

AGENDA [18/04/2018]

Transition Resource Group for IFRS 17 *Insurance Contracts*

DATE 2 MAY 2018

LOCATION **IFRS FOUNDATION**
30 CANNON STREET
LONDON EC4M 6XH

ADDITIONAL
INFORMATION

Wednesday 2 May

UK time	Agenda item	Agenda ref.
09:30 – 09:45	Welcome and introductory remarks	-
09:45 – 10:30	Combination of insurance contracts	AP01
10:30 – 11:00	Determining the risk adjustment for non-financial risk in a group of entities	AP02
11:00 – 11:15	Break	-
11:15 – 12:15	Cash flows within the contract boundary	AP03
12:15 – 13:00	Boundary of reinsurance contracts held with repricing mechanisms	AP04
13:00 – 14:00	Lunch	-
14:00 – 15:30	Determining the quantity of benefits for identifying coverage units	AP05
15:30 – 15:45	Break	-
15:45 – 16:15	Implementation challenges outreach report	AP06
16:15 – 16:45	Reporting on other questions submitted	AP07
16:45 – 17:00	Administration	-

STAFF PAPER

May 2018

Project	Transition Resource Group for IFRS 17 <i>Insurance Contracts</i>		
Paper topic	Combination of insurance contracts		
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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 when a set or series of insurance contracts should be combined and treated as a whole, applying paragraph 9 of IFRS 17 *Insurance Contracts*.
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 (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 6 February 2018 with respect to Agenda Paper 1; and
 - (b) Appendix B—Scenario and factors described in the submission.

Background information

5. Paragraph 2 of IFRS 17 states:

A contract is an agreement between two or more parties that creates enforceable rights and obligations.
6. Paragraph 9 of IFRS 17 states:

A set or series of insurance contracts with the same or a related counterparty may achieve, or be designed to achieve, an overall commercial effect. In order to report the substance of such contracts, it may be necessary to treat the set or series of contracts as a whole. For example, if the rights or obligations in one contract do nothing other than entirely negate the rights or obligations in another contract entered into at the same time with the same counterparty, the combined effect is that no rights or obligations exist.
7. Paragraph 9 of IFRS 17 is consistent with the *Conceptual Framework for Financial Reporting*, published in March 2018.

8. Paragraph 4.51 of the *Conceptual Framework* provides examples of circumstances where treating a group of rights and obligations as a single unit of account may provide more relevant information. These examples include circumstances where those rights and obligations:

- (i) cannot (or are unlikely to) be the subject of separate transactions;
- (ii) cannot (or are unlikely to) expire in different patterns;
- (iii) have similar economic characteristics and risks and hence are likely to have similar implications for the prospects for future net cash inflows to the entity or net cash outflows from the entity; or
- (iv) are used together in the business activities conducted by an entity to produce cash flows and are measured by reference to estimates of their interdependent future cash flows.

9. Paragraph 4.59 of the *Conceptual Framework* states:

The terms of a contract create rights and obligations for an entity that is a party to that contract. To represent those rights and obligations faithfully, financial statements report their substance. In some cases, the substance of the rights and obligations is clear from the legal form of the contract. In other cases, the terms of the contract or a group or series of contracts requires analysis to identify the substance of the rights and obligations.

10. Paragraph 4.62 of the *Conceptual Framework* states:

A group or series of contracts may achieve or be designed to achieve an overall commercial effect. To report the substance of such contracts, it may be necessary to treat rights and obligations arising from that group or series as a single unit of account. For example, if the rights or obligations in one contract merely nullify all the rights or obligations in another contract entered into at the same time with the same counterparty, the combined effect is that the two contracts create no rights or obligations. Conversely, if a single contract creates two or more sets of rights and obligations that could have been created through two or more separate

contracts, an entity may need to account for each set as if it arose from separate contracts in order to faithfully represent the rights and obligations (...).

11. In February 2018 the TRG discussed a related topic in Agenda Paper 1 *Separation of insurance components of a single insurance contract*. An extract from the meeting summary detailing the outcome of that discussion is included in Appendix A to this paper.

Implementation question

12. The submission asks when it may be necessary to treat a set or series of insurance contracts as a whole applying paragraph 9 of IFRS 17.
13. The submission considers that the following factors could indicate that a set or series of insurance contracts are in substance a single contract:
- (a) the contracts are priced as a single risk;
 - (b) the lapse of one contract changes the rights and obligations of the other contract(s); and
 - (c) measuring the contracts separately would result in one/some of the contract(s) being onerous whereas when measured as a whole the contract is profitable.
14. The submission observes that different views could be reached based on whether each of these factors is considered determinative in applying the requirements of paragraph 9 of IFRS 17, and that the existence of these different views may result in diversity in practice. In a single scenario presented in the submission (see Appendix B to this paper), the submission describes one view that two contracts should be combined and another view that they should not be combined. The difference depends on which factors shown above are considered most indicative of the substance of the contracts.

Review of accounting requirements

15. When developing paragraph 9 of IFRS 17 with respect to combining separate insurance contracts into a single insurance contract, the Board intended to provide a principle on contract combination that is consistent with the principle set out in the *Conceptual Framework*.¹ The purpose of this paper is to discuss the circumstances in which multiple insurance contracts should be combined and treated as a single contract.
16. It is expected that entities would usually design contracts in a way that reflects their substance. Therefore, a contract with the legal form of a single contract would generally be considered on its own to be a single contract in substance.
17. Paragraph 9 of IFRS 17 acknowledges that there may be circumstances where a set or series of insurance contracts with the same or a related counterparty reflect a single contract in substance. This is when the contracts may achieve, or be designed to achieve, an overall commercial effect.
18. The staff view is that the fact that a set or series of insurance contracts with the same counterparty are entered into at the same time is not, in itself, sufficient to conclude that they achieve, or are designed to achieve, an overall commercial effect. Determining whether it is necessary to treat a set or series of insurance contracts as a single contract involves significant judgement and careful consideration of all relevant facts and circumstances.
19. Below are some considerations that might be relevant in the assessment of whether a set or series of insurance contracts achieve, or are designed to achieve, an overall commercial effect:
 - (a) the rights and obligations are different when looked at together compared to when look at individually (for example, the rights and

¹ When developing IFRS 17, the Board considered consistency with the principle set out in the 2015 Exposure Draft of the *Conceptual Framework for Financial Reporting* that contracts should be combined as necessary to report their substance. The *Conceptual Framework* was published in March 2018 and this principle has remained the same.

obligations of one contract negate the rights and obligations of another contract)

- (b) the entity is unable to measure one contract without considering the other. This may be the case where there is interdependency between the different risks covered in each contract and the contracts lapse together. When cash flows are interdependent, separating them can be arbitrary. This principle is reflected in the requirements of separating investment components, derivatives and other non-insurance services in paragraphs 10–13 and B31–B35 of IFRS 17 and explained in paragraph BC114 of the Basis for Conclusions on IFRS 17.

- 20. The staff observe that while no single factor is determinative in applying this assessment, when the lapse or maturity of one contract causes the lapse or maturity of another contract, there is a strong indication that the contracts were designed to achieve an overall commercial effect.
- 21. Conversely, the staff observe that the existence of a discount, in itself, does not mean that a set or series of contracts achieve an overall commercial effect. The staff observe that a discount exists when there is a price that the entity generally charges for an insurance policy and the entity offers the policyholder a price that is lower than that amount. An entity may offer the policyholder a discount if they purchase more than one insurance coverage (ie enter into more than one contract). The overall commercial effect of such contracts looked at in combination may not be any different to the commercial effect when looked at separately if the discount is allocated appropriately to each of the contracts.
- 22. IFRS 17 does not prescribe how to appropriately allocate a discount given between multiple contracts. The staff observe that it may be helpful to consider paragraph BC112 of the Basis for Conclusions on IFRS 17 relating to the allocation of discounts between separate components of a contract. It states:

Applying IFRS 15, any discounts and cross-subsidies are allocated to components proportionately or on the basis of observable evidence. In the Board’s view, this approach ensures that the allocation of cross-

subsidies and discounts/supplements reflects the economics of the separated components.

23. The analysis in this paper is consistent with the observations of the TRG on the separation of insurance components of a single contract at the February 2018 meeting of the TRG.
24. The scenario and factors considered in the submission are included in Appendix B 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 for IFRS 17 meeting held on 6 February 2018 with respect to Agenda Paper 1

Separation of insurance components of a single insurance contract (Agenda Paper 1)

A.1 Sometimes entities combine different types of coverage that have different risks into one legal insurance contract. Similarly, reinsurance contracts held can provide coverage to underlying contracts that are included in different groups of insurance contracts. Agenda Paper 1 addresses two submissions received about whether:

- (a) IFRS 17 permits the separation of insurance components of a single insurance contract for measurement purposes.
- (b) when applying IFRS 17, a reinsurance contract held should be separated into components for measurement purposes to reflect the underlying contracts covered. For example, whether a reinsurance contract held that provides coverage to underlying contracts that are included in different groups of insurance contracts should be separated.

A.2 TRG members discussed the analysis in Agenda Paper 1 and observed that:

- (a) the lowest unit of account that is used in IFRS 17 is the contract that includes all insurance components.
- (b) entities would usually design contracts in a way that reflects their substance. Therefore a contract with the legal form of a single contract would generally be considered a single contract in substance. However:
 - (i) there might be circumstances where the legal form of a single contract would not reflect the substance of its contractual rights and obligations.
 - (ii) overriding the contract unit of account presumption by separating insurance components of a single insurance contract involves significant judgement and careful consideration of all relevant facts and circumstances. It is not an accounting policy choice.

- (c) combining different types of products or coverages that have different risks into one legal insurance contract is not, in itself, sufficient to conclude that the legal form of the contract does not reflect the substance of its contractual rights and obligations. Similarly, the availability of information to separate cash flows for different risks is not, in itself, sufficient to conclude that the contract does not reflect the substance of its contractual rights and obligations.
- (d) the fact that a reinsurance contract held provides cover for underlying contracts that are included in different groups is not, in itself, sufficient to conclude that accounting for the reinsurance contract held as a single contract does not reflect the substance of its contractual rights and obligations.

A.3 TRG members also observed that:

- (a) considerations that might be relevant in the assessment of whether the legal form of a single contract reflects the substance of its contractual rights and contractual obligations include:
 - (i) interdependency between the different risks covered;
 - (ii) whether components lapse together; and
 - (iii) whether components can be priced and sold separately.
- (b) an example of when it may be appropriate to override the presumption that a single legal contract is the lowest unit of account is when more than one type of insurance cover is included in one legal contract solely for the administrative convenience of the policyholder and the price is simply the aggregate of the standalone prices for the different insurance covers provided.
- (c) Appendix A to Agenda Paper 1 provides specified fact pattern of a contract containing a long term life coverage with annual renewable health riders. At each annual renewal date the entity can reassess the risks and can set a price that fully reflects these risks with respect to the

renewable health riders, but cannot reprice or cancel the life coverage of the contract. The following factors indicate its substance as a single contract:

- (i) the renewable health riders are not sold separately;
- (ii) if the life coverage is cancelled by the policyholder, the renewable riders are cancelled at the same time; and
- (iii) the renewable riders are rarely cancelled and most of them remain until the end of the coverage period of the life contract.

Therefore, in relation to the example in Appendix A to Agenda Paper 1:

- (i) the contract is included in its entirety in a single portfolio and in a single group and is not split to reflect the ways its components would be allocated to portfolios and groups as if there were issued as separate contracts.
- (ii) the cash flows within the boundary of the contract would be assessed for the contract in its entirety. The assessment of when a substantive obligation to provide the policyholder with services ends will be performed for the contract in its entirety. Therefore, in this example, cash flows related to the premiums within the contract boundaries include cash flows related to the renewable health riders beyond the annual re-pricing date.
- (iii) the contract would be evaluated against the criteria for applying the premium allocation approach in its entirety.

Appendix B—Scenario and factors described in the submission

Scenario and factors described in the submission

- B.1 Scenario: a homeowner’s policy and a motor policy are sold together with a discount. The policies are entered into at the same time and sold by the insurer to the same policyholder. The following factors were described:
- (a) in pricing the contracts the insurer takes into account the risks associated with policyholder’s location and their interaction, such as the likelihood of both the home and the vehicle being damaged (fire, flood, burglary), as well as other risks specific only to home or motor policies.
 - (b) in determining the price, the insurer also takes into account the recovery of its acquisition costs (including direct commissions) associated with signing up the same customer for two products, as opposed to issuing those products to two different customers. Additionally, the same policyholder applying for only one of the products would not get the same level of discount as it applied when purchasing two. If the contracts are considered separately, then due to the level of discount given, one of the contracts may be onerous, however, the combination of contracts overall would not be onerous if viewed together.
 - (c) in some cases, the policies may lapse independently of one another, without affecting the terms of the remaining contract. In other cases, the policies cannot be lapsed independently, so that by cancelling one policy, the other one also lapses at the same time.

- B.2 Submission view: the submission expresses some views that two contracts should be combined and other views that they should not be combined depending on which factors shown above are considered most indicative of the substance of the contracts.

Factors considered by staff

- B.3 Determining whether it is necessary to treat a set or series of insurance contracts as a single contract involves significant judgement and careful consideration of all relevant facts and circumstances. Below are some factors considered by the staff based on the fact pattern provided.
- B.4 **Considering B.1(a)** – interdependency between the different risks covered by a set or series of contracts could be indicative that the contracts are designed to achieve an overall commercial effect. There is an interdependency between risks if different risks are dependent on each other; for example, when one offsets or reduces the other. An example of risks that are interdependent is mortality risk and longevity risk. Conversely, two separate contracts being subject to the same common risk may not reflect an interdependency between risks.
- B.5 **Considering B.1(b)** – in this example, the two policies are sold separately and a discount is offered if the policyholder buys both. The staff view is that the existence of a discount, in itself, does not mean that a set or series of contracts achieves an overall commercial effect. The staff observe that IFRS 17 does not prescribe how to appropriately allocate a discount given between multiple contracts.
- B.6 **Considering B.1(c)** – when the lapse or maturity of one contract causes the lapse or maturity of another contract, the staff view is that this strongly indicates that these contracts achieve an overall commercial effect and should be treated as a single contract.

STAFF PAPER

May 2018

Project	Transition Resource Group for IFRS 17 <i>Insurance Contracts</i>		
Paper topic	Determining the risk adjustment for non-financial risk in a group of entities		
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Introduction

1. We have received a submission about the level at which the risk adjustment for non-financial risk is determined:
 - (a) in the individual financial statements of entities that are part of a consolidated group (ie parent and subsidiary entities that issue insurance contracts); and
 - (b) in the consolidated financial statements of the group of entities.
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. Appendix A—Example provided in the submission.

Background information

5. On determining the risk adjustment for non-financial risk, 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.
6. In Appendix A of IFRS 17 the risk adjustment for non-financial risk is defined 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.
7. 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.
8. 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, the risk adjustment for non-financial risk also reflects:

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

9. Paragraph BC211(c) of the Basis for Conclusions on IFRS 17 explains that the International Accounting Standards Board (Board) decided the requirements for a separate risk adjustment for non-financial risk:

will faithfully represent circumstances in which the entity has charged insufficient premiums for bearing the risk that the claims might ultimately exceed expected premiums.

10. Paragraph BC213(b) of the Basis for Conclusions on IFRS 17 explains:

the objective of the risk adjustment for non-financial risk is to reflect the entity's perception of the economic burden of its non-financial risks. Specifying a level of aggregation for determining the risk adjustment for non-financial risk that was inconsistent with the entity's view of the burden of non-financial risk would contradict the objective of reflecting the entity's perception in the risk adjustment for non-financial risk.

Implementation question

11. The submission asks at which level the risk adjustment for non-financial risk is required to be determined:
- (a) in the individual financial statements of entities that are part of a consolidated group (ie parent and subsidiary entities that issue insurance contracts); and
 - (b) in the consolidated financial statements of the group of entities.
12. In the fact pattern considered (see Appendix A to this paper), at the individual entity level the risk adjustment for non-financial risk reflects the compensation the

entity requires for the groups of insurance contracts it issues and it does not reflect the degree of risk diversification that is available at the group of entities level.

13. 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. The submission expresses three views:
- (a) View A—The risk adjustment for non-financial risk for contracts issued by the subsidiary can be determined considering the degree of risk diversification available at the group of entities level. This is because IFRS 17 discusses the compensation the entity **would** require and not the compensation the entity actually charges [emphasis added].
 - (b) View B—The risk adjustment for non-financial risk is determined considering the issuing entity’s perception, which does not reflect the degree risk diversification that is not available to the entity.
 - (c) View C—Both approaches are acceptable. Judgement should be applied.
14. 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. The submission expresses three views:
- (a) View A—In the consolidated financial statements, the risk adjustment for non-financial risk can be determined considering the degree of risk diversification available only at the group of entities level. This is consistent with the view that the reporting entity is the group.

- (b) View B—The risk adjustment for non-financial risk is determined considering the issuing entity’s perception, which does not reflect the degree of risk diversification that is not available to the entity.
- (c) View C—Both approaches are acceptable. Judgement should be applied.

Review of accounting requirements

15. The risk adjustment for non-financial risk reflects ‘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’, as stated in the definition of the risk adjustment for non-financial risk in Appendix A of IFRS 17. The objective of the risk adjustment for non-financial risk is to reflect the entity’s perception of the economic burden of its non-financial risks, as explained in paragraph BC213(b) of the Basis for Conclusions on IFRS 17. IFRS 17 does not specify the level of aggregation at which to determine the risk adjustment for non-financial risk, to do so would contradict with the objective.
16. Paragraph B88 of IFRS 17 says ‘the compensation the entity **would require** for bearing the non-financial risk’ [emphasis added]. The entity does not charge the policyholder an explicit separate amount for bearing non-financial risk. Rather, this is implicit within the overall actual amount charged by the entity. Therefore, the risk adjustment for non-financial risk represents the compensation that the entity would require if it was to charge the policyholder an explicit separate amount for bearing non-financial risk.
17. An entity may choose or be required, for reasons unconnected with bearing that non-financial risk, to charge a premium which does not result in a full recovery of the risk-adjusted cash flows. This could be for legal, commercial or regulatory reasons. Such pricing decisions are reflected in the loss component and consequently in profit or loss. The faithful representation of circumstances in

which the entity has charged insufficient premiums for bearing the risk that the claims might ultimately exceed expected premiums was considered by the Board when it decided that a separate risk adjustment was required, as explained in paragraph BC211(c) of the Basis for Conclusions on IFRS 17.

18. The staff view is that the term ‘would require’ should not be interpreted in a manner that is inconsistent with the objective of the risk adjustment for non-financial risk. Therefore, ‘the compensation the entity would require’ does not extend to consider the theoretical amount that would have been required if the entity had considered different compensation for bearing non-financial risk.

Individual financial statements of an entity that is part of a consolidated group

19. Applying paragraph B88 of IFRS 17, an entity shall only reflect diversification benefit in the risk adjustment for non-financial risk to the extent that the diversification benefit has been included when determining the compensation the entity would require for bearing non-financial risk. Therefore, the degree of risk diversification that occurs at a level that is higher than the 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 entity would require for bearing non-financial risk related to insurance contracts issued by the entity. Equally, risk diversification that occurs at a level that is higher than the entity level must not be considered in the determination of the risk adjustment for non-financial risk if it is not considered when determining the compensation the entity would require for bearing non-financial risk related to insurance contracts issued by the entity.

Consolidated financial statements of the group of entities

20. The submission also asks whether the risk adjustment for non-financial risk for a group of insurance contracts presented in the consolidated financial statements of

the group should reflect the degree of risk diversification available only to the consolidated group as a whole (see paragraph 14 of this paper). In other words, the submission asks whether the risk adjustment for non-financial risk can be smaller at a consolidated group level when compared to the risk adjustment for non-financial risk at the individual entity level to reflect the diversification benefit of the group of entities.

21. Determining the compensation that the entity would require for bearing non-financial risk related to insurance contracts issued by the entity is a single decision that is made by the entity that is party to the contract (ie the issuer of the insurance contract). In making that decision the entity chooses what factors to consider, including whether or not to consider the degree of risk diversification benefit available to the group of entities. Therefore, the staff view is 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 entity level. Determining a different risk adjustment for non-financial risk at a consolidated group level would be inconsistent with the principles of the risk adjustment for non-financial risk in IFRS 17.

TRG Discussion

Question to TRG members

What are your views on the implementation question presented above?

Appendix A—Example provided in the submission

A.1 The submission considers the following example:

- (a) P is a parent holding company with two subsidiaries: subsidiary A and subsidiary L. The group prepares consolidated financial statements that include the results of P, A and L.
- (b) Subsidiary A sells annuity policies and the risk adjustment for non-financial risk reflects the compensation it requires for taking on the risk of policyholders living longer than expected. Subsidiary L sells term life policies paying lump sums on death and the risk adjustment for non-financial risk reflects the compensation it requires for taking on the risk of policyholders dying earlier than expected.
- (c) The overall group of entities is less sensitive to the mortality risk than subsidiaries A or L are individually, given that economically the mortality risk in A and L partly offset each other. In considering whether the group of entities is less sensitive to mortality risk, the group management considers capital requirements of individual legal entities and availability of profit of one entity to offset losses of another entity.

A.2 Staff view: according to A.1(b)–(c) above, subsidiaries A and L do not consider any diversification benefit available at a higher level than at an individual entity level when setting the price. Therefore, any diversification benefit available higher than at that level shall not be considered in the determination of the risk adjustment for non-financial risk. Furthermore, 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 entity level. The staff view for this example aligns with View B in the submission.

STAFF PAPER

May 2018

Project	Transition Resource Group for IFRS 17 <i>Insurance Contracts</i>		
Paper topic	Cash flows within the contract boundary		
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Introduction

1. We have received a number of submissions about the cash flows within the boundary of an insurance contract. Some submissions ask how to apply the requirements in paragraph 34 of IFRS 17 *Insurance Contracts* regarding:
 - (a) the practical ability to set a price at a future date that fully reflects the risks of a contract or portfolio from that date; and
 - (b) options to add insurance coverage.
2. Some submissions ask for further information about a few aspects discussed at the February 2018 meeting of the Transition Resource Group for IFRS 17 (TRG). Those aspects are included in the background section of this paper. Those submissions do not include any new information for the TRG to consider.
3. The objective of this paper is to provide background and an accounting analysis to support discussion at the TRG.

Structure of the paper

4. As background information, this paper includes:
 - (a) an extract of the requirements on contract boundary in IFRS 17 that are relevant for the topics discussed in this paper; and
 - (b) some observations on aspects already discussed at the February 2018 meeting of the TRG.
5. In addition, for each of the topics mentioned in paragraph 1 above, this paper includes:
 - (a) an implementation question; and
 - (b) review of accounting requirements.
6. There is an appendix to this paper (Appendix A) that includes a flowchart that may assist the discussion.

Background information

Extract of the requirements on contract boundary in IFRS 17

7. 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.

8. Paragraph 35 of IFRS 17 states:

An entity shall not recognise as a liability or as an asset any amounts relating to expected premiums or expected claims outside the boundary of the insurance contract. Such amounts relate to future insurance contracts.

9. Paragraph B61 of IFRS 17 states:

Estimates of cash flows in a scenario shall include all cash flows within the boundary of an existing contract and no other cash flows. An entity shall apply paragraph 2 in determining the boundary of an existing contract.

10. 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).

11. Paragraph B62 of IFRS 17 states:

Many insurance contracts have features that enable policyholders to take actions that change the amount, timing, nature or uncertainty of the amounts they will receive. Such features include renewal options, surrender options, conversion options and options to stop paying premiums while still receiving benefits under the contracts. The measurement of a group of insurance contracts shall reflect, on an expected value basis, the entity's current estimates of how the policyholders in the group will exercise the options available, and the risk adjustment for non-financial risk shall reflect the entity's current estimates of how the actual behaviour of the policyholders may differ from the expected behaviour. This requirement to determine the expected value applies regardless of the number of contracts in a group; for example it applies even if the group comprises a single contract. Thus, the measurement of a group of insurance contracts shall not assume a 100 per cent probability that policyholders will:

- (a) surrender their contracts, if there is some probability that some of the policyholders will not; or
- (b) continue their contracts, if there is some probability that some of the policyholders will not.

12. Paragraph B63 of IFRS 17 states:

When an issuer of an insurance contract is required by the contract to renew or otherwise continue the contract, it shall apply paragraph 34 to assess whether premiums and related cash flows that arise from the renewed contract are within the boundary of the original contract.

13. Paragraph B64 of IFRS 17 states:

Paragraph 34 refers to an entity's practical ability to set a price at a future date (a renewal date) that fully reflects the risks in the contract from that date. An entity has that practical ability in the absence of constraints that prevent the entity from setting the same price it would for a new contract with the same characteristics as the existing contract issued on that date, or if it can amend the benefits to be consistent with the price it will charge. Similarly, an entity has that practical ability to set a price when it can reprice an existing contract so that the price reflects overall changes in the risks in a portfolio of insurance contracts, even if the price set for each individual policyholder does not reflect the change in risk for that specific policyholder. When assessing whether the entity has the practical ability to set a price that fully reflects the risks in the contract or portfolio, it shall consider all the risks that it would consider when underwriting equivalent contracts on the renewal date for the remaining coverage. In determining the estimates of future cash flows at the end of a reporting period, an entity shall reassess the boundary of an insurance contract to include the effect of changes in circumstances on the entity's substantive rights and obligations.

Observations on aspects already discussed at the February 2018 meeting of the TRG

Risks of the particular policyholder or of the portfolio of insurance contracts that contains the contract

14. At the February 2018 meeting of the TRG it was observed that:

- (a) paragraph 34(a) of IFRS 17 refers to the practical ability to reassess the risks of the policyholder (ie policyholder risk);
- (b) paragraph 34(b) of IFRS 17 should be read as an extension of the risk assessment in paragraph 34(a) from the individual to portfolio level (ie policyholder risks in the portfolio), without extending policyholder

risks to all types of risks and considerations applied by an entity when pricing a contract; and

- (c) policyholder risk includes the risk transferred from the policyholder to the entity, such as insurance risk and financial risk, and therefore excludes lapse risk and expense risk.

15. Paragraph B64 of IFRS 17 provides guidance on paragraph 34 of IFRS 17 and requires that, when assessing whether an entity has the practical ability to set a price at a renewal date that fully reflects the risks in the contract or portfolio, the entity shall consider all the risks that it would consider when underwriting equivalent contracts on the renewal date for the remaining coverage. Two submissions question the meaning of ‘all the risks’ in the light of the discussion held at the February 2018 meeting of the TRG.
16. Paragraph B64 of IFRS 17 refers to ‘all the risks’ that are assessed as part of the underwriting process of the contracts. Reading paragraph B64 of IFRS 17 in its context of providing guidance on paragraph 34 of IFRS 17, the risks referred to by ‘all the risks’ are policyholder risks—ie risks transferred from the policyholder to the entity. This observation is consistent with the observations made at the February 2018 meeting of the TRG, which are summarised in paragraph 14 of this paper.

Contracts with multiple coverages

17. At the February 2018 meeting of the TRG it was observed that:
 - (a) the lowest unit of account that is used in IFRS 17 is the contract that includes all insurance components.
 - (b) a contract with the legal form of a single contract would generally be considered a single contract in substance. However, there might be circumstances where the legal form of a single contract would not reflect the substance of its contractual rights and obligations.

- (c) combining different types of coverages that have different risks into one legal insurance contract is not, in itself, sufficient to conclude that the legal form of the contract does not reflect the substance of its contractual rights and obligations.
 - (d) considerations that might be relevant in the assessment of whether the legal form of a single contract reflects the substance of its contractual rights and contractual obligations include:
 - (i) interdependency between the different risks covered;
 - (ii) whether components lapse together; and
 - (iii) whether components can be priced and sold separately.
18. For a contract that includes two insurance components and that is considered a single contract, the assessment of the cash flows within the boundary is performed for the contract in its entirety. The contract is not split into two separate insurance components to assess the contract boundary of each component as if they were issued as separate contracts.
19. One submission questions the determination of the contract boundary in the following example:
- (a) an entity issues a single contract with both life and health coverages, which the entity also sells separately;
 - (b) every year, the entity has the practical ability to reassess the risks of the life coverage and, as a result, can set a price or level of benefits for the life coverage that fully reflects those risks; and
 - (c) every two years, the entity has the practical ability to reassess the risks of the health coverage and, as a result, can set a price or level of benefits for the health coverage that fully reflects those risks.

20. The staff note that the entity needs to assess whether separating life and health coverages would reflect the substance of contractual rights and obligations. The fact that the life and health coverages can be sold separately is a factor to consider in performing this assessment.
21. In this example, assuming that the contract is accounted for as a single contract, in applying paragraph 34 of IFRS 17, the cash flows used to measure the contract would be those related to premiums arising up to the health coverage repricing date—ie premiums for two years. This is because the entity cannot set a price to reflect reassessed risks of the entire contract at the life coverage repricing date (refer to Appendix A to Agenda Paper 1 of the February 2018 meeting of the TRG).

A. Practical ability to set a price at a future date that fully reflects the risks of a contract or portfolio from that date

A. Implementation question

22. The submissions ask what constraints or limitations, other than those arising from the terms of an insurance contract, would be relevant in assessing the practical ability of an entity to reassess the risks of the particular policyholder (or of the portfolio of insurance contracts that contains the contract) and set a price or level of benefits that fully reflects those risks.
23. For example, the submissions note that market competitiveness and commercial considerations might affect the entity's ability to reprice an insurance contract to fully reflect the reassessed risks of the contract or portfolio. This is because, although permitted by the terms of the contract, an increase in the price (or a decrease in the level of benefits) of the contract to reflect an increase in the risks of the particular policyholder or portfolio might result in unfavourable economic consequences for the entity. Policyholders might decide to switch to a competitor

of the entity if that competitor can or is willing to write an equivalent contract at a price or level of benefits that is better for the policyholders.

24. One submission also notes that setting a price that fully reflects the reassessed risks of the contract or portfolio might expose the entity to reputational risks or to negative reactions from its distribution channels—for example, negative publicity regarding the entity’s repricing practice might cause a decline in its customer base.
25. One submission notes that, in applying paragraph B64 of IFRS 17, an entity’s practical ability is not constrained if the entity can set the same price it would for a new contract with the same characteristics as the existing contract issued on that date, or if it can amend the benefits to be consistent with the price it will charge. The submission provides two views:
- (a) View A—Commercial considerations might not be relevant when considering the requirements in paragraph 34 of IFRS 17. Market pressure to remain competitive is likely to apply to new contracts as well as to existing contracts. Consequently, the entity’s practical ability to reprice would not be constrained by commercial considerations.
 - (b) View B—Commercial considerations might be relevant when considering the requirements in paragraph 34 of IFRS 17. Market pressure might prevent the entity from fully repricing contracts with policyholders that are riskier to insure than the average individual policyholder (for example, policyholders with specific health conditions). If the equivalent new contract with the same risks is priced higher than the existing contract, the entity’s practical ability to reprice would be constrained by commercial considerations.

A. Review of accounting requirements

26. A constraint that equally applies to new contracts and existing contracts would not limit an entity's practical ability to reprice existing contracts to reflect their reassessed risks. This is because, as explained in paragraph B64 of IFRS 17, the entity could either:
- (a) set the same price for an existing contract and a new contract with the same characteristics (see paragraph 34(a) of IFRS 17); or
 - (b) reprice an existing contract to reflect overall changes in the risks in a portfolio, even if the price set for each individual policyholder does not reflect the change in risk for that specific policyholder (see paragraph 34(b) of IFRS 17).
27. In applying paragraphs B61 and 2 of IFRS 17, when determining the boundary of an insurance contract, an entity shall consider its substantive rights and obligations, whether they arise from a contract, law or regulation. However, the entity shall disregard terms that have no commercial substance (ie no discernible effect on the economics of the contract). As noted in paragraph BC161 of the Basis for Conclusions on IFRS 17, if an entity has the practical ability to reassess the risk presented by a policyholder, but does not have the right to set a price that fully reflects the reassessed risk, the contract still binds the entity. Thus, cash flows after that point would be within the boundary of the existing contract, unless the restriction on the entity's ability to reprice the contract is so minimal that it is expected to have no commercial substance.
28. Consequently, when determining whether it has the practical ability to set a price at a future date that fully reflects the reassessed risks of a contract or a portfolio, an entity shall:
- (a) consider contractual, legal and regulatory restrictions; and
 - (b) ignore restrictions that have no commercial substance.

29. Regulatory restrictions might be relevant in assessing the practical ability of an entity to set a level of benefits that fully reflect the reassessed risks of a policyholder or a portfolio. The staff believe that considerations similar to those discussed in paragraph 26 of this paper would be relevant when assessing whether regulatory constraints affect the entity's practical ability to reprice contracts.
30. One submission provides an example where some local regulations might:
- (a) require an entity to fix contractual benefits at contract inception; and
 - (b) prevent an entity from reducing those benefits over the whole term of the contract (benefits enhancements might instead be allowed).
31. Although such regulatory restrictions might prevent the entity from amending the benefits of an existing contract, in applying paragraph B64 of IFRS 17, the entity shall assess whether those restrictions would also affect the pricing of existing contracts and new contracts to the same extent. If the entity can set the same price for the existing contract it would for a new contract with the same characteristics issued on that date, or can reprice the existing contract to reflect overall changes in the risks in a portfolio, the entity's practical ability to set a price that fully reflects the risks of the policyholders would not be constrained by such regulatory restrictions.
32. IFRS 17 uses the term practical ability and does not specify the sources of constraints. Therefore, it does not limit pricing constraints to contractual, legal and regulatory constraints. Market competitiveness and commercial considerations are factors that an entity typically considers when pricing new contracts and repricing existing contracts. When considering the requirements in paragraph 34 of IFRS 17, and consistent with paragraph 26 of this paper, constraints are irrelevant to the contract boundary assessment if they equally apply to new and existing policyholders in the same market.
33. A constraint that limits an entity's practical ability to price or reprice contracts differs from choices that an entity makes (pricing decisions), which may not limit

the entity's practical ability to reprice existing contracts in the way envisaged by paragraph B64 of IFRS 17.

A. TRG discussion

Question to TRG members

What are your views on the implementation question presented above?

B. Options to add insurance coverage

B. Implementation question

34. The submissions ask how to determine the contract boundary of insurance contracts that include an option to add insurance coverage at a future date. For those contracts the entity is obligated to provide additional coverage if the policyholder exercises the option. The submissions distinguish between:
- (a) terms that are guaranteed by the entity—ie the entity sets the premiums for the additional coverage at inception and cannot reprice the premiums for the additional coverage to reflect reassessed risks of the policyholder (or of the portfolio that contains the contract); and
 - (b) terms that are not guaranteed by the entity—ie the entity sets the premiums for the additional coverage only when the policyholder exercises the option.
35. The submissions provide two alternative views:
- (a) View A—The option to add insurance coverage is a feature of the insurance contract. The cash flows resulting from the option are included in the contract boundary. The measurement of the group of insurance contracts reflects the entity's estimates of how the policyholders in the group will exercise the option.
 - (b) View B—The cash flows resulting from the option to add insurance coverage would be excluded from the contract boundary if the entity has the practical ability to set the premiums for the additional coverage to reflect the reassessed risks of the policyholder. In that case, when the policyholder exercises the option to add insurance coverage the entity would need either to (i) change the estimates of the fulfilment cash flows of the original contract or (ii) treat the entire contract (original and new addition) as a new contract.

B. Review of accounting requirements

36. Paragraph B62 of IFRS 17 provides guidance for insurance contracts that have features that enable policyholders to take actions that change the amount, timing, nature or uncertainty of the amounts of the insurance contracts, such as renewal options. In particular, that paragraph requires that the measurement of a group of insurance contracts shall reflect, on an expected value basis, the entity's current estimates of how the policyholders in the group will exercise the options available.
37. The staff therefore think that it is clear that an option to add insurance coverage is a feature of the insurance contract. Unless the entity considers that such an option is a separate contract (see paragraph 17 of this paper), the option is an insurance component that is not measured separately from the remainder of the insurance contract. The assessment about whether the cash flows arising from that option are within the boundary of the insurance contract is performed together with the assessment of all the other cash flows arising from other features of the insurance contract. That assessment is performed applying paragraph 34 of IFRS 17.
38. In applying paragraph 34 of IFRS 17, an entity is no longer bound by an existing contract at the point at which the contract confers on the entity the practical ability to reassess the risks and, as a result, the right to set a price for the contract that fully reflects those risks. Thus, any cash flows arising beyond that point occur beyond the boundary of the existing contract and relate to a future contract, not to the existing contract.
39. For an option with terms that are guaranteed by the entity, the staff think that it is clear that the cash flows arising from the option are within the boundary of the contract because the entity cannot reprice the contract, in its entirety, to reflect the reassessed risks when it has guaranteed the price for one of the risks included in the contract. As noted in paragraph BC162(b) of the Basis for Conclusions on IFRS 17, renewal options bind the entity, but not the policyholder, by requiring the entity to continue to accept premiums and provide coverage but permitting the

policyholder to stop paying premiums. The premiums the entity is required to accept and the resulting coverage it is required to provide fall within the boundary of the contract.

40. For an option with terms that are not guaranteed by the entity, the cash flows arising from the option might be either within or outside of the contract boundary. This would depend on whether the entity has the practical ability to set a price for the contract (including the option) that fully reflects the reassessed risk.
41. If the entity has the practical ability to reprice the whole contract when the policyholder exercises the option to add coverage, the cash flows related to premiums after the option exercise date would be outside the contract boundary. In applying paragraph 35 of IFRS 17, those cash flows relate to future contracts. Consequently, when the policyholder exercises the option to add coverage, the entity treats the contract as a new contract.
42. If the entity does not have the practical ability to reprice the whole contract when the policyholder exercises the option to add coverage, the cash flows arising from the premiums after the option exercise date would be within the contract boundary and would therefore be included in the measurement of the contract on initial recognition. When the policyholder exercises the option to add coverage, the entity treats changes in cash flows as changes in estimates of fulfilment cash flows by applying paragraphs 40–52 of IFRS 17.
43. In applying paragraph 72 of IFRS 17, the exercise of a right included in the terms of a contract is not a modification. If, conversely, the entity subsequently modifies the contract to include an option to add coverage, the entity should apply the requirements about the modification of an insurance contract in paragraph 72 of IFRS 17.

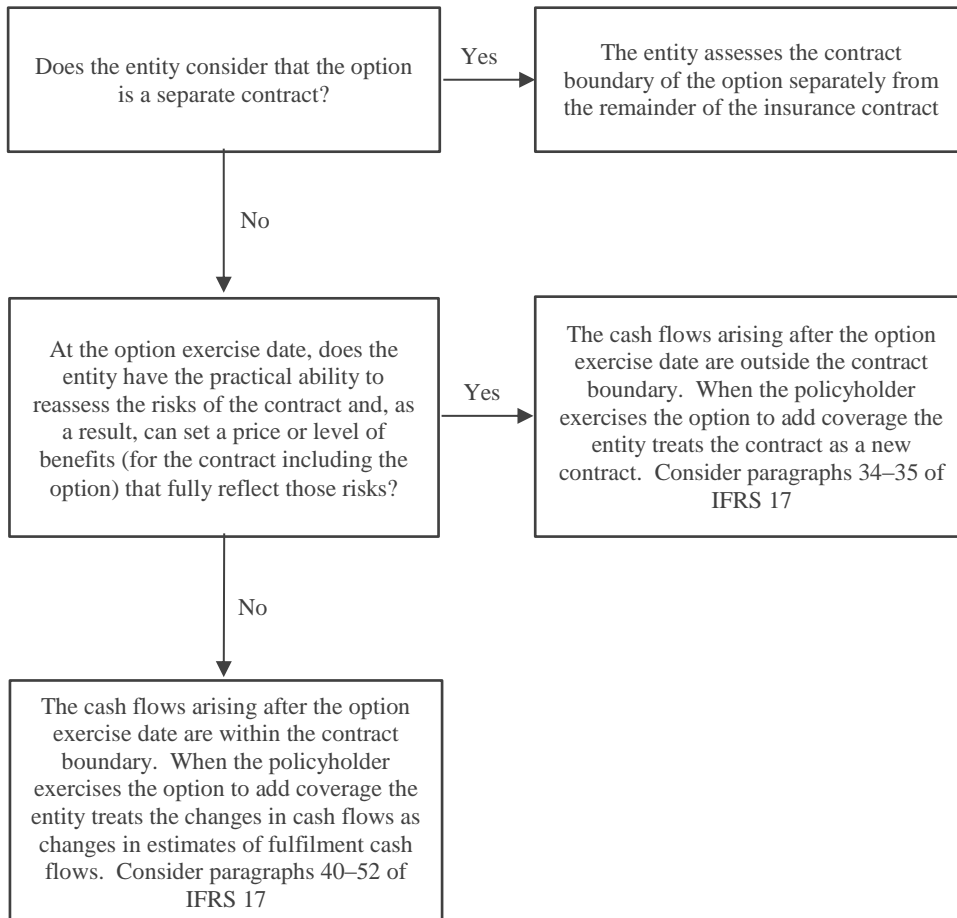
B. TRG Discussion

Question to TRG members

What are your views on the implementation question presented above?

Appendix A—Flowchart

A.1 The following flowchart may assist the assessment of the cash flows within the boundary of a contract that includes an option to add coverage.



STAFF PAPER

May 2018

Project	Transition Resource Group for IFRS 17 <i>Insurance Contracts</i>		
Paper topic	Boundary of reinsurance contracts held with repricing mechanisms		
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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 how the boundary of a reinsurance contract held should be determined when the reinsurer has the right to reprice remaining coverage prospectively. In the fact pattern provided in the submission the reinsurer can choose:
 - (a) not to exercise the right to reprice. In this case, the entity (the holder of the contract) is committed to continue paying premiums to the reinsurer; or
 - (b) to exercise the right to reprice. In this case, the entity has the right to terminate coverage.
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 6 February 2018 with respect to Agenda Paper 3; and
 - (b) Appendix B—Fact set provided in the submission.

Background information

5. Paragraph 33 of IFRS 17 states that all future cash flows within the boundary of each contract in a group of insurance contracts shall be included in the measurement of that group.
6. Paragraph 34 of IFRS 17 sets out the following on how to determine whether cash flows are within the boundary of an insurance contract:

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. 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.

7. In February 2018 the TRG discussed Agenda Paper 3 *Boundary of reinsurance contracts held*, on the topic of reading paragraph 34 of IFRS 17 with respect to reinsurance contracts held. TRG members observed that the application of the requirements in paragraph 34 of IFRS 17 to reinsurance contracts held means that cash flows within the boundary of a reinsurance contract held arise from the substantive rights and obligations of the entity—ie the holder of the contract, therefore:

- (a) the substantive right is to receive services from the reinsurer; and
- (b) the substantive obligation is to pay amounts to the reinsurer.

The discussion was focused on when the substantive right to receive services from the reinsurer ends. An extract from the meeting summary detailing the outcome of that discussion is included in Appendix A to this paper.

Implementation question

8. The submission asks how the boundary of a reinsurance contract held should be determined when the reinsurer has the right to reprice remaining coverage prospectively. In the fact pattern provided in the submission the reinsurer can choose:

- (a) not to exercise the right to reprice. In this case, the entity (the holder of the contract) is committed to continue paying premiums to the reinsurer; or
 - (b) to exercise the right to reprice. In this case, the entity has the right to terminate coverage.
9. In the fact pattern provided, the reinsurer can adjust premium rates at any time, subject to a minimum notice period of three months.
10. The fact set provided in the submission is included in Appendix B to this paper.
11. The submission expresses two views:
- (a) View A—The entity has a substantive obligation to pay premiums to the reinsurer for the full duration of the underlying contracts. Therefore, the contract boundary would reflect the full duration of underlying contracts. The projected future cash flows of the reinsurance contract held could (if considered the best estimate) reflect assumptions including future premium adjustments and recapture decisions.
 - (b) View B—The contract boundary should end at the first point at which the reinsurer has the right to increase premium rates, as the entity as the holder of the contract has no substantive right to receive service beyond such date.

Review of accounting requirements

12. In the February 2018 meeting, the TRG observed that the cash flows within the boundary of a reinsurance contract held arise from the substantive rights and obligations of the entity as the holder of the contract. Therefore:
- (a) the substantive right is to receive services from the reinsurer; and
 - (b) the substantive obligation is to pay amounts to the reinsurer.

13. Applying paragraph 34 of IFRS 17 to reinsurance contracts held, cash flows are within the contract boundary if they arise from substantive rights and obligations that exist during the reporting period in which the entity is compelled to pay amounts to the reinsurer **or** in which the entity has a substantive right to receive services from the reinsurer [emphasis added]. Therefore, when determining the boundary of the contract an entity needs to consider both the substantive right and substantive obligation.
14. In the February 2018 meeting, the TRG discussed what was meant by the substantive right to receive services from the reinsurer. The TRG observed that a substantive right to receive services from the reinsurer ends when the reinsurer has the practical ability to reassess the risks transferred to the reinsurer and can set a price or level of benefits for the contract to fully reflect the reassessed risk.
15. The TRG also observed that for some reinsurance contracts, the reinsurer can terminate the coverage at any time with a three month notice period. In these circumstances, the contract boundary would exclude cash flows arising from the reinsurance contract held that are related to underlying insurance contracts issued outside of that three month notice period because the entity no longer has a right to receive services from the reinsurer.
16. The staff observe that the above observations are valid in the context of assessing when the substantive right to receive services from the reinsurer ends. The discussion at the TRG was based on a fact pattern where no substantive obligation to pay premiums to the reinsurer exists, and therefore TRG members did not discuss this aspect of the requirements of paragraph 34 of IFRS 17. The fact pattern in this paper considers when the entity must continue to pay premiums to the reinsurer if the reinsurer does not reprice the contract.
17. The staff view is that a right to terminate coverage that is triggered by the reinsurer's decision to reprice the reinsurance contract is not relevant when considering whether a substantive obligation to pay premiums exists. Such a right is not within the entity's control and therefore the entity would continue to be compelled to pay premiums for the entire contractual term.

18. The staff note that the fact that the entity may receive services for a shorter period because of the reinsurer's right to reprice would not result in a shorter period contract boundary. This is because the entity must consider whether it has either a substantive right to receive services **or** a substantive obligation to pay amounts for each reporting period. In the fact pattern provided, the obligation to pay premiums extends to reporting periods after the entity's right to receive service ceases to exist. Therefore, the staff disagree with View B of the submission.
19. The staff view is that the entity's expectations about the amount and timing of future cash flows, including with respect to the probability of the reinsurer repricing the contract, would be reflected in the fulfilment cash flows. This view is consistent with View A of the submission.
20. The staff observe that this paper considers a reinsurer's right to reprice remaining coverage prospectively. The submission notes that there could be other fact patterns where a reinsurer has the right to reprice all coverage provided by a contract (including coverage already provided). The staff note that in these fact pattern, entities would need to consider whether the reinsurance contract transfers significant insurance risk applying paragraph B27(b) of IFRS 17.

TRG Discussion

Question to TRG members

What are your views on the implementation question presented above?

Appendix A—Extract: summary of the TRG for IFRS 17 meeting held on 6 February 2018 with respect to Agenda Paper 3

Boundary of reinsurance contracts held (Agenda Paper 3)

- A.1 Agenda Paper 3 addresses a submission received about how to read paragraph 34 of IFRS 17 regarding the boundary of an insurance contract with respect to reinsurance contracts held.
- A.2 TRG members discussed the analysis in Agenda Paper 3 and observed that:
- (a) the application of the requirements in paragraph 34 of IFRS 17 to reinsurance contracts held means that cash flows within the boundary of a reinsurance contract held arise from the substantive rights and obligations of the entity—ie the holder of the contract, therefore:
 - (i) the substantive right is to receive services from the reinsurer; and
 - (ii) the substantive obligation is to pay amounts to the reinsurer.
 - (b) a substantive right to receive services from the reinsurer ends when the reinsurer has the practical ability to reassess the risks transferred to the reinsurer and can set a price or level of benefits for the contract to fully reflect the reassessed risk or the reinsurer has a substantive right to terminate the coverage.
 - (c) accordingly, the boundary of a reinsurance contract held could include cash flows from underlying contracts covered by the reinsurance contract that are expected to be issued in the future.

A.3. TRG members also observed that:

- (a) for some reinsurance contracts, the reinsurer can terminate the coverage at any time with a three month notice period. In these circumstances, the contract boundary would exclude cash flows related to premiums outside of that three month notice periods.
- (b) there is operational complexity involved in applying paragraph 34 of IFRS 17 to reinsurance contracts held because it is a change from existing practice. Those existing accounting practices for reinsurance contracts held generally:
 - (i) do not require cash flows related to future underlying insurance contracts to be estimated; and
 - (ii) net the effect in profit or loss of holding reinsurance in accounting for the insurance contract.

A Board member observed that those existing accounting practices are inconsistent with accounting for reinsurance contracts held separately to the underlying insurance contracts using measurement principles for reinsurance contracts held that are consistent with the measurement of the insurance contracts issued.

A.4. Some TRG members questioned the interaction between paragraphs 34 and 62(a) of IFRS 17. The staff noted that paragraph 62(a) of IFRS 17 is a recognition requirement for reinsurance contracts held that provide proportionate coverage, and is not a measurement requirement.

Appendix B—Fact set provided in the submission

Fact set provided in the submission

B.1 The submission describes a situation whereby the reinsurer has the right to change premium rates for reinsurance contracts already ceded. An increase in premium rates would trigger the right of the entity to recapture the business (ie terminate the reinsurance coverage). These are the facts applicable for this situation:

- (a) the reinsurer has the right to adjust the premium rates it will charge for remaining coverage related to underlying insurance contracts that have already been issued and that are covered by the reinsurance contract;
- (b) premium adjustments apply prospectively and would not allow the reinsurer to recover losses already incurred for coverage already provided under the contract;
- (c) there are no substantive restrictions on the reinsurers ability to reassess the risks of the reinsurance contract and to adjust premium rates to reflect those risks;
- (d) the reinsurer can adjust premium rates at any time, subject to a minimum notice period of three months;
- (e) if the reinsurer does not increase premium rates, the holder of the contract has no right to recapture the business and must continue to pay premiums to the reinsurer;
- (f) if the reinsurer provides notice that it intends to increase premium rates, the entity as the holder of the contract has the right to recapture the business; and
- (g) if the entity recaptures the business, the entity would cease paying premiums and the reinsurer would cease providing coverage as of the recapture date. There is no financial settlement associated with the recapture (besides the refund of paid but unearned premium).

B.2 The submission expresses two views:

- (a) View A—The entity has a substantive obligation to pay premiums to the reinsurer for the full duration of the underlying contracts. Therefore, the contract boundary would reflect the full duration of underlying contracts. The projected future cash flows of the reinsurance contract held could (if considered the best estimate) reflect assumptions including future premium adjustments and recapture decisions.
- (b) View B—The contract boundary should end at the first point at which the reinsurer has the right to increase premium rates, as the entity as the holder of the contract has no substantive right to receive service beyond such date.

Staff view

- B.3 Based on the facts in B.1(c)–(d), the entity has no substantive right to receive services from the reinsurer after the first three months of coverage. This is because at any time, with three months' notice, the reinsurer has the practical ability to reassess the risks transferred to the reinsurer and can set a price or level of benefits for the contract to fully reflect the reassessed risk. Therefore, whether or not the boundary of the contract extends beyond the first three months of coverage depends on whether the entity has a substantive obligation to pay amounts to the reinsurer.
- B.4 Based on the facts in B.1(f)–(g), the entity is not compelled to pay amounts to the reinsurer after the three month notice period if the reinsurer increases premium rates. However, based on the facts in B.1(e), in this scenario it is assumed that the entity is compelled to pay amounts to the reinsurer if the reinsurer does not increase premium rates. This is not in the control of the entity. Therefore, it is the staff view that the entity has a substantive obligation to pay amounts to the reinsurer for the full contract term (ie for the duration of the underlying insurance contracts).

B.5 For this example, the staff view is that the boundary of the contract reflects the full contract term. The reinsurers right to reprice the contract, and the entity's resulting right to recapture the business will be reflected in the estimates of future cash flows. This view aligns with View A in the submission.

STAFF PAPER

May 2018

Project	Transition Resource Group for IFRS 17 <i>Insurance Contracts</i>		
Paper topic	Determining the quantity of benefits for identifying coverage units		
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Introduction

1. At its February 2018 meeting, the Transition Resource Group for IFRS 17 *Insurance Contracts* (TRG) considered a submission about how to determine the quantity of benefits in an insurance contract when determining the coverage units for a group of contracts. The coverage units establish the amount of the contractual service margin recognised in profit or loss in the period.
2. At the February 2018 meeting, the TRG considered only the questions raised in the submission relating to insurance contracts without investment components. This paper:
 - (a) continues the discussion on insurance contracts without investment components; and
 - (b) discusses insurance contracts with investment components.
3. The objective of the paper is to provide background and an accounting analysis to support discussion at the 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—Extract: summary of the TRG meeting held on 6 February 2018 relating to Agenda Paper 5;
 - (b) Appendix B—Examples of insurance contracts without investment components; and
 - (c) Appendix C—Examples of insurance contracts with investment components.

Background information

6. IFRS 17 requires an entity to recognise the contractual service margin of a group of insurance contracts over the coverage period of the group. The relevant paragraphs of IFRS 17 are shown below.
 - (a) paragraphs 44(e) (and 45(e)) of IFRS 17:

[The contractual service margin is adjusted for] the amount recognised as insurance revenue because of the transfer of services in the period, determined by the allocation of the contractual service margin remaining at the end of the reporting period (before any allocation) over the current and remaining coverage period applying paragraph B119.
 - (b) the definition of coverage period in Appendix A of IFRS 17:

The period during which the entity provides coverage for insured events. This period includes the coverage that relates to all premiums within the boundary of the insurance contract.

- (c) the definition of an insured event in Appendix A of IFRS 17:

An uncertain future event covered by an insurance contract that creates insurance risk.

- (d) paragraph B119 of IFRS 17:

An amount of the contractual service margin for a group of insurance contracts is recognised in profit or loss in each period to reflect the services provided under the group of insurance contracts in that period (see paragraphs 44(e), 45(e) and 66(e)). The amount is determined by:

- (a) identifying the coverage units in the group. The number of coverage units in a group is the quantity of coverage provided by the contracts in the group, determined by considering for each contract the quantity of the benefits provided under a contract and its expected coverage duration.
- (b) allocating the contractual service margin at the end of the period (before recognising any amounts in profit or loss to reflect the services provided in the period) equally to each coverage unit provided in the current period and expected to be provided in the future.
- (c) recognising in profit or loss the amount allocated to coverage units provided in the period.

7. Appendix A of this paper sets out the summary of the discussion of this topic at the February 2018 meeting of the TRG.

Implementation question

8. The submission asks what is the definition of ‘quantity of benefits’ in paragraph B119(a) of IFRS 17. The submission identifies different factors that could be included in the determination of coverage units and uses examples to illustrate the effect of including or excluding those factors.
9. At the February 2018 meeting, TRG members discussed the analysis of the submission in Agenda Paper 5 from that meeting and observed that:
 - (a) coverage units reflect the likelihood of insured events occurring only to the extent that they affect the expected duration of contracts in the group; and
 - (b) coverage units do not reflect the likelihood of insurance events occurring to the extent that they affect the amount expected to be claimed in the period.
10. TRG members also discussed the extent to which the determination of coverage units should reflect variability across periods in the level of cover provided by contracts in the group, based on the narrow scope fact patterns presented. However, they observed that a view could not be reached before they also considered a wider scope including insurance contracts with investment components.
11. This paper:
 - (a) develops further the factors to be considered in the determination of coverage units for insurance contracts without investment components;
 - (b) addresses the determination of coverage units for contracts with investment components; and
 - (c) considers the balance to be struck between high-level principles and specific guidance, given the wide variety of insurance products that need to be considered.

12. At the February 2018 meeting of the TRG, to assist in the preparation of this paper, the staff asked TRG members for their comments on the examples from the submission included in Agenda Paper 5 from that meeting. The staff also asked TRG members for their reflections on the determination of coverage units for insurance contracts with investment components.
13. Having considered the responses from TRG members, the staff have developed the analysis set out below. In Appendices B and C to this paper, the staff have selected examples from those given by TRG members to illustrate key points.

Review of accounting requirements

14. This section is structured as follows:
 - (a) points relevant to insurance contracts with and without investment components;
 - (b) an analysis of the accounting requirements for insurance contracts without investment components; and
 - (c) an analysis of the accounting requirements for insurance contracts with investment components.

Points relevant to insurance contracts with and without investment components

15. Paragraphs 16–20 of this paper set out a number of aspects of IFRS 17 that are relevant to insurance contracts with and without investment components.
16. First, the recognition of the contractual service margin in profit or loss is not the only component of profit recognised in the insurance service result. The release of the risk adjustment for non-financial risk and some experience adjustments also create profit. The relative size of the contractual service margin and risk adjustment will vary across contracts.

17. Second, the period in which an entity bears insurance risk is not necessarily the same as the insurance coverage period. This is clear from the following discussion of recognition in paragraphs BC140–BC142 of the Basis for Conclusions on IFRS 17:

BC140 The Board considered whether an entity should recognise the obligations and associated benefits arising from a group of insurance contracts from the time at which it accepts risk. Doing so would be consistent with the aspects of IFRS 17 that focus on measuring the obligations accepted by the entity. However, such an approach would differ from that required for revenue contracts within the scope of IFRS 15, which focuses on measuring performance. Under IFRS 15, an entity recognises no rights or obligations until one party has performed under the contract. That model would be consistent with the aspects of IFRS 17 that focus on measuring performance.

BC141 Further, some stakeholders were concerned that a requirement to recognise the group of insurance contracts from the time the entity accepts risk would mean that the entity would need to track and account for the group even before the coverage period begins. Those expressing that view stated that accounting for the group of insurance contracts before the coverage period begins would require system changes whose high costs outweigh the benefits of doing so, particularly because the amount recognised before the coverage period begins might be immaterial, or even nil. In the view of these respondents, even if amounts recognised before the coverage period begins are insignificant, requiring an entity to account for groups of insurance contracts in the pre-coverage period would impose on the entity the requirement to track groups to demonstrate that the amounts are insignificant.

BC142 The Board was sympathetic to those concerns. Accordingly, the Board adopted an approach that combines aspects of both approaches set out in paragraph BC140 by requiring that an entity recognise a group of insurance contracts from the earliest of:

- (a) the beginning of the coverage period of the group of contracts;
- (b) the date on which the first payment from a policyholder in the group becomes due; or
- (c) for a group of onerous contracts, when the group becomes onerous.

18. Third, paragraph B119(a) of IFRS 17 requires coverage units to be determined for a group of insurance contracts, by considering for each contract the quantity of benefits provided under the contract and its expected coverage duration. The examples in the submission and many of the examples sent in by TRG members focus on individual contracts, or groups of contracts, providing a single type of benefit. The examples therefore illustrate how coverage units might reflect the quantity of benefits provided by the group over the duration of the coverage of the group. However, if contracts in a group provide different types of benefits (for example, insurance cover with a maximum limit compared to insurance cover with no maximum limit), the assessment of the quantity of benefits in the group requires a method of comparing those different benefits as well as how the benefits change over the coverage duration of a group. Such a comparison will require the application of judgement by the entity. This is illustrated in example 11 in Appendix B to this paper and examples 14-16 in Appendix C to this paper.
19. Fourth, expectations of lapses of contracts are included in the determination of coverage units because they affect the expected duration of the coverage.
20. Fifth, the staff observe in paragraph 30 of this paper that the objective in IFRS 17 for the allocation of the contractual service margin is to reflect the services provided in the period. The staff think the determination of coverage units to achieve this objective is not an accounting policy choice but involves judgement and estimates to best reflect the provision of service. That judgement and estimates should be determined systematically and rationally. The disclosure

requirements of paragraph 125 of IAS 1 *Presentation of Financial Statements* apply. Paragraph 125 of IAS 1 states:

An entity shall disclose information about the assumptions it makes about the future, and other major sources of estimation uncertainty at the end of the reporting period, that have a significant risk of resulting in a material adjustment to the carrying amounts of assets and liabilities within the next financial year. In respect of those assets and liabilities, the notes shall include details of:

- (a) their nature, and
- (b) their carrying amount as at the end of the reporting period.

Insurance contracts without investment components

21. At the February 2018 meeting of the TRG, TRG members concurred with the views in Agenda Paper 5 from that meeting that:
 - (a) coverage units reflect the likelihood of insured events occurring only to the extent that they affect the expected coverage duration of contracts in the group; and
 - (b) coverage units do not reflect the likelihood of insurance events occurring to the extent that they affect the amount expected to be claimed in the period.

22. In paragraph 12 of Agenda Paper 5 from the February 2018 meeting of the TRG, the staff observed:
 - (a) coverage units were introduced to achieve an appropriate allocation of the contractual service margin of a group that contains contracts of different sizes. So if, for example, a group contains some contracts that offer a death benefit of CU10m and some that offer a death benefit of CU1m, the Board wanted to recognise an appropriate amount of the contractual service margin if the CU10m contracts have a different coverage duration from the CU1m contracts. The staff think reflecting

different levels of cover across periods (for example, a death benefit that fell from CU10m to CU1m over the duration of the contract) would be consistent with the principle of reflecting different levels of cover across contracts.

- (b) paragraph B119 of IFRS 17 requires coverage units to be reassessed at the end of each reporting period based on the coverage provided in the period and to be provided in the future. The implied objective is to achieve an allocation of the contractual service margin over time that reflects the insurance service provided by the entity in each period.

23. The staff therefore suggested in paragraph 13 of Agenda Paper 5 from the February 2018 meeting of the TRG that the principle implicit in the words of IFRS 17 is that different levels of cover across periods should be included in the determination of the quantity of benefits.
24. In the comments received from TRG members, many specifically agreed that the determination of coverage units should reflect different levels of cover provided by contracts in different periods. No TRG members expressed opposition to that view.
25. However, many TRG members expressed concern about the staff view expressed in the paragraph 15 of Agenda Paper 5 from the February 2018 meeting of the TRG that the benefit provided under a contract is the entity standing ready to meet the contractual maximum cover.
26. Some TRG members observed that in some cases the contractual maximum cover gave a good depiction of the benefits provided under a contract, but many TRG members gave examples where they thought that the contractual maximum cover would not faithfully represent the quantity of benefits provided by:
 - (a) a contract in different periods; and
 - (b) different contracts in a group.

27. TRG members thought the contractual maximum cover would not always represent faithfully different quantity of benefits because:
- (a) the contractual maximum cover sometimes does not depict a benefit that has relevant commercial substance; and
 - (b) some insurance contracts do not specify a contractual maximum cover, making this approach difficult to apply when comparing contracts that do specify a maximum contractual cover with those that do not.
28. TRG members instead identified different methods of identifying the benefits provided under a contract. These are illustrated in Appendix B to this paper.
29. The staff have considered the comments from TRG members. The staff observe the wide variety of types of insurance cover and different ways in which they are combined. The staff also acknowledge the calls from TRG members for a principle-based approach—it is not possible to set detailed requirements that will apply appropriately to the wide variety of products.
30. The staff observe:
- (a) paragraph B119 of IFRS 17 requires that ‘An amount of the contractual service margin for a group of insurance contracts is recognised in profit or loss in each period to reflect the services provided under the group of insurance contracts in that period’.
 - (b) because the objective is to reflect the insurance service provided in each period, different levels of service across periods should be reflected.
 - (c) paragraph B119(a) of IFRS 17 requires an entity to determine the services provided by the group considering for each contract the quantity of benefits provided under a contract and its expected coverage duration.
 - (d) determining the quantity of benefits provided under a contract requires an entity to consider the benefits expected to be received by the

policyholder, not the costs of providing those benefits expected to be incurred by the entity.

- (e) a policyholder benefits from the entity standing ready to meet valid claims, not just from making a claim if an insured event occurs. The quantity of benefits provided therefore depends on the amounts that can be claimed by the policyholder. The entity is standing ready to meet those claims. The amount that a policyholder can claim affects the benefit of being able to make a claim. The probability of a policyholder making a claim does not affect the benefit of it being able to make a claim.
- (f) IFRS 17 does not specify a particular method or methods to determine the quantity of benefits. Therefore, different methods can be used to determine the quantity of benefits as long as they achieve the objective of reflecting the insurance service provided in each period. Judgement needs to be applied to determine the method that best reflects the insurance service provided. Possible methods include the use of:
 - (i) the maximum contractual cover in each period; and
 - (ii) the amount the entity expects the policyholder to be able to validly claim in each period if an insured event occurs.
- (g) The following methods would not meet the objective:
 - (i) for an insurance contract without an investment component, methods in which the quantity of benefits is affected by the performance of any of the entity's assets. The quantity of benefits provided under an insurance contract without an investment component depends solely on the insurance service provided (see paragraphs 31–43 of this paper for a discussion of insurance contracts with investment components).
 - (ii) methods that result in no allocation of the contractual service margin to periods in which the entity is standing ready to meet valid claims.

- (iii) methods based on premiums, unless they can be demonstrated to be reasonable proxies for the services provided by the entity in each period. For example, premiums will not be a reasonable proxy when comparing service across periods if they are receivable in different periods to those in which services are provided, or reflect different probabilities of claims in different periods rather than different levels of service of standing ready to meet claims. Additionally, premiums will not be a reasonable proxy when comparing contracts in a group if the premiums reflect different levels of profitability in contracts or different probabilities of claims rather than different levels of the service of standing ready to meet claims. The level of profitability in a contract does not affect the services provided by the contract.
- (iv) methods based on expected cash flows, unless they can be demonstrated to be reasonable proxies for the services provided by the entity in each period. For example, expected cash flows will not be a reasonable proxy if they reflect different probabilities of claims rather than different levels of the service of standing ready to meet claims.

Insurance contracts with investment components

- 31. The key question for insurance contracts with investment components is whether the coverage period and coverage units should be determined by reference to insurance coverage only, or by reference to insurance coverage and some aspect of the investment component.
- 32. The staff, by email on 7 March 2018, asked TRG members for their views on the recognition of the contractual service margin in profit or loss for insurance contracts with investment components in accordance with IFRS 17. Many, but not all TRG members, indicated that aspects of the investment component should be reflected in the determination of coverage units.
- 33. The staff think that the analysis of the IFRS 17 requirements on this question differs for insurance contracts with direct participation features (variable fee

approach (VFA) contracts) and insurance contracts without direct participation features (general model contracts).

Variable fee approach contracts

34. IFRS 17 identifies VFA contracts as contracts that provide both insurance services and investment-related services. Paragraph BC241 of the Basis for Conclusions on IFRS 17 contrasts these contracts with those to which the general model applies as follows:

The Board decided that these differences [in the adjustments made to the contractual service margin applying the VFA and general model] are necessary to give a faithful representation of the different nature of the fee in these contracts. As explained in paragraphs BC228–BC231 [reproduced in paragraph 41 of this paper], the Board concluded that for many insurance contracts it is appropriate to depict the gains and losses on any investment portfolio related to the contracts in the same way as gains and losses on an investment portfolio unrelated to insurance contracts. However, the Board also considered a contrasting view that, for some contracts, the returns to the entity from a pool of underlying items should be viewed as the compensation that the entity charges the policyholder for service provided by the insurance contract, rather than as a share of returns from an unrelated investment. Under this contrasting view, changes in the estimate of the entity’s share of returns are regarded as a change in the entity’s compensation for the contract. Such changes in the entity’s compensation should be recognised over the periods in which the entity provides the service promised in the contract, in the same way that changes in the estimates of the costs of providing the contract are recognised.

35. Paragraph BC280 of the Basis for Conclusions on IFRS 17 also confirms the Board’s view that VFA contracts provide investment-related services:

The Board considered whether the allocation of the contractual service margin based on coverage units would result in profit being recognised

too early for insurance contracts with fees determined based on the returns on underlying items. For such contracts, IFRS 17 requires the contractual service margin to be determined based on the total expected fee over the duration of the contracts, including expectations of an increase in the fee because of an increase in underlying items arising from investment returns and additional policyholder contributions over time. The Board rejected the view that the allocation based on coverage units results in premature profit recognition. The Board noted that the investment component of such contracts is accounted for as part of the insurance contract only when the cash flows from the investment component and from insurance and other services are highly interrelated and hence cannot be accounted for as distinct components. In such circumstances, the entity provides multiple services in return for an expected fee based on the expected duration of contracts, and the Board concluded the entity should recognise that fee over the coverage period as the insurance services are provided, not when the returns on the underlying items occur.

36. In responding to the staff request for views, some TRG members commented that they interpret paragraph BC280 of the Basis for Conclusions on IFRS 17 as saying coverage for VFA contracts includes investment-related services, and coverage units should reflect the pattern of those services, not when returns on underlying items occur. Others questioned what the coverage period in the last sentence of paragraph BC280 of the Basis for Conclusions on IFRS 17 refers to.
37. The staff think a consequence of VFA contracts providing both insurance services and investment-related services is that:
- (a) the references to services in paragraphs 45 and B119 of IFRS 17 relate to insurance and investment-related services;
 - (b) the reference to quantity of benefits in paragraph B119(a) of IFRS 17 relates to insurance and investment-related benefits; and

(c) the reference to expected coverage duration in paragraph B119(a) of IFRS 17 relates to duration of insurance and investment-related services.

38. The staff acknowledge that the definition of coverage period as the period during which the entity provides coverage for insured events is a barrier to interpreting the references in this way. The staff also acknowledge the last sentence of paragraph BC280 of the Basis for Conclusions on IFRS 17 may be unclear. The staff plan to recommend to the Board that it proposes a narrow amendment to IFRS 17 to modify the definition of coverage period for VFA contracts to clarify that it includes the period in which investment-related services are provided.
39. Including investment-related services in the determination of coverage units means an entity must assess how both investment-related services and insurance services are provided. This requires an assessment of the pattern of service provision reflecting both types of services. The staff think this assessment will be a matter of judgement.
40. The consequences of this approach for VFA contracts are illustrated in Appendix C to this paper.

General model contracts

41. In contrast to the VFA, the staff observe the general model in IFRS 17 does not treat contracts as providing investment-related services. The Basis for Conclusions on IFRS 17 states:

BC228 For insurance contracts without direct participation features, the Board concluded that changes in the effects of the time value of money and financial risk do not affect the amount of unearned profit. This is the case even if the payments to policyholders vary with returns on underlying items through a participation mechanism, for the reasons set out in paragraphs BC229–BC231. Accordingly, the entity does not adjust the contractual service margin to reflect the effects of changes in these assumptions.

BC229 For insurance contracts without direct participation features, the underwriting result is regarded as the difference between the amount of premiums the entity charges (less any investment component) and the payments the entity makes because of the occurrence of the insured event. The insurance finance result reflects the interest arising on the group of insurance contracts because of the passage of time and the effect of changes in assumptions relating to financial risk. The statement(s) of financial performance also reflect gains and losses from the investments in which the premiums are invested. Such gains and losses would be recognised in profit or loss according to other applicable IFRS Standards.

BC230 Thus, for insurance contracts without direct participation features, the entity's profit from financing activities arises from the difference between:

- (a) the gains (or losses) from the investments; and
- (b) the change in the insurance contract liability depicted by the insurance finance income or expenses including the gains (or losses) the entity passes to the policyholder through any indirect participation mechanism.

BC231 This approach to determining profit from financing activities reflects the separate accounting for the investment portfolio and the group of insurance contracts, regardless of any participation mechanism in the insurance contracts, consistent with the following:

- (a) the entity controls the cash flows of the investments, even when the entity is required to act in a fiduciary capacity for the policyholder.
- (b) in most cases, an entity would be unlikely to have a legally enforceable right to set off the insurance contract liability with the investment portfolio, even if the investment portfolio were to be invested in assets that exactly match the entity's obligation, because the entity retains the obligation to pay the policyholders the amounts that are determined on the basis of the investments in the portfolio, irrespective of the entity's investment strategy.

42. These paragraphs, together with paragraph BC241 of the Basis for Conclusions for IFRS 17 (reproduced in paragraph 34 of this paper), demonstrate that IFRS 17 uses the scope of the VFA to identify insurance contracts that provide investment-related services as well as insurance services. For contracts outside the scope of the VFA, there is not a sufficient link between the amounts promised to policyholders and the returns on assets for the entity to receive a fee from the policyholder for investment-related services. Instead, the assets arising from the premiums received are the entity's assets that it manages on its own behalf. The amounts promised to policyholders other than insurance benefits (ie the investment components) are not related to service, but are instead a form of financial instrument. The difference between the investment income from the entity's assets and insurance finance expenses is presented as a finance result.
43. Hence, for general model contracts, coverage units and the coverage period (duration of coverage) are determined by reference to insurance services only. The consequences of this approach are illustrated in Appendix C 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 for IFRS 17 meeting held on 6 February 2018

Determining the quantity of benefits for identifying coverage units (Agenda Paper 5)

- A.1 Coverage units establish the amount of the contractual service margin to be recognised in profit or loss for services provided in a period. Agenda Paper 5 addresses a submission received about how to determine the coverage units of a group of insurance contracts with no investment component. Insurance contracts with investment components will be discussed at a later meeting.
- A.2 TRG members discussed the analysis in Agenda Paper 5 and observed that:
- (a) coverage units reflect the likelihood of insured events occurring only to the extent that they affect the expected duration of contracts in the group; and
 - (b) coverage units do not reflect the likelihood of insurance events occurring to the extent that they affect the amount expected to be claimed in the period.
- A.3 TRG members discussed the extent to which the determination of coverage units should reflect variability across periods in the level of cover provided by contracts in the group based on the narrow scope fact patterns presented. However, they observed that a view could not be reached before they also considered a wider scope including insurance contracts with investment components. Accordingly, the staff will bring a paper to a later TRG meeting that will address the determination of coverage units for contracts with investment components and will also develop further:
- (a) the use of the maximum level of cover and the expected level of cover in periods. For example, the TRG considered a contract that provides cover for fire damage up to CU50m per year on a five-year construction project. The value of the property covered is expected to increase over

the five years. The maximum level of cover is the contract CU50m limit. The expected level of cover is the increasing value on which the entity is exposed to insurance risk.

- (b) the balance to be struck between high-level principles and specific guidance, given the wide variety of insurance products that need to be considered.

A.4 TRG members agreed to send in their comments on the examples in Agenda Paper 5 by the end of February to help the development of the next paper.

Appendix B—Examples of insurance contracts without investment components

Example	Type of contract	Paragraphs
1	Credit life loan insurance	B.2–B.5
2	Credit life product with variable amount of cover	B.6–B.9
3	Mortgage loss cover	B.10–B.13
4	Product warranty	B.14–B.17
5	Extended product warranty	B.18–B.20
6	Health cover	B.21–B.24
7	Proportional reinsurance issued	B.25–B.28
8	Reinsurance adverse development of claims with claim limit	B.29–B.32
9	Reinsurance adverse development of claims without claim limit	B.33–B.36
10	Transaction liability	B.37–B.39
11	Combination of different types of cover	B.40–B.43
12	Life contingent annuity	B.44–B.46
13	Forward purchase of fixed rate annuity	B.47–B.49

B.1 As set out in paragraph 20 of this paper, the staff think the determination of coverage units is not an accounting policy choice but involves judgements and estimates on how best to reflect the provision of services. In the following examples, the staff comment on whether suggested methods of determining the quantity of benefits and the coverage duration might be valid ways of reflecting the provision of services. Which method gives the best reflection of the provision of service is a matter of judgment that depends on facts and circumstances.

Example 1—Credit life loan insurance

- B.2 Example: a life insurance policy pays a death benefit equal to the principal and interest outstanding on a loan at the time of death. The balance of the loan will decline because of contractually scheduled payments and cannot be increased.
- B.3 Method suggested for determining the expected coverage duration: the expected coverage duration should reflect expected deaths and lapses.
- B.4 Methods suggested for determining the quantity of benefits:
- (a) constant cover, being cover of a death benefit; and
 - (b) cover for the contractual balance outstanding.
- B.5 Staff comments:
- (a) the staff agree that the expected coverage duration should reflect expected deaths and lapses.
 - (b) for determining the quantity of benefits, the staff think method B.4(b) is valid because it is both the maximum contractual cover and the amount the entity expects the policyholder to be able to make a valid claim for if the insured event occurs. The staff do not think method B.4(a) is valid because it does not reflect different levels of cover provided across periods.

Example 2—Credit life product with variable amount of cover

- B.6 Example: credit life products where the amount payable on an insured event varies (for example, claims might relate to an outstanding credit card balance). In these cases the sum assured will vary over time, rather than simply reducing. In addition, the sum assured may be limited based on the lender's credit limits.
- B.7 No comments were made about the expected coverage duration.
- B.8 Methods suggested for determining the quantity of benefits:
- (a) constant cover of contractual maximum amount of the credit limit; and

- (b) cover based on expected credit card balances.

B.9 Staff comments:

- (a) the staff think the expected coverage duration is the period during which cover is provided, adjusted for any expectations of lapses.
- (b) for determining the quantity of benefits, the staff think either method suggested could be valid. Method B.8(a) is the maximum contractual cover and method B.8(b) is the amount the entity expects the policyholder to be able to make a valid claim for if the insured event occurs.

Example 3—Mortgage loss cover

B.10 Example: a contract provides cover for five years for default losses on a mortgage, after recovering the value of the property on which the mortgage is secured. The balance of the mortgage will decline because of contractually scheduled payments and cannot be increased.

B.11 No comments were made about the expected coverage duration.

B.12 Methods suggested for determining the quantity of benefits:

- (a) contractual balance of mortgage; and
- (b) the amount for which the policyholder has the ability to make a valid claim, ie the contractual balance of the mortgage, less the expected value of the property.

B.13 Staff comments:

- (a) the staff think the expected coverage duration is the five years during which cover is provided, adjusted for any expectations of lapses.
- (b) for determining the quantity of benefits, the staff think either method suggested could be valid. Method B.12(a) is the maximum contractual cover and method B.12(b) is the amount the entity expects the

policyholder to be able to make a valid claim for if the insured event occurs.

Example 4—Product warranty

- B.14 Example: a five-year warranty coverage contract provides for replacement of a purchased item if it fails to work properly within five years of the date of purchase.¹ Claims are typically skewed toward the end of the coverage period as the purchased item ages.
- B.15 No comments were made on the expected coverage duration.
- B.16 Methods suggested for determining the quantity of benefits:
- (a) the cover provided is constant until a claim is made; and
 - (b) the coverage units should include expectations about the cost of replacing the item, for example, inflation.
- B.17 Staff comments:
- (a) the staff think that the expected coverage duration is the five years the cover is provided, adjusted for any expected lapses.
 - (b) for determining the quantity of benefits, the staff think method B.16(a) is valid if the price of the product is expected to remain constant. The staff think method B.16(b) is valid if the price of the product increases. The benefit to the policyholder is not having to buy a replacement product.

¹ The contract is not a warranty provided by a manufacturer, dealer or retailer in connection with the sale of its goods to a customer and so is within the scope of IFRS 17.

Example 5—Extended product warranty

- B.18 Example: extended warranty policies cover the policyholders after the manufacturer's original warranty has expired. The policies provide new for old cover in the event of a major defect to the covered asset.
- B.19 Comments on the expected coverage period: the expected coverage duration does not start until the manufacturer's original warranty has expired.
- B.20 Staff comments: the staff agree the expected coverage duration does not start until the manufacturer's original warranty has expired. The policyholder cannot make a valid claim to the entity until then.

Example 6—Health cover

- B.21 Example: a contract provides health cover for 10 years for specified types of medical costs up to CU1m over the life of the contract, with the expected amount and expected number of claims increasing with age.
- B.22 No comments were made about the expected coverage duration.
- B.23 Methods suggested for determining the quantity of benefits:
- (a) compare the contractual maximum amount that could have been claimed in the period with the remaining contractual maximum amount that can be claimed as a constant amount for each future coverage period. So, if a claim of CU100,000 were made in the first year, at the end of the year the entity would compare CU1m coverage provided in the year with coverage of CU900,000 for the following nine years, resulting in an allocation of 1/9.1 of the contractual service margin for the first year.
 - (b) compare the maximum amount that could be claimed in the period with the expected maximum amounts that could be claimed in each of the future coverage periods, reflecting the expected reduction in cover because of claims made. The staff acknowledge that this approach

involves looking at the probabilities of claims in different periods to determine the expected maximum amounts in future periods. However, in this case, the probability of claims in one period affects the amount of cover for future periods, so does affect the level of service provided in those periods. So if a claim of CU100,000 were expected in each year, at the end of the year the entity would compare CU1m coverage provided in the year with coverage of CU4.5m (900k + 800k + ...) over the following nine years, resulting in an allocation of 1/5.5 of the contractual service margin for the first year.

- (c) compare the amount expected to be claimed in the period with the amounts expected to be claimed in future periods.

B.24 Staff comments:

- (a) the staff think the expected coverage duration is the 10 years during which cover is provided, adjusted for any expectations of the limit being reached during the ten years and lapses.
- (b) for determining the quantity of benefits, the staff think that either method B.23(a) or B.23(b) could be valid. The staff do not think method B.23(c) is a valid method because if no claims are expected in a period, there would be no contractual service margin recognised, contrary to the principles discussed in paragraph 30 of this paper. In addition, it appears that applying method B.23(c) the amount representing the contractual cover remaining is not reduced as claims are made.

Example 7—Proportional reinsurance issued

B.25 Example: a reinsurance contract issued provides proportional cover for underlying contracts issued during the contract period. The reinsurance contract issued is for a period of one year. Underlying contracts are written uniformly throughout the

year and are annual policies that are reasonably homogenous and provide relatively even cover over their one-year coverage periods.

- B.26 Methods suggested for determining the expected coverage duration: the insurer has a substantive obligation to provide services under the contract for a period of two years as the risks attaching over a single policy year will cover two-years of exposure to risk. The expected coverage duration of the reinsurance contract issued is therefore two years.
- B.27 Method suggested for determining the quantity of benefits: the amount for which the policyholder has the ability to make a valid claim—ie the pattern of coverage—should reflect the expected pattern of underwriting of the underlying contracts because the level of service provided depends on the number of underlying contracts in-force—the more contracts in force, the higher the level of service.
- B.28 Staff comments:
- (a) the staff agree that the expected duration is two years, adjusted for any expectations of lapse; and
 - (b) for determining the quantity of benefits, the staff think that method B.27 is valid.

Example 8—Reinsurance adverse development of claims with claim limit

- B.29 Example: a reinsurance adverse development cover contract will pay claims in excess of a stated aggregate amount on a group of underlying property and casualty contracts where the claim event has already been incurred. There is a total aggregate limit to the amount payable under the contract. Because there is uncertainty in the ultimate amount and timing of the final settlements of the underlying claims, the insured event is the determination of the ultimate cost of settling those claims.
- B.30 Methods suggested for determining the expected coverage duration: if the contract has an upper limit that is expected to be reached, the expected coverage duration

would be the period from inception of the contract to the time at which the limit of cover is expected to be reached, adjusted for expected lapses, if any.

B.31 Methods suggested for determining the quantity of benefits:

- (a) compare the contractual maximum amount that could have been claimed in the period with the remaining contractual maximum amount that can be claimed as a constant amount for each future coverage period;
- (b) straight line over the life of the contract which would end at the date of the last expected settlement payment; and
- (c) compare the expected amount of underlying claims covered in the period with the expected amount of underlying claims remaining to be covered in future periods.

B.32 Staff comments:

- (a) the staff agree that the expected coverage duration would be the period from inception of the contract to the time at which the limit of cover is expected to be reached, adjusted for expected lapses.
- (b) for determining the quantity of benefits, the staff think that methods B.31(a) and B.31(c) could be valid methods. The staff do not think that method B.31(b) is valid because it does not reflect different levels of cover provided across periods.

Example 9—Reinsurance adverse development of claims without claim limit

B.33 Example: a reinsurance adverse development cover contract will pay claims in excess of a stated aggregate amount on a group of underlying property and casualty contracts where the claim event has already been incurred. There is no total aggregate limit to the amount payable under the contract. Because there is uncertainty in the ultimate amount and timing of the final settlements of the

underlying claims, the insured event is the determination of the ultimate cost of settling those claims.

B.34 Coverage period comments:

- (a) in the case of an unlimited cover, the expected coverage duration would be the period to when it is expected there will be no other cash payments—ie the end of the expected claims settlement period.
- (b) some contracts for adverse claims development have no limit on the period in which claims can be made. For example, asbestos claims were still being made in 2017 under 1950s commercial liability policies in the US. Other examples will arise when an entity acquires claims in their settlement period in a business combination. In such situations there is no ‘date of the last expected settlement payment’. There is no clear date when potential claims are no longer possible. The time period for complete runoff of such liabilities is not reliably estimable for the purposes of the accounting proposed in Agenda Paper 5 from the February 2018 meeting of the TRG. Where a range of possible outcomes can be produced, possible guidance choices for the time period for contractual service margin amortisation would be basing it on the low estimate, basing it on the high estimate, or basing it on the midpoint of the low and high. There can also be situations where ranges do not exist. In any event, the lack of guidance is likely to result in significant diversity in practice.

B.35 Methods suggested for determining the quantity of benefits:

- (a) equal benefits in each coverage period, which would end at the date of the last expected settlement payment;
- (b) compare the number of underlying claims covered in the period with the number of underlying claims remaining to be covered in future periods; and

- (c) compare the expected amount of underlying claims covered in the period with the expected amount of underlying claims remaining to be covered in future periods

B.36 Staff comments:

- (a) the staff think the expected coverage duration would be the period to when the financial effect of the claims become certain. This may be before the claims are paid if certainty has been achieved prior to the actual payment. The staff observe that an entity will need to estimate the expected duration of the period in which claims will be made and payments will be made to estimate the fulfilment cash flows.
- (b) for determining the quantity of benefits, the staff think methods B.35(a) and B.35(c) could be valid. The staff think method B.35(a) could be valid in this example, while the same method was not valid in the previous example (method B.31(b) in the previous example). This is because unlike the first example, the amount of contractual cover remaining is not reduced as claims are made. The staff observe that equal benefits in each coverage period for each contract (method B.35(a)) will not necessarily result in a straight-line allocation of the contractual service margin of a group because different numbers of contracts will provide cover in different periods. Method B.35(b) could be valid if the underlying claims were expected to be of similar size.

Example 10—Transaction liability

B.37 Example: a transaction liability policy will pay claims for financial losses arising as a result of breaches of representations and warranties made in a specified and executed acquisition transaction. The policy period (contract term) is for 10 years from the policy start date. The insurer will pay claims for financial losses reported during the 10-year policy period up to the maximum sum insured.

B.38 Comments on the expected coverage duration:

- (a) the insured event is the representations and warranties made in the final executed transaction agreement which is dated the transaction closing date. Therefore, the coverage period (expected coverage duration) is one day, which is the transaction closing date. The policy period has been included in the contract to limit the reporting period for claims so it is not an indefinite period. This limits the timescale for loss reporting in the same way that the maximum sum insured limits the quantum of loss. Given the insured event arises from representations and warranties the concept of an ‘insurable interest’ is difficult to apply without needing to assess the expected frequency and severity of the loss, ie incidence of risk. However, a valid claim is only permitted in relation to the executed representations and warranties and therefore limited to a one-day period.
- (b) the insured event is the discovery of breaches of representations and warranties. Coverage starts at the moment the contract is signed and lasts for 10 years.

B.39 Staff comments: the staff think view B.38(b) is valid. The staff do not agree with the interpretation of the insured event in view B.38(a). The insured event is not that the policyholder will knowingly make false representations. The insured event is the future event that indicates that the representations made in good faith were in fact misrepresentations and resulted in financial losses. This is consistent with paragraph B18(i) of IFRS 4 *Insurance Contracts* which states:

title insurance (ie insurance against the discovery of defects in title to land that were not apparent when the insurance contract was written). In this case, the insured event is the discovery of a defect in the title, not the defect itself.

Example 11—Combination of different types of cover

B.40 Example: combinations of different benefits. Assume there are five different contracts (A-E) in a single group of insurance contracts. Each contract has a

different combination of four coverages (accidental death, cancer diagnosis, surgery and inpatient treatment²). Also, each contract has a different coverage period. Coverages have a high level of interdependency in the same insurance contract; if a coverage of an insurance contract in the group of insurance contracts lapses, other coverages of the same insurance contract lapse simultaneously.

Presented in the table below is the summary of the contracts.

Contract	Coverage				Coverage period
	Accidental death	Cancer diagnosis	Surgery	Inpatient treatment	
A	Cover of 2000	Cover of 1000	Cover of 500	Cover of 50	2 years
B	N/A	Cover of 1000	Cover of 500	N/A	5 years
C	N/A	N/A	Cover of 500	Cover of 50	2 years
D	N/A	N/A	Cover of 500	Cover of 50	5 years
E	Cover of 2000	N/A	N/A	N/A	10 years

The entity charges the same annual premiums for each type of cover, and the total annual premium for a contract is the sum of the premiums for each type of cover included in the contract.

B.41 No comments were made on the expected coverage duration.

B.42 Methods suggested for determining the quantity of benefits:

- (a) the quantity of benefits is the same for each contract.
- (b) the quantity of benefits for each contract is the maximum level of cover given by any of the benefits, ignoring the amounts of cover for the other benefits. So if, for example, the highest level of cover for contract A

² The example provided by the TRG member included an investment component. The discussion of a combination of insurance service and an investment component is discussed as example 14 in Appendix C to this paper.

was 2,000 for accidental death and for contract B was 1,000 for cancer diagnosis, the coverage units would be determined by reference to those amounts.

- (c) the quantity of benefits for each contract is the sum of all the levels of cover provided. So, based on the cover set out in the table, the coverage units for contract A for each year would be 3,550 and for contract B 1,500.
- (d) the annual premiums can be used to determine the coverage units because they reflect the amount of insurance service provided.

B.43 Staff comments:

- (a) the staff think the expected coverage duration is the period in which cover is provided, adjusted for expectations of lapses.
- (b) for determining the quantity of benefits, the staff think that method B.42(c) is valid. The staff think that method B.42(a) is not valid because it does not reflect the different amounts of cover provided by each contract. The staff think that method B.42(b) is also not valid for the same reason. The staff think that whether method B.42(d) is valid depends on the factors set out in paragraph 30(g)(iii) of this paper.

Example 12—Life contingent annuity

B.44 Example: a life contingent pay out annuity pays a fixed monthly amount of CU10 each period until the annuitant dies.

B.45 Combined comments on the expected coverage duration and the quantity of benefits:

- (a) there is a constant level of benefits provided over the life of the annuitant. The contractual service margin would be amortised straight line over the remaining expected life of the annuitant. That is the quantity of benefit is 10 per year, and the coverage duration is the

length of time until there is zero probability of making a payment to the policyholder (40 years).

- (b) the contract is a series of individual promises to pay a fixed amount at a future point in time if the annuitant is alive at that point in time. The cumulative coverage units in the first period are the total expected dates a payment will be made. The second period cumulative coverage units would be one less coverage unit as a coverage unit expired with the reaching of the first promise to pay at a point in time. That is the quantity of benefit and coverage duration are determined together by multiplying the face amount by the probability of making payment in each year (not the probability weighted cash flow).
- (c) the coverage units are determined by the quantity of benefits and the expected duration. The quantity of benefits is a constant benefit of 10 per year. The expected duration is the probability-weighted average duration of the contract.

B.46 Staff comments:

- (a) the staff think the expected coverage duration is the probability-weighted average expected duration of the contract. The expected coverage duration is reassessed each period (same as view B.45(c)).
- (b) the staff think the quantity of benefits is the fixed monthly amount of CU10 (same as view B.45(c)).
- (c) the staff do not agree with view B.45(a) because it does not reflect the expected duration of the contract. The staff do not agree with view B.45(b) because it requires an entity to split a contract into multiple individual contracts. It also does not seem to require reassessment of the expected coverage duration.

Example 13—Forward purchase of fixed rate annuity

- B.47 Example: forward contract to buy an annuity in the future at a fixed rate. The premium is payable when the annuity is bought. If the policyholder dies, or cancels the contract, before the date the annuity can be purchased, the policyholder receives no benefit.
- B.48 Comments on the coverage period:
- (a) the entity bears insurance risk from the date the forward contract is issued. Hence, the coverage period starts at that date.
 - (b) the entity bears insurance risk from the date the forward contract is issued, but the coverage period does not start until the date the annuity starts. The insured event is that the policyholder lives long enough to receive payments under the annuity.
- B.49 Staff comments: The staff think view B.48(b) is valid. The staff do not think an insured event can happen in the period before the annuity starts.

Appendix C—Examples of insurance contracts with investment components

Example	Type of contract	Paragraphs
14	Insurance services and investment component with different durations	C.2–C.5
15	Endowment policy	C.6–C.9
16	Benefit of higher of investment component and multiple of salary	C.10–C.12

C.1 As set out in paragraph 20 of this paper, the staff think the determination of coverage units is not an accounting policy choice but involves judgement and estimates on how best to reflect the provision of service. In the following examples, the staff comment on whether suggested methods of determining the quantity of benefits and the coverage duration might be valid ways of reflecting the provision of service. Which method gives the best reflection of the provision of service is a matter of judgment that depends on facts and circumstances.

Example 14—Insurance services and investment component with different durations

C.2 Example: an investment contract matures in year 10 and pays the customer the account value at maturity. The contract also includes a death benefit that varies depending on which year in the 10 year period the death occurs. Specifically, if the customer dies during the 1–5 year period, the customer’s beneficiary would receive a death benefit that is the higher of 110 per cent of the premium paid or the accumulated account value (assume the death benefit for years 1–5 results in significant insurance risk). However, if the customer dies in years 6 to 10 the customer’s beneficiary only gets the account value. There is no surrender penalty. Does the insurer only have to consider years 1 to 5 for determining the coverage units to determine the amortisation of the contractual service margin? Or does the

insurer need to consider all 10 years for determining coverage units and amortisation of the contractual service margin?

C.3 Comments on the expected coverage duration:

- (a) View A—Years 1 to 5 are the only years in the 10 year period that could expose the insurer to paying an amount higher than the account value due to an insured event. Therefore, the portion of the contractual service margin allocated to the insurance risk portion of the contract is recognized over those five years. The portion of the contractual service margin allocated to the investment management portion will be recognised over the 10 years following the guidance in paragraph 71(c) of IFRS 17.
- (b) View B—Paying a death benefit equal to the account value is a benefit payment despite the fact that the insurer is not exposed to a risk of insurance loss. The entire contractual service margin is recognised over 10 years.
- (c) View C—Coverage units are defined as insurance units. The insurance coverage is in force in only the first five years. The contractual service margin should be amortised over the first five years. However, the contractual service margin is developed at inception and, as illustrated in Example 6 (IE 56–80) and Example 15 (IE 152–172) in the Illustrative Examples on IFRS 17, contains the present value of the expected spread in establishing crediting rates to the account balance if it is an indirect par policy. Recognising the entire contractual service margin in the first five years would also result in recognising the entire expected spread of the 10-year life over the first five years.

C.4 Comments on quantity of benefits: a practical approach for assessing the quantity of benefits for investment-related services is to use the amount of the investment component in the period, because this reflects the quantity of assets being managed for the policyholder under the contract.

C.5 Staff comments:

- (a) if the contract falls within the scope of the VFA:

- (i) the contract provides insurance and investment-related services. The coverage period for total services is 10 years.
- (ii) the coverage units should be determined reflecting the benefits to the policyholder of the insurance services and the investment-related services. Determining the amount and pattern of the insurance and investment-related services is a matter of judgement. Methods that rely solely on the amount of the investment component or solely on the death benefit would not be a faithful representation of the provision of services.
- (b) if the contract does not fall within the scope of the VFA, the contract provides only insurance services for the purpose of applying IFRS 17. The coverage period for those services is the first five years. In years 6–10, the policyholder can make no valid insurance claim and receives no insurance services from the entity.

Example 15—Endowment policy

C.6 Example: the entity has issued conventional participating insurance with the following features:

- (a) the policyholder pays a regular level premium to the insurance entity.
- (b) in return, the policyholder receives:
 - (i) insurance coverage, payable upon death of the life insured, of a specified sum insured; and
 - (ii) a share of the investment returns from an underlying pool of assets to which the policy refers.
- (c) the investment returns are allocated to the policyholder through bonuses that are added to the policy’s sum insured.
- (d) the insurance entity may allocate ‘reversionary bonuses’ (ie an annual incremental addition to the sum insured) or ‘terminal bonuses’ (ie an

amount in addition to the sum insured and reversionary bonuses that is payable to the policyholder upon maturity or death).

- (e) there are three ways in which the policy can terminate. The policyholder could:
 - (i) die. In this case the sum insured including all reversionary bonuses accumulated at the time of death and the terminal bonus would be payable.
 - (ii) survive and reach the maturity date of the policy. In this case the maturity value consisting of the sum insured, all reversionary bonuses accumulated at maturity and the terminal bonus would be payable.
 - (iii) voluntarily surrender their policy before the maturity date. In this case, a surrender value would be payable to the policyholder. The surrender value is generally based on a set schedule such that the surrender value is low in the early years of the policy and increases with policy duration. At maturity, the surrender value equals the maturity value.

A key point of these contracts is that the insurance component of the policy dominates at early durations and the investment component dominates at later durations as the policyholder accumulates investment returns.

- C.7 No comments were made about the expected coverage duration (there is insurance risk until maturity of the contract because the surrender value is always lower than the amount payable on death).
- C.8 The following methods were suggested for determining the quantity of benefits:
 - (a) coverage units are determined by reference to the amount payable on death, which reflects the quantity of benefits for both insurance and investment services provided by the entity; and
 - (b) coverage units are determined by reference to the difference between the amount payable on death and the surrender value, which reflects the

quantity of benefits only for the insurance services provided by the entity.

C.9 Staff comments:

- (a) for both VFA and general model contracts, the staff think the expected coverage duration is the expected duration of the contract, including expectations of surrender.
- (b) for the quantity of benefits, the staff think the analysis differs for VFA and general model contracts:
 - (i) if the contract falls within the scope of the VFA, the coverage units should be determined reflecting the benefits to the policyholder of the insurance services and the investment-related services. One method of doing this would be by using the amount payable on death (ie including the surrender value). (Same as method in C.8(a)).
 - (ii) if the contract does not fall within the scope of the VFA, the contract provides only insurance services for the purpose of applying IFRS 17. In principle, the coverage units should be determined by the insurance benefit only, ie excluding the surrender value. (Same as method C.8(b)). However, IFRS 17 does not require entities to separately identify investment components before a claim is incurred, because of the difficulties in doing so.³ Therefore, the staff think that determining the quantity of benefits by excluding the surrender value is a possible approach if an entity has reasonable and supportable information to do so. If the entity does not have such reasonable and supportable information, it will need to use its judgement to determine the quantity of benefits.

Example 16—Benefit of higher of investment component and multiple of salary

C.10 Example: the entity issues a contract comprising:

- (a) an investment linked account; and

³ See paragraphs BC10 and BC12 of the Basis for Conclusions on IFRS 17.

- (b) an insurance rider which insures payment of five times salary upon death or account balance if greater.

The entity prices for a 10 per cent profit margin in investment services and a 15 per cent return on insurance services. The investment component cannot be separated in applying paragraph 11(b) of IFRS 17 as it is not distinct.

There are three ways in which the contract can terminate:

- (a) the insured could die. In this case the higher of five times salary and the investment linked account balance are paid at the time.
- (b) the insured could reach retirement age. In this case the investment linked account balance would be paid and the contract including any insurance component would cease.
- (c) the policyholder could move to another employer and transfer the investment linked balance to another superannuation scheme, which also ceases the insurance cover provided the entity.

A key point of these contracts is that the insurance component of the policy dominates at early durations and the investment component dominates at later durations as the policyholder accumulates investment returns.

C.11 Combined comments on the expected coverage duration and the quantity of benefits:

- (a) coverage units should be based on the benefit payable on death—ie the higher of five times salary and the investment-linked account balance, which reflects the quantity of benefits for both insurance and investment services provided by the entity.
- (b) coverage units should be based on the difference between the benefit payable on death and the investment-linked account balance, which reflects only the quantity of benefits for only the insurance services provided by the entity. This difference is nil once the investment-linked

account balance exceeds five times salary, so the expected coverage duration would end at that point.

C.12 Staff comments:

- (a) if the contract falls within the scope of the VFA: the expected coverage duration and quantity of benefits should be determined reflecting the benefits to the policyholder of both the insurance services and the investment-related services. One method of doing this would be by using the sum payable on death, ie including the investment-linked account balance.
- (b) if the contract does not fall within the scope of the VFA: the contract provides only insurance services for the purpose of applying IFRS 17. If the investment-linked account is not guaranteed, one way of determining the insurance benefit would be to consider the maximum contractual amount of cover—ie five times salary. If the investment-linked account is guaranteed, or if the insurance benefit is determined by considering the expected amount of a valid claim rather than the maximum contractual amount, in principle, the coverage units should exclude the investment-linked account. However, IFRS 17 does not require entities to identify separately investment components before a claim is incurred, because of the difficulties in doing so⁴. The staff think determining the quantity of benefits by excluding the investment-linked account is a possible approach if an entity has reasonable and supportable information to do so. If the entity does not have such reasonable and supportable information, it will need to use its judgement to determine the quantity of benefits.

⁴ See paragraphs BC10 and BC12 of the Basis for Conclusions on IFRS 17.

STAFF PAPER

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Project	Transition Resource Group for IFRS 17 <i>Insurance Contracts</i>		
Paper topic	Implementation challenges outreach report		
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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 reports comments from members of the Transition Resource Group for IFRS 17 *Insurance Contracts* (TRG) in response to staff outreach about implementation concerns that arise in applying the following requirements in IFRS 17:
 - (a) presentation of groups of insurance contracts in the statement of financial position;
 - (b) premiums received applying the premium allocation approach (PAA);
and
 - (c) subsequent treatment of insurance contracts acquired in their settlement period.

This paper does not reflect the full responses received from each TRG member for each topic.

2. The outreach was performed following the discussion at the February 2018 meeting of the TRG. TRG members indicated that implementation challenges

arising because of the requirements listed in paragraph 1 would cause significant changes from existing practice (see Appendices A and B to this paper).

3. The focus of the outreach, and therefore the focus of this paper, is the implementation challenges identified in applying the requirements of IFRS 17. This paper also reports information provided by TRG members about what they think would be useful information for users of financial statements.
4. The staff ask TRG members whether the report appropriately reflects their comments.
5. The staff will provide this report to the International Accounting Standards Board (Board) at a future meeting.

Structure of the paper

6. This paper includes the following sections:
 - (a) level of aggregation:
 - (i) applying the requirements of IFRS 17;
 - (ii) applying existing practice;
 - (iii) implementation challenges in identifying premiums received related to groups of insurance contracts;
 - (iv) implementation challenges in identifying the liability for incurred claims related to groups of insurance contracts; and
 - (v) supporting materials.
 - (b) treatment of contracts acquired in their settlement period:
 - (i) applying the requirements of IFRS 17;
 - (ii) applying existing practice;
 - (iii) implementation challenges identified as a result of the change from existing practice; and
 - (iv) additional notes.
7. There are three appendices to this paper:
 - (a) Appendix A—Relevant extracts from Agenda Paper 7 and the meeting summary of the February 2018 TRG meeting
 - (b) Appendix B—Questions sent to TRG members in performing the outreach
 - (c) Appendix C—Examples of the PAA mechanics (with comparison to the accounting under existing practice)

Level of aggregation

Applying the requirements of IFRS 17

8. Paragraph 78 of IFRS 17 requires an entity to present separately in the statement of financial position the carrying amount of groups of insurance contracts issued that are assets and those that are liabilities. This requirement applies both when a group of contracts is measured using the general model, or when measured using the PAA.
9. A group of insurance contracts (either asset or liability) is disaggregated into a liability for remaining coverage and a liability for incurred claims. Both components need to be identified at the level of a group of insurance contracts.
10. The receipt of premiums during each reporting period affects the measurement of the liability for remaining coverage, as follows:
 - (a) applying the general model in paragraphs 33–37 of IFRS 17, the liability for remaining coverage of each group is measured using the fulfilment cash flows, which reflects the current estimate of future cash flows, and the contractual service margin (CSM) for each group. In other words, the measurement excludes the premiums already received and includes premiums that are due but that have not been received.
 - (b) applying the PAA, the liability for remaining coverage is measured based on the premiums received less those that have been recognised as revenue.
11. Accordingly, the requirements in IFRS 17 would require entities to identify premiums received for a group of insurance contracts.
12. In contrast, the revenue recognised in each reporting period is not based on actual receipts of premium at each reporting period (see Appendix C to this paper), both applying the requirements of the general model in paragraphs 83 and B120–B125 of IFRS 17 and the requirements of the PAA in paragraphs 55(b)(v) and B126–127 of IFRS 17.

13. TRG members observed that to identify the premiums received for a group of insurance contracts, amounts that they previously presented aggregated as line items (see paragraph 15 of this paper) would need to be disaggregated into groups of insurance contracts that are assets and groups of insurance contracts that are liabilities.
14. A few TRG members suggested that IFRS 17 should be amended to require aggregation at a portfolio or entity level for presentation purposes.

Applying existing practice

15. TRG members explained that under existing practice, line items of the statement of financial position reflect a relatively high level of aggregation of insurance contracts (for example, at an entity level) however, they are disaggregated in a manner that is consistent with the way that entities manage their operations and systems. For example, these line items identify separately:
 - (a) insurance receivables—produced by cash management/credit management systems. These represent the amounts due to be received, including overdue amounts and invoiced that are outstanding.
 - (b) unearned premium reserve (UPR) and other insurance reserves that relate to future coverage—produced by the policy administration system or an earning engine. The UPR is the amount that reflects the contract premium received or due to be received that has yet to be recognised as revenue. It is primarily used for non-life contracts.
 - (c) liability for incurred claims, including incurred but not reported claims (IBNR)—based on claims management systems and actuarial models. This represents the obligation to pay claims that have been incurred but not paid at the reporting date.
 - (d) deferred acquisition costs—based on commission administration systems or general cost administration system.

16. A few TRG members explained that under their existing practice for non-life contracts and some protection life contracts, the presentation in the statements of financial position reflects a gross presentation of the premiums invoiced to the policyholders and a liability that reflects the unearned premium. This method of presentation is illustrated in the examples in Appendix C to this paper.
17. TRG members explained that the presentation of these disaggregated line items at an entity level under existing practice reflects critical measures used for both internal and external users of financial statements. In particular, they regard the following as key management metrics for non-life contracts and some protection life contracts:
 - (a) premiums receivable—provides information about the entity’s exposure to credit risk; and
 - (b) UPR—provides information about the entity’s obligation to fulfil the contracts.
18. Some TRG members expressed concern that this information would be lost in applying IFRS 17. Furthermore, some TRG members noted that in their view, users of financial statements may consider the information provided by the requirement to present groups of insurance contracts that are assets separately from groups of contracts that are liabilities less relevant. Additionally, in their view, users of financial statements may misinterpret this information.
19. In addition:
 - (a) some TRG members stated that since the actual receipt of premiums affects the measurement of the group of contracts, a group can change from asset position to liability position over time;
 - (b) a few TRG members noted that they believe that investors and prudential regulators are likely to demand information that is based on existing practice and that preparers would continue producing this information for management purposes;

- (c) a few TRG members suggested that the existing practice reflects the information on an accrual basis, whereas they believe the requirements of IFRS 17 are on cash basis and therefore provide less transparent information; and
- (d) a few TRG members suggested that IFRS 17 should be amended to bring premiums receivables into the scope of IFRS 9 *Financial Instruments* instead of IFRS 17.

Implementation challenges in identifying premiums received related to groups of insurance contracts

- 20. TRG members stated that a significant implementation challenge results from the need to identify premiums received with each group of contracts. TRG members explained that the challenge is primarily due to a need for new systems or a significant change to existing systems because existing systems do not link the system that registers premiums received and the system that generates the information necessary to determine the liability for remaining coverage. The latter processes information based on the assumption that premiums were received or are received when due.
- 21. In addition, TRG members noted that, under existing practice, information is managed using systems based on different granularity levels that reflect the manner in which an entity operates its business. For example, some TRG members noted that the system that registers premiums received, which is focused on the collection of premiums receivable and the management of credit risk, generally aggregates contracts by distribution network (for example, contracts may be aggregated by a broker or an agent).
- 22. A few TRG members noted that insurers reconcile the receivables generated from the system that registers the premiums received with the information included in the general accounting systems as part of the overall control framework that insurers have developed around their working capital cycle and the close of the

financial reporting. However, this is performed at a higher level of aggregation than a group of contracts.

23. Some TRG members suggested that the challenge of identifying premiums received relating to groups of contracts is equally relevant to life and non-life contracts. Other TRG members suggested that this challenge would be more relevant to non-life contracts mainly because:
- (a) for most life contracts the amounts identified as premiums due to be received are less significant than for non-life contracts. For non-life contracts the beginning of the coverage period and the premium due date are contractually defined independently from whether the premium has been paid (a few TRG members noted that this is also relevant to health and protection business). Conversely, for most life insurance contracts with an investment component the contract only begins when the premium is paid.
 - (b) it is expected that an immaterial number of groups of life contracts would switch between asset and liability positions due to the long-term coverage.
24. TRG members suggested that to integrate a system solution that would provide entities with the capabilities to identify premiums received with groups of insurance contracts is likely to be complex and costly. The demands come from a greater need for memory storage, computational capabilities and from the work necessary for this new/upgraded technology to be integrated with the legacy systems of insurers.
25. TRG members noted a concern that, in their view, the costs related to the implementation challenges would be higher than the benefit related to presenting information in the statement of financial position based on groups of insurance contracts.
26. A few TRG members observed that an alternative solution may be to apply an approximation approach for allocating premium receipts amongst the groups of insurance contracts, noting that paragraph 24 of IFRS 17 allows for reasonable

approximations to allocate fulfilment cash flow components to groups of contracts. It was observed that challenges in achieving consistency, reacting to changes in policyholder payment behaviour and validation of the allocation method may arise.

Implementation challenges in identifying the liability for incurred claims related to groups of insurance contracts

27. TRG members stated that a significant implementation challenge results from the need to identify the liability for incurred claims for each group of insurance contracts. They regarded this basis as inconsistent with actuarial valuation principles and stated that it would result in significant implementation costs.
28. TRG members explained that claims are managed and administrated in separate, independent systems (claims administration systems) that are not linked to the system that generates the information necessary to determine the liability for remaining coverage. TRG members also noted that the information about the liability for incurred claims is managed at a granularity level that reflects the manner in which an entity operates its business. For example, some TRG members observed that typically claims are actuarially managed on an accident year claim basis or underwriting year contract basis in order to most appropriately reflect specific characteristics and actuarial principles. TRG members explained that information based at this level of aggregation is a necessary basis for the calculation of the liability for incurred claims including IBNR.
29. A few TRG members noted that, applying IFRS 17, there are other expenses an insurance entity incurs to fulfil the insurance contract obligations that are a level higher than the group of insurance contracts—for example, insurance acquisition cash flows—and that an allocation to groups of insurance contracts would be required regardless of the presentation requirements of IFRS 17. Some of these members expected that the guidance in paragraph 24 of IFRS 17 would be used.
30. Some TRG members suggested that the challenge of identifying the liability for incurred claims with groups of contracts is equally relevant to life and to non-life

contracts. Other TRG members suggested that this challenge would be more relevant to non-life contracts where contracts tend to have a long settlement period.

Supporting materials

31. Based on the responses received from the TRG members, the staff have identified a few areas that the staff believe would benefit from the development of additional supporting materials. The topics that are expected to form the base for these materials, including an illustrative example, are provided below and in Appendix C to this paper. These materials could be useful in facilitating a better understanding of the requirements of the Standard and may be helpful in mitigating some of the implementation concerns expressed by preparers. The topics are the following:

- (a) entities should consider the disclosure requirements included in paragraphs 121–132 of IFRS 17 to provide information about the entity’s exposure to insurance and financial risks arising from insurance contracts. In particular, the disclosures related to credit risk that arises from insurance contracts may be relevant in considering whether there is a loss of information that TRG members view as useful to users of financial statements.
- (b) the requirements in IFRS 17 specify the amounts to be reported, not the methodology to be used to determine those amounts.
- (c) paragraph 24 of IFRS 17 states that an entity may estimate the fulfilment cash flows at a higher level of aggregation than a group or portfolio, provided it is able to include the appropriate fulfilment cash flows in the measurement of the group by way of allocation. Paragraph 33(a) of IFRS 17 specifies that the estimates of future cash flows shall incorporate all reasonable and supportable information available without undue cost or effort about the amount, timing and uncertainty of those future cash flows. An allocation that incorporates all

reasonable and supportable information without undue cost or effort may provide an alternative approach to identifying the premiums received and the liability for incurred claims for each group of insurance contracts.

- (d) in a few of the responses received, there may be a misunderstanding of the mechanics of the PAA. The staff have developed a few examples based on a fact pattern provided by a TRG member to illustrate the mechanics of the PAA approach together with the accounting under existing practice. The staff think it would be helpful to communicate these examples as supporting material (see Appendix C to this paper).

Treatment of contracts acquired in their settlement period

Applying the requirements of IFRS 17

32. Some insurance contracts cover events that have already occurred but the financial effect of which is still uncertain. Paragraph B5 of IFRS 17 states that for these contracts the insured event is the determination of the ultimate cost of the claim.
33. When an entity acquires contracts in their settlement period, the entity essentially provides coverage for the adverse development of claims. The period over which the claims could develop extends to the settlement period for the entity that issued the original contract. Thus, the settlement period for the entity that issued the original contract becomes the coverage period for the entity that acquires the contracts. Therefore, contracts acquired in their settlement period will be considered part of the liability for remaining coverage for the entity that acquired the contract and not part of the liability for incurred claims.
34. This results in entities accounting differently for similar contracts depending on whether those contracts are issued by the entity or whether the entity acquired those contracts in their settlement period. The most notable outcomes of this distinction include:
- (a) an entity applies the general model for the contracts acquired in their settlement period (because the period over which claims could develop is longer than one year) while entities expect to apply the PAA for similar contracts they issue; and
 - (b) an entity recognises revenue for the contracts acquired in their settlement period over the period the claims can develop, while revenue is no longer recognised over this period for similar contracts issued.

Applying existing practice

35. TRG members noted that applying these requirements reflects a significant change from existing practice and this change results in implementation

challenges and costs. Most members noted their concern is primarily relevant to entities that expect to account for all the contracts they issue using the PAA, which include mainly non-life and health contracts.

36. TRG members explained that, applying existing practice, contracts acquired in their settlement period are accounted for as liability for incurred claims of the acquirer.
37. Some TRG members observed that, in their view, users of financial statements could consider the information provided applying the requirements of IFRS 17 to be misleading or counterintuitive as it distinguishes similar contracts based on whether they have been issued by the entity or acquired by it in their settlement period.
38. A few TRG members suggested that revenue recognition for contracts acquired in their settlement period could affect the incentive or pricing of business combination transactions in the market place. They state that this is because revenue for the same contract would be recognised twice; once by the issuer of the contract, and again (not necessarily the same amount) by the acquirer of the claims that result from that contract. The different accounting under US GAAP was also noted.

Implementation challenges identified as a result of the change from existing practice

39. TRG members noted that entities that expect to apply the PAA for all contracts they issue would need to develop systems to support the accounting for contracts acquired in their settlement period applying the general model of IFRS 17.
40. A few TRG members commented on the uncertainty involved with estimating cash flows that relate to the ultimate settlement of such contracts and the challenges in determining the coverage units for CSM allocation.

Additional notes

41. There is some similarity to the treatment of some contracts that are acquired in a business combination when the transaction is accounted for differently by the entity that issued the contract and the reporting entity after the business combination. As in such cases, additional disclosures might be necessary to provide information that enables users of financial statements to evaluate the nature and financial effect of a business combination according to paragraph 59 of IFRS 3 *Business Combinations*. These disclosures, together with those required by IFRS 17, may mitigate some of the concerns raised above.

Appendix A—Relevant extracts from Agenda Paper 7 and the meeting summary of the February 2018 TRG meeting

Topic 1—Presentation of groups of insurance contracts in the statement of financial position

S03—Presentation of groups of insurance contracts in the statement of financial position

- A.1 Question—The submission asks whether the requirement in paragraph 78 of IFRS 17 to present separately in the statement of financial position groups of insurance contracts issued that are assets and groups of insurance contracts that are liabilities is appropriate and whether presentation at a portfolio level would be more appropriate considering groups share similar risks and are managed together. The submission notes that as a result of implementation of paragraph 78 of IFRS 17 preparers will provide information which will not add value to users of financial statements and will be produced at significant cost for preparers on and after transition.
- A.2 Response—The submission acknowledges the IFRS 17 requirements for the separate presentation of groups of insurance contracts that are assets and groups of insurance contracts that are liabilities. A group of insurance contracts is the unit of account applying IFRS 17. The *Conceptual Framework for Financial Reporting* states:
- Offsetting occurs when an entity recognises and measures both an asset and liability as separate units of account, but combines them into a single net amount in the statement of financial position. Offsetting classifies dissimilar items together and therefore is generally not appropriate.
- The requirements in IFRS 17 are therefore consistent with the *Conceptual Framework*.
- A.3 Summary note—The requirements in IFRS 17 are clear. Applying these requirements reflects a significant change from existing practice and this change results in implementation complexities and costs.

Topic 2—Premiums received applying the premium allocation approach*S23—Premiums received applying the premium allocation approach*

A.4 Question—The submission questions what is meant by ‘premiums, if any, received’ in paragraphs 55(a)(i) and 55(b)(i) of IFRS 17 with respect to the measurement of the liability for remaining coverage applying the premium allocation approach. The submission considers three interpretations. The first based on a literal reading of the Standard refers to premiums actually received. The other interpretations are broader and include premiums due and premiums expected.

A.5 Response—‘Premiums, if any, received’ as included in paragraphs 55(a)(i) and 55(b)(i) of IFRS 17 means premiums actually received at the reporting date. It does not include premiums due or premiums expected.

We have received, very recently, a separate submission (#27 in the submissions log) that raises a question that relates to this submission. This new submission will be assessed for a future TRG discussion.

A.6 Summary note—The requirements in IFRS 17 are clear. Applying these requirements reflects a significant change from existing practice and this change results in implementation complexities and costs.

S27—Premiums received applying the premium allocation approach

A.7 Question—The submission states that paragraphs 55(a)(i) and 55(b)(i) of IFRS 17 appear to preclude the recognition of future premiums already invoiced but not yet paid and future premiums not yet invoiced in the measurement of the liability for remaining coverage applying the premium allocation approach. The submission asks whether this interpretation is correct and states that some preparers are looking to interpret the requirements of IFRS 17 to permit the inclusion of premiums receivable because they consider it would provide more transparent information and because of practical difficulties and costs in identifying premiums received on a group of insurance contracts basis. The submission requests that the Board amend IFRS 17 to allow the recognition of premiums receivable when

measuring the liability for remaining coverage applying the premium allocation approach. The submission requests that, if the Board does not amend IFRS 17, further examples and guidance of applying this treatment are provided.

- A.8 Response—The question raised in this submission is related to submission S23. This new submission will be assessed for a future TRG discussion.

Topic 3—Subsequent treatment of contracts acquired in their settlement period

S04—Subsequent treatment of contracts acquired in their settlement period

- A.9 Question—The submission asks how insurance revenue and insurance service expenses should be presented for insurance contracts acquired in conjunction with a business combination or similar acquisition in their settlement period. More specifically, whether revenue would reflect the entire expected claims or not.
- A.10 Response—Some insurance contracts cover events that have already occurred but the financial effect of which is still uncertain. Paragraph B5 of IFRS 17 states that for these contracts the insured event is the determination of the ultimate cost of the claim. Therefore, acquiring contracts in their settlement period is essentially providing coverage for the adverse development of claims.

The subsequent treatment for the liability for remaining coverage is set out in paragraph 41 of IFRS 17. Accordingly, revenue would reflect the entire expected claims. If some cash flows meet the definition of an investment component, those cash flows will not be reflected in revenue or expenses.

- A.11 Summary note—The requirements in IFRS 17 are clear. Applying these requirements reflects a significant change from existing practice and this change results in implementation complexities and costs.

Appendix B—Questions sent to TRG members in performing the outreach

Topic 1—Presentation of groups of insurance contracts in the statement of financial position (S03 in Agenda Paper 7 of the February 2018 TRG meeting)

- B.1 Please describe any specific implementation challenges that you have identified as a result of applying the presentation requirement in paragraph 78 of IFRS 17.
- B.2 Do these challenges apply to the presentation aspect alone (paragraph 78 of IFRS 17) or any other aspects of the measurement of insurance contracts?
- B.3 Are these challenges relevant equally for life and non-life contracts issued?

Topic 2—Premiums received applying the premium allocation approach (S23 in Agenda Paper 7 of the February 2018 TRG meeting)

- B.4 Please describe any specific implementation challenges that you have identified as a result of applying the measurement requirements in paragraphs 55(a)(i) and 55(b)(i) of IFRS 17.
- B.5 Are your observations relevant equally for life and non-life contracts issued?
- B.6 Are your observations relevant equally in applying the general measurement model instead of the optional premium allocation approach?
- B.7 If those challenges arise from identifying amounts actually received for each contract, please explain how you currently identify those amounts at each reporting date.

Topic 3—Subsequent treatment of contracts acquired in their settlement period (S04 in Agenda Paper 7 of the February 2018 TRG meeting)

- B.8 Please describe any specific implementation challenges that you have identified as a result of applying the requirements in IFRS 17 for contracts acquired in their settlement periods.
- B.9 Do your observations apply equally for life and non-life contracts acquired?

B.10 Please specify whether your comments relate to measuring such contracts or determining the amount of insurance revenue and insurance service costs related to such contracts or both.

Appendix C—Examples of the PAA mechanics (with comparison to the accounting under existing practice)

Fact pattern¹

- C.1 A contract is issued with a period of insurance coverage 1 July 20X1–30 June 20X2. The contractually agreed premium is CU1,200. Insurance acquisition cash flows of CU180 are paid on 1 July 20X1.
- C.2 The premium is paid at different timing in the three scenarios:
- (a) Scenario 1—Premium paid up front;
 - (b) Scenario 2—Premium paid at the end of the coverage period; and
 - (c) Scenario 3—Premium paid on a monthly basis.
- C.3 The example illustrates the accounting for the contract applying the PAA at each interim reporting period. The example:
- (a) is simplified, however it illustrates that the timing of premium receipts do not directly affect the revenue recognition pattern applying IFRS 17;
 - (b) assumes, for simplicity, that no claims are incurred (the liability for incurred claims is part of the insurance contract liability or asset); and
 - (c) illustrates the presentation of items on the statement of financial position applying existing practice and applying IFRS 17.

¹ The fact pattern and accounting under existing practice is based on examples provided by a TRG member.

Scenario 1—Premium paid up front

Reporting date	01.07.X1	30.09.X1	31.12.X1	31.3.X2	30.6.X2
Existing practice—insurance line items on the statement of financial position and revenue reported					
Premium receivable	0	0	0	0	0
Unearned premium reserve (UPR)	(1200)	(900)	(600)	(300)	0
Deferred acquisition cost (DAC)	180	135	90	45	0
Sum of insurance line items on the statement of financial position (overall liability position)	(1020)	(765)	(510)	(255)	0
Revenue for each period (change in UPR)		300	300	300	300
IFRS 17 PAA—insurance contract asset / (liability) on the statement of financial position and revenue reported					
Opening balance	0	(1020)	(765)	(510)	(255)
55(a)(i) Premium received on initial recognition	(1200)				
55(a)(ii) Insurance acquisition cash flows	180				
55(b)(i) Premiums received in the period		0	0	0	0
55(b)(iii) Amortisation of insurance acquisition cash flows		(45)	(45)	(45)	(45)
55(b)(v) Insurance revenue applying B126²		300	300	300	300
Closing balance of insurance contract asset / (liability)	(1020)	(765)	(510)	(255)	0

IFRS 17 PAA—journal entries

At initial recognition - 01.07.X1

Receipt of premiums	Dr	Cash	1200
	Cr	Insurance contract liability	1200
Insurance acquisition cash flows	Dr	Insurance contract liability	180
	Cr	Cash	180

At each reporting date (30.09.X1, 31.12.X1, 31.03.X1 and 30.06.X1)

Amortisation of insurance acquisition cash flows	Dr	Insurance service expenses	45
	Cr	Insurance contract liability	45
Insurance revenue	Dr	Insurance contract liability	300
	Cr	Insurance revenue	300

² Expected premium receipts allocated to coverage periods (CU1200 / 4 periods = CU300)

Scenario 2—Premium paid at the end of the coverage period

Reporting date	01.07.X1	30.09.X1	31.12.X1	31.3.X2	30.6.X2
Existing practice—insurance line items on the statement of financial position and revenue reported					
Premium receivable	1200	1200	1200	1200	0
Unearned premium reserve (UPR)	(1200)	(900)	(600)	(300)	0
Deferred acquisition cost (DAC)	180	135	90	45	0
Sum of insurance line items on the statement of financial position (overall asset position)	180	435	690	945	0
Revenue for each period (change in UPR)		300	300	300	300
IFRS 17 PAA—insurance contract asset / (liability) on the statement of financial position and revenue reported					
Opening balance	0	180	435	690	945
55(a)(i) Premium received on initial recognition	0				
55(a)(ii) Insurance acquisition cash flows	180				
55(b)(i) Premiums received in the period		0	0	0	(1200)
55(b)(iii) Amortisation of insurance acquisition cash flows		(45)	(45)	(45)	(45)
55(b)(v) Insurance revenue applying B126²		300	300	300	300
Closing balance of insurance contract asset / (liability)	180	435	690	945	0

IFRS 17 PAA—journal entries

At initial recognition - 01.07.X1

Insurance acquisition cash flows	Dr	Insurance contract asset	180
	Cr	Cash	180

At each reporting date (30.09.X1, 31.12.X1, 31.03.X1 and 30.06.X1)

Amortisation of insurance acquisition cash flows	Dr	Insurance service expenses	45
	Cr	Insurance contract asset	45
Insurance revenue	Dr	Insurance contract asset	300
	Cr	Insurance revenue	300

At the end of the coverage period (30.06.X1)

Receipt of premium³	Dr	Cash	1200
	Cr	Insurance contract asset	1200

³ Entities should consider the disclosure requirements included in paragraphs 121–132 of IFRS 17 to provide information about the entity’s exposure to credit risk that arises from insurance contracts.

Scenario 3—Premium paid on a monthly basis

Reporting date	01.07.X1	30.09.X1	31.12.X1	31.3.X2	30.6.X2
Existing practice—insurance line items on the statement of financial position and revenue reported					
Premium receivable	1200	900	600	300	0
Unearned premium reserve (UPR)	(1200)	(900)	(600)	(300)	0
Deferred acquisition cost (DAC)	180	135	90	45	0
Sum of insurance line items on the statement of financial position (overall asset position)	180	135	90	45	0
Revenue for each period (change in UPR)		300	300	300	300
IFRS 17 PAA—insurance contract asset / (liability) on the statement of financial position and revenue reported					
Opening balance	0	180	135	90	45
55(a)(i) Premium received on initial recognition	0				
55(a)(ii) Insurance acquisition cash flows	180				
55(b)(i) Premiums received in the period		(300)	(300)	(300)	(300)
55(b)(iii) Amortisation of insurance acquisition cash flows		(45)	(45)	(45)	(45)
55(b)(v) Insurance revenue applying B126²		300	300	300	300
Closing balance of insurance contract asset / (liability)	180	135	90	45	0

IFRS 17 PAA—journal entries

At initial recognition - 01.07.X1

Insurance acquisition cash flows	Dr	Insurance contract asset	180
	Cr	Cash	180

At each reporting date (30.09.X1, 31.12.X1, 31.03.X1 and 30.06.X1)

Receipt of premiums	Dr	Cash	300
	Cr	Insurance contract asset	300
Amortisation of insurance acquisition cash flows	Dr	Insurance service expenses	45
	Cr	Insurance contract asset	45
Insurance revenue	Dr	Insurance contract asset	300
	Cr	Insurance revenue	300

STAFF PAPER

May 2018

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
S13	Modifications to retrospective application	This submission is about applying the full retrospective approach to transition. The submission asks what modifications are permitted when applying IFRS 17 retrospectively. Specifically, the submission questions whether reasonable approximations are permitted when applying IFRS 17 retrospectively or whether the existence of specified modifications in the modified retrospective approach suggests that other modifications should not be used when applying IFRS 17 retrospectively.	<p>Applying paragraph C3 of IFRS 17, an entity shall apply IFRS 17 retrospectively unless impracticable. Paragraphs 50–53 of IAS 8 <i>Accounting Policies, Changes in Accounting Estimates and Errors</i> provide requirements on determining whether retrospective application is impracticable. Paragraph 51 of IAS 8 states:</p> <p style="padding-left: 40px;">[...] the objective of estimates related to prior periods remains the same as for estimates made in the current period, namely, for the estimates to reflect the circumstances that existed when the transaction, other event or condition occurred.</p>

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

TRG for IFRS 17 | Reporting on other questions submitted

Log #	Topic	Question	Response
S14	Projected returns on assets	<p>The submission asks whether ‘risk neutral’ or ‘real world’ scenarios should be used for stochastic modelling techniques to project future returns on assets, applying paragraph B48 of IFRS 17.</p> <p>The submission describes a ‘real world’ approach to be based on an assumed distribution of scenarios that is intended to reflect realistic assumptions about actual future asset returns.</p> <p>The submission describes a ‘risk neutral’ approach to be based on an assumed distribution of scenarios that is not intended to reflect realistic assumptions about actual future asset returns. Instead, there is an underlying assumption that, on average, all assets earn the same risk-free return, with a range of scenarios analysed reflecting the assumed volatility of returns for an asset class consistent with volatility implied by option prices.</p>	<p>Applying paragraph B48 of IFRS 17, an entity is required to apply judgement to determine the technique for estimating market variables to meet the objective of achieving consistency with observable market variables.</p> <p>Paragraph B74(b) of IFRS 17 states the requirements for discounting cash flows that vary based on the returns of any financial underlying items.</p> <p>Applying paragraph B77 of IFRS 17 an entity is not required to divide estimated cash flows into those that vary based on the return on underlying items and those that do not. If not divided, the discount rate should be appropriate for the estimated cash flows as a whole. Any consideration beyond this is actuarial in nature and therefore does not fall within the remit of the TRG.</p>

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

TRG for IFRS 17 | Reporting on other questions submitted

Log #	Topic	Question	Response
S28	Insurance contracts with direct participation features – adjustments to the contractual service margin	<p>The submission states that within IFRS 17 there are two different definitions of the adjustments to the contractual service margin for insurance contracts with direct participation features. The submission considers these two different definitions to result in different mathematical outcomes. Specifically, the submission compares:</p> <ul style="list-style-type: none"> – Paragraph 45(b) of IFRS 17 'the entity's share of the change in the fair value of the underlying items'; and, – Paragraph B112 of IFRS 17 'changes in the entity's share of the fair value of the underlying items'. 	<p>The adjustment to the contractual service margin in paragraph 45(b) of IFRS 17 provides the same mathematical outcome as paragraph B112 of IFRS 17.</p> <p>The staff will consider this topic for future educational materials.</p>
S29	Discount rates used in the allocation of insurance finance income or expenses to profit or loss	<p>The submission considers the discount rate used to determine the amount of the insurance finance income or expenses to be included in profit or loss if an entity chooses to disaggregate insurance finance income or expenses between profit or loss and other comprehensive income. Specifically, the submission considers paragraph B72(e)(i) of IFRS 17 for a group of insurance contracts for which changes in assumptions that relate to financial risk do not have a substantial effect on the amounts paid to policyholders. The submission asks whether an entity should use an effective yield rate or a yield curve.</p>	<p>Applying paragraph B72(e)(i) of IFRS 17, an entity shall use the discount rate determined at the date of initial recognition of a group of contracts applying paragraph 36 of IFRS 17 to nominal cash flows that do not vary based on the returns on any underlying items. Paragraph B72(e)(i) of IFRS 17 does not mandate the use of an effective yield rate or a yield curve, as long as the rate is the rate that applies to nominal cash flows that do not vary based on any underlying items, applying paragraph 36.</p>

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

Log #	Topic	Question	Response
S32	Issued adverse loss cover and contracts acquired in their settlement period	<p>The submission states that for issued adverse loss cover and contracts acquired in their settlement period, it is not clear how the liability for remaining coverage will be reduced because service has been provided. The submission asks when claims are incurred for these contracts.</p> <p>The submission also asks, for contracts acquired in their settlement period, what subsequent treatment should be applied if the liability for remaining coverage is determined to have nil contractual service margin at initial recognition (ie insurance contracts are measured at zero with nil contractual service margin) and estimates of future cash outflows decrease subsequently.</p>	<p><i>When claims are incurred for issued adverse loss cover and contracts acquired in their settlement period</i></p> <p>Applying paragraph B5 of IFRS 17 (for insurance contracts that cover events that have already occurred but the financial effect of which is still uncertain), the claims are incurred when the financial effect becomes certain. This is not when an entity has a reliable estimate if there is still uncertainty involved. Conversely, this is not necessarily when the claims are paid if certainty has been achieved prior to the actual payment.</p> <p><i>Subsequent treatment if the contractual service margin is nil at initial recognition</i></p> <p>Paragraphs B93-B95 of IFRS 17 state the requirements for determining a contractual service margin at initial recognition for insurance contracts acquired. In the scenario presented in the submission, there is a contractual service margin of zero at initial recognition. Subsequent measurement of insurance contracts acquired, including changes in estimates that adjust the contractual service margin, is the same as for insurance contracts issued applying paragraphs 40–52 of IFRS 17. Therefore, a contractual service margin larger than zero may be recognised post acquisition.</p>

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

TRG for IFRS 17 | Reporting on other questions submitted

Log #	Topic	Question	Response
S35	Level of aggregation – no significant possibility of becoming onerous	The submission asks how ‘no significant possibility’ should be interpreted as set out in paragraph 16(b) of IFRS 17. The submission expresses a view that one possible interpretation is by analogy to the concept of significant insurance risk in paragraphs B17-B23 of IFRS 17.	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 to identify contracts with no significant possibility of becoming onerous at initial recognition in order 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. ‘No significant possibility of becoming onerous’ is different from ‘significant insurance risk’ and the concept of significant insurance risk should not be used by analogy.
S37	Projected economic conditions	<p>The submission asks whether an entity’s estimate of future economic conditions is ever required to estimate future cash flows. Specifically, the submission considers the estimates of non-market variables that correlate to market variables applying paragraph B53 of IFRS 17.</p> <p>The submission considers scenarios using either a risk-neutral approach or an approach based on the entity’s actual expectations.</p>	Paragraph B48 of IFRS 17 requires an entity to apply judgement to determine the technique for estimating market variables to meet the objective of achieving consistency with observable market variables. Paragraph B74(b) of IFRS 17 sets out the requirements for discounting cash flows that vary based on the returns of any financial underlying items. Applying paragraph B77 of IFRS 17 an entity is not required to divide estimated cash flows into those that vary based on the return on underlying items and those that do not. If not divided, the discount rate used should be appropriate for the estimated cash flows as a whole. Any consideration beyond this is actuarial in nature and therefore does not fall within the remit of the TRG.

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

TRG for IFRS 17 | Reporting on other questions submitted

Log #	Topic	Question	Response
S38	Reflecting minimum guarantees	<p>The submission asks whether paragraph B76 of IFRS 17 restricts how minimum guarantees are reflected in the present value of future cash flows.</p> <p>Specifically, the submission asks if it is required that the minimum guarantees are reflected through adjusting the discount rate (and not through adjustments to the cash flows).</p>	<p>IFRS 17 requires that the time value of a guarantee be reflected in the measurement of the fulfilment cash flows; however, it does not require the use of a specific approach to do this. Applying B86 of IFRS 17, financial risk is included in the estimates of the future cash flows or the discount rate used to adjust the cash flows. Paragraph B48 of IFRS 17 explains that judgement is required to determine the technique for measuring market variables and that the technique used must result in the measurement of any options and guarantees being consistent with observable market prices for such options and guarantees. Any consideration beyond this is actuarial in nature and therefore does not fall within the remit of the TRG.</p>

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

TRG for IFRS 17 | Reporting on other questions submitted

Log #	Topic	Question	Response
S40	Discount rate for reinsurance contracts held	The submission questions what discount rate should be used to measure the present value of future cash flows of a reinsurance contract held if the liquidity characteristics of the underlying contracts are different from those of the reinsurance contract held.	Paragraph 63 of IFRS 17 requires an entity to use consistent assumptions to measure the estimates of the present value of the future cash flows for the group of reinsurance contracts held and the estimates of the present value of the future cash flows for the group(s) of underlying insurance contracts. This consistency is required to the extent that the same assumptions apply to both the underlying contracts and the reinsurance contracts held. This requirement does not require/permit the entity to use the same assumptions used for measuring the underlying contracts when measuring the reinsurance contracts held if those assumptions are not valid for the terms of the reinsurance contracts held. If different assumptions apply for the reinsurance contract held, the entity uses those different assumptions when measuring that contract.

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

TRG for IFRS 17 | Reporting on other questions submitted

Log #	Topic	Question	Response
S41	Coverage units for reinsurance contracts held	The submission asks whether, for reinsurance contracts held, coverage units are determined based on the services provided by the reinsurer or the coverage units of the underlying insurance contracts.	<p>Applying paragraph B119 of IFRS 17, the coverage units in a group of insurance contracts are determined based on the quantity of coverage provided by the contracts in the group. For a group of reinsurance contracts held, this is the coverage received by the insurer from those reinsurance contracts held, and not the coverage provided by the insurer to its policyholders through the underlying insurance contracts. When determining the quantity of benefits received from a reinsurance contract held, an entity may consider relevant facts and circumstances related to the underlying insurance contracts.</p> <p>Determining the quantity of benefits for identifying coverage units was discussed at the February 2018 meeting of the TRG and will be discussed at the May 2018 meeting. Example 8 in Appendix B of Agenda Paper 5 of the May 2018 meeting considers proportional reinsurance coverage.</p>
S42	Risk of non-performance of the issuer of a reinsurance contract	The submission asks whether, for reinsurance contracts held, the risk of non-performance of the issuer of the reinsurance contracts is considered within the estimates of the present value of future cash flows or the risk adjustment for non-financial risk.	Paragraph 63 of IFRS 17 explicitly requires the effect of any risk of non-performance by the reinsurer to be included in the estimates of the present value of the future cash flows. Applying paragraph 64 of IFRS 17, the risk adjustment for non-financial risk represents the amount of risk being transferred by the entity to the reinsurer.

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

TRG for IFRS 17 | Reporting on other questions submitted

(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
No submissions reported in this category.			

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

Log #	Topic	Question	Response
S33	Scope of IFRS 17	<p>The submission asks whether IFRS 17 would apply to six examples of contracts typically issued by non-insurance entities. Those examples can be grouped in the following three categories:</p> <ul style="list-style-type: none"> (a) loan contracts that may waive some or all of the payments due under the contract in specified circumstances; (b) service contracts including a form of EBITDA guarantee; and (c) credit card contracts providing coverage for a supplier failure. 	<p>The definition of an insurance contract—which determines which contracts are within the scope of IFRS 17—is the same as the definition in IFRS 4 <i>Insurance Contracts</i>, with clarifications to the related guidance in Appendix B of IFRS 4 to require that (a) an insurer should consider the time value of money in assessing whether the additional benefits payable in any scenario are significant; and (b) a contract does not transfer significant insurance risk if there is no scenario with commercial substance in which the insurer can suffer a loss on a present value basis. Therefore, a contract that is an insurance contract in applying IFRS 4 is expected to be an insurance contract in applying IFRS 17. The consequences of being within the scope of IFRS 17, which sets out recognition and measurement requirements for insurance contracts, are however different.</p> <p>Outreach will be performed to better understand the nature of the contracts described in the submission and how they are accounted for today.</p>

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

**Transition Resource Group for IFRS 17 Insurance Contracts
Submissions Log
As at 18 April 2018**

Log #	Submission Date	Topic	Question	TRG Meeting	TRG paper reference	Current Status	Comments
S01	18-Dec-17	Determining the quantity of benefits for identifying coverage units	The submission asks what the definition of "quantity of benefits" in paragraph B119(a) of IFRS 17 is for use in determining the amortisation pattern of the contractual service margin.	February 2018	AP05	To be discussed at the TRG	
				May 2018	AP05		
S02	18-Dec-17	Separation of insurance components of a single contract	The submission noted that insurers may combine different types of products or coverages that have different risks into one insurance contract. The submission asks if it is permitted to separate insurance components from the host insurance contract and measure the components separately.	February 2018	AP01	No further discussion planned at this time	
S03	18-Dec-17	Presentation of groups of insurance contracts in the statement of financial position	The submission asks whether the requirement in paragraph 78 of IFRS 17 to present separately in the statement of financial position groups of insurance contracts that are assets and groups of insurance contracts that are liabilities is appropriate and whether presentation at a portfolio level would be more appropriate considering groups share similar risks and are managed together. The submission notes that as a result of implementation of paragraph 78 of IFRS 17 preparers will provide information which will not add value to the users of the financial statements and will be produced at significant cost for preparers on and after transition.	February 2018	AP07	Implementation challenges outreach to be reported to the TRG and the Board	
				May 2018	AP06		
S04	18-Dec-17	Subsequent treatment of contracts acquired in their settlement period	The submission asks how insurance revenue and insurance service expenses should be presented for insurance contracts acquired in conjunction with a business combination or similar acquisition in their settlement period. More specifically, whether revenue would reflect the entire expected claims or not.	February 2018	AP07	Implementation challenges outreach to be reported to the TRG and the Board	
				May 2018	AP06		
S05	21-Dec-17	Insurance acquisition cash flows when using fair value transition	The submission asks if and how insurance acquisition cash flows that occurred prior to the IFRS 17 transition date are determined if the fair value approach to transition is applied. The submission notes that to do this would be burdensome and largely impracticable and so requests that if IFRS 17 does require these past cash flows to be determined, that an amendment is made to the Standard to change that requirement.	February 2018	AP06	No further discussion planned at this time	
S06	22-Dec-17	Business combinations on transition - classification date	The submission asks what the relevant date is for determining whether contracts acquired in previous business combinations are classified as insurance contracts when an entity transitions to IFRS 17 retrospectively. The submission notes that there is an inconsistency in the requirements of the Standard and the intention of the Board set out in Agenda Paper 2C of the February 2017 Board meeting.	February 2018	AP07	No further discussion planned at this time	This question will be considered as part of the annual improvements process
S07	22-Dec-17	Insurance acquisition cash flows paid on an initially written contract	The submission asks whether all insurance acquisition cash flows are allocated to the initial contract issued if they are partly associated with future renewals.	February 2018	AP04	No further discussion planned at this time	
S08	02-Jan-18	Insurance acquisition cash flows when using fair value transition	The submission asks whether when applying the fair value transition approach insurance acquisition cash flows should be considered.	February 2018	AP06	No further discussion planned at this time	
S09	02-Jan-18	Allocating the contractual service margin at the end of a period to coverage units	The submission questions how to allocate the contractual service margin to coverage units provided in the current period and expected to be provided in the future applying paragraph B119(b) of IFRS 17.	February 2018	AP07	No further discussion planned at this time	
S10	02-Jan-18	Classification of contracts acquired in a business combination	The submission notes that according to the consequential amendments to IFRS 3 <i>Business Combinations</i> , classification of contracts acquired in a business combination transaction is based on the terms and conditions at the transaction date. The submission acknowledges that this could result in different contract classifications for an acquirer and an acquiree. The submission states that this will result in onerous system implications and various consolidation complexities.	February 2018	AP07	No further discussion planned at this time	
S11	02-Jan-18	Contract boundary	The submission questions how entities should interpret the phrase "practical ability to reassess the risks" of a policyholder or a portfolio of insurance contracts when assessing the boundary of an insurance contract.	May 2018	AP03	To be discussed at the TRG	
S12	02-Jan-18	Coverage units	The submission asks whether coverage units, and the corresponding quantity of coverage provided by contracts, should be defined in terms of insurance coverage and insurance benefits only or in terms of all contract benefits including investment components.	May 2018	AP05	To be discussed at the TRG	
S13	02-Jan-18	Modifications to retrospective application	This submission is about applying the full retrospective approach to transition. The submission asks what modifications are permitted when applying IFRS 17 retrospectively. Specifically, the submission questions whether reasonable approximations are permitted when applying IFRS 17 retrospectively or whether the existence of specified modifications in the modified retrospective approach suggests that other modifications should not be used when applying IFRS 17 retrospectively.	May 2018	AP07	To be reported to the TRG	

**Transition Resource Group for IFRS 17 Insurance Contracts
Submissions Log
As at 18 April 2018**

Log #	Submission Date	Topic	Question	TRG Meeting	TRG paper reference	Current Status	Comments
S14	02-Jan-18	Projected returns on assets	The submission asks whether 'risk neutral' or 'real world' scenarios should be used for stochastic modelling techniques to project future returns on assets, applying paragraph B48 of IFRS 17. The submission describes a 'real world' approach to be based on an assumed distribution of scenarios that is intended to reflect realistic assumptions about actual future asset returns. The submission describes a 'risk neutral' approach to be based on an assumed distribution of scenarios that is not intended to reflect realistic assumptions about actual future asset returns. Instead, there is an underlying assumption that, on average, all assets earn the same risk-free return, with a range of scenarios analysed reflecting the assumed volatility of returns for an asset class consistent with volatility implied by option prices.	May 2018	AP07	To be reported to the TRG	
S15	02-Jan-18	Boundary of reinsurance contracts held	The submission questions how to read paragraph 34 of IFRS 17 regarding the boundary of an insurance contract with respect to reinsurance contracts held.	February 2018	AP03	No further discussion planned at this time	
S16	02-Jan-18	Discount rate to be used to adjust the contractual service margin of reinsurance contracts held	The submission asks what discount rate is used to adjust the contractual service margin of reinsurance contracts held applying paragraph 66(c) of IFRS 17.	February 2018	AP07	No further discussion planned at this time	An editorial correction will be made to add a reference to paragraph B72(c) in paragraph 66(c) of IFRS 17
S17	02-Jan-18	Using consistent assumptions for the measurement of reinsurance contracts held and the underlying insurance contracts	The submission notes that paragraph 63 of IFRS 17 requires the use of assumptions for the measurement of the estimates of the present value of the future cash flows for a group of reinsurance contracts held that are consistent with those used to measure the underlying insurance contracts. The submission questions whether this means that the use of an identical discount rate is required.	February 2018	AP07	No further discussion planned at this time	
S18	02-Jan-18	Boundary of reinsurance contracts held - future cessions	The submission asks whether future cash flows for reinsurance contracts held should include cash flows related to the ceding of assumed future sales of insurance contracts issued. The submission notes that if this is required, the implementation would lead to development of assumptions not currently used in practice and auditors would be challenged with evaluating the appropriateness of such assumptions.	February 2018	AP03	No further discussion planned at this time	
S19	02-Jan-18	Reinsurance contracts held - treaty vs cession	The submission asks, for purposes of establishing the unit of account for reinsurance contracts held, whether a "contract" should be defined as an individual treaty (i.e. legal agreement) or as an individual cession (i.e. the reinsurance coverage provided for an individual insurance contract issued).	February 2018	AP01	No further discussion planned at this time	
S20	02-Jan-18	Grouping contracts using the modified retrospective approach to transition	The submission notes that applying the modified retrospective approach to transition, paragraphs C8 and C10 of IFRS 17 require that groups of insurance contracts do not include contracts issued more than one year apart if the entity has reasonable and supportable information to do that. The submission questions whether the wording in paragraph BC392 of Basis for Conclusions on IFRS 17 and example 17 in Illustrative Examples on IFRS 17 might suggest otherwise.	February 2018	AP07	No further discussion planned at this time	
S21	02-Jan-18	Mutual entities	The submission 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.			On hold	The submitter has requested to put this question on hold because they are performing further analysis
S22	02-Jan-18	Boundary of contracts with annual repricing mechanisms	The submission asks how to interpret the term "contract boundary" described in paragraph 34 of IFRS 17 in the context of contracts with annual repricing mechanisms.	February 2018	AP02	No further discussion planned at this time	
S23	02-Jan-18	Premiums received applying the premium allocation approach	The submission questions what is meant by "premiums, if any, received" in paragraphs 55(a)(i) and 55(b)(i) of IFRS 17 with respect to the measurement of the liability for remaining coverage applying the premium allocation approach. The submission considers three interpretations. The first based on a literal reading of the standard refers to premiums actually received. The other interpretations are broader and include premiums due and premiums expected.	February 2018	AP07	Implementation challenges outreach to be reported to the TRG and the Board	
				May 2018	AP06		
S24	02-Jan-18	Discount rates applied to the contractual service margin for contracts without direct participation features	The submission outlines the differing discount rates to be used for initial measurement (B72(a)) and subsequent measurement (B72(b)) of insurance contracts without direct participating features. The submission considers that this will result in diversity between insurance revenue recognised for insurance contracts without direct participating features but that have some asset dependent cash flows and for insurance contracts with direct participation features accounted for applying the variable fee approach.	February 2018	AP07	No further discussion planned at this time	

**Transition Resource Group for IFRS 17 Insurance Contracts
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Log #	Submission Date	Topic	Question	TRG Meeting	TRG paper reference	Current Status	Comments
S25	02-Jan-18	Investment components	The submission notes that paragraph B96 of IFRS 17 requires the carrying amount of the contractual service margin to be adjusted for a difference in the investment component as a result of the acceleration or delay of repayment. The submission questions whether this is appropriate because a result of this requirement is that the contractual service margin will be adjusted for changes solely in timing of payments. The submission considers that this appears to conflict with the principle underpinning insurance revenue set out in paragraph B120. The submission also provides examples of an alternative approach.	February 2018	AP07	No further discussion planned at this time	
S26	02-Jan-18	Variable fee approach when the return is shared based on amortised cost measurement of the underlying items	The submission questions whether contracts where the return is based on an amortised cost measurement of the underlying items would fail the definition of insurance contract with direct participation features.	February 2018	AP07	No further discussion planned at this time	
S27	16-Jan-18	Premiums received applying the premium allocation approach	The submission states that paragraphs 55(a)(i) and 55(b)(i) of IFRS 17 appear to preclude the recognition of future premiums already invoiced but not yet paid and future premiums not yet invoiced in the measurement of the liability for remaining coverage applying the premium allocation approach. The submission asks whether this interpretation is correct and states that some preparers are looking to interpret the requirements of IFRS 17 to permit the inclusion of premiums receivable because they consider it would provide more transparent information and because of practical difficulties and costs in identifying premiums received on a group of insurance contracts basis. The submission requests that the Board amends IFRS 17 to allow the recognition of premiums receivable when measuring the liability for remaining coverage applying the premium allocation approach. The submission requests that, if the Board does not amend IFRS 17, further examples and guidance of applying this treatment are provided.	May 2018	AP06	Implementation outreach to be reported to the TRG and the Board	
S28	12-Feb-18	Insurance contracts with direct participation features - adjustments to the contractual service margin	The submission states that within IFRS 17 there are two different definitions of the adjustments to the contractual service margin for insurance contracts with direct participation features. The submission considers these two different definitions to result in different mathematical outcomes. Specifically, the submission compares: (a) Paragraph 45(b) of IFRS 17 'the entity's share of the change in the fair value of the underlying items'; and, (b) Paragraph B112 of IFRS 17 'changes in the entity's share of the fair value of the underlying items'.	May 2018	AP07	To be reported to the TRG	
S29	20-Mar-18	Discount rates applied in the allocation of insurance finance income or expenses	The submission considers the discount rate used to determine the amount of the insurance finance income or expenses to be included in profit or loss if an entity chooses to disaggregate insurance finance income or expenses between profit or loss and other comprehensive income. Specifically, the submission considers paragraph B72(e)(i) of IFRS 17 for a group of insurance contracts for which changes in assumptions that relate to financial risk do not have a substantial effect on the amounts paid to policyholders. The submission asks whether an entity should use an effective yield rate or a yield curve.	May 2018	AP07	To be reported to the TRG	
S30	21-Mar-18	Determining the coverage period and allocating the CSM for contracts where there is no absolute limit for the coverage period	The submission refers to situations whereby the coverage period is indeterminable or not reliably estimable because the underlying claims can have payments over decades, with no limit on when claims can be made. For example, asbestos claims were still being made in 2017 that triggered coverage on 1950s commercial liability policies in the U.S. Another example is when claims in their settlement period acquired via a business combination. The submission asks how the contractual service margin should be allocated if this is the case.	May 2018	AP05	To be discussed at the TRG	
S31	21-Mar-18	Reinsurance contracts issued - accounting for commissions	The submission asks, for reinsurance contracts issued, whether some specific common features such as commissions should be accounted for as separate or net cash flows.			To be considered for a future TRG meeting	Further information was requested from the submitter
S32	21-Mar-18	Issued adverse loss cover and contracts acquired in their settlement period	The submission states that for issued adverse loss cover and contracts acquired in their settlement period, it is not clear how the liability for remaining coverage will be reduced because service has been provided. The submission asks when claims are incurred for these contracts. The submission also asks, for contracts acquired in their settlement period, what subsequent treatment should be applied if the liability for remaining coverage is determined to have nil contractual service margin at initial recognition (ie insurance contracts are measured at zero with nil contractual service margin) and estimates of future cash outflows decrease subsequently.	May 2018	AP07	To be reported to the TRG	

**Transition Resource Group for IFRS 17 Insurance Contracts
Submissions Log
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Log #	Submission Date	Topic	Question	TRG Meeting	TRG paper reference	Current Status	Comments
S33	21-Mar-18	Scope of IFRS 17	The submission asks whether IFRS 17 would apply to six examples of contracts typically issued by non-insurance entities. Those examples can be grouped in the following three categories: (a) loan contracts that may waive some or all of the payments due under the contract; (b) service contracts including a form of EBITDA guarantee; and (c) credit card contracts providing coverage for a supplier failure.	May 2018	AP07	To be reported to the TRG	Outreach will be performed to better understand the nature of the contracts described in the submission and how they are accounted for today
S34	21-Mar-18	Contract boundary - more than one type of coverage	The submission asks how the boundary should be determined for contracts that contain multiple coverages, each of which would have a different boundary if sold on a stand-alone basis.	May 2018	AP03	To be discussed at the TRG	
S35	21-Mar-18	Level of aggregation - no significant possibility of becoming onerous	The submission asks how 'no significant possibility' should be interpreted as set out in paragraph 16(b) of IFRS 17. The submission expresses a view that one possible interpretation is by analogy to the concept of significant insurance risk in paragraphs B17-B23 of IFRS 17.	May 2018	AP07	To be reported to the TRG	
S36	21-Mar-18	Contracts with optional additions	The submission asks how an option to add coverage to an existing coverage on terms that are not guaranteed should be accounted for. Specifically, the submission considers whether or not cash flows associated with these options are within the boundary of the existing contract.	May 2018	AP03	To be discussed at the TRG	
S37	21-Mar-18	Projecting economic conditions	The submission asks whether an entity's estimate of future economic conditions is ever required to estimate future cash flows. Specifically, the submission considers the estimates of non-market variables that correlate to market variables applying paragraph B53 of IFRS 17. The submission considers scenarios using either a risk-neutral approach or an approach based on the entity's actual expectations.	May 2018	AP07	To be reported to the TRG	
S38	21-Mar-18	Reflecting minimum guarantees	The submission asks whether paragraph B76 of IFRS 17 restricts how minimum guarantees are reflected in the present value of future cash flows. Specifically, the submission asks if it is required that the minimum guarantees are reflected through adjusting the discount rate (and not through adjustments to the cash flows).	May 2018	AP07	To be reported to the TRG	
S39	21-Mar-18	Boundary of reinsurance contracts held with repricing mechanisms	The submission asks how the boundary of a reinsurance contract held should be determined when the reinsurer has the right to reprice remaining coverage prospectively. In the fact pattern provided in the submission the reinsurer can choose: (a) not to exercise the right to reprice. In this case, the entity (the holder of the contract) is committed to continue paying premiums to the reinsurer; or (b) to exercise the right to reprice. In this case, the entity has the right to terminate coverage.	May 2018	AP04	To be discussed at the TRG	
S40	21-Mar-18	Discount rate for reinsurance contracts held	The submission questions what discount rate should be used to measure the present value of future cash flows of a reinsurance contract held if the liquidity characteristics of the underlying contracts are different from those of the reinsurance contract held.	May 2018	AP07	To be reported to the TRG	
S41	21-Mar-18	Coverage units for reinsurance contracts held	The submission asks whether, for reinsurance contracts held, coverage units are determined based on the services provided by the reinsurer or the coverage units of the underlying insurance contracts.	May 2018	AP07	To be reported to the TRG	
S42	21-Mar-18	Risk of non-performance of the issuer of a reinsurance contract held	The submission asks whether, for reinsurance contracts held, the risk of non-performance of the issuer of the reinsurance contracts is considered within the estimates of the present value of future cash flows or the risk adjustment for non-financial risk.	May 2018	AP07	To be reported to the TRG	
S43	21-Mar-18	Risks considered in assessing contract boundary	The submission asks what risks should be considered when applying paragraph 34(b) of IFRS 17 regarding cash flows within the boundary of an insurance contract.	May 2018	AP03	To be discussed at the TRG	
S44	21-Mar-18	Contracts in a group with varying quantity of benefit	The submission asks how coverage units should be allocated if a group of insurance contracts consists of insurance contracts with various quantities of benefits.	May 2018	AP05	To be discussed at the TRG	
S45	21-Mar-18	Accounting for insurance contracts issued by mutual entities	The submission asks whether a contractual service margin should be recognised for participating insurance contracts and non-participating insurance contracts issued by a mutual entity.			To be considered for a future TRG meeting	To be considered with S21 which is on hold

**Transition Resource Group for IFRS 17 Insurance Contracts
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Log #	Submission Date	Topic	Question	TRG Meeting	TRG paper reference	Current Status	Comments
S46	21-Mar-18	Determining the risk adjustment for non-financial risk in a group of entities	The submission asks at which level the risk adjustment for non-financial risk is required to be determined: (a) in the individual financial statements of entities that are part of a consolidated group (ie parent and subsidiary entities that issue insurance contracts); and (b) in the consolidated financial statements of the group of entities.	May 2018	AP02	To be discussed at the TRG	
S47	21-Mar-18	Combining insurance contracts	The submission asks when it may be necessary to treat a set or series of insurance contracts as a whole, applying paragraph 9 of IFRS 17. Additionally, the submission also considers some scenarios of how to account for contract riders.	May 2018	AP02	To be discussed at the TRG	
					AP03		
S48	21-Mar-18	Coverage units - contracts with other services	The submission asks how to apply paragraph B119 of IFRS 17 when identifying and allocate coverage units in a group of insurance contracts that provide insurance coverage and other services.	May 2018	AP05	To be discussed at the TRG	
S49	23-Mar-18	Contract boundary	The submissions asks four questions on paragraphs 34(b) and B64 of IFRS 17: (a) what is meant by 'risk'? (b) are commercial considerations relevant when considering 'practical ability to reassess risk' (c) is it relevant whether an entity takes a long term view of risk when setting the pricing structure if the pricing structure is presented in a way which aligns to risks up to the reassessment date? (d) does guaranteed renewability represent a substantive right or obligation?	May 2018	AP03	To be discussed at the TRG	Questions (c) and (d) were discussed at the February 2018 meeting