IFRS Accounting Standards discussion fora:
IFRS 17 *Insurance contracts*

2023

Addis Ababa, Ethiopia

WORLD BANK GROUP

AABE

Accounting and Audit Board of Ethiopia

የኢትዮጵያ የሂሳብ አያያዝ እና ኦዲት ቦርድ

Established under proclamation no 847/2006

The consensus views expressed in this presentation are those of the discussion participants and not necessarily those of any organization with which they are associated.

1

Disclaimer

» The sponsors, the authors, the discussants and the publishers do not accept responsibility for loss caused to any person who acts or refrains from acting in reliance on the material in this document, whether such loss is caused by negligence or otherwise.

» When evaluating accounting treatments all the relevant facts and circumstances need to be fully considered. A discussion forum, because of its format and for reasons of simplification, can only consider a particular, constrained set of facts. The consensus views arrived at in this material are based on the assumption that there are no other relevant facts that, if they had been considered, might have altered that view. Consequently, such consensus views can only be considered likely conclusions, and cannot be considered to be determinative, without full consideration of all the facts and circumstances that would be present in reality.

2

Aims

» Develop a more cohesive understanding of IFRS accounting and reporting for insurance contracts in Ethiopia

» Enhance capacity in Ethiopia to apply IFRS 17 *Insurance Contracts* more consistently

Applicable version of IFRS Accounting Standards

Unless specified otherwise, the accounting requirements that are the subject matter of this discussion forum are IFRS Accounting Standards as issued by the International Accounting Standards Board that are applicable for annual period beginning on or after 1 January 2023 without early applying new and amended IFRS Accounting Standards that have a later mandatory application date.

Index of issues
IFRS 17 Insurance contracts

- Issue 1: Investment contracts with DPF
- Issue 2: Annual cohorts
- Issue 3: Risk free interest rate
- Issue 4: Acquisition cash flows
- Issue 5: Insurers and IFRS

5

Issue 1: Investment contracts with discretionary participation features (DPF)

Investment contracts with DPF
What do you think?

IFRS 17 has a core measurement model for insurance contracts (building block method). That model is modified for specified contracts including for Investment contracts with discretionary participation features.

What is an investment contract with DPF? How does it differ from a conventional investment contract? How does the accounting differ?

Investment contracts with DPF
Summary of discussion

» **What is an investment contract with DPF?**

Discussants' consensus view:

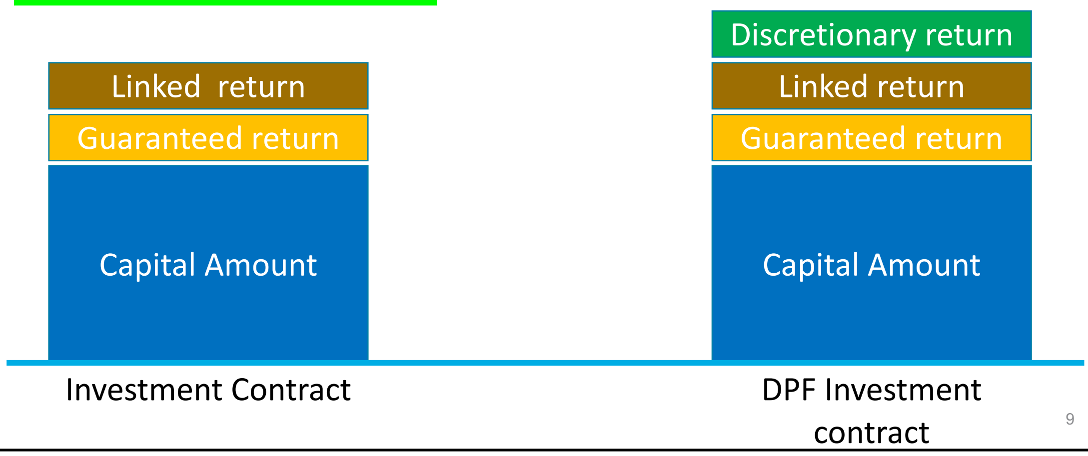
A contract that provides right to receive:

- amounts expected to be a significant portion of total benefits;
- timing/amount contractually at discretion of issuer; and
- contractually based on:
  - returns on a specified pool of contracts;
  - realised/unrealised returns on specified pool of assets; or
  - profit or loss of the entity or fund that issues the contract.

Investment contracts with DPF
Summary of discussion

» **How does it differ from a conventional investment contract?**

Discussants' consensus view:



Investment contracts with DPF
Summary of discussion

» **How does the accounting differ?**

Discussants' consensus view:

- In short, for contracts where the assets are carried on balance sheet:
  - A conventional investment contract:
    - Contract liability is measured applying IFRS 9 *Financial Instruments*
    - Measurement is based on the contractually obligatory payments
  - An Investment DPF
    - Contract liability is measured applying IFRS 17 *Insurance Contracts*
    - Measurement is based on the expected future cash flows

Issue 2: Level of aggregation – annual cohorts

Level of aggregation – annual cohorts
What do you think?

IFRS 17 requires an insurer group contracts based on portfolio, profitability and cohort (annual). Some written contracts have a duration of longer then 12 months.

How are contracts with a duration of more than one year grouped applying the cohort requirement?

Split operations
Summary of discussion

How are contracts with a duration of more than one year grouped applying the cohort requirement?

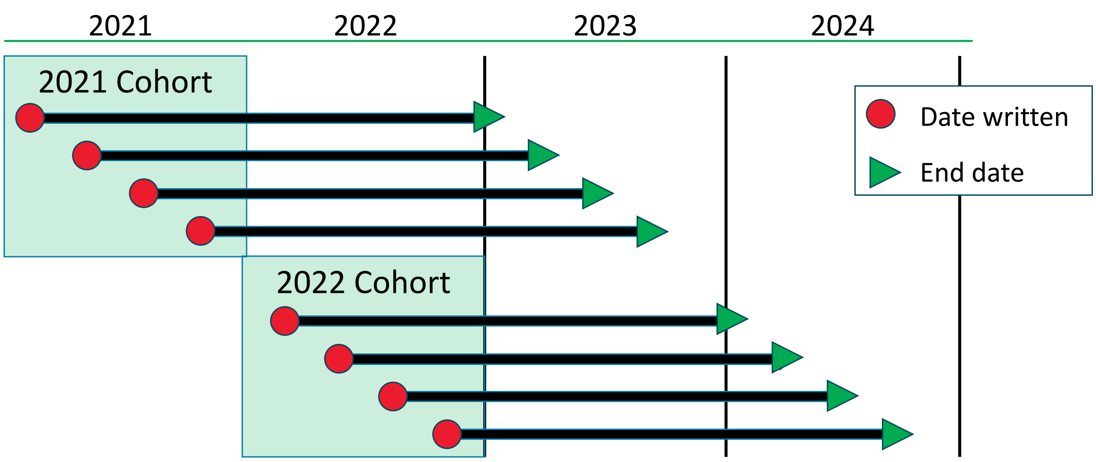
Discussants' consensus view

- The cohort requirement in IFRS 17:
  - Permits inclusion of contracts issued with 12 months of each other in a group, and
  - Forbids contracts issued more then 12 months apart from being included in a group.
- The basis for the test is the date of issue of the contract, not the year the contract is in-force.

13

13

Annual cohorts for contracts longer then 1 year



14

14

Issue 3: Risk free interest rate

15

Risk free interest rate
What do you think?

IFRS 17 requires discounting of future cash flows. The standard permits an insurer to use either a bottom-up (risk free rate), or a top-down market rate.[1] Risk free interest rates in some emerging economies are subject to distortion.

If an insurer elects the bottom-up approach, and the government interest rate is subject supply and demand distortions, must the insurer still use the observed rate?

[1] IFRS 17.B80 and B81

Risk free interest rate
Summary of discussion

If an insurer elects the bottom-up approach, and the government interest rate is distorted, must the insurer still use the observed rate?

Discussants' consensus view

» In Ethiopia, the main observable interest rate is the government rate

» Government own currency rate is assumed to be a risk-free rate

» However, this rate may be subject to supply demand distortions

» IFRS 17 requires using an observable rate as a starting point, but also requires that that rate be adjusted to reflect the characteristics of the insurance contract cash flows

» In the case, it would require adjustment for the effect of the distortions

Issue 4: Acquisition cash flows

Acquisition cash flows
What do you think?

IFRS 17 defines acquisition cash flows as cash flows arising from the costs of selling, underwriting and starting a group of insurance contracts (issued or expected to be issued).

What are some examples of acquisition cash flows?

Acquisition cash flows
Summary of discussion

What are some examples of acquisition cash flows?

Discussants' consensus view

- Acquisition cash flows include:
  - Commission paid to agents
  - Internal costs of insurers’ own sales team
  - Pre-contract vehicle inspection costs
  - Pre-contract medical checks
  - Pre contract inspection by insurers own staff

Issue 5: Onerous contracts

Onerous contracts
What do you think?

Onerous contract groups are accounted separately under IFRS 17. The expected loss is accounted for in profit or loss as soon as it is identified.

How do you account for a previously onerous contract group that is reassessed and is now expected to be profitable?

Onerous contracts
Summary of discussion

» **How do you account for a previously onerous contract group that is reassessed and is now expected to be profitable?**

Discussants' consensus view:

	Core model	Simplified model
1	Identify the remaining unrealised loss in liability before the change	
2	Reverse the remaining loss through the income statement: Dr Insurance Liability, Cr Profit and loss	
3	Any remaining profit is taken to CSM Dr Insurance Liability, Cr CSM	Any additional profit is ignored
4	Continue normal core accounting	Continue normal PAA accounting

Issue 6: Insurers and IFRS

Insurers and IFRS
What do you think?

IFRS 17 is applicable to insurance contracts as defined in the standard.

Do insurers have to apply any other IFRS standards?

Awareness of changes in IFRS
Summary of discussion

Do insurers have to apply any other IFRS standards?

Discussants' consensus view

» IFRS 17 is a standard for insurance contracts

» Insurers are the most regular issuers of insurance contracts, but other companies that issue insurance contracts must also apply IFRS 17

» IFRS is applied only to the insurance contracts of issuers, other IFRSs are applied to the other activities of the issuers of insurance contracts

» See examples on next slide

Examples of applicable standards

IFRS 9
Financial instruments

IFRS 13
Fair value

IFRS 16
Leases

IAS 16
PPE

IFRS 17
Insurance contracts

IFRS 7
FI Disclosures

IAS 38
Intangibles

IAS 12
Taxation

IFRS 15
Revenue not from Insurance