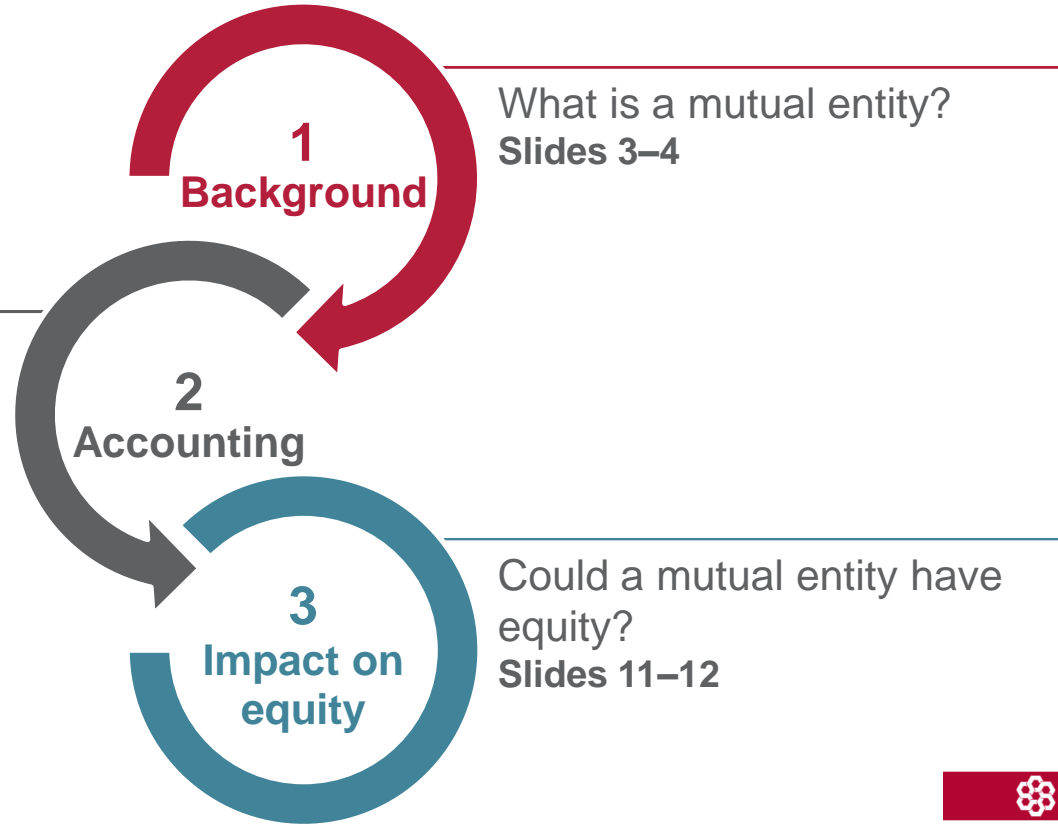


Insurance contracts issued by mutual entities

IFRS 17 *Insurance Contracts*
July 2018

This educational material describes the outcome of applying IFRS 17 to entities for which the most residual interest of the entity is due to a policyholder (referred to in this educational material as mutual entities). When developing the June 2020 amendments to IFRS 17, the International Accounting Standards Board noted that some entities described in practice as mutual entities do not have the feature that the most residual interest of the entity is due to a policyholder.

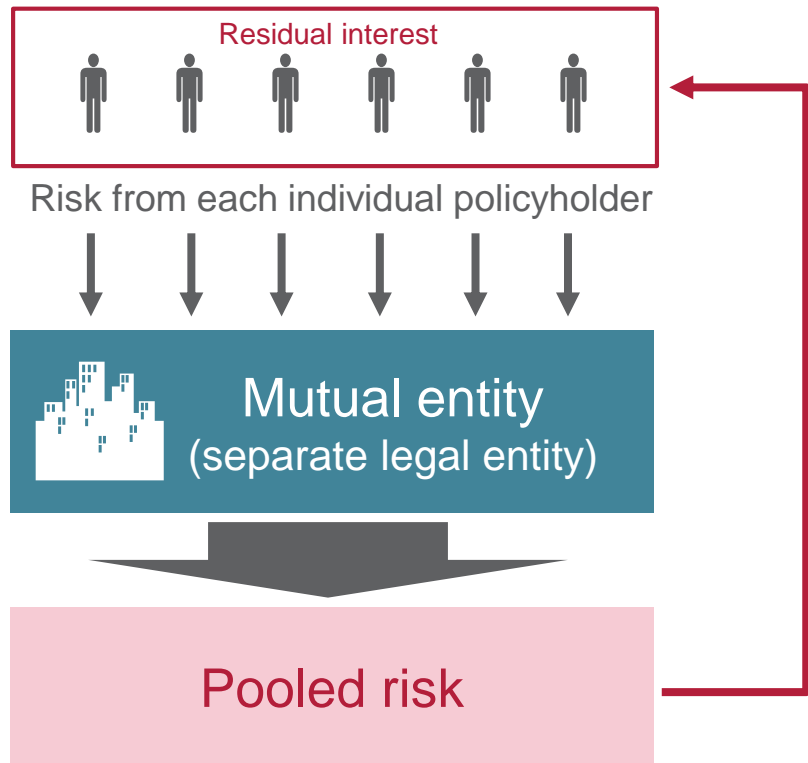


Contracts issued by a mutual entity:

- Contracts that do not provide policyholders with a residual interest in the mutual entity (conventional insurance contracts)
- Contracts that provide policyholders with a residual interest in the mutual entity

Slides 5–10

① Background

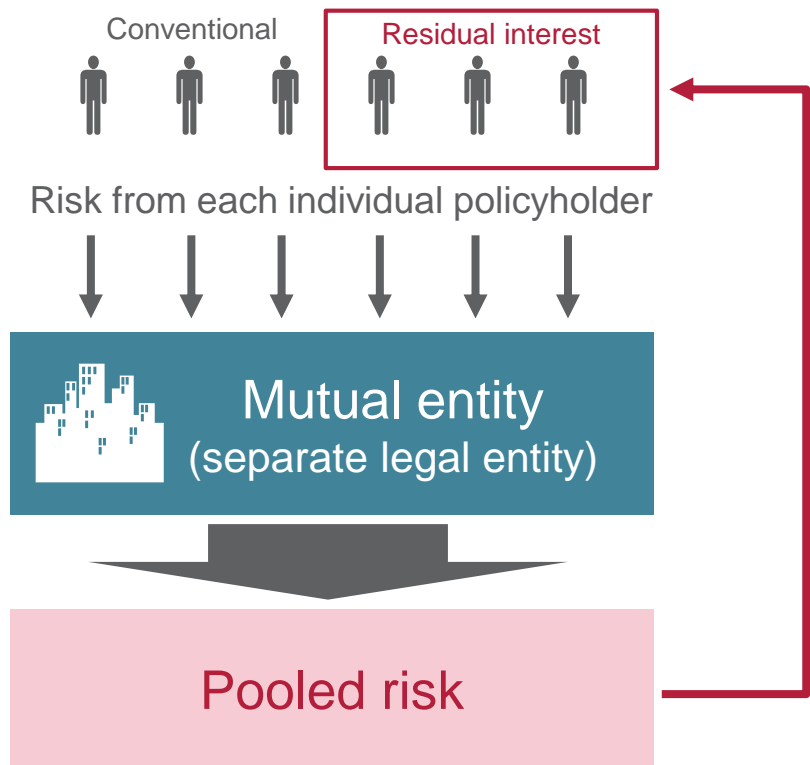


A mutual entity accepts risks from each policyholder and pools that risk

Policyholders hold the residual interest in a mutual entity (in comparison to companies which are owned by shareholders)

The policyholders with a residual interest in the mutual entity bear the pooled risk collectively in their capacity as owners

① Background



Mutual entities may also issue conventional insurance contracts (contracts that do not provide the policyholder with a residual interest in the mutual entity)

Determining whether a contract provides the policyholder with a residual interest in the mutual entity requires consideration of all substantive rights and obligations

Paragraph 2 of IFRS 17:
‘An entity shall consider its substantive rights and obligations, whether they arise from a contract, law or regulation’

② Accounting

Contracts issued by a mutual entity

5



IFRS 17 applies to **insurance contracts** within its scope, regardless of the legal form of the issuing entity

IFRS 17 applies to both:

Conventional insurance contracts issued by a mutual entity
(see slide 7)

and

Insurance contracts that provide the policyholder with a residual interest in the mutual
(see slides 8–10)

Contracts that affect cash flows to other policyholders

Some insurance contracts affect or are affected by the cash flows to policyholders of other insurance contracts (see slide 6). This is the case for insurance contracts that provide the policyholder with a residual interest in a mutual entity. It may also be the case for some conventional insurance contracts issued by any entity, including a mutual entity.

The fulfilment cash flows of a group of contracts reflect the extent to which the contracts in the group cause the entity to be affected by expected cash flows, whether to policyholders in that group or policyholders in another group (including both current and future policyholders).

② Accounting

Contracts that affect cash flows to other policyholders

6

Some insurance contracts affect or are affected by the cash flows to policyholders of other contracts by requiring:

A the policyholder to share with policyholders of other contracts the returns on the same specified pool of underlying items

+

B Either:

- i. the policyholder to bear a reduction in their share of the returns on the underlying items because of payments to policyholders of other contracts that share in that pool, including payments arising under guarantees made to policyholders of those other contracts or
- ii. policyholders of other contracts to bear a reduction in their share of returns on the underlying items because of payments to the policyholder, including payments arising from guarantees made to the policyholder

② Accounting

Conventional insurance contracts issued by a mutual entity

7

Mutual entities may issue conventional insurance contracts that do not provide policyholders with a residual interest in the mutual entity, for example non-participating insurance contracts

The requirements of IFRS 17 apply to these contracts regardless of the fact that they:

- have been issued by a mutual entity; and
- are underlying items for other contracts

Consequently, groups of such contracts are expected to have a CSM

Accounting for other assets and liabilities of a mutual entity

All other relevant IFRS Standards apply to other assets and liabilities of a mutual entity
Some IFRS Standards provide a fair value measurement option for assets and liabilities held by a mutual entity

② Accounting

Policyholders with a residual interest – cash flows

Payments to policyholders with a residual interest in a mutual entity vary depending on the returns on underlying items – the net assets of the mutual entity

Paragraph B65(c) of IFRS 17:

‘Cash flows within the boundary of an insurance contract include payments to a policyholder that vary depending on returns on underlying items’

Paragraph BC265 of the Basis for Conclusions on IFRS 17:

‘payments to policyholders form part of the fulfilment cash flows regardless of whether those payments are expected to be made to current or future policyholders.’

Payments to
policyholders

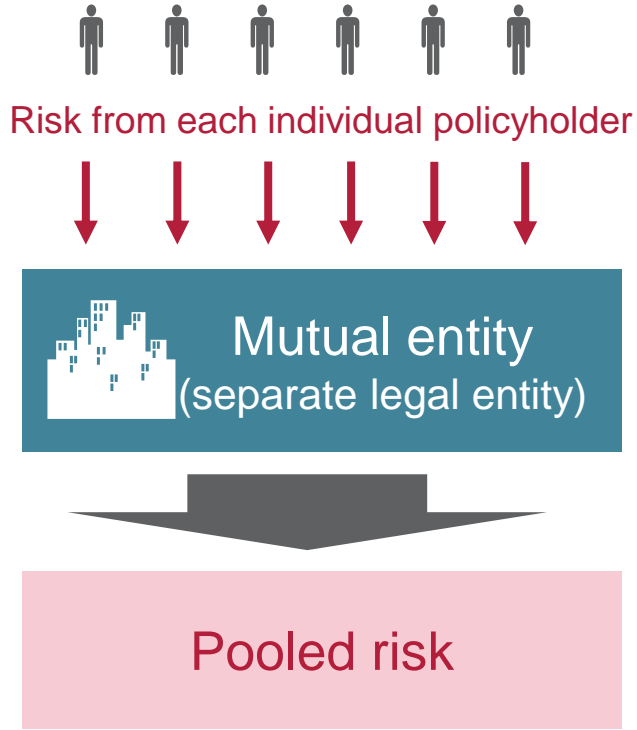
Current

Future

② Accounting

Policyholders with a residual interest – risk adjustment

9



Risk adjustment for non-financial risk in IFRS 17:
‘The compensation an entity requires for bearing the uncertainty about the amount and timing of the cash flows that arises from non-financial risk’

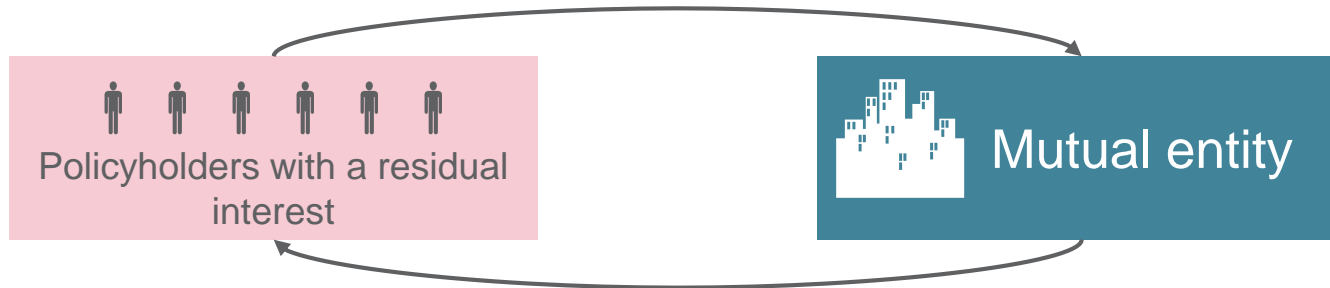
Although the policyholders with a residual interest as a whole bear the pooled risk collectively, the mutual, as a separate entity, has accepted risk from each individual policyholder

The risk adjustment for contracts with policyholders that have a residual interest in a mutual entity reflects the compensation the mutual entity requires for bearing the uncertainty from the non-financial risk in those contracts

② Accounting

② Policyholders with a residual interest - CSM

The net cash flows of the mutual entity are eventually returned to policyholders with a residual interest (either current or future policyholders)



Applying the IFRS 17 requirements to contracts with policyholders with a residual interest in the mutual entity will result in **no contractual service margin (CSM)** for those contracts

③ Impact on equity

Applying IFRS 17, for a mutual entity, the fulfilment cash flows include the rights of policyholders with a residual interest to the whole of any surplus of assets over liabilities. This means that, in principle, there should normally be no equity remaining

However, the fulfilment cash flows are measured at current value whereas some other assets and liabilities are not required or permitted to be measured at fair value in accordance with IFRS Standards

This accounting mismatch **may result in reported equity for financial reporting purposes** even if the mutual entity has no equity for regulatory purposes. The reported equity is likely to be negative (in a debit position)

Conceptual Framework:
‘Equity is the residual interest in the assets of the entity after deducting all its liabilities’

Examples in which fair value is not required and / or permitted by IFRS Standards:

- amortised cost financial assets;
- deferred tax balances
- goodwill in subsidiaries

③ Impact on equity

To provide useful information about its financial position and financial performance, an insurer that is a mutual entity can distinguish:

Statement of financial position

Liability attributable to policyholders in their capacity as policyholders

Liability attributable to policyholders with the most residual interest in the entity

Statement(s) of financial performance

Income or expenses attributable to policyholders in their capacity as policyholders before determination of the amounts attributable to policyholders with most residual interest in the entity

Further information

- Paragraphs 2, B16 and B67–B71 of IFRS 17
- Paragraphs BC264–BC269 of the Basis for Conclusions on IFRS 17

Contact us

Keep up to date



@IFRSFoundation



IFRS Foundation



www.ifrs.org



IFRS Foundation

Comment on our work



go.ifrs.org/comment