style-type: none"> (a) a universal life contract that pays the higher of a guaranteed sum or an account balance; and (b) a deferred annuity. 	Determining the quantity of benefits for identifying coverage units was discussed both at the February 2018 TRG meeting and the May 2018 TRG meeting. The examples described in the submission illustrate similar considerations to the examples included in Appendix B to Agenda Paper 5 of the May 2018 TRG meeting, in particular examples 13 and 16. At the June 2018 Board meeting, the Board tentatively decided to propose to clarify the definition of the coverage period for insurance contracts with direct participation features. The proposed amendment would clarify that the coverage period for such contracts includes periods in which the entity provides investment-related services.

(c) Questions that are being considered through a process other than a TRG discussion

TRG for IFRS 17 | Reporting on other questions submitted