STAFF PAPER

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Project	**Insurance Contracts**		
Paper topic	Presentation of insurance contracts on the statement of financial position		
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Purpose and structure of the paper

1. This paper discusses the following topics:
   (a) the need to allocate premium cash flows and the liability for incurred claims to each group of insurance contracts; and
   (b) separate presentation and measurement of premiums receivable and claims payable.
2. For each topic, this paper provides:
   (a) an overview of the requirements in IFRS 17 *Insurance Contracts*;
   (b) a summary of the International Accounting Standards Board's (Board) rationale for setting those requirements, including an overview of the Board's previous discussions;
   (c) an overview of the concerns and implementation challenges expressed since IFRS 17 was issued; and
   (d) the staff analysis, recommendations and a question for Board members.
3. Appendix A to this paper includes extracts from Agenda Paper 2C *Implementation challenges outreach report* which was discussed at the May 2018 Board meeting. That report provides a wider context of the implementation challenges related to the

topics discussed in this paper, and examples of the PAA mechanics with comparison to the accounting under existing practice.

Summary of staff recommendations

4. The staff recommend that the Board should:
   (a) amend paragraph 78 of IFRS 17 to require that an entity presents separately in the statement of financial position the carrying amount of portfolios of:
      (i) insurance contracts issued that are assets;
      (ii) insurance contracts issued that are liabilities;
      (iii) reinsurance contracts held that are assets; and
      (iv) reinsurance contracts held that are liabilities.
   (b) not amend the requirements in IFRS 17 to require separate presentation and measurement of premiums receivable and claims payable.

The need to allocate premium cash flows and the liability for incurred claims to each group of insurance contracts

IFRS 17 requirements

5. IFRS 17 specifies requirements for the recognition, measurement, presentation and disclosure of groups of insurance contracts. Those requirements reflect all the rights and obligations arising from a group of insurance contracts as a single asset or liability. In other words, the unit of account for IFRS 17 is a group of insurance contracts.

6. Applying the general model, an entity is required to include in the measurement of a group of insurance contracts all the future cash flows within the boundary of each contract in the group. Those future cash flows include premiums expected to be received and claims and expenses expected to be paid.

7. The measurement of a group of contracts can be disaggregated into two components: a liability for remaining coverage (which includes the fulfilment cash flows and the

contractual service margin related to future coverage) and a liability for incurred claims (which includes the fulfilment cash flows relating to claims for insured events that have occurred).

8. Paragraph 78 of IFRS 17 states:

> An entity shall present separately in the statement of financial position the carrying amount of groups of:
>
> (a) insurance contracts issued that are assets;
>
> (b) insurance contracts issued that are liabilities;
>
> (c) reinsurance contracts held that are assets; and
>
> (d) reinsurance contracts held that are liabilities.

9. Therefore, IFRS 17:

   (a) requires an entity to present the combination of rights and obligations arising from a group of insurance contracts as a single asset or liability for insurance contracts; and

   (b) prohibits the entity from offsetting groups of insurance contracts in an asset position with groups of insurance contracts in a liability position.

Premium allocation approach

10. The PAA in IFRS 17 simplifies the measurement of the liability for remaining coverage for contracts meeting specified criteria. IFRS 17 permits, but does not require, an entity to apply the PAA when that approach provides a reasonable approximation to the general model in IFRS 17.

11. Applying the PAA, an entity measures the liability for remaining coverage of a group of insurance contracts on initial recognition at the premiums received less any insurance acquisition cash flows paid. Subsequently, the liability for remaining coverage of a group of insurance contracts increases with premiums received and decreases to reflect an allocation of the total amount of the expected premiums receipts to profit or loss as insurance services are provided. Appendix A to this paper

include examples of the PAA mechanics with comparison to the accounting under existing practice.

12. The requirements for the presentation on the statement of financial position and the unit of account for contracts to which the PAA applies are the same as in the general model. Therefore, the PAA applies to a group of contracts and offsetting of groups of contracts to which the PAA applies is prohibited.

Board's rationale

13. A group of insurance contracts is the unit of account applying IFRS 17. Paragraph BC328 of the Basis for Conclusions on IFRS 17 explains:

> IFRS 17 requires an entity to present the combination of rights and obligations arising from a group of insurance contracts as a single insurance contract asset or liability in the statement of financial position. This requirement is consistent with the measurement of a group of insurance contracts as a package of cash inflows and cash outflows. Consistent with the requirement in IAS 1 [*Presentation of Financial Statements*] that an entity not offset assets and liabilities, IFRS 17 prohibits entities from offsetting groups of insurance contracts in an asset position with groups of insurance contracts in a liability position.

14. This requirement is also consistent with the *Conceptual Framework for Financial Reporting,* which states:

> The unit of account is the right or the group of rights, the obligation or the group of obligations, or the group of rights and obligations, to which recognition criteria and measurement concepts are applied.[1]
>
> Offsetting occurs when an entity recognises and measures both an asset and liability as separate units of account, but groups them into a single net amount in the statement of financial position. Offsetting classifies dissimilar items together and therefore is generally not appropriate.

[1] Paragraph 4.48 of the *Conceptual Framework for Financial Reporting.*

Offsetting assets and liabilities differs from treating a set of rights and obligations as a single unit of account.[2]

Premium allocation approach

15. The Board views the PAA as a simplification of the general model requirements. Accordingly, the level of aggregation requirements and the presentation in the statement of financial position requirements described in paragraphs 8–9 of this paper are equally applicable when applying the PAA.

Concerns and implementation challenges expressed since IFRS 17 was issued

16. Some stakeholders state that a significant implementation challenge arises because IFRS 17 requires entities to present groups of contracts that are in an asset position separately from groups of contracts in a liability position in the statement of financial position. This requirement results in the need for an entity to allocate premium cash flows and the liability for incurred claims to each group of insurance contracts to determine if that group of insurance contracts is in an asset or a liability position.

17. Those stakeholders observe that when applying many existing insurance accounting practices, insurance line items on the statement of financial position reflect a high level of aggregation (for example, at an entity level). However, separate line items are presented for different amounts arising from insurance contracts and those line items reflect a level of aggregation that is consistent with the way that entities manage their operations and systems. For example, entities typically manage separately and at a high level of aggregation the information about premiums receivable and claims payable, and, therefore entities maintain information about cash receipts and payments only at this aggregated level. Similarly, entities typically record the liability for incurred claims only at an aggregated level.

[2] Paragraphs 7.10–7.11 of the *Conceptual Framework for Financial Reporting*.

18. The following illustration shows the likely changes introduced by the IFRS 17 presentation requirements:

Today*	**IFRS 17**
Assets	**Assets**
Deferred acquisition costs Premiums receivable	Insurance contract assets (for groups that are assets)
Liabilities	**Liabilities**
Insurance contract liabilities Unearned premiums Claims payable	Insurance contract liabilities (for groups that are liabilities)

(*) Common presentation in the statement of financial position applying IFRS 4 *Insurance Contracts*

19. Some stakeholders are concerned that they will need to develop new systems to identify premiums received, claims incurred and other separately managed balances (such as insurance acquisition cash flows or collateral deposits related to reinsurance) for each group of contracts so that they can allocate these amounts to each group of contracts. Those stakeholders state that the need to identify such amounts at a group of contracts level represents a significant implementation challenge because:

   (a) existing systems do not typically link the system that registers premiums received and the system that generates the information necessary to measure the insurance contracts asset or liability. The latter processes information based on the assumption that premiums were received or are received when due.

   (b) existing systems typically manage and administer claims in separate, independent systems that are not linked to the system that generates the information necessary to determine the liability for remaining coverage.

20. Some stakeholders think the presentation requirements in IFRS 17 would result in significant additional costs related to new systems or significant changes to existing systems. For many types of insurance contracts they think that they could apply the

requirements of IFRS 17 other than the presentation requirements without the need to allocate premiums received and claims incurred to groups of contracts.

21. Developing new systems is likely to be complex and costly. Consequently, stakeholders question whether the usefulness of the information to the users of financial statements arising from applying the presentation requirements is sufficient to justify such costs.

22. Feedback so far indicates that users of financial statements may not regard the presentation of insurance contract assets and liabilities at a portfolio level, rather than a group level, as significantly diminishing the usefulness of information.

23. Some stakeholders think that IFRS 17 should be amended to require aggregation at a portfolio or entity level for presentation purposes. Some stakeholders told us that even though they would prefer a presentation on an entity level, a presentation at a portfolio level will significantly reduce their implementation costs.

24. Some stakeholders suggest that the challenge of identifying premiums received and incurred claims for groups of contracts is relevant for all insurance contracts. Other stakeholders suggest that this challenge is more relevant to contracts measured applying the PAA. Some stakeholders also think that the PAA results in a measurement that is based on a cash flow basis rather than accrual basis and therefore suggest amending the measurement requirements of the PAA.

Staff analysis and recommendation

Premiums

25. In both the general model and the PAA, insurance revenue is recognised as services are provided and the receipt of premium does not affect the timing of revenue recognition.

26. However, the measurement of the insurance contract asset or liability is affected by the receipt of premiums. This is because the insurance contract asset or liability reflects the financial position resulting from an entity’s rights and obligations at the reporting date. In the general model, when premiums are received those amounts are

no longer included in the fulfilment cash flows of a group of insurance contracts. This reflects that the premiums received are no longer future cash flows. In other words, the cash asset increases and the insurance liability increases. Consistently, applying the PAA, when premiums are received the cash asset increases and the insurance liability increases.

Incurred claims

27. The measurement of an insurance contract asset or liability can be disaggregated into two components: a liability for remaining coverage and a liability for incurred claims. In the statement of financial position:

    (a) the liability for incurred claims is a credit.

    (b) the liability for remaining coverage may be a debit or a credit as it is affected by the timing of cash flows received and paid for a group of insurance contracts. If, for example, an entity pays expenses sooner than it receives premiums, the liability for remaining coverage may be a debit.

28. Since the insurance contract asset or liability includes both a liability for remaining coverage and a liability for incurred claims, the measurement of the insurance contract balance as an overall asset (debit) or liability (credit) can only be determined if the liability for remaining coverage and the liability for incurred claims are identified for each group of contracts.

29. In addition, to determine the liability for incurred claims—similar to premium receipts—any payments relating to claims or expenses need to be allocated to each group of contracts.

30. However, applying IFRS 17, claims and expenses (including any subsequent change in the liability for incurred claims)[3] are recognised as insurance service expenses in the period they are incurred. Therefore the identification of the liability for incurred

[3] The effect of time value of money and the effect of financial risk are recognised as insurance finance income or expenses.

claims and the related payments with each group of contracts has no direct effect on the determination of the insurance service result.

Staff recommendations

31. The staff observe that stakeholders made two different suggestions to address the implementation challenges discussed in paragraphs 19−24 of this paper.

32. With respect to the suggestion to change the measurement requirements of the PAA, the staff observe that:

    (a) applying the PAA, consistently with the general model, insurance revenue is recognised as services are provided and the receipt of premiums does not affect the timing of revenue recognition. Therefore, the PAA does not result in revenue that is determined on a cash flow basis.

    (b) applying the PAA, consistently with the general model, when premiums are received the cash asset increases and the insurance liability increases. Therefore, the receipt of premiums does not have an effect on the net asset or liability position of the entity.

    (a) the Board view’s the PAA as a simplification of the requirements in the general model. To change the measurement requirements for the PAA would result in the PAA being a different measurement model.

33. With respect to the suggestion to amend the level of aggregation requirements for presentation purposes, the staff think that there is merit in providing a practical relief for entities by requiring entities to present insurance contracts at a higher level of aggregation than the group level.

34. The question then arises as to which level would be appropriate. The staff considered only presentation at a portfolio level or at an entity level, because these are levels of aggregation already specified in IFRS 17.

35. The staff observe that offsetting generally does not meet the objective of financial reporting as set out in the *Conceptual Framework*. Presenting items on a net basis might:

(a) obscure the existence of some transactions and change amounts often used as an indication of the size of an entity, for example, total assets; and

(b) detract from the ability of users of financial statements to understand the transactions and to assess an entity's future cash flows, except when offsetting reflects the substance of the transaction or other event.

36. The staff therefore note that any practical relief the Board provides would be contrary to the general requirements of the *Conceptual Framework*. Although it will be more costly to implement the requirements at a portfolio level when compared to an entity level, the staff think that any practical relief should limit the loss of information for users of financial statements.

37. On balance, the staff recommend that entities are required to offset groups at the portfolio level for presentation purposes. This means that an entity would present separately assets and liabilities for insurance contracts subject to similar risks that are managed together. The staff think that offsetting at an entity level risks a greater loss of useful information. The staff also note that in the 2010 Exposure Draft *Insurance Contracts* and 2013 Exposure Draft *Insurance Contracts*, the Board proposed presentation at a portfolio level when the unit of account was a single contract.

38. The staff consider the proposed amendment against the criteria set by the Board at its October 2018 meeting and observe that:

(a) although offsetting groups in the statement of financial position would result in a loss of useful information relative to that which would be provided by IFRS 17 for users of financial statements, preliminary discussions with users of financial statements suggest that the loss of information could be regarded as acceptable when balanced against the significant cost relief for preparers of financial statements; and

(b) amending IFRS 17 in this way would not unduly disrupt implementation processes that are already under way—the staff have been told that such an amendment might significantly reduce implementation costs and simplify implementation for many entities.

39. The staff note that, in some circumstances an entity would need to identify premiums received and the liability for incurred claims at the level of a group of contracts regardless of the presentation requirements. This is because such amounts may affect the measurement of a group of contracts and the amounts recognised in the statement(s) of financial performance. For example, when applying the other comprehensive income (OCI) option for disaggregating insurance finance income or expenses to specific types of contracts that are measured using the general model, the discount rate used for recognising insurance finance income or expenses in profit or loss is determined by reference to the discount rates determined at the date of initial recognition of a group of contracts. Therefore, identifying the liability for incurred claims with the relevant group is essential to determine the appropriate discount rate to measure the insurance finance income or expenses in profit or loss.

Question 1 for Board members

Do you agree that the Board should amend paragraph 78 of IFRS 17 as follows?

An entity shall present separately in the statement of financial position the carrying amount of ~~groups~~ portfolios of:

(a) insurance contracts issued that are assets;

(b) insurance contracts issued that are liabilities;

(c) reinsurance contracts held that are assets; and

(d) reinsurance contracts held that are liabilities.

Separate presentation and measurement of premiums receivable and claims payable

IFRS 17 requirements

40. IFRS 17 requires an entity to measure a group of insurance contracts on the basis of all the cash flows expected to arise from fulfilling the contracts in the group, including premiums receivable and claims payable.

Board's rationale

41. The fundamental principle in IFRS 17 is that an insurance contract should be measured using a current estimate of all expected cash flows within the contract boundary that will arise as the contract is fulfilled. Consistent with that measurement approach, the presentation in the statement of financial position reflects the combination of rights and obligations created by the contract as giving rise to a single insurance contract asset or liability.

Concerns and implementation challenges expressed since IFRS 17 was issued

42. Some stakeholders express concern that the rights and obligations of a group of insurance contracts is measured as a whole and presented as a single line item representing the insurance contract asset or liability in the statement of financial position.

43. As illustrated in paragraph 18 of this paper, many entities currently account for premiums receivable as financial assets and claims payable as a liability, separate from the rest of the insurance contract liability.

44. Some stakeholders think that the nature of premiums receivable and claims payable would be better reflected if entities were to measure and present them separately applying IFRS 9 *Financial Instruments*. The remaining insurance contract asset or liability would be measured applying IFRS 17 assuming amounts are received and paid when they are due to be received or due to be paid.

45. Those stakeholders suggest that measuring and presenting such amounts applying IFRS 9 would provide better information about the risks relating to those amounts, particularly their credit risk. They note that measuring and presenting such amounts applying IFRS 9 would also alleviate their implementation challenges.

Staff analysis and recommendation

46. The measurement of a group of insurance contracts applying IFRS 17:

(a) includes an estimate of the expected present value of the cash flows generated by the contracts. The expected present value is the probability-weighted mean of the present value of the possible cash flows, discounted using current estimates of discount rates. The measurement model in IFRS 17 therefore reflects the risk of non-payment of premiums by policyholders.

(b) reflects current estimates of the expected future cash flows relating to claims measured using the discount rates applied to future cash flows. Therefore, future cash flows related to the settlement of claims are also measured at a current value basis, compared to most types of financial liabilities measured applying IFRS 9 which are measured on a cost basis.

47. The staff think that measuring premiums receivable and claims payable separately from insurance contracts would result in internal inconsistencies in IFRS 17. The principle of IFRS 17 recognises that a contract, and by extension groups of contracts, create a single bundle of rights and obligations. Measuring premiums receivable and claims payable separately and differently from the corresponding obligations and rights is inconsistent with this principle.

48. The requirements for the measurement of groups of insurance contracts are a fundamental feature of IFRS 17. The staff do not think that the concerns raised by some stakeholders warrant a significant change to the measurement principle in IFRS 17. This principle has been subject to extensive discussions and has remained substantially unchanged since the initial proposals of the Board.

49. In developing the Standard, the Board considered whether to retain presentation approaches, commonly used in many existing accounting practices, that measure and present components of insurance contracts as separate line items. The Board concluded that measuring and presenting components of the net insurance contract asset or liability as separate assets and liabilities in the statement of financial position suggests that those assets and liabilities are different and are not related to each other. In particular, showing a component of the overall insurance contract asset or liability as a separate line item could be misleading if that asset were not measured as a standalone asset, but rather would be measured on an expected basis together with other insurance expected cash flows.

50. The staff think that amending IFRS 17 to require the separate presentation of premiums receivable and claims payable from the insurance contract asset or liability could:

    (a) reduce comparability between entities—the staff understand that systems currently used by entities recognise premiums receivable over different periods for different contracts. For example, one entity may only recognise premiums due in the current month that were not yet received, while another entity may reflect premiums due in the next 12 months in premiums receivable.

    (b) unduly disrupt implementation already under way and risk undue delays in the effective date of IFRS 17 if the Board were to develop a consistent definition of premiums receivable and claims payable.

51. The staff note that paragraph 55 of IAS 1 *Presentation of Financial Statements* permits the presentation of additional line items including by disaggregation of required line items, headings and subtotals in the statement of financial position when such presentation is relevant to an understanding of the entity's financial position. Applying that requirement, an entity may be able to present a disaggregation which shows the components of each of those line items (for example, to present the amounts of premiums receivable and claims payable included in the carrying amount of the insurance contract liability). The staff observe that requirement does not permit an entity to present premiums receivable or claims payable as separate line items, it only permits for the required line items to be disaggregated when such presentation is relevant to an understanding of the entity's financial position.

Question 2 for Board members
Do you agree that the Board should not amend the requirements of IFRS 17 to require separate presentation and measurement of premiums receivable and claims payable?

Appendix A—Extracts from Agenda paper 2C *Implementation challenges outreach report* of the May 2018 Board meeting

Level of aggregation

Applying the requirements of IFRS 17

A1. 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.

A2. 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.

A3. 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.

A4. Accordingly, the requirements in IFRS 17 would require entities to identify premiums received for a group of insurance contracts.

A5. In contrast, the revenue recognised in each reporting period is not based on actual receipts of premium at each reporting period (see examples in Appendix A 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.

A6. 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 A8 of this appendix) would need to be disaggregated into groups of insurance contracts that are assets and groups of insurance contracts that are liabilities.

A7. 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

A8. 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.

A9. 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 A to this paper.

A10. 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.

A11. 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.

A12. 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 instead of IFRS 17.

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

A13. 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.

A14. 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).

A15. 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.

A16. 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.

A17. 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.

A18. 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.

A19. 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

A20. 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.

A21. 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.

A22. 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.

A23. 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

A24. 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 the examples in Appendix A 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 examples below).

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

Fact pattern[4]

A25. 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.

A26. 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.

A27. 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.

[4] 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 B126[5]		**300**	**300**	**300**	**300**
Closing balance of insurance contract asset / (liability)	**(1020)**	**(765)**	**(510)**	**(255)**	**0**

IFRS 17 PAA—journal entries

<u>At initial recognition - 01.07.X1</u>

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

<u>At each reporting date (30.09.X1, 31.12.X1, 31.03.X1 and 30.06.X1)</u>

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

[5] 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 B126[2]		**300**	**300**	**300**	**300**
Closing balance of insurance contract asset / (liability)	**180**	**435**	**690**	**945**	**0**

IFRS 17 PAA—journal entries

<u>At initial recognition - 01.07.X1</u>

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

<u>At each reporting date (30.09.X1, 31.12.X1, 31.03.X1 and 30.06.X1)</u>

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

<u>At the end of the coverage period (30.06.X1)</u>

Receipt of premium[6]	Dr	Cash	1200
	Cr	Insurance contract asset	1200

[6] 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 B126[2]		**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