

IFRS 17

Insurance Contracts

March 2023
Addis Ababa



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IFRS 17 Programme	
Session 1 & 2	Introduction to IFRS 17 and Important concepts
Session 3 & 4	Measurement of contracts (general approach)
Session 5 & 6	Measurement of contracts (premium allocation approach)
Session 7	Reinsurance
Session 8	Transition

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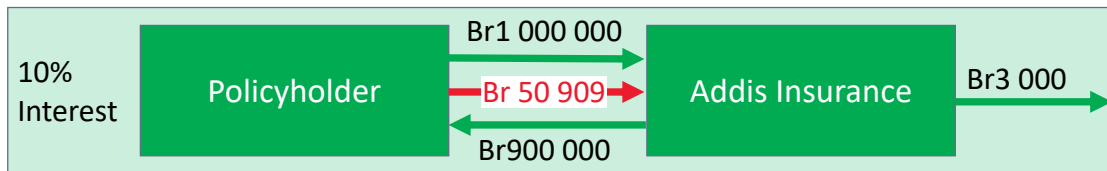
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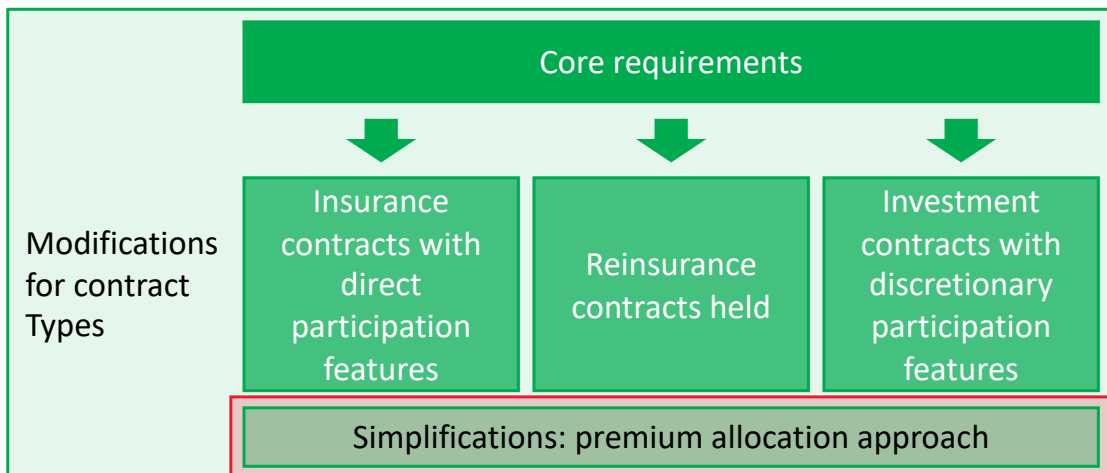
Example Recap and amend

- » Addis Insurance writes 100 car contracts and expects that:
 - » Interest rate is 10%
 - » Addis pays Br3 000 in car inspection costs on 1 January
 - » Policyholders pay an annual premium of Br10 000 each on 2 January
 - » Risk premium is Br50 909
 - » **Addis expects claims of Br900 000, Br 50 000 per month for 1st 6 months, Br100 000 per month for 2nd 6 months**



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Core Requirements Snapshot of IFRS 17 Approaches



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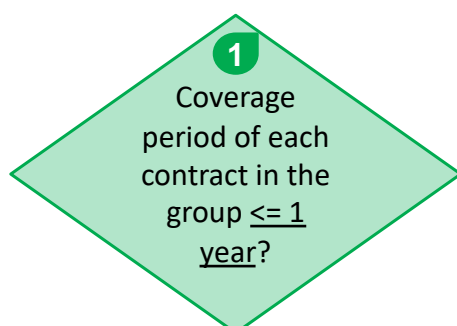
Introduction

- » Optional simplified approach for eligible contracts
 - » Similar outcome to core model but in a simplified, less costly way
- » Decision made at inception of the group based on assessment at that date
- » The decision is:
 - » made on a group by group basis, and
 - » is irrevocable

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Premium allocation approach Criteria



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Example Contract Boundary

» Addis Insurer issues four types of car insurance contracts:

	A contract that....	Automatically eligible (Y/N)
1	Can be cancelled by either party with 30 days notice, expected to continue for 2 years	
2	Signed for 1 year, automatic renewal, annual inflation increase, only policyholder can cancel	
3	Signed for 1 year, automatic renewal, annual increase decided by Addis, only policyholder can cancel	
4	Signed for one year, no automatic renewal	

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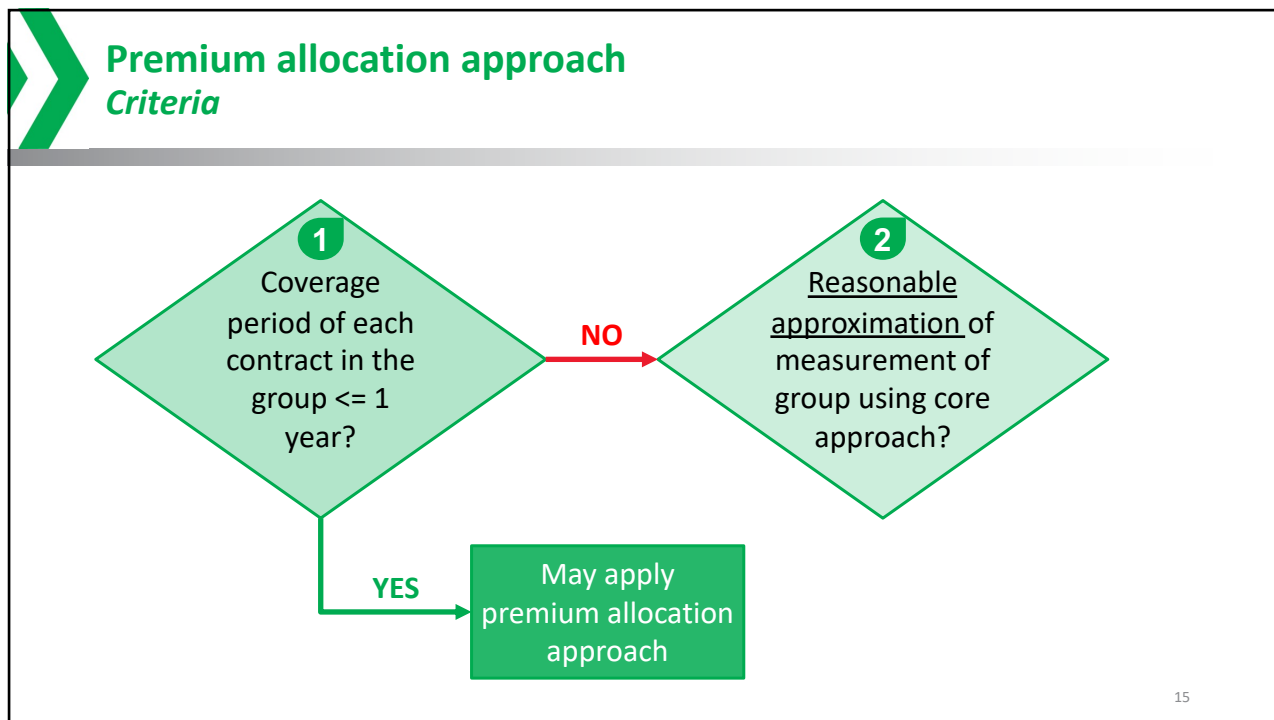
Example Contract Boundary

» Addis Insurer issues four types of car insurance contracts:

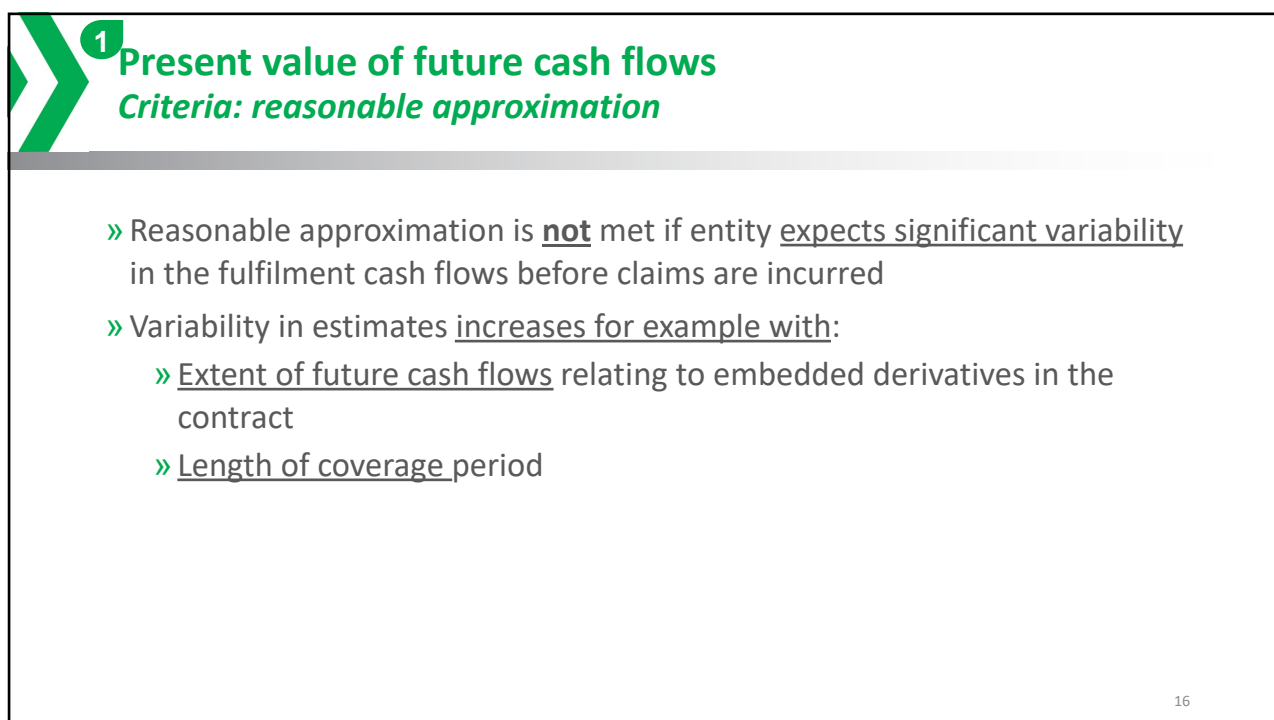
	A contract that....	Automatically eligible (Y/N)
1	Can be cancelled by either party with 30 days notice, expected to continue for 2 years	Yes
2	Signed for 1 year, automatic renewal, annual inflation increase, only policyholder can cancel	No
3	Signed for 1 year, automatic renewal, annual increase decided by Addis, only policyholder can cancel	Yes
4	Signed for one year, no automatic renewal	Yes

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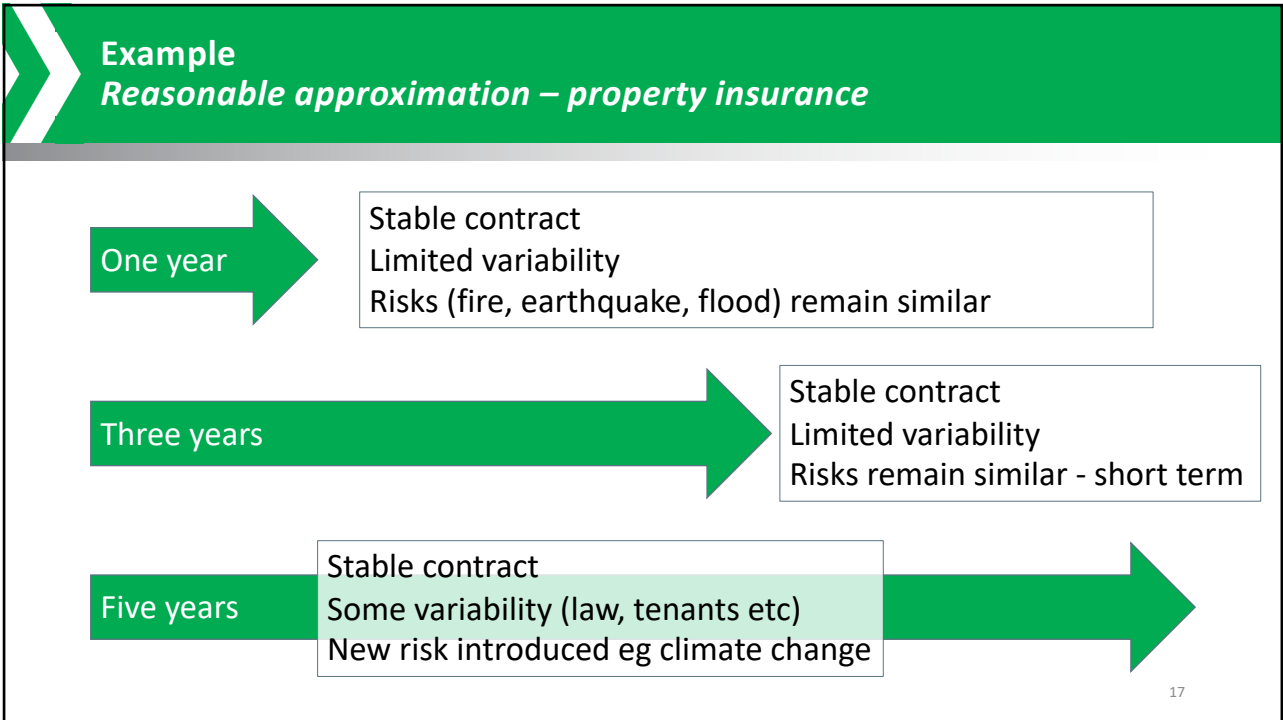
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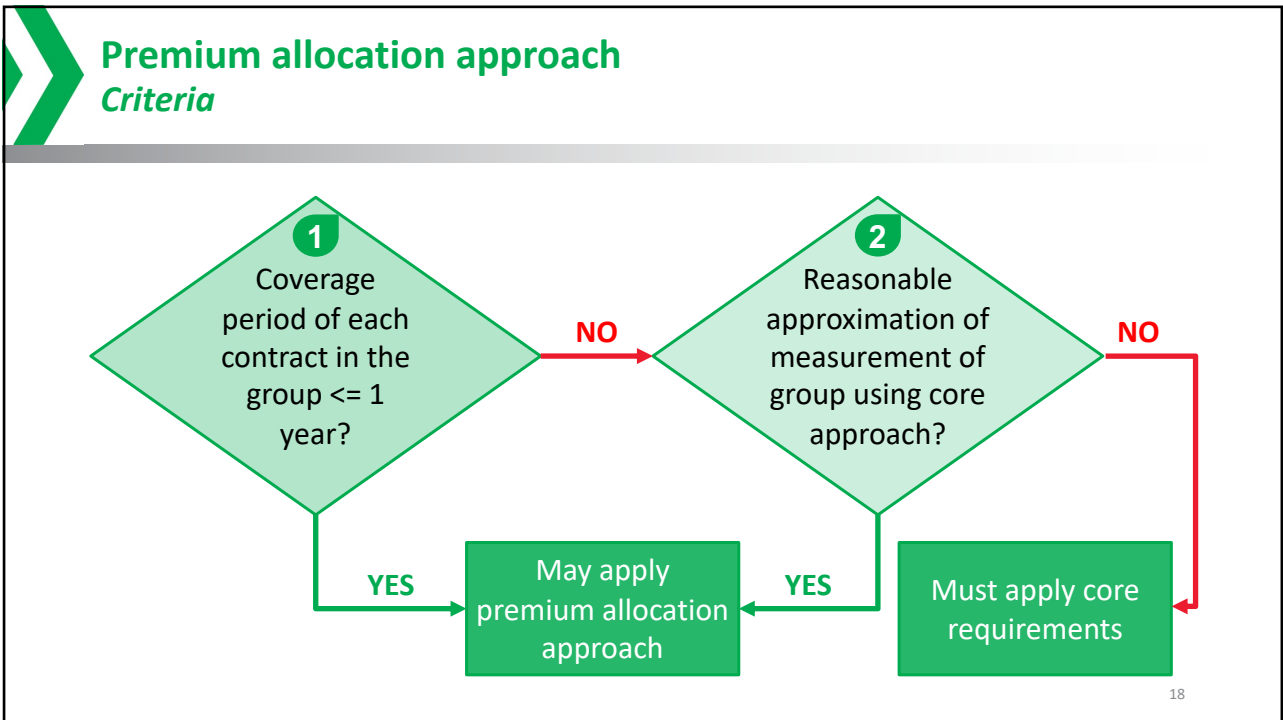
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Level of aggregation

- » For contracts applying premium allocation approach
 - » assume no contracts are onerous unless facts and circumstances indicate otherwise
 - » assess whether contracts not onerous have no significant possibility of becoming onerous subsequently by assessing likelihood of changes in applicable facts and circumstances

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How are contracts grouped? Step

The diagram illustrates the following steps:

- Step 1:** A box labeled "Portfolio 1" contains 6 contract icons.
- Step 2:** The portfolio is divided into three categories:
 - Onerous*:** 1 contract icon.
 - Remaining contracts in the portfolio*:** 2 contract icons.
 - No significant possibility of becoming onerous*:** 3 contract icons.
 A red vertical box labeled "Simplified" is positioned to the right of these categories.
- Step 3:** The contracts are grouped into "Issuance period (annual cohorts)".
 - The 1 onerous contract forms its own cohort.
 - The 2 remaining contracts form a cohort.
 - The 3 contracts with no significant possibility of becoming onerous form a cohort.

* At initial recognition, if any 20

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Core Requirements

Reminder: 'Building block Approach'

All insurance contracts measured as the sum of:

- » Fulfilment cash flows (FCF)
 1. Present value of probability-weighted expected cash flows
 2. Plus an explicit risk adjustment for non-financial risk (eg insurance risk)
- » Contractual service margin (CSM)
 3. The unearned profit from the contracts

The diagram illustrates the calculation of IFRS 17 liability. It shows three components in boxes: 1. PV future cash flows, 2. Risk adjustment, and 3. Unearned profit. Brackets group the first two as 'Fulfilment cash flows' and the last one as 'CSM'. These are summed to equal 'IFRS 17 liability'.

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Core requirements

Reminder

The diagram shows the breakdown of IFRS 17 liability. It is composed of two main parts: A. Core Liability for remaining coverage, which includes PV future cash flows, Risk adjustment, and Unearned profit; and B. Core Liability for Incurred claims, which includes PV future cash flows and Risk adjustment. These two parts are summed to equal 'IFRS 17 liability'.

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Premium Allocation Approach *Simplifications*

A

Core Liability for remaining coverage

PV future cash flows

+

Risk adjustment

+

Unearned profit

Simplifications

Optional practical expedients

- » No split required
- » Limited use of future estimates
- » optional practical expedients

- » If coverage less than 1 year, then:
 - » not required to accrete interest
 - » recognise acq cash flows as expense

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Premium allocation approach *Simplifications - initial measurement*

Premiums
(if any)
received at
initial
recognition

CF

Cash premium
received at initial
recognition
creates/increases
liability

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Example One year contract

» Receives premium of Br1 million (2 Jan 2022),

	Debit	Credit
Cash	1 000 000	
Insurance liability		1 000 000

» What is the journal entry?

- 1) Dr cash received, cr Insurance Liability, *same as for core approach*
- 2) Dr cash received, cr Premium receivable, *reverses accrual for premium*
- 3) Dr cash received, dr Premium liability *liability for unperformed service*

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Example One year contract

» Expects premium of Br1 million (2 Jan 2022), and **claims of Br900 000, Br 50 000 per month for 1st 6 months, Br100 000 per month for 2nd 6 months**

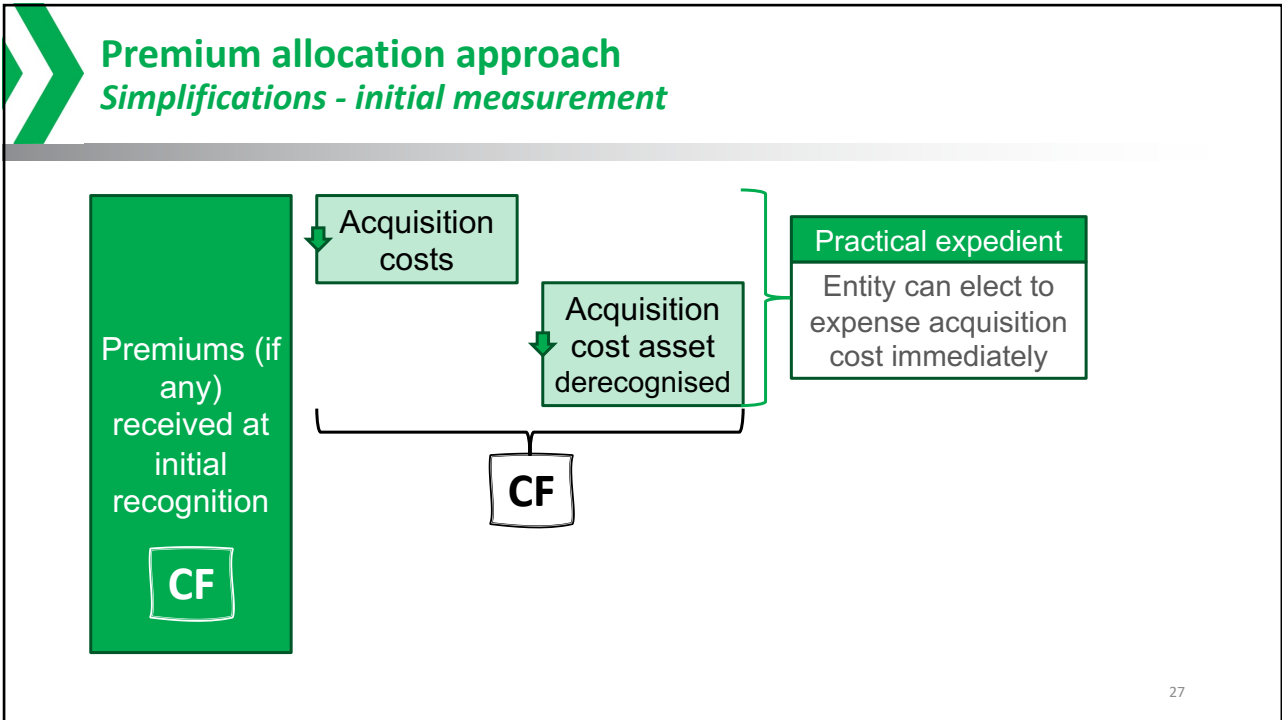
No journal required until cash flows happen

» What is the journal for the expected claims?

- 1) Dr Insurance liability, Cr Cash
- 2) Dr Insurance claims expense, Cr Insurance liability
- 3) No journal

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Example One year contract

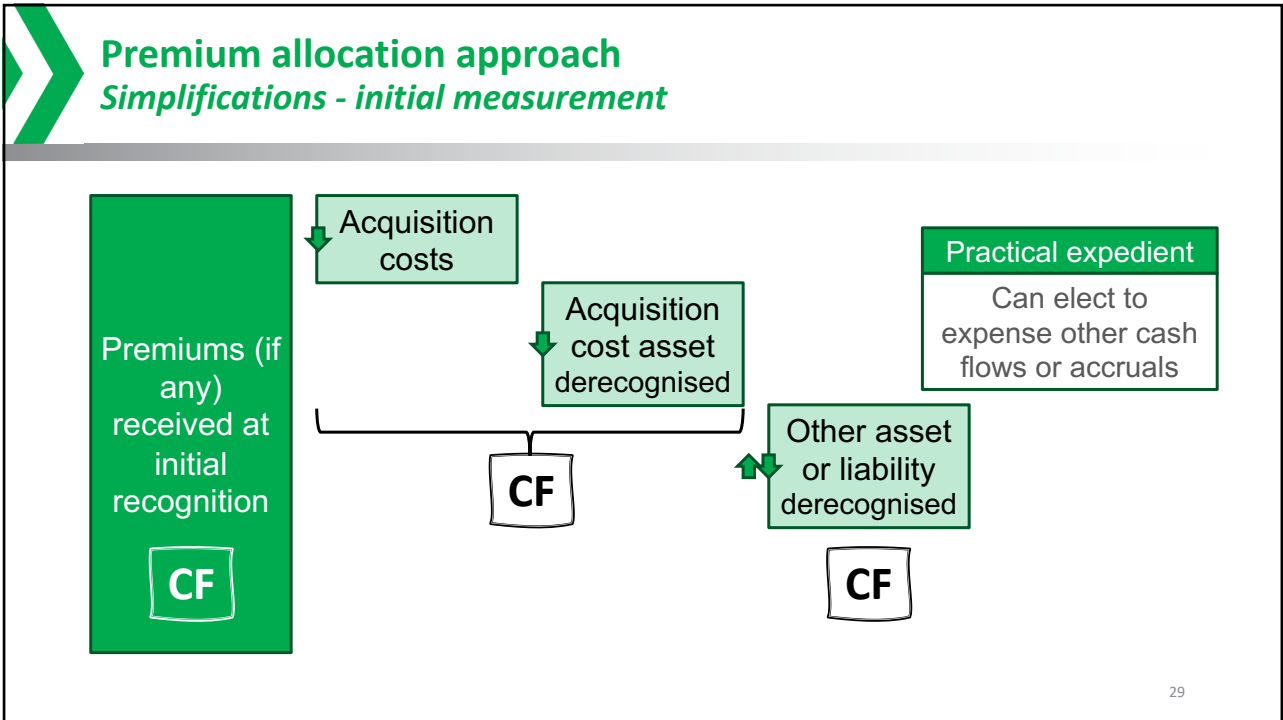
» Expects premium of Br1 million (2 Jan 2022), and claims of Br900 000, **pays Br3 000 in car inspection costs on 1 January**

	Debit	Credit
Acquisition cost expense (1 January)	3 000	
Cash		3 000

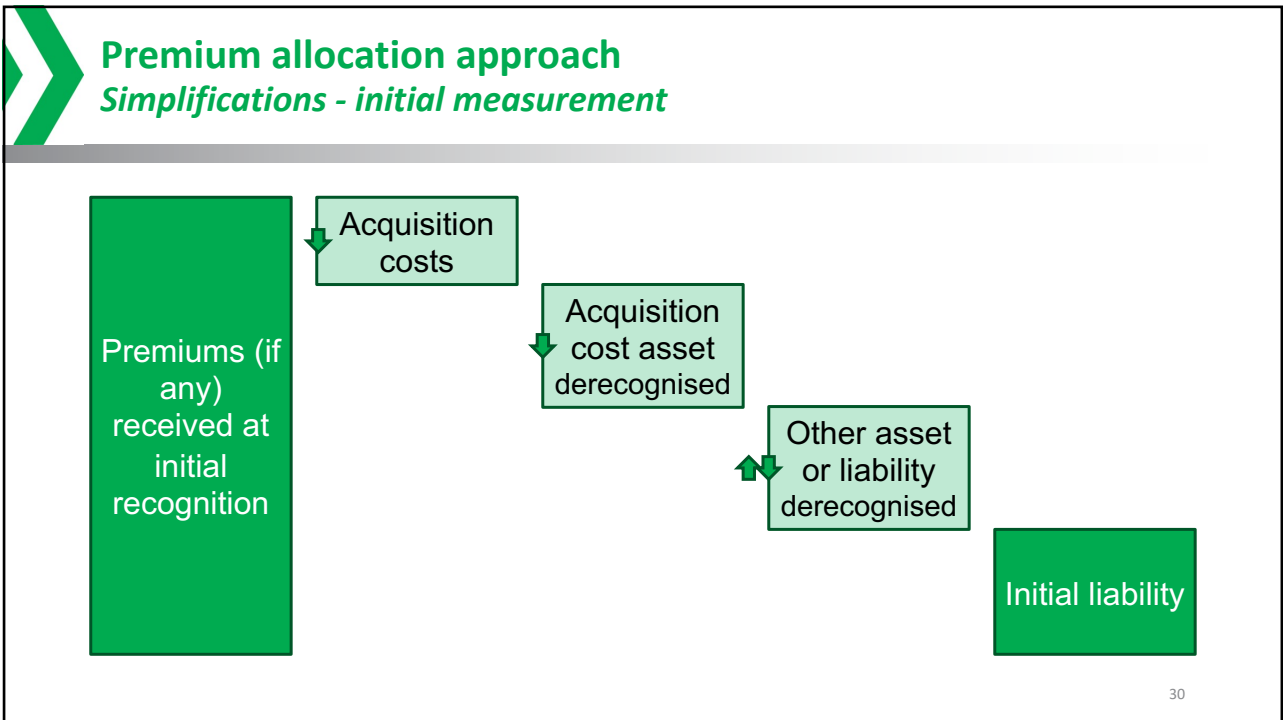
OR

Acquisition cost asset (1 January)	3 000	
Cash		3 000
Insurance contract liability (2 January)	3 000	
Acquisition cost asset		3 000

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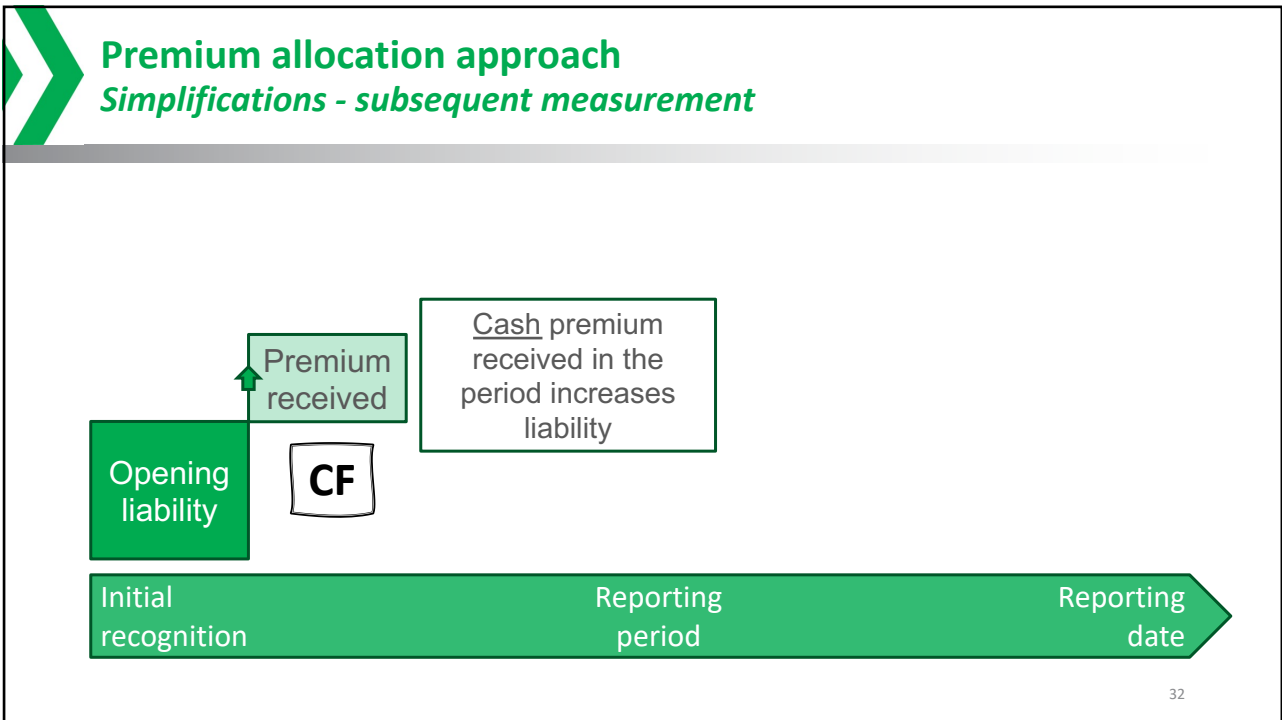
Example Balance sheet at 2 January 2022

Dr/(cr)	Cash	Acq asset	Insure liab.
Acquisition cost paid	-3 000	3 000	
Premium received	1 000 000		-1 000 000
Acquisition cost subsumed		-3 000	3 000
2 January Total	997 000	0	-997 000

Total under building block method	997 000	0	-997 000
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Example 6 months to June on one year contract

» Receives premium of Br1 million (2 Jan 2022),

Annual premium contract, no further premiums received

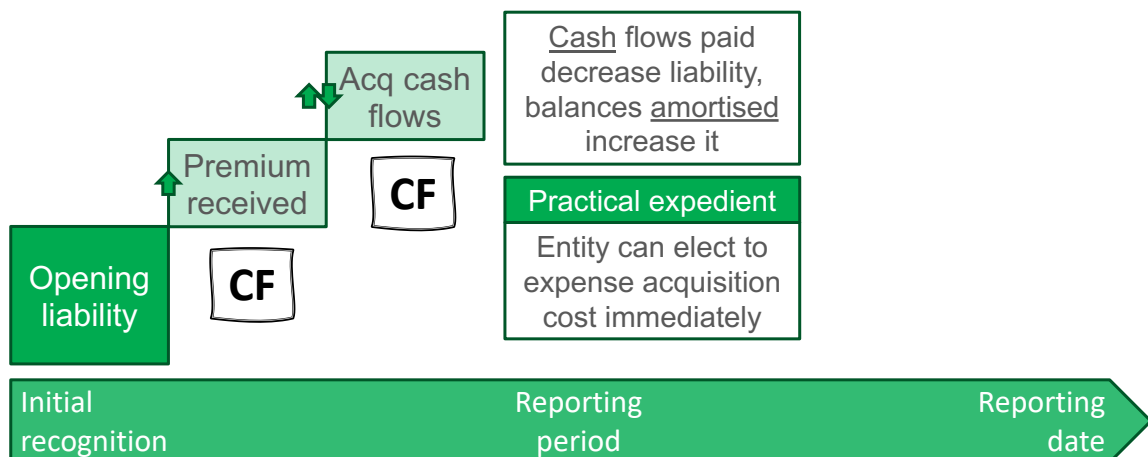
» What is the journal entry?

- 1) Dr cash received, cr Insurance Liability, *same as for core approach*
- 2) Dr cash received, cr Premium receivable, *reverses accrual for premium*
- 3) Dr cash received, dr Premium liability *liability for unperformed*
- 4) *No Journal*

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Premium allocation approach Simplifications - subsequent measurement



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Example 6 months to June on one year contract

» Expects premium of Br1 million (2 Jan 2022), and claims of Br900 000, allocation of acquisition cost of **Br3 000**

	Debit	Credit
Acquisition cost expense	1 000	
Insurance liability		1 000

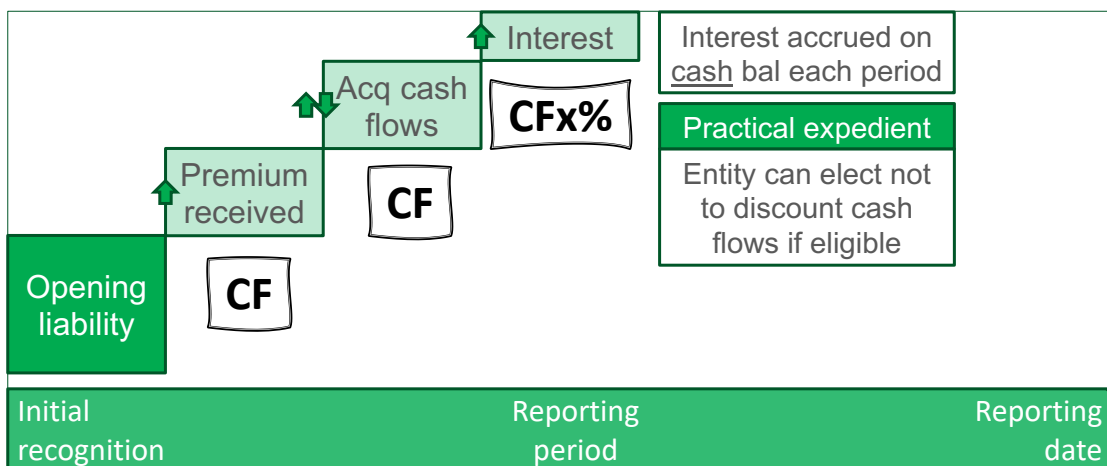
» What is the journal entry amount?

- 1) Br0, no entry is required
- 2) Br1 000, acquisition cost allocated to the 6 month period (1/3 of total)
- 3) Br1 500, acquisition cost allocated to the 6 month period (1/2 of total)

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Premium allocation approach Simplifications - subsequent measurement



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Example
6 months to June on one year contract

» Interest is at 10%, amounts to Br42 617 for the 6 months

	Debit	Credit
Interest paid	0	
Insurance liability		0

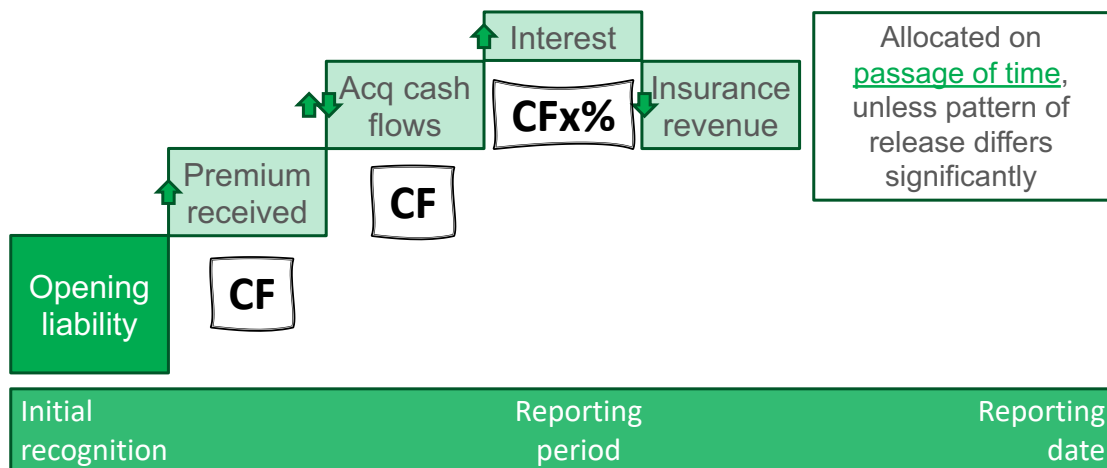
What is the Journal for 1st half interest expense?

- 1) Dr Interest paid, Cr Insurance liability
- 2) Dr Insurance liability, Cr interest received,
- 3) No entry required

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Premium allocation approach
Simplifications - subsequent measurement



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Example 6 months to June on one year contract

» Expects premium of Br1 million (2 Jan 2022), claims of Br300 000 in the 1st half, Br600 000 in the 2nd half

	Debit	Credit
Insurance liability	333 333	
Revenue		333 333

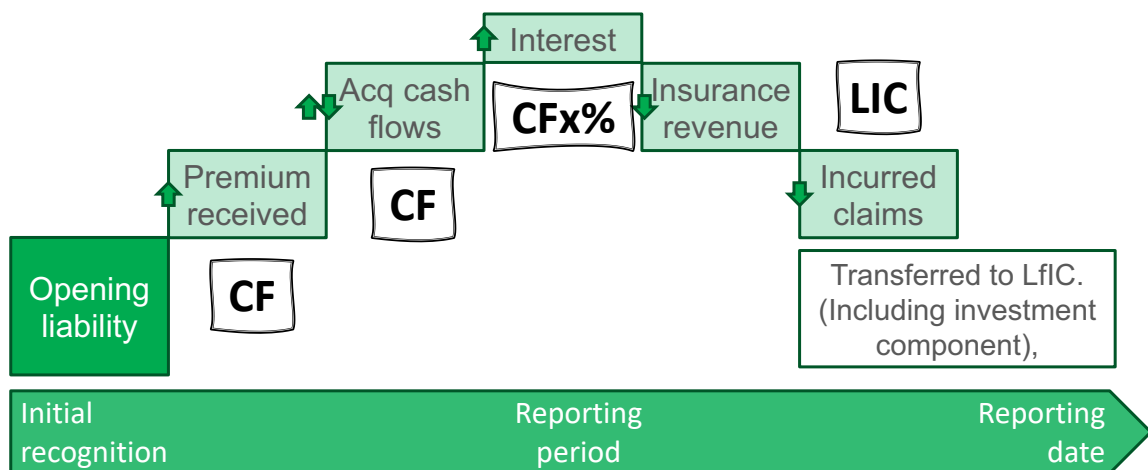
What is the Journal for 1st half revenue?

- 1) Credit revenue, Dr Cash Br333 333
- 2) Credit revenue, Dr Insurance liability Br333 333
- 3) Credit revenue, Dr Insurance liability Br 500 000

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Premium allocation approach Simplifications - subsequent measurement



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Example

6 months to June on one year contract

» Received notification of claims of Br300 000, not yet paid

	Debit	Credit
Insurance claims expense	300 000	
Insurance liability (LfIC)		300 000

What is the Journal for claims received (not yet paid)?

- 1) No journal required (no cash movement)
- 2) Debit claims expense, credit Insurance liability (LfRC)
- 3) Debit claims expense, credit Insurance liability (LfIC)

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Example

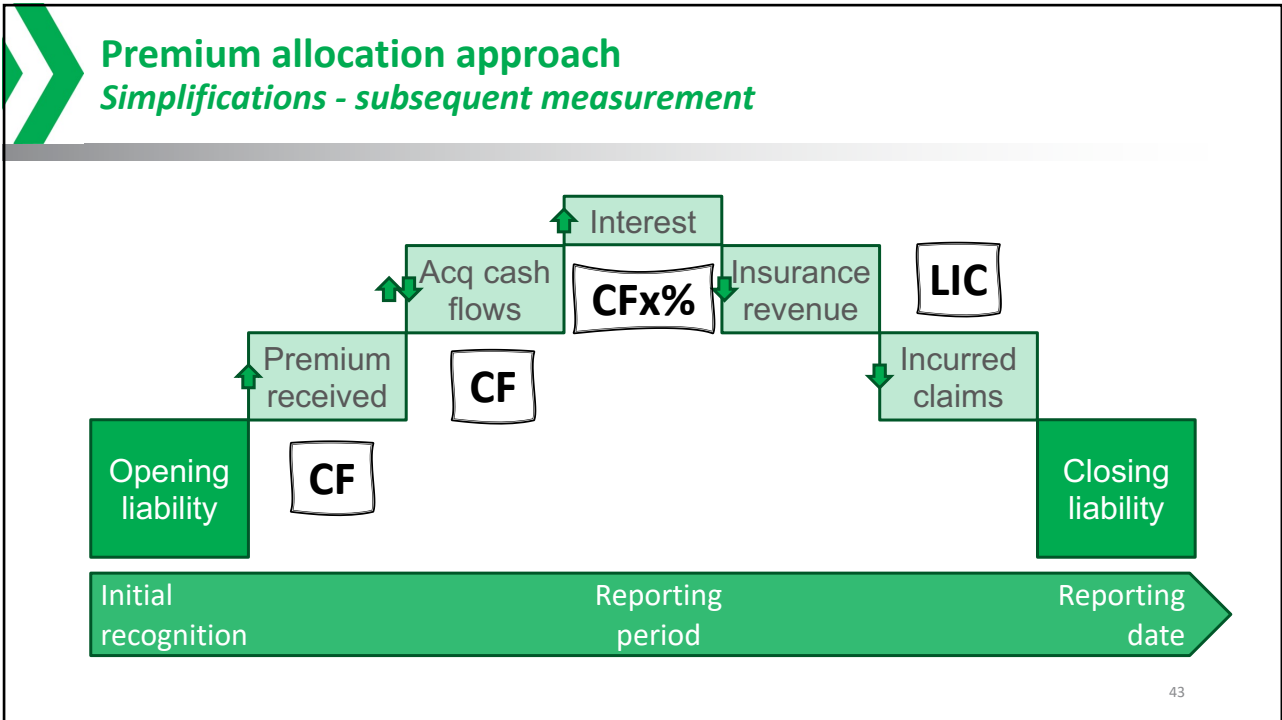
6 months to June on one year contract

» Paid claims of Br300 000,

	Debit	Credit
Insurance liability (LfIC)	300 000	
Cash		300 000

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Example

Balance sheet and P&L at 30 June 2022

Dr/(cr)	Cash	Insure Liab	P&L
Acquisition cost paid	997 000	-997 000	
Revenue		333 333	-333 333
Claims	-300 000		300 000
Acquisition costs		-1 000	1 000
2 January Total	697 000	-664 667	-32 333
Total under building block method	697 000	-660 062	-36 838

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Unearned premium reserve

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New example

Addis writes two groups of vehicle insurance contracts:

- » Premium income of Br12 000 000, either
 - » Group 1: Paid in full in advance, or
 - » Group 2: Paid In 12 monthly payments of Br1 000 000 per month
- » Service will be provided evenly over 12 month period,
- » Expected claims for both groups is Br500 000 per month, paid on the last day of the month

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Simple Example IFRS 17 annual premium

» Annual premium in advance of Br12 m, claims of Br500 00 in the 1st month

	Br 'thousands	Debit	Credit
Day 1	Cash	12 000	
	Insurance liability		12 000

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Simple Example IFRS 17 annual premium

» Annual premium in advance of Br12 m, claims of Br500 00 in the 1st month

	Br 'thousands	Debit	Credit
Day 1	Cash	12 000	
	Insurance liability		12 000
Month 1	Insurance liability	1 000	
	Revenue allocation month 1		1 000

» What is the journal for the revenue allocation for month 1?

- 1) Dr Insurance liability Br1 000, credit revenue Br1 000
- 2) Dr Insurance liability Br1 000, credit premium Br 12 000, debit unearned premium Br11 000

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Simple Example

IFRS 17 annual premium

» Annual premium in advance of Br12 m, claims of Br500 00 in the 1st month

	Br 'thousands	Debit	Credit
Day 1	Cash	12 000	
	Insurance liability		12 000
Month 1	Insurance liability	1 000	
	Revenue allocation month 1		1 000
	Insurance liability	500	
	Cash claims month 1		500
	Claims expense allocation	500	
	Insurance liability		500

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Simple Example

UPE annual premium

» Annual premium in advance of Br12 m, claims of Br500 00 in the 1st month

	Br 'thousands	Debit	Credit
Day 1	Cash	12 000	
	Insurance liability		12 000
End of Month 1	Insurance liability	1 000	
	Revenue allocation month 1		1 000

» What is the journal for the revenue allocation for month 1?

- 1) Dr Insurance liability Br1 000, credit revenue Br1 000
- 2) Dr Insurance liability Br1 000, credit premium Br 12 000, debit unearned premium Br11 000

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Simple Example
UPE annual premium

» Annual premium in advance of Br12 m, claims of Br500 00 in the 1st month

	Br 'thousands	Debit	Credit
Day 1	Cash	12 000	
	Insurance liability		12 000
End of Month 1	Insurance liability	1 000	
	Revenue allocation month 1		1 000
	Insurance liability	500	
	Cash claims month 1		500
	Claims expense allocation	500	
	Insurance liability		500

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Simple Example
UPE annual premium

» Annual premium in advance of Br12 m, claims of Br500 00 in the 1st month

	Br 'thousands	Debit	Credit
Day 1	Cash	12 000	
	Insurance liability		12 000
End of Month 1	Insurance liability	1 000	
	Revenue allocation month 1		1 000
	Insurance liability	500	
	Cash claims month 1		500
	Claims expense allocation	500	
	Insurance liability		500

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Simple Example
IFRS 17 monthly premium

» Annual premium in advance of Br12 m, claims of Br500 00 in the 1st month

	Br 'thousands	Debit	Credit
Day 1	Cash	1 000	
	Insurance liability		1 000
Month 1	Insurance liability	1 000	
	Revenue allocation month 1		1 000
	Insurance liability	500	
	Cash claims month 1		500
	Claims expense allocation	500	
	Insurance liability		500

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Example
UPE Method

» Annual premium in advance of Br12 m, claims of Br500 00 in the 1st month

	Br 'thousands	Debit	Credit
Day 1	Cash	1 000	
	Premium receivable	11 000	
	Insurance liability		12 000
Month 1	Insurance liability	1 000	
	Revenue allocation month 1		1 000
	Insurance liability	500	
	Cash claims month 1		500
	Etc.....		

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Example UPR vs IFRS 17 presentation

» Annual premium in advance of Br12 m, claims of Br500 00 in the 1st month

Income Statement – for month 1 Br 'thousands	UPR	PAA
Premium/Revenue	-12 000	-1 000
Transfer to UPR	11 000	-
Less claims	500	500
Profit or loss	-500	-500

Balance sheet – end month 1 Br 'thousands	UPR	PAA
Cash	11 500	11 500
Insurance liability	-11 000	-11 000
Retained income	-500	-500

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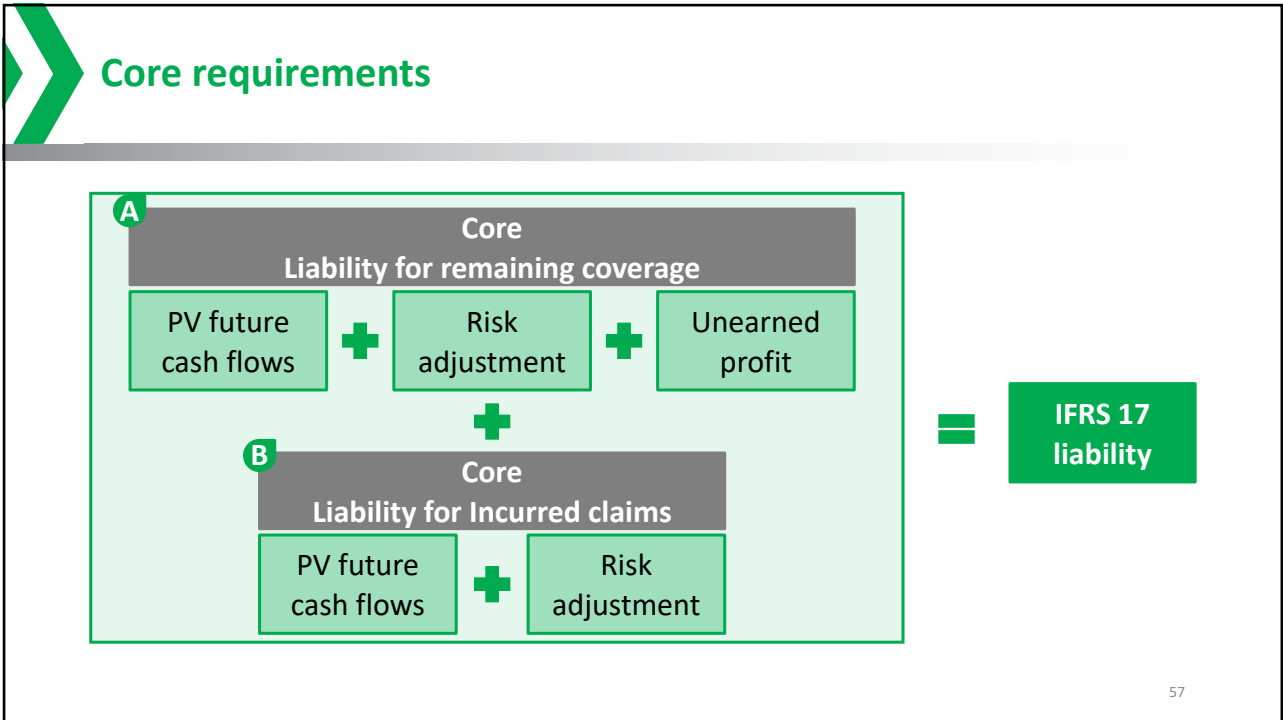
Example UPR vs IFRS 17 presentation

» Annual premium in advance of Br12 m, claims of Br500 00 in the 1st month

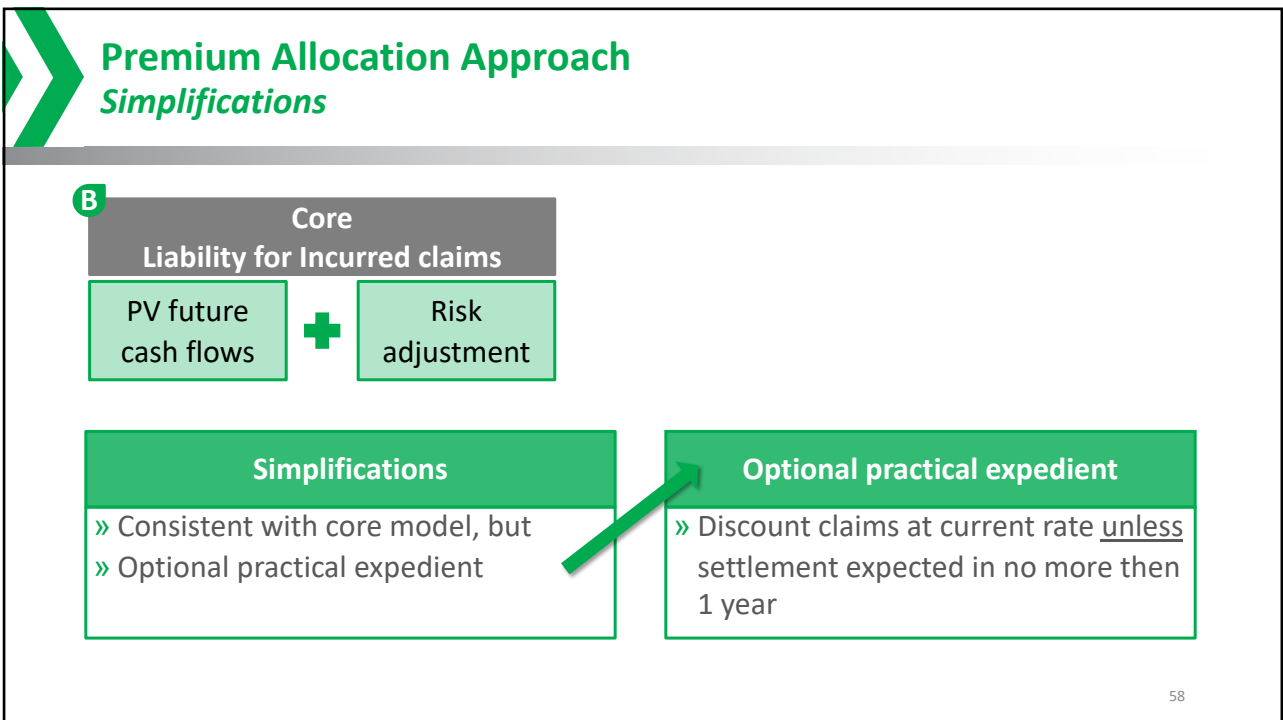
Income Statement – for month 1 Br 'thousands	UPR	PAA
Premium receivable/Revenue	-12 000	-1 000
Transfer to UPR	11 000	-
Less claims	500	500
Profit or loss	-500	-500

Balance sheet – end month 1 Br 'thousands	UPR	PAA
Cash	500	500
Premium receivable	11 000	-
insurance liability	-11 000	-
Retained income	-500	-500

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Premium Allocation Approach Simplifications

Core Liability for remaining coverage	+	Core Liability for Incurred claims	=	IFRS 17 liability					
<table border="1" style="width: 100%; border-collapse: collapse;"> <tr> <td style="padding: 5px;">PV future cash flows</td> <td style="padding: 5px;">Risk adjustment</td> <td style="padding: 5px;">Unearned profit</td> </tr> </table>	PV future cash flows	Risk adjustment	Unearned profit		<table border="1" style="width: 100%; border-collapse: collapse;"> <tr> <td style="padding: 5px;">PV future cash flows</td> <td style="padding: 5px;">Risk adjustment</td> </tr> </table>	PV future cash flows	Risk adjustment		
PV future cash flows	Risk adjustment	Unearned profit							
PV future cash flows	Risk adjustment								
Premium allocation Liability for remaining coverage	+	Premium allocation Liability for incurred claims	=	IFRS 17 liability					
» No split required » <u>Cash flows based</u> , limited forecasting » Other practical expedients		» Consistent with core » Practical expedient for discount rate							

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Onerous Contracts

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Onerous contracts

Recognition

- » *If at any time during the coverage period, facts and circumstances indicate that a group of insurance contracts is onerous, an entity shall calculate the difference between:*
 - » The carrying amount determined above and
 - » **The fulfilment cash flows calculated applying the core model (ignoring discounting if that is what the entity has elected)**
- » Determined:
 - » **Only if** facts and circumstances indicate (don't have to test otherwise)
 - » At a group level
 - » At initial inception or subsequently

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Onerous contracts

Loss component

- » If a PAA contract is initially or subsequently onerous, entity recognises the expected loss in profit or loss immediately (*loss component*)
- » General requirements of IFRS 17 require establishing, tracking and running-off of a 'loss component'
 - » Loss component is 'amortised' over the life of the contract until it is zero (it must be zero at the end of the contract)
 - » The standard does not specify the pattern for the pattern of recognition.

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Onerous contracts

Example

- » 2 year contract,
- » Immediate premium of CU1 000,
- » Expected claims of 550 in year 1 and 550 year 2

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Onerous contract example

Example

- » Addis issues a 2 year vehicle insurance contract:
 - » Premium in advance of Br24 000,
 - » Expected claims year 1 & year 2 Br12 500,
 - » For simplicity
 - » Interest is zero,
 - » risk margin is zero,

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Onerous contract example
Example

» 2 year contract, premium Br24 000, expected claims yr 1 & 2 Br12 500, interest is zero, risk margin is zero, what is the expected loss?

	Cash flow	Present value
Cash inflow (premium)	24 000	
Immediate		
Cash out flow (claims)	-25 000	
Interest rate is zero		
Risk margin (zero)		
Expect loss		

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Onerous contracts
Example

2 yr contract, premium Br24 000, expected claims yr 1 & 2 Br12 500, interest is zero, risk margin is zero

Balance sheet	Inception	Ref
<i>Insurance liability OB</i>	-	
Premium received	-	
Revenue recognised	-	
Loss component	-1 000	17.58
Closing balance	-1 000	

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Onerous contracts
Example

2 yr contract, premium Br24 000, expected claims yr 1 and 2 Br12 500

Balance sheet	Inception	Ref
Insurance liability OB	-	
Premium received	-	
Revenue recognised	-	
Loss component	-1 000	17.58
Closing balance	-1 000	
Revenue	-	
Claims	-	
Loss component	1 000	
Underwriting loss	1 000	

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Onerous contracts
Example

2 yr contract, premium Br24 000, expected claims yr 1 and 2 Br12 500

Balance sheet	Inception	Year 0	Ref
Insurance liability OB	-	-1 000	
Premium received	-	-24 000	17.55(a)
Revenue recognised	-	-	
Loss component	-1 000	-	17.58
Closing balance	-1 000	-25 000	
Revenue	-		
Claims	-		
Loss component	1 000		
Underwriting loss	1 000		

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Onerous contracts

Example

2 yr contract, premium Br24 000, expected claims yr 1 and 2 Br12 500

Balance sheet	Inception	Year 0	Year 1	Ref
Insurance liability OB	-	-1 000	-25 000	
Premium received	-	-24 000	-	17.55(a)
Revenue recognised	-	-	12 000	17.55(b)
Loss component	-1 000	-	500	17.58
Closing balance	-1 000	-25 000	-12 500	
Revenue	-			
Claims	-			
Loss component	1 000			
Underwriting loss	1 000			

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Onerous contracts

Example

2 yr contract, premium Br24 000, expected claims yr 1 and 2 Br12 500

Balance sheet	Inception	Year 0	Year 1	Year 2	Ref
Insurance liability OB	-	-1 000	-25 000	-12 500	
Premium received	-	-24 000	-	-	17.55(a)
Revenue recognised	-	-	12 000	12 000	17.55(b)
Loss component	-1 000	-	500	500	17.58
Closing balance	-1 000	-25 000	-12 500	-	
Revenue	-		-12 000		
Claims	-		12 500		
Loss component	1 000		-500		
Underwriting loss	1 000		-		

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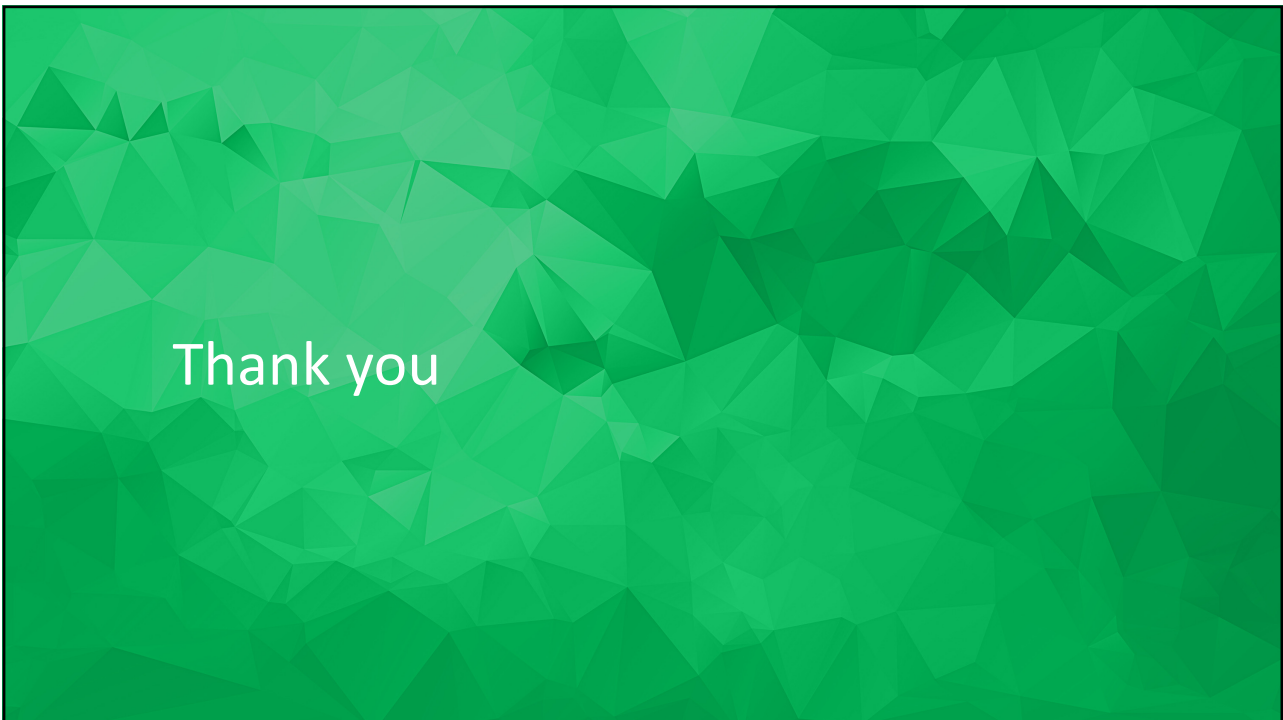
Onerous contracts
Example

2 yr contract, premium Br24 000, expected claims yr 1 and 2 Br12 500

Balance sheet	Inception	Year 0	Year 1	Year 2	Ref
Insurance liability OB	-	-1 000	-25 000	-12 500	
Premium received	-	-24 000	-	-	17.55(a)
Revenue recognised	-	-	12 000	12 000	17.55(b)
Loss component	-1 000	-	500	500	17.58
Closing balance	-1 000	-25 000	-12 500	-	
Revenue	-		-12 000	-12 000	
Claims	-		12 500	12 500	
Loss component	1 000		-500	-500	
Underwriting loss	1 000		-	-	

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