

PUBLIC BENEFIT ENTITY INTERNATIONAL FINANCIAL REPORTING STANDARD 17 INSURANCE CONTRACTS (PBE IFRS 17)

Originally issued in July 2019 and incorporates amendments up to and including 22 June 2023

This Standard applies to Tier 1 and Tier 2 Public Benefit Entities and establishes principles for the recognition, measurement, presentation, and disclosure of insurance contracts.

This New Zealand Tier 1 and Tier 2 Public Benefit Entity Accounting Standard has been issued to align the requirements for insurance contracts for Tier 1 and Tier 2 public benefit entities with the requirements for Tier 1 and Tier 2 for-profit entities applying New Zealand Equivalent to International Financial Reporting Standard 17 *Insurance Contracts* (NZ IFRS 17).

In finalising this Standard, the New Zealand Accounting Standards Board has carried out appropriate consultation in accordance with section 22(1) of the Financial Reporting Act 2013.

This Standard, when applied, supersedes PBE IFRS 4 *Insurance Contracts*.

Legal status of Standard

This Standard was issued on 4 July 2019 by the New Zealand Accounting Standards Board of the External Reporting Board pursuant to section 12(a) of the Financial Reporting Act 2013.

The Standard, pursuant to section 27(1) of the Financial Reporting Act 2013, takes effect on 1 August 2019, i.e. the 28th day after the date of its publication.

When this Standard was first issued, it was applicable only to Tier 1 and Tier 2 not-for-profit public benefit entities. The scope of this Standard was subsequently expanded by the amending Standard *Insurance Contracts in the Public Sector* to include Tier 1 and Tier 2 public sector public benefit entities. The amending Standard *Insurance Contracts in the Public Sector*, issued on 22 June 2023, pursuant to section 27(1) of the Financial Reporting Act 2023, takes effect on 20 July 2023.

This Standard is secondary legislation for the purposes of the Legislation Act 2019.

Commencement and application

Reporting entities that are subject to this Standard are required to apply it in accordance with the commencement and application provisions set out in paragraphs 132.1–132.2B.6. This Standard shall be applied by Tier 1 and Tier 2 public benefit entities for accounting periods that begin on or after:

- 1 January 2023, for not-for-profit public benefit entities; and
- 1 January 2026, for public sector public benefit entities.

Application of this Standard to an earlier accounting period by public sector public benefit entities is permitted for accounting periods that end after the amending Standard *Insurance Contracts in the Public Sector* takes effect – refer to paragraphs 132.2B.4–132.2B.6 of this Standard.

PBE IFRS 17 INSURANCE CONTRACTS

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PBE IFRS 17 INSURANCE CONTRACTS

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History of Amendments

The following is available within New Zealand on the XRB website as additional material

IASB Basis for Conclusions

IASB Illustrative Examples

Public Benefit Entity International Financial Reporting Standard 17 *Insurance Contracts* (PBE IFRS 17) is set out in paragraphs 1–132.34 and Appendices A–E. PBE IFRS 17 is based on International Financial Reporting Standard 17 *Insurance Contracts* issued by the International Accounting Standards Board and NZ IFRS 17 *Insurance Contracts*. All the paragraphs have equal authority. PBE IFRS 17 should be read in the context of its objective, the NZASB’s Basis for Conclusions on PBE IFRS 17, the IASB’s Basis for Conclusions on IFRS 17, the *Public Benefit Entities’ Conceptual Framework* and Standard XRB A1 *Application of the Accounting Standards Framework*. PBE IPSAS 3 *Accounting Policies, Changes in Accounting Estimates and Errors* provides a basis for selecting and applying accounting policies in the absence of explicit guidance.

Objective

1. **PBE IFRS 17 *Insurance Contracts* establishes principles for the recognition, measurement, presentation and disclosure of insurance contracts within the scope of the Standard. The objective of PBE IFRS 17 is to ensure that an entity provides relevant information that faithfully represents those contracts. This information gives a basis for users of financial statements to assess the effect that insurance contracts have on the entity's financial position, financial performance and cash flows.**
2. An entity shall consider its substantive rights and obligations, whether they arise from a contract, law or regulation, when applying PBE 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 (i.e., 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).
- 2.1 For a public sector entity to determine whether, in substance, there is a contract, it is necessary to identify all the relevant sources of the terms of an arrangement, whether they arise from a contract, law or regulation. In a public sector context, a contract may exist by virtue of some or all of the substantive rights and obligations for an insurance arrangement being set out in law or regulation. In some cases, there may also be separate contracts between the public sector entity and individual policyholders or a policyholder group. In other cases, there may be little or no separate documentation between the public sector entity and an individual policyholder or policyholder group.

Scope

- 2.2 **This Standard applies to Tier 1 and Tier 2 public benefit entities.**
3. An entity shall apply PBE IFRS 17 to:
 - (a) Insurance contracts, including reinsurance contracts, it issues;
 - (b) Reinsurance contracts it holds; and
 - (c) Investment contracts with discretionary participation features it issues, provided the entity also issues insurance contracts.
4. All references in PBE IFRS 17 to insurance contracts also apply to:
 - (a) Reinsurance contracts held, except:
 - (i) For references to insurance contracts issued; and
 - (ii) As described in paragraphs 60–70A.
 - (b) Investment contracts with discretionary participation features as set out in paragraph 3(c), except for the reference to insurance contracts in paragraph 3(c) and as described in paragraph 71.
5. All references in PBE IFRS 17 to insurance contracts issued also apply to insurance contracts acquired by the entity in a transfer of insurance contracts or a PBE combination other than reinsurance contracts held.
6. Paragraph 13.1 defines an insurance contract and paragraphs AG2–AG30 provide guidance on the definition of an insurance contract.
- 6.1 In addition to considering paragraph 13.1 definition of an insurance contract and paragraphs AG2–AG30, a public sector entity shall apply PBE IFRS 17 to an arrangement if, and only if, the arrangement is judged to:
 - (a) Be enforceable;

- (b) Have an identifiable coverage period; and
- (c) Give rise to insurance contracts based on the indicators in paragraph 6.2(a) and the other considerations in paragraph 6.2(b).

Paragraphs E9–E17 of Appendix E provide guidance for determining whether an arrangement is enforceable and has an identifiable coverage period, which are pre-requisites for applying PBE IFRS 17. When an arrangement is not enforceable or does not have an identifiable coverage period, the arrangement is outside the scope of PBE IFRS 17.

6.2 When a public sector entity arrangement is enforceable and has an identifiable coverage period, subject to paragraphs 8 and 8A the entity shall:

- (a) apply the following indicators on a collective basis to judge whether the arrangement gives rise to insurance contracts that fall within the scope of PBE IFRS 17:
 - (i) The source and extent of funding – refer to guidance in paragraphs E18–E22; and
 - (ii) The similarity of risks covered and benefits provided – refer to guidance in paragraphs E23–E30; and
- (b) in the event that the indicators in (a) are not definitive, apply the following other considerations on a collective basis to judge whether the arrangement gives rise to insurance contracts that fall within the scope of PBE IFRS 17:
 - (i) The management practices and assessment of financial performance applied – refer to guidance in paragraphs E31–E33; and
 - (ii) Whether there are assets held to meet benefits – refer to guidance in paragraphs E34–E36.

7. An entity shall not apply PBE IFRS 17 to:

- (a) Warranties provided by a manufacturer, dealer or retailer in connection with the sale of its goods or services to a customer (see PBE IPSAS 9 *Revenue from Exchange Transactions* and PBE IPSAS 19 *Provisions, Contingent Liabilities and Contingent Assets*).
- (b) Employers' assets and liabilities from employee benefit plans (see PBE IPSAS 39 *Employee Benefits*) and retirement benefit obligations reported by defined benefit retirement plans (see the relevant international or national standard dealing with reporting by retirement benefit plans).
- (c) Contractual rights or contractual obligations contingent on the future use of, or the right to use, a non-financial item (for example, some licence fees, royalties, contingent lease payments and similar items: see PBE IPSAS 9, PBE IPSAS 13 *Leases* and PBE IPSAS 31 *Intangible Assets*).
- (d) Residual value guarantees provided by a manufacturer, dealer or retailer and a lessee's residual value guarantees when they are embedded in a lease (see PBE IPSAS 13).
- (e) Financial guarantee contracts, unless the issuer has previously applied accounting applicable to insurance contracts and adopted an accounting policy that treated financial guarantee contracts as insurance contracts. The issuer shall choose to apply either PBE IFRS 17 or PBE IPSAS 28 *Financial Instruments: Presentation*, PBE IPSAS 30 *Financial Instruments: Disclosures* and PBE IPSAS 41 *Financial Instruments* to such financial guarantee contracts. The issuer may make that choice contract by contract, but the choice for each contract is irrevocable.
- (f) Contingent consideration payable or receivable in a PBE combination (see PBE IPSAS 40 *PBE Combinations*).
- (g) Insurance contracts in which the entity is the policyholder, unless those contracts are reinsurance contracts held (see paragraph 3(b)).
- (h) Credit card contracts, or similar contracts that provide credit or payment arrangements, that meet the definition of an insurance contract if, and only if, the entity does not reflect an assessment of the insurance risk associated with an individual customer in setting the price of the contract with that customer (see PBE IPSAS 41 and other applicable Standards). However, if, and only if, PBE IPSAS 41 requires an entity to separate an insurance coverage component (see paragraph 2(e)(iv) of PBE IPSAS 41) that is embedded in such a contract, the entity shall apply PBE IFRS 17 to that component.

8. Some contracts meet the definition of an insurance contract but have as their primary purpose the provision of services for a fixed fee. An entity may choose to apply PBE IPSAS 9 instead of PBE IFRS 17 to such contracts that it issues if, and only if, specified conditions are met. The entity may make that choice contract by contract, but the choice for each contract is irrevocable. The conditions are:
 - (a) The entity does not reflect an assessment of the risk associated with an individual customer in setting the price of the contract with that customer;
 - (b) The contract compensates the customer by providing services, rather than by making cash payments to the customer; and
 - (c) The insurance risk transferred by the contract arises primarily from the customer's use of services rather than from uncertainty over the cost of those services.
- 8A Some contracts meet the definition of an insurance contract but limit the compensation for insured events to the amount otherwise required to settle the policyholder's obligation created by the contract (for example, loans with death waivers). An entity shall choose to apply either PBE IFRS 17 or PBE IPSAS 41 to such contracts that it issues unless such contracts are excluded from the scope of PBE IFRS 17 by paragraph 7. The entity shall make that choice for each portfolio of insurance contracts, and the choice for each portfolio is irrevocable.

Combination of Insurance Contracts

9. 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.

Separating Components from an Insurance Contract (paragraphs AG31–AG35)

10. An insurance contract may contain one or more components that would be within the scope of another Standard if they were separate contracts. For example, an insurance contract may include an investment component or a component for services other than insurance contract services (or both). An entity shall apply paragraphs 11–13 to identify and account for the components of the contract.
11. An entity shall:
 - (a) Apply PBE IPSAS 41 to determine whether there is an embedded derivative to be separated and, if there is, how to account for that derivative.
 - (b) Separate from a host insurance contract an investment component if, and only if, that investment component is distinct (see paragraphs AG31–AG32). The entity shall apply PBE IPSAS 41 to account for the separated investment component unless it is an investment contract with discretionary participation features within the scope of PBE IFRS 17 (see paragraph 3(c)).
12. After applying paragraph 11 to separate any cash flows related to embedded derivatives and distinct investment components, an entity shall separate from the host insurance contract any promise to transfer to a policyholder distinct goods or services other than insurance contract services. To separate the promise, the entity shall apply paragraphs AG33–AG35 of PBE IFRS 17 and, on initial recognition, shall:
 - (a) Attribute the cash inflows between the insurance component and any promises to provide distinct goods or services other than insurance contract services; and
 - (b) Attribute the cash outflows between the insurance component and any promised goods or services other than insurance contract services accounted for so that:
 - (i) Cash outflows that relate directly to each component are attributed to that component; and
 - (ii) Any remaining cash outflows are attributed on a systematic and rational basis, reflecting the cash outflows the entity would expect to arise if that component were a separate contract.
13. After applying paragraphs 11–12, an entity shall apply PBE IFRS 17 to all remaining components of the host insurance contract. Hereafter, all references in PBE IFRS 17 to embedded derivatives refer to

derivatives that have not been separated from the host insurance contract and all references to investment components refer to investment components that have not been separated from the host insurance contract (except those references in paragraphs AG31–AG32).

Definitions

13.1 The following terms are used in this Standard with the meanings specified:

The **contractual service margin** is a component of the carrying amount of the asset or liability for a group of insurance contracts representing the unearned surplus the entity will recognise as it provides insurance contract services under the insurance contracts in the group.

The **coverage period** is the period during which the entity provides insurance contract services. This period includes the insurance contract services that relate to all premiums within the boundary of the insurance contract.

Experience adjustment: A difference between:

- (a) For premium receipts (and any related cash flows such as insurance acquisition cash flows and insurance premium taxes)—the estimate at the beginning of the period of the amounts expected in the period and the actual cash flows in the period; or
- (b) For insurance service expenses (excluding insurance acquisition expenses)—the estimate at the beginning of the period of the amounts expected to be incurred in the period and the actual amounts incurred in the period.

Financial risk is the risk of a possible future change in one or more of a specified interest rate, financial instrument price, commodity price, currency exchange rate, index of prices or rates, credit rating or credit index or other variable, provided in the case of a non-financial variable that the variable is not specific to a party to the contract.

Fulfilment cash flows is an explicit, unbiased and probability-weighted estimate (i.e., expected value) of the present value of the future cash outflows minus the present value of the future cash inflows that will arise as the entity fulfils insurance contracts, including a risk adjustment for non-financial risk.

A **group of insurance contracts** is a set of insurance contracts resulting from the division of a portfolio of insurance contracts into, at a minimum, contracts issued within a period of no longer than one year and that, at initial recognition:

- (a) Are onerous, if any;
- (b) Have no significant possibility of becoming onerous subsequently, if any; or
- (c) Do not fall into either (a) or (b), if any.

Insurance acquisition cash flows are cash flows arising from the costs of selling, underwriting and starting a group of insurance contracts (issued or expected to be issued) that are directly attributable to the portfolio of insurance contracts to which the group belongs. Such cash flows include cash flows that are not directly attributable to individual contracts or groups of insurance contracts within the portfolio.

An **insurance contract** is a contract under which one party (the issuer) accepts significant insurance risk from another party (the policyholder) by agreeing to compensate the policyholder if a specified uncertain future event (the insured event) adversely affects the policyholder.

Insurance contract services are the following services that an entity provides to a policyholder of an insurance contract:

- (a) Coverage for an insured event (insurance coverage);
- (b) For insurance contracts without direct participation features, the generation of an investment return for the policyholder, if applicable (investment-return service); and
- (c) For insurance contracts with direct participation features, the management of underlying items on behalf of the policyholder (investment-related service).

An **insurance contract with direct participation features** is an insurance contract for which, at inception:

- (a) The contractual terms specify that the policyholder participates in a share of a clearly identified pool of underlying items;
- (b) The entity expects to pay to the policyholder an amount equal to a substantial share of the fair value returns on the underlying items; and
- (c) The entity expects a substantial proportion of any change in the amounts to be paid to the policyholder to vary with the change in fair value of the underlying items.

An **insurance contract without direct participation features** is an insurance contract that is not an insurance contract with direct participation features.

Insurance risk is risk, other than financial risk, transferred from the holder of a contract to the issuer.

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

Investment component: The amounts that an insurance contract requires the entity to repay to a policyholder in all circumstances, regardless of whether an insured event occurs.

An **investment contract with discretionary participation features** is a financial instrument that provides a particular investor with the contractual right to receive, as a supplement to an amount not subject to the discretion of the issuer, additional amounts:

- (a) That are expected to be a significant portion of the total contractual benefits;
- (b) The timing or amount of which are contractually at the discretion of the issuer; and
- (c) That are contractually based on:
 - (i) The returns on a specified pool of contracts or a specified type of contract;
 - (ii) Realised and/or unrealised investment returns on a specified pool of assets held by the issuer; or
 - (iii) The surplus or deficit of the entity or fund that issues the contract.

Liability for incurred claims: An entity's obligation to:

- (a) Investigate and pay valid claims for insured events that have already occurred, including events that have occurred but for which claims have not been reported, and other incurred insurance expenses; and
- (b) Pay amounts that are not included in (a) and that relate to:
 - (i) Insurance contract services that have already been provided; or
 - (ii) Any investment components or other amounts that are not related to the provision of insurance contract services and that are not in the liability for remaining coverage.

Liability for remaining coverage: An entity's obligation to:

- (a) Investigate and pay valid claims under existing insurance contracts for insured events that have not yet occurred (i.e., the obligation that relates to the unexpired portion of the insurance coverage); and
- (b) Pay amounts under existing insurance contracts that are not included in (a) and that relate to:
 - (i) Insurance contract services not yet provided (i.e., the obligations that relate to future provision of insurance contract services); or
 - (ii) Any investment components or other amounts that are not related to the provision of insurance contract services and that have not been transferred to the liability for incurred claims.

Non-performance risk is the risk that an entity will not fulfil an obligation. Non-performance risk includes, but may not be limited to, the entity's own credit risk.

A **policyholder** is a party that has a right to compensation under an insurance contract if an insured event occurs.

Portfolio of insurance contracts: Insurance contracts subject to similar risks and managed together.

A **reinsurance contract** is an insurance contract issued by one entity (the reinsurer) to compensate another entity for claims arising from one or more insurance contracts issued by that other entity (underlying contracts).

Risk adjustment for non-financial risk: is 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.

Underlying items are items that determine some of the amounts payable to a policyholder. Underlying items can comprise any items; for example, a reference portfolio of assets, the net assets of the entity, or a specified subset of the net assets of the entity.

Terms defined in other PBE Standards are used in this Standard with the same meaning as in those standards, and are reproduced in the *Glossary of Defined Terms* published separately.

Level of Aggregation of Insurance Contracts

14. An entity shall identify portfolios of insurance contracts. A portfolio comprises contracts subject to similar risks and managed together. Contracts within a product line would be expected to have similar risks and hence would be expected to be in the same portfolio if they are managed together. Contracts in different product lines (for example single premium fixed annuities compared with regular term life assurance) would not be expected to have similar risks and hence would be expected to be in different portfolios.
- 14.1 For a public sector entity applying the modifications in paragraphs 16.1 and 22.1, a portfolio of insurance contracts would be the main unit of account, not groups of insurance contracts.
15. Paragraphs 16–24 apply to insurance contracts issued. The requirements for the level of aggregation of reinsurance contracts held are set out in paragraph 61.
16. An entity shall divide a portfolio of insurance contracts issued into a minimum of:
 - (a) A group of contracts that are onerous at initial recognition, if any;
 - (b) A group of contracts that at initial recognition have no significant possibility of becoming onerous subsequently, if any; and
 - (c) A group of the remaining contracts in the portfolio, if any.
- 16.1 Notwithstanding paragraph 16, a public sector entity is not required to divide a portfolio of insurance contracts based on the minimum groups identified in paragraph 16.
17. If an entity has reasonable and supportable information to conclude that a set of contracts will all be in the same group applying paragraph 16, it may measure the set of contracts to determine if the contracts are onerous (see paragraph 47) and assess the set of contracts to determine if the contracts have no significant possibility of becoming onerous subsequently (see paragraph 19). If the entity does not have reasonable and supportable information to conclude that a set of contracts will all be in the same group, it shall determine the group to which contracts belong by considering individual contracts.
18. For contracts issued to which an entity applies the premium allocation approach (see paragraphs 53–59), the entity shall assume no contracts in the portfolio are onerous at initial recognition, unless facts and circumstances indicate otherwise. An entity shall assess whether contracts that are not onerous at initial recognition have no significant possibility of becoming onerous subsequently by assessing the likelihood of changes in applicable facts and circumstances.

19. For contracts issued to which an entity does not apply the premium allocation approach (see paragraphs 53–54), an entity shall assess whether contracts that are not onerous at initial recognition have no significant possibility of becoming onerous:
 - (a) Based on the likelihood of changes in assumptions which, if they occurred, would result in the contracts becoming onerous.
 - (b) Using information about estimates provided by the entity's internal reporting. Hence, in assessing whether contracts that are not onerous at initial recognition have no significant possibility of becoming onerous:
 - (i) An entity shall not disregard information provided by its internal reporting about the effect of changes in assumptions on different contracts on the possibility of their becoming onerous; but
 - (ii) An entity is not required to gather additional information beyond that provided by the entity's internal reporting about the effect of changes in assumptions on different contracts.
20. If, applying paragraphs 14–19, contracts within a portfolio would fall into different groups only because law or regulation specifically constrains the entity's practical ability to set a different price or level of benefits for policyholders with different characteristics, the entity may include those contracts in the same group. The entity shall not apply this paragraph by analogy to other items.
21. An entity is permitted to subdivide the groups described in paragraph 16. For example, an entity may choose to divide the portfolios into:
 - (a) More groups that are not onerous at initial recognition—if the entity's internal reporting provides information that distinguishes:
 - (i) Different levels of profitability; or
 - (ii) Different possibilities of contracts becoming onerous after initial recognition; and
 - (b) More than one group of contracts that are onerous at initial recognition—if the entity's internal reporting provides information at a more detailed level about the extent to which the contracts are onerous.
22. **An entity shall not include contracts issued more than one year apart in the same group. To achieve this the entity shall, if necessary, further divide the groups described in paragraphs 16–21.**
- 22.1 **Notwithstanding paragraph 22, a public sector entity is not required to divide a portfolio of insurance contracts based on when they are issued.**
23. A group of insurance contracts shall comprise a single contract if that is the result of applying paragraphs 14–22.
24. An entity shall apply the recognition and measurement requirements of PBE IFRS 17 to the groups of contracts determined by applying paragraphs 14–23. An entity shall establish the groups at initial recognition and add contracts to the groups applying paragraph 28. The entity shall not reassess the composition of the groups subsequently. To measure a group of contracts, an entity may estimate the fulfilment cash flows at a higher level of aggregation than the group or portfolio, provided the entity is able to include the appropriate fulfilment cash flows in the measurement of the group, applying paragraphs 32(a), 40(a)(i) and 40(b), by allocating such estimates to groups of contracts.

Recognition

25. **An entity shall recognise a group of insurance contracts it issues from the earliest of the following:**
 - (a) **The beginning of the coverage period of the group of contracts;**
 - (b) **The date when the first payment from a policyholder in the group becomes due; and**
 - (c) **For a group of onerous contracts, when the group becomes onerous.**
- 25.1 **Notwithstanding paragraph 25, a public sector entity shall recognise insurance contracts it issues from the earliest of the following:**
 - (a) **The beginning of the coverage period of an insurance contract; and**

(b) The date when the first payment from a policyholder of an insurance contract becomes due.

26. If there is no contractual due date, the first payment from the policyholder is deemed to be due when it is received. An entity is required to determine whether any contracts form a group of onerous contracts applying paragraph 16 before the earlier of the dates set out in paragraphs 25(a) and 25(b) if facts and circumstances indicate there is such a group.
27. [Deleted by IASB]
28. In recognising a group of insurance contracts in a reporting period, an entity shall include only contracts that individually meet one of the criteria set out in paragraph 25 and shall make estimates for the discount rates at the date of initial recognition (see paragraph AG73) and the coverage units provided in the reporting period (see paragraph AG119). An entity may include more contracts in the group after the end of a reporting period, subject to paragraphs 14–22. An entity shall add a contract to the group in the reporting period in which that contract meets one of the criteria set out in paragraph 25. This may result in a change to the determination of the discount rates at the date of initial recognition applying paragraph AG73. An entity shall apply the revised rates from the start of the reporting period in which new contracts are added to the group.

Insurance Acquisition Cash Flows (paragraphs AG35A–AG35D)

- 28A An entity shall allocate insurance acquisition cash flows to groups of insurance contracts using a systematic and rational method applying paragraphs AG35A–AG35B, unless it chooses to recognise them as expenses applying paragraph 59(a).
- 28B An entity not applying paragraph 59(a) shall recognise as an asset insurance acquisition cash flows paid (or insurance acquisition cash flows for which a liability has been recognised applying another Standard) before the related group of insurance contracts is recognised. An entity shall recognise such an asset for each related group of insurance contracts.
- 28C An entity shall derecognise an asset for insurance acquisition cash flows when the insurance acquisition cash flows are included in the measurement of the related group of insurance contracts applying paragraph 38(c)(i) or paragraph 55(a)(iii).
- 28D If paragraph 28 applies, an entity shall apply paragraphs 28B–28C in accordance with paragraph AG35C.
- 28E At the end of each reporting period, an entity shall assess the recoverability of an asset for insurance acquisition cash flows if facts and circumstances indicate the asset may be impaired (see paragraph AG35D). If an entity identifies an impairment loss, the entity shall adjust the carrying amount of the asset and recognise the impairment loss in surplus or deficit.
- 28F An entity shall recognise in surplus or deficit a reversal of some or all of an impairment loss previously recognised applying paragraph 28E and increase the carrying amount of the asset, to the extent that the impairment conditions no longer exist or have improved.

Measurement (paragraphs AG36–AG119F)

29. An entity shall apply paragraphs 30–52 to all groups of insurance contracts within the scope of PBE IFRS 17, with the following exceptions:
- (a) For groups of insurance contracts meeting either of the criteria specified in paragraph 53, an entity may simplify the measurement of the group using the premium allocation approach in paragraphs 55–59.
 - (b) For groups of reinsurance contracts held, an entity shall apply paragraphs 32–46 as required by paragraphs 63–70A. Paragraph 45 (on insurance contracts with direct participation features) and paragraphs 47–52 (on onerous contracts) do not apply to groups of reinsurance contracts held.
 - (c) For groups of investment contracts with discretionary participation features, an entity shall apply paragraphs 32–52 as modified by paragraph 71.
30. When applying PBE IPSAS 4 *The Effects of Changes in Foreign Exchange Rates* to a group of insurance contracts that generate cash flows in a foreign currency, an entity shall treat the group of contracts, including the contractual service margin, as a monetary item.

31. In the financial statements of an entity that issues insurance contracts, the fulfilment cash flows shall not reflect the non-performance risk of that entity.

Measurement on Initial Recognition (paragraphs AG36–AG95F)

32. **On initial recognition, an entity shall measure a group of insurance contracts at the total of:**
- (a) **The fulfilment cash flows, which comprise:**
 - (i) **Estimates of future cash flows (paragraphs 33–35);**
 - (ii) **An adjustment to reflect the time value of money and the financial risks related to the future cash flows, to the extent that the financial risks are not included in the estimates of the future cash flows (paragraph 36); and**
 - (iii) **A risk adjustment for non-financial risk (paragraph 37).**
 - (b) **The contractual service margin, measured applying paragraphs 38–39.**

Estimates of Future Cash Flows (paragraphs AG36–AG71)

33. **An entity shall include in the measurement of a group of insurance contracts all the future cash flows within the boundary of each contract in the group (see paragraph 34). Applying paragraph 24, an entity may estimate the future cash flows at a higher level of aggregation and then allocate the resulting fulfilment cash flows to individual groups of contracts. The estimates of future cash flows shall:**
- (a) **Incorporate, in an unbiased way, all reasonable and supportable information available without undue cost or effort about the amount, timing and uncertainty of those future cash flows (see paragraphs AG37–AG41). To do this, an entity shall estimate the expected value (i.e., the probability-weighted mean) of the full range of possible outcomes.**
 - (b) **Reflect the perspective of the entity, provided that the estimates of any relevant market variables are consistent with observable market prices for those variables (see paragraphs AG42–AG53).**
 - (c) **Be current—the estimates shall reflect conditions existing at the measurement date, including assumptions at that date about the future (see paragraphs AG54–AG60).**
 - (d) **Be explicit—the entity shall estimate the adjustment for non-financial risk separately from the other estimates (see paragraph AG90). The entity also shall estimate the cash flows separately from the adjustment for the time value of money and financial risk, unless the most appropriate measurement technique combines these estimates (see paragraph AG46).**
34. 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 insurance contract services (see paragraphs AG61–AG71). A substantive obligation to provide insurance contract 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 up to the date when the risks are reassessed does not take into account the risks that relate to periods after the reassessment date.
- 34.1 In respect of paragraphs 34(a) and 34(b)(i):
- (a) Assessing a public sector entity’s practical ability to fully price for risks or benefits would include assessing the ability of its controlling government, and any relevant Minister(s), to decide on pricing or benefits;

- (b) A public sector entity's monopoly position in providing coverage for risks in a particular community, of itself, would not affect the entity's practical ability to fully price for risks or benefits; and
 - (c) Any legislated obligation for a public sector entity to stand ready to insure future policyholders, of itself, is not an obligation that would affect the practical ability to fully price for risks or benefits.
- 34.2 Notwithstanding paragraph 34(b)(ii), a public sector entity would not be regarded as failing to meet the criterion in paragraph 34(b)(ii) simply because its premium pricing for coverage up to the date when the risks are reassessed takes into account the risks that relate to periods after the reassessment date, due to having a policy of determining prices and benefits based on a medium- to long-term view.
- 34.3 Public sector entities may have an established system of, or regulatory requirement for, periodic pricing and benefit reviews, for example once every three years. However, in many cases, this is effectively a minimum frequency for review and it would be feasible for an entity to respond to current experience and events outside this process. In these cases, the established system does not remove the practical ability for the entity to change prices and benefits on a more frequent basis, for example annually. In addition, a public sector entity's established system for setting prices and benefits may ordinarily take many months to complete, but may not in fact remove the practical ability in the context of paragraph 34(b)(i) to set prices and benefits on a more timely basis.
- 34.4 A public sector entity shall disclose:
- (a) Timeframes for which pricing and benefits are typically determined; and
 - (b) The titles of the relevant laws or regulations under which prices and benefits are set.
35. 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.

Discount Rates (paragraphs AG72–AG85)

36. **An entity shall adjust the estimates of future cash flows to reflect the time value of money and the financial risks related to those cash flows, to the extent that the financial risks are not included in the estimates of cash flows. The discount rates applied to the estimates of the future cash flows described in paragraph 33 shall:**
- (a) **Reflect the time value of money, the characteristics of the cash flows and the liquidity characteristics of the insurance contracts;**
 - (b) **Be consistent with observable current market prices (if any) for financial instruments with cash flows whose characteristics are consistent with those of the insurance contracts, in terms of, for example, timing, currency and liquidity; and**
 - (c) **Exclude the effect of factors that influence such observable market prices but do not affect the future cash flows of the insurance contracts.**

Risk Adjustment for Non-Financial Risk (paragraphs AG86–AG92)

37. **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.**

Contractual Service Margin

38. **The contractual service margin is a component of the asset or liability for the group of insurance contracts that represents the unearned surplus the entity will recognise as it provides insurance contract services in the future. An entity shall measure the contractual service margin on initial recognition of a group of insurance contracts at an amount that, unless paragraph 47 (on onerous contracts) or paragraphs 123A (on insurance revenue relating to paragraphs 38(c)(ii)) applies, results in no revenue or expenses arising from:**
- (a) **The initial recognition of an amount for the fulfilment cash flows, measured by applying paragraphs 32–37;**

- (b) **Any cash flows arising from the contracts in the group at that date;**
 - (c) **The derecognition at the date of initial recognition of;**
 - (i) **Any asset recognised for insurance acquisition cash flows applying paragraph 28C; and**
 - (ii) **Any other asset or liability previously recognised for cash flows related to the group of contracts as specified in paragraph AG66A.**
39. For insurance contracts acquired in a transfer of insurance contracts or a PBE combination within the scope of PBE IPSAS 40, an entity shall apply paragraph 38 in accordance with paragraphs AG93–AG95.

Subsequent Measurement

40. **The carrying amount of a group of insurance contracts at the end of each reporting period shall be the sum of:**
- (a) **The liability for remaining coverage comprising:**
 - (i) **The fulfilment cash flows related to future service allocated to the group at that date, measured applying paragraphs 33–37 and AG36–AG92;**
 - (ii) **The contractual service margin of the group at that date, measured applying paragraphs 43–46; and**
 - (b) **The liability for incurred claims, comprising the fulfilment cash flows related to past service allocated to the group at that date, measured applying paragraphs 33–37 and AG36–AG92.**
41. **An entity shall recognise revenue and expenses for the following changes in the carrying amount of the liability for remaining coverage:**
- (a) **Insurance revenue—for the reduction in the liability for remaining coverage because of services provided in the period, measured applying paragraphs AG120–AG124;**
 - (b) **Insurance service expenses—for losses on groups of onerous contracts, and reversals of such losses (see paragraphs 47–52); and**
 - (c) **Insurance finance revenue or expenses—for the effect of the time value of money and the effect of financial risk as specified in paragraph 87.**
42. **An entity shall recognise revenue and expenses for the following changes in the carrying amount of the liability for incurred claims:**
- (a) **Insurance service expenses—for the increase in the liability because of claims and expenses incurred in the period, excluding any investment components;**
 - (b) **Insurance service expenses—for any subsequent changes in fulfilment cash flows relating to incurred claims and incurred expenses; and**
 - (c) **Insurance finance revenue or expenses—for the effect of the time value of money and the effect of financial risk as specified in paragraph 87.**

Contractual Service Margin (paragraphs AG96–AG119B)

43. **The contractual service margin at the end of the reporting period represents the surplus in the group of insurance contracts that has not yet been recognised in surplus or deficit because it relates to the future service to be provided under the contracts in the group.**
44. For insurance contracts without direct participation features, the carrying amount of the contractual service margin of a group of contracts at the end of the reporting period equals the carrying amount at the start of the reporting period adjusted for:
- (a) The effect of any new contracts added to the group (see paragraph 28);
 - (b) Interest accreted on the carrying amount of the contractual service margin during the reporting period, measured at the discount rates specified in paragraph AG72(b);

- (c) The changes in fulfilment cash flows relating to future service as specified in paragraphs AG96–AG100, except to the extent that:
 - (i) Such increases in the fulfilment cash flows exceed the carrying amount of the contractual service margin, giving rise to a loss (see paragraph 48(a)); or
 - (ii) Such decreases in the fulfilment cash flows are allocated to the loss component of the liability for remaining coverage applying paragraph 50(b).
 - (d) The effect of any currency exchange differences on the contractual service margin; and
 - (e) The amount recognised as insurance revenue because of the transfer of insurance contract 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 AG119.
45. For insurance contracts with direct participation features (see paragraphs AG101–AG118), the carrying amount of the contractual service margin of a group of contracts at the end of the reporting period equals the carrying amount at the start of the reporting period adjusted for the amounts specified in subparagraphs (a)–(e) below. An entity is not required to identify these adjustments separately. Instead, a combined amount may be determined for some, or all, of the adjustments. The adjustments are:
- (a) The effect of any new contracts added to the group (see paragraph 28);
 - (b) The change in the amount of the entity's share of the fair value of the underlying items (see paragraph AG104(b)(i)), except to the extent that:
 - (i) Paragraph AG115 (on risk mitigation) applies;
 - (ii) The decrease in the amount of the entity's share of the fair value of the underlying items exceeds the carrying amount of the contractual service margin, giving rise to a loss (see paragraph 48); or
 - (iii) The increase in the amount of the entity's share of the fair value of the underlying items reverses the amount in (ii).
 - (c) The changes in fulfilment cash flows relating to future service, as specified in paragraphs AG101–AG118, except to the extent that:
 - (i) Paragraph AG115 (on risk mitigation) applies;
 - (ii) Such increases in the fulfilment cash flows exceed the carrying amount of the contractual service margin, giving rise to a loss (see paragraph 48); or
 - (iii) Such decreases in the fulfilment cash flows are allocated to the loss component of the liability for remaining coverage applying paragraph 50(b).
 - (d) The effect of any currency exchange differences arising on the contractual service margin; and
 - (e) The amount recognised as insurance revenue because of the transfer of insurance contract 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 AG119.
46. Some changes in the contractual service margin offset changes in the fulfilment cash flows for the liability for remaining coverage, resulting in no change in the total carrying amount of the liability for remaining coverage. To the extent that changes in the contractual service margin do not offset changes in the fulfilment cash flows for the liability for remaining coverage, an entity shall recognise revenue and expenses for the changes, applying paragraph 41.

Onerous Contracts

47. An insurance contract is onerous at the date of initial recognition if the fulfilment cash flows allocated to the contract, any previously recognised insurance acquisition cash flows and any cash flows arising from the contract at the date of initial recognition in total are a net outflow. Applying paragraph 16(a), an entity shall group such contracts separately from contracts that are not onerous. To the extent that paragraph 17 applies, an entity may identify the group of onerous contracts by measuring a set of contracts rather than

individual contracts. An entity shall recognise a loss in surplus or deficit for the net outflow for the group of onerous contracts, resulting in the carrying amount of the liability for the group being equal to the fulfilment cash flows and the contractual service margin of the group being zero.

48. A group of insurance contracts becomes onerous (or more onerous) on subsequent measurement if the following amounts exceed the carrying amount of the contractual service margin:

- (a) Unfavourable changes relating to future service in the fulfilment cash flows allocated to the group arising from changes in estimates of future cash flows and the risk adjustment for non-financial risk; and
- (b) For a group of insurance contracts with direct participation features, the decrease in the amount of the entity's share of the fair value of the underlying items.

Applying paragraphs 44(c)(i), 45(b)(ii) and 45(c)(ii), an entity shall recognise a loss in surplus or deficit to the extent of that excess.

49. An entity shall establish (or increase) a loss component of the liability for remaining coverage for an onerous group depicting the losses recognised applying paragraphs 47–48. The loss component determines the amounts that are presented in surplus or deficit as reversals of losses on onerous groups and are consequently excluded from the determination of insurance revenue.

50. After an entity has recognised a loss on an onerous group of insurance contracts, it shall allocate:

- (a) The subsequent changes in fulfilment cash flows of the liability for remaining coverage specified in paragraph 51 on a systematic basis between:
 - (i) The loss component of the liability for remaining coverage; and
 - (ii) The liability for remaining coverage, excluding the loss component.
- (b) Solely to the loss component until that component is reduced to zero:
 - (i) Any subsequent decrease relating to future service in fulfilment cash flows allocated to the group arising from changes in estimates of future cash flows and the risk adjustment for non-financial risk; and
 - (ii) Any subsequent increases in the amount of the entity's share of the fair value of the underlying items.

Applying paragraphs 44(c)(ii), 45(b)(iii) and 45(c)(iii), an entity shall adjust the contractual service margin only for the excess of the decrease over the amount allocated to the loss component.

51. The subsequent changes in the fulfilment cash flows of the liability for remaining coverage to be allocated applying paragraph 50(a) are:

- (a) Estimates of the present value of future cash flows for claims and expenses released from the liability for remaining coverage because of incurred insurance service expenses;
- (b) Changes in the risk adjustment for non-financial risk recognised in surplus or deficit because of the release from risk; and
- (c) Insurance finance revenue or expenses.

52. The systematic allocation required by paragraph 50(a) shall result in the total amounts allocated to the loss component in accordance with paragraphs 48–50 being equal to zero by the end of the coverage period of a group of contracts.

Premium Allocation Approach

53. An entity may simplify the measurement of a group of insurance contracts using the premium allocation approach set out in paragraphs 55–59 if, and only if, at the inception of the group:

- (a) The entity reasonably expects that such simplification would produce a measurement of the liability for remaining coverage for the group that would not differ materially from the one that would be produced applying the requirements in paragraphs 32–52; or

- (b) The coverage period of each contract in the group (including insurance contract services arising from all premiums within the contract boundary determined at that date applying paragraph 34) is one year or less.
- 53.1 Notwithstanding paragraph 53, a public sector entity may choose to apply the premium allocation approach to insurance contracts issued.
- 54. The criterion in paragraph 53(a) is not met if at the inception of the group an entity expects significant variability in the fulfilment cash flows that would affect the measurement of the liability for remaining coverage during the period before a claim is incurred. Variability in the fulfilment cash flows increases with, for example:
 - (a) The extent of future cash flows relating to any derivatives embedded in the contracts; and
 - (b) The length of the coverage period of the group of contracts.
- 55. Using the premium allocation approach, an entity shall measure the liability for remaining coverage as follows:
 - (a) On initial recognition, the carrying amount of the liability is:
 - (i) The premiums, if any, received at initial recognition;
 - (ii) Minus any insurance acquisition cash flows at that date, unless the entity chooses to recognise the payments as an expense applying paragraph 59(a); and
 - (iii) Plus or minus any amount arising from the derecognition at that date of:
 - 1. Any asset for insurance acquisition cash flows applying paragraph 28C; and
 - 2. Any other asset or liability previously recognised for cash flows related to the group of contracts as specified in paragraph AG66A.
 - (b) At the end of each subsequent reporting period, the carrying amount of the liability is the carrying amount at the start of the reporting period:
 - (i) Plus the premiums received in the period;
 - (ii) Minus insurance acquisition cash flows; unless the entity chooses to recognise the payments as an expense applying paragraph 59(a);
 - (iii) Plus any amounts relating to the amortisation of insurance acquisition cash flows recognised as an expense in the reporting period; unless the entity chooses to recognise insurance acquisition cash flows as an expense applying paragraph 59(a);
 - (iv) Plus any adjustment to a financing component, applying paragraph 56;
 - (v) Minus the amount recognised as insurance revenue for services provided in that period (see paragraph AG126); and
 - (vi) Minus any investment component paid or transferred to the liability for incurred claims.
- 56. If insurance contracts in the group have a significant financing component, an entity shall adjust the carrying amount of the liability for remaining coverage to reflect the time value of money and the effect of financial risk using the discount rates specified in paragraph 36, as determined on initial recognition. The entity is not required to adjust the carrying amount of the liability for remaining coverage to reflect the time value of money and the effect of financial risk if, at initial recognition, the entity expects that the time between providing each part of the services and the related premium due date is no more than a year.
- 57. 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:
 - (a) The carrying amount of the liability for remaining coverage determined applying paragraph 55; and
 - (b) The fulfilment cash flows that relate to remaining coverage of the group, applying paragraphs 33–37 and AG36–AG92. However, if, in applying paragraph 59(b), the entity does not adjust the

liability for incurred claims for the time value of money and the effect of financial risk, it shall not include in the fulfilment cash flows any such adjustment.

58. To the extent that the fulfilment cash flows described in paragraph 57(b) exceed the carrying amount described in paragraph 57(a), the entity shall recognise a loss in surplus or deficit and increase the liability for remaining coverage.
59. In applying the premium allocation approach, an entity:
 - (a) May choose to recognise any insurance acquisition cash flows as expenses when it incurs those costs, provided that the coverage period of each contract in the group at initial recognition is no more than one year.
 - (b) Shall measure the liability for incurred claims for the group of insurance contracts at the fulfilment cash flows relating to incurred claims, applying paragraphs 33–37 and AG36–AG92. However, the entity is not required to adjust future cash flows for the time value of money and the effect of financial risk if those cash flows are expected to be paid or received in one year or less from the date the claims are incurred.

Reinsurance Contracts Held

60. The requirements in PBE IFRS 17 are modified for reinsurance contracts held, as set out in paragraphs 61–70A.
61. An entity shall divide portfolios of reinsurance contracts held applying paragraphs 14–24, except that the references to onerous contracts in those paragraphs shall be replaced with a reference to contracts on which there is a net gain on initial recognition. For some reinsurance contracts held, applying paragraphs 14–24 will result in a group that comprises a single contract.

Recognition

62. Instead of applying paragraph 25, an entity shall recognise a group of reinsurance contracts held from the earlier of the following:
 - (a) The beginning of the coverage period of the group of reinsurance contracts held; and
 - (b) The date the entity recognises an onerous group of underlying insurance contracts applying paragraph 25(c), if the entity entered into the related reinsurance contract held in the group of reinsurance contracts held at or before that date.
- 62A. Notwithstanding paragraph 62(a), an entity shall delay the recognition of a group of reinsurance contracts held that provide proportionate coverage until the date that any underlying insurance contract is initially recognised, if that date is later than the beginning of the coverage period of the group of reinsurance contracts held.

Measurement

63. In applying the measurement requirements of paragraphs 32–36 to reinsurance contracts held, to the extent that the underlying contracts are also measured applying those paragraphs, the entity shall 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. In addition, the entity shall include in the estimates of the present value of the future cash flows for the group of reinsurance contracts held the effect of any risk of non-performance by the issuer of the reinsurance contract, including the effects of collateral and losses from disputes.
64. Instead of applying paragraph 37, an entity shall determine the risk adjustment for non-financial risk so that it represents the amount of risk being transferred by the holder of the group of reinsurance contracts to the issuer of those contracts.
65. The requirements of paragraph 38 that relate to determining the contractual service margin on initial recognition are modified to reflect the fact that for a group of reinsurance contracts held there is no unearned surplus but instead a net cost or net gain on purchasing the reinsurance. Hence, unless paragraph 65A applies, on initial recognition the entity shall recognise any net cost or net gain on

purchasing the group of reinsurance contracts held as a contractual service margin measured at an amount equal to the sum of:

- (a) The fulfilment cash flows;
- (b) The amount derecognised at that date of any asset or liability previously recognised for cash flows related to the group of reinsurance contracts held;
- (c) Any cash flows arising at that date; and
- (d) Any revenue recognised in surplus or deficit applying paragraph 66A.

65A If the net cost of purchasing reinsurance coverage relates to events that occurred before the purchase of the group of reinsurance contracts held, notwithstanding the requirements of paragraph AG5, the entity shall recognise such a cost immediately in surplus or deficit as an expense.

66. Instead of applying paragraph 44, an entity shall measure the contractual service margin at the end of the reporting period for a group of reinsurance contracts held as the carrying amount determined at the start of the reporting period, adjusted for:

- (a) The effect of any new contracts added to the group (see paragraph 28);
- (b) Interest accreted on the carrying amount of the contractual service margin, measured at the discount rates specified in paragraph AG72(b);
- (ba) Revenue recognised in surplus or deficit in the reporting period applying paragraph 66A;
- (bb) Reversals of a loss-recovery component recognised applying paragraph 66B (see paragraph AG119F) to the extent those reversals are not changes in the fulfilment cash flows of the group of reinsurance contracts held;
- (c) Changes in the fulfilment cash flows, measured at the discount rates specified in paragraph AG72(c), to the extent that the change relates to future service, unless:
 - (i) The change results from a change in fulfilment cash flows allocated to a group of underlying insurance contracts that does not adjust the contractual service margin for the group of underlying insurance contracts; or
 - (ii) The change results from applying paragraphs 57–58 (on onerous contracts), if the entity measures a group of underlying insurance contracts applying the premium allocation approach.
- (d) The effect of any currency exchange differences arising on the contractual service margin; and
- (e) The amount recognised in surplus or deficit because of services received 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 of the group of reinsurance contracts held, applying paragraph AG119.

66A An entity shall adjust the contractual service margin of a group of reinsurance contracts held, and as a result recognise revenue, when the entity recognises a loss on initial recognition of an onerous group of underlying insurance contracts or on addition of onerous underlying insurance contracts to a group (see paragraphs AG119C–AG119E).

66B An entity shall establish (or adjust) a loss-recovery component of the asset for remaining coverage for a group of reinsurance contracts held depicting the recovery of losses recognised applying paragraphs 66(c)(i)–(ii) and 66A. The loss-recovery component determines the amounts that are presented in surplus or deficit as reversals of recoveries of losses from reinsurance contracts held and are consequently excluded from the allocation of premiums paid to the reinsurer (see paragraph AG119F).

67. Changes in the fulfilment cash flows that result from changes in the risk of non-performance by the issuer of a reinsurance contract held do not relate to future service and shall not adjust the contractual service margin.

68. Reinsurance contracts held cannot be onerous. Accordingly, the requirements of paragraphs 47–52 do not apply.

Premium Allocation Approach for Reinsurance Contracts Held

69. An entity may use the premium allocation approach set out in paragraphs 55–56 and 59 (adapted to reflect the features of reinsurance contracts held that differ from insurance contracts issued, for example the generation of expenses or reduction in expenses rather than revenue) to simplify the measurement of a group of reinsurance contracts held, if at the inception of the group:
- (a) The entity reasonably expects the resulting measurement would not differ materially from the result of applying the requirements in paragraphs 63–68; or
 - (b) The coverage period of each contract in the group of reinsurance contracts held (including insurance coverage from all premiums within the contract boundary determined at that date applying paragraph 34) is one year or less.
- 69.1 Notwithstanding paragraph 69, a public sector entity may choose to apply the premium allocation approach to reinsurance contracts held.
70. An entity cannot meet the condition in paragraph 69(a) if, at the inception of the group, an entity expects significant variability in the fulfilment cash flows that would affect the measurement of the asset for remaining coverage during the period before a claim is incurred. Variability in the fulfilment cash flows increases with, for example:
- (a) The extent of future cash flows relating to any derivatives embedded in the contracts; and
 - (b) The length of the coverage period of the group of reinsurance contracts held.
- 70A If an entity measures a group of reinsurance contracts held applying the premium allocation approach, the entity shall apply paragraph 66A by adjusting the carrying amount of the asset for remaining coverage instead of adjusting the contractual service margin.

Investment Contracts with Discretionary Participation Features

71. An investment contract with discretionary participation features does not include a transfer of significant insurance risk. Consequently, the requirements in PBE IFRS 17 for insurance contracts are modified for investment contracts with discretionary participation features as follows:
- (a) The date of initial recognition (see paragraphs 25 and 28) is the date the entity becomes party to the contract.
 - (b) The contract boundary (see paragraph 34) is modified so that cash flows are within the contract boundary if they result from a substantive obligation of the entity to deliver cash at a present or future date. The entity has no substantive obligation to deliver cash if it has the practical ability to set a price for the promise to deliver the cash that fully reflects the amount of cash promised and related risks.
 - (c) The allocation of the contractual service margin (see paragraphs 44(e) and 45(e)) is modified so that the entity shall recognise the contractual service margin over the duration of the group of contracts in a systematic way that reflects the transfer of investment services under the contract.

Modification and Derecognition**Modification of an Insurance Contract**

72. If the terms of an insurance contract are modified, for example by agreement between the parties to the contract or by a change in regulation, an entity shall derecognise the original contract and recognise the modified contract as a new contract, applying PBE IFRS 17 or other applicable Standards if, and only if, any of the conditions in (a)–(c) are satisfied. The exercise of a right included in the terms of a contract is not a modification. The conditions are that:
- (a) If the modified terms had been included at contract inception:
 - (i) The modified contract would have been excluded from the scope of PBE IFRS 17, applying paragraphs 3–8A;

- (ii) An entity would have separated different components from the host insurance contract applying paragraphs 10–13, resulting in a different insurance contract to which PBE IFRS 17 would have applied;
 - (iii) The modified contract would have had a substantially different contract boundary applying paragraph 34; or
 - (iv) The modified contract would have been included in a different group of contracts applying paragraphs 14–24.
- (b) The original contract met the definition of an insurance contract with direct participation features, but the modified contract no longer meets that definition, or vice versa; or
- (c) The entity applied the premium allocation approach in paragraphs 53–59 or paragraphs 69–70 to the original contract, but the modifications mean that the contract no longer meets the eligibility criteria for that approach in paragraph 53 or paragraph 69.
73. If a contract modification meets none of the conditions in paragraph 72, the entity shall treat changes in cash flows caused by the modification as changes in estimates of fulfilment cash flows by applying paragraphs 40–52.

Derecognition

74. **An entity shall derecognise an insurance contract when, and only when:**
- (a) **It is extinguished, i.e., when the obligation specified in the insurance contract expires or is discharged or cancelled; or**
 - (b) **Any of the conditions in paragraph 72 are met.**
75. When an insurance contract is extinguished, the entity is no longer at risk and is therefore no longer required to transfer any economic resources to satisfy the insurance contract. For example, when an entity buys reinsurance, it shall derecognise the underlying insurance contract(s) when, and only when, the underlying insurance contract(s) is or are extinguished.
76. An entity derecognises an insurance contract from within a group of contracts by applying the following requirements in PBE IFRS 17:
- (a) The fulfilment cash flows allocated to the group are adjusted to eliminate the present value of the future cash flows and risk adjustment for non-financial risk relating to the rights and obligations that have been derecognised from the group, applying paragraphs 40(a)(i) and 40(b);
 - (b) The contractual service margin of the group is adjusted for the change in fulfilment cash flows described in (a), to the extent required by paragraphs 44(c) and 45(c), unless paragraph 77 applies; and
 - (c) The number of coverage units for expected remaining insurance contract services is adjusted to reflect the coverage units derecognised from the group, and the amount of the contractual service margin recognised in surplus or deficit in the period is based on that adjusted number, applying paragraph AG119.
77. When an entity derecognises an insurance contract because it transfers the contract to a third party or derecognises an insurance contract and recognises a new contract applying paragraph 72, the entity shall instead of applying paragraph 76(b):
- (a) Adjust the contractual service margin of the group from which the contract has been derecognised, to the extent required by paragraphs 44(c) and 45(c), for the difference between (i) and either (ii) for contracts transferred to a third party or (iii) for contracts derecognised applying paragraph 72:
 - (i) The change in the carrying amount of the group of insurance contracts resulting from the derecognition of the contract, applying paragraph 76(a).
 - (ii) The premium charged by the third party.

- (iii) The premium the entity would have charged had it entered into a contract with equivalent terms as the new contract at the date of the contract modification, less any additional premium charged for the modification.
- (b) Measure the new contract recognised applying paragraph 72 assuming that the entity received the premium described in (a)(iii) at the date of the modification.

Presentation in the Statement of Financial Position

78. **An entity shall present separately in the statement of financial position the carrying amount of 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.**
79. An entity shall include any assets for insurance acquisition cash flows recognised applying paragraph 28B in the carrying amount of the related portfolios of insurance contracts issued, and any assets or liabilities for cash flows related to portfolios of reinsurance contracts held (see paragraph 65(b)) in the carrying amount of the portfolios of reinsurance contracts held.

Recognition and Presentation in the Statement of Comprehensive Revenue and Expense (paragraphs AG120–AG136)

80. **Applying paragraphs 41 and 42, an entity shall disaggregate the amounts recognised in the statement of comprehensive revenue and expense into:**
- (a) **An insurance service result (paragraphs 83–86), comprising insurance revenue and insurance service expenses; and**
 - (b) **Insurance finance revenue or expenses (paragraphs 87–92).**
81. An entity is not required to disaggregate the change in the risk adjustment for non-financial risk between the insurance service result and insurance finance revenue or expenses. If an entity does not make such a disaggregation, it shall include the entire change in the risk adjustment for non-financial risk as part of the insurance service result.
82. **An entity shall present revenue or expenses from reinsurance contracts held separately from the expenses or revenue from insurance contracts issued.**

Insurance Service Result

83. **An entity shall present in surplus or deficit insurance revenue arising from the groups of insurance contracts issued. Insurance revenue shall depict the provision of services arising from the group of insurance contracts at an amount that reflects the consideration to which the entity expects to be entitled in exchange for those services. Paragraphs AG120–AG127 specify how an entity measures insurance revenue.**
84. **An entity shall present in surplus or deficit insurance service expenses arising from a group of insurance contracts issued, comprising incurred claims (excluding repayments of investment components), other incurred insurance service expenses and other amounts as described in paragraph 103(b).**
85. **Insurance revenue and insurance service expenses presented in surplus or deficit shall exclude any investment components. An entity shall not present premium information in surplus or deficit if that information is inconsistent with paragraph 83.**
86. An entity may present the revenue or expenses from a group of reinsurance contracts held (see paragraphs 60–70), other than insurance finance revenue or expenses, as a single amount; or the entity may present separately the amounts recovered from the reinsurer and an allocation of the premiums paid that together give a net amount equal to that single amount. If an entity presents separately the amounts recovered from the reinsurer and an allocation of the premiums paid, it shall:

- (a) Treat reinsurance cash flows that are contingent on claims on the underlying contracts as part of the claims that are expected to be reimbursed under the reinsurance contract held;
- (b) Treat amounts from the reinsurer that it expects to receive that are not contingent on claims of the underlying contracts (for example, some types of ceding commissions) as a reduction in the premiums to be paid to the reinsurer;
- (ba) Treat amounts recognised relating to recovery of losses applying paragraphs 66(c)(i)–(ii) and 66A–66B as amounts recovered from the reinsurer; and
- (c) Not present the allocation of premiums paid as a reduction in revenue.

Insurance Finance Revenue or Expenses (see paragraphs AG128–AG136)

87. **Insurance finance revenue or expenses comprises the change in the carrying amount of the group of insurance contracts arising from:**
- (a) The effect of the time value of money and changes in the time value of money; and
 - (b) The effect of financial risk and changes in financial risk; but
 - (c) Excluding any such changes for groups of insurance contracts with direct participation features that would adjust the contractual service margin but do not do so when applying paragraphs 45(b)(ii), 45(b)(iii), 45(c)(ii) or 45(c)(iii). These are included in insurance service expenses.
- 87A **An entity shall apply:**
- (a) Paragraph AG117A to insurance finance revenue or expenses arising from the application of paragraph AG115 (risk mitigation); and
 - (b) Paragraphs 88 and 89 to all other insurance finance revenue or expenses.
88. **In applying paragraph 87A(b), unless paragraph 89 applies, an entity shall make an accounting policy choice between:**
- (a) Including insurance finance revenue or expenses for the period in surplus or deficit; or
 - (b) Disaggregating insurance finance revenue or expenses for the period to include in surplus or deficit an amount determined by a systematic allocation of the expected total insurance finance revenue or expenses over the duration of the group of contracts, applying paragraphs AG130–AG133.
89. **In applying paragraph 87A(b), for insurance contracts with direct participation features, for which the entity holds the underlying items, an entity shall make an accounting policy choice between:**
- (a) Including insurance finance revenue or expenses for the period in surplus or deficit; or
 - (b) Disaggregating insurance finance revenue or expenses for the period to include in surplus or deficit an amount that eliminates accounting mismatches with revenue or expenses included in surplus or deficit on the underlying items held, applying paragraphs AG134–AG136.
90. **If an entity chooses the accounting policy set out in paragraph 88(b) or in paragraph 89(b), it shall include in other comprehensive revenue and expense the difference between the insurance finance revenue or expenses measured on the basis set out in those paragraphs and the total insurance finance revenue or expenses for the period.**
91. **If an entity transfers a group of insurance contracts or derecognises an insurance contract applying paragraph 77:**
- (a) It shall reclassify to surplus or deficit as a reclassification adjustment (see PBE IPSAS 1 *Presentation of Financial Reports*) any remaining amounts for the group (or contract) that were previously recognised in other comprehensive revenue and expense because the entity chose the accounting policy set out in paragraph 88(b).
 - (b) It shall not reclassify to surplus or deficit as a reclassification adjustment (see PBE IPSAS 1) any remaining amounts for the group (or contract) that were previously recognised in other

comprehensive revenue and expense because the entity chose the accounting policy set out in paragraph 89(b).

92. Paragraph 30 requires an entity to treat an insurance contract as a monetary item under PBE IPSAS 4 for the purpose of translating foreign exchange items into the entity's functional currency. An entity includes exchange differences on changes in the carrying amount of groups of insurance contracts in the statement of surplus or deficit, unless they relate to changes in the carrying amount of groups of insurance contracts included in other comprehensive revenue and expense applying paragraph 90, in which case they shall be included in other comprehensive revenue and expense.

Disclosure

93. **The objective of the disclosure requirements is for an entity to disclose information in the notes that, together with the information provided in the statement of financial position, statement of comprehensive revenue and expense and cash flow statement, gives a basis for users of financial statements to assess the effect that contracts within the scope of PBE IFRS 17 have on the entity's financial position, financial performance and cash flows. To achieve that objective, an entity shall disclose qualitative and quantitative information about:**
- (a) **The amounts recognised in its financial statements for contracts within the scope of PBE IFRS 17 (see paragraphs 97–116);**
 - (b) **The significant judgements, and changes in those judgements, made when applying PBE IFRS 17 (see paragraphs 117–120); and**
 - (c) **The nature and extent of the risks from contracts within the scope of PBE IFRS 17 (see paragraphs 121–132).**
94. An entity shall consider the level of detail necessary to satisfy the disclosure objective and how much emphasis to place on each of the various requirements. If the disclosures provided, applying paragraphs 97–132, are not enough to meet the objective in paragraph 93, an entity shall disclose additional information necessary to meet that objective.
95. An entity shall aggregate or disaggregate information so that useful information is not obscured either by the inclusion of a large amount of insignificant detail or by the aggregation of items that have different characteristics.
96. Paragraphs 45–47 of PBE IPSAS 1 set out requirements relating to materiality and aggregation of information. Examples of aggregation bases that might be appropriate for information disclosed about insurance contracts are:
- (a) Type of contract (for example, major product lines); or
 - (b) Geographical area (for example, country or region).
 - (c) [Not used]

Explanation of Recognised Amounts

97. Of the disclosures required by paragraphs 98–109A, only those in paragraphs 98–100, 102–103, 105–105B and 109A apply to contracts to which the premium allocation approach has been applied. If an entity uses the premium allocation approach, it shall also disclose:
- (a) Which of the criteria in paragraphs 53 and 69 it has satisfied;
 - (b) Whether it makes an adjustment for the time value of money and the effect of financial risk applying paragraphs 56 and 57(b); and
 - (c) The method it has chosen to recognise insurance acquisition cash flows applying paragraph 59(a).
98. An entity shall disclose reconciliations that show how the net carrying amounts of contracts within the scope of PBE IFRS 17 changed during the period because of cash flows and revenue and expenses recognised in the statement of comprehensive revenue and expense. Separate reconciliations shall be disclosed for insurance contracts issued and reinsurance contracts held. An entity shall adapt the requirements of paragraphs 100–109 to reflect the features of reinsurance contracts held that differ from

- insurance contracts issued; for example, the generation of expenses or reduction in expenses rather than revenue.
99. An entity shall provide enough information in the reconciliations to enable users of financial statements to identify changes from cash flows and amounts that are recognised in the statement of comprehensive revenue and expense. To comply with this requirement, an entity shall:
 - (a) Disclose, in a table, the reconciliations set out in paragraphs 100–105B; and
 - (b) For each reconciliation, present the net carrying amounts at the beginning and at the end of the period, disaggregated into a total for portfolios of contracts that are assets and a total for portfolios of contracts that are liabilities, that equal the amounts presented in the statement of financial position applying paragraph 78.
 100. An entity shall disclose reconciliations from the opening to the closing balances separately for each of:
 - (a) The net liabilities (or assets) for the remaining coverage component, excluding any loss component.
 - (b) Any loss component (see paragraphs 47–52 and 57–58).
 - (c) The liabilities for incurred claims. For insurance contracts to which the premium allocation approach described in paragraphs 53–59 or 69–70A has been applied, an entity shall disclose separate reconciliations for:
 - (i) The estimates of the present value of the future cash flows; and
 - (ii) The risk adjustment for non-financial risk.
 101. For insurance contracts other than those to which the premium allocation approach described in paragraphs 53–59 or 69–70A has been applied, an entity shall also disclose reconciliations from the opening to the closing balances separately for each of:
 - (a) The estimates of the present value of the future cash flows;
 - (b) The risk adjustment for non-financial risk; and
 - (c) The contractual service margin.
 102. The objective of the reconciliations in paragraphs 100–101 is to provide different types of information about the insurance service result.
 103. An entity shall separately disclose in the reconciliations required in paragraph 100 each of the following amounts related to services, if applicable:
 - (a) Insurance revenue.
 - (b) Insurance service expenses, showing separately:
 - (i) Incurred claims (excluding investment components) and other incurred insurance service expenses;
 - (ii) Amortisation of insurance acquisition cash flows;
 - (iii) Changes that relate to past service, i.e., changes in fulfilment cash flows relating to the liability for incurred claims; and
 - (iv) Changes that relate to future service, i.e., losses on onerous groups of contracts and reversals of such losses.
 - (c) Investment components excluded from insurance revenue and insurance service expenses (combined with refunds of premiums unless refunds of premiums are presented as part of the cash flows in the period described in paragraph 105(a)(i)).
 104. An entity shall separately disclose in the reconciliations required in paragraph 101 each of the following amounts related to services, if applicable:
 - (a) Changes that relate to future service, applying paragraphs AG96–AG118, showing separately:
 - (i) Changes in estimates that adjust the contractual service margin;

- (ii) Changes in estimates that do not adjust the contractual service margin, i.e., losses on groups of onerous contracts and reversals of such losses; and
 - (iii) The effects of contracts initially recognised in the period.
 - (b) Changes that relate to current service, i.e.,:
 - (i) The amount of the contractual service margin recognised in surplus or deficit to reflect the transfer of services;
 - (ii) The change in the risk adjustment for non-financial risk that does not relate to future service or past service; and
 - (iii) Experience adjustments (see paragraphs AG97(c) and AG113(a)), excluding amounts relating to the risk adjustment for non-financial risk included in (ii).
 - (c) Changes that relate to past service, i.e., changes in fulfilment cash flows relating to incurred claims (see paragraphs AG97(b) and AG113(a)).
105. To complete the reconciliations in paragraphs 100–101, an entity shall also disclose separately each of the following amounts not related to services provided in the period, if applicable:
- (a) Cash flows in the period, including:
 - (i) Premiums received for insurance contracts issued (or paid for reinsurance contracts held);
 - (ii) Insurance acquisition cash flows; and
 - (iii) Incurred claims paid and other insurance service expenses paid for insurance contracts issued (or recovered under reinsurance contracts held), excluding insurance acquisition cash flows.
 - (b) The effect of changes in the risk of non-performance by the issuer of reinsurance contracts held;
 - (c) Insurance finance revenue or expenses; and
 - (d) Any additional line items that may be necessary to understand the change in the net carrying amount of the insurance contracts.
- 105A An entity shall disclose a reconciliation from the opening to the closing balance of assets for insurance acquisition cash flows recognised applying paragraph 28B. An entity shall aggregate information for the reconciliation at a level that is consistent with that for the reconciliation of insurance contracts, applying paragraph 98.
- 105B An entity shall separately disclose in the reconciliation required by paragraph 105A any impairment losses and reversals of impairment losses recognised applying paragraph 28E–28F.
106. For insurance contracts issued other than those to which the premium allocation approach described in paragraphs 53–59 has been applied, an entity shall disclose an analysis of the insurance revenue recognised in the period comprising:
- (a) The amounts relating to the changes in the liability for remaining coverage as specified in paragraph AG124, separately disclosing:
 - (i) The insurance service expenses incurred during the period as specified in paragraph AG124(a);
 - (ii) The change in the risk adjustment for non-financial risk, as specified in paragraph AG124(b);
 - (iii) The amount of the contractual service margin recognised in surplus or deficit because of the transfer of insurance contract services in the period, as specified in paragraph AG124(c); and
 - (iv) Other amounts, if any, for example, experience adjustments for premium receipts other than those that relate to future service as specified in paragraph AG124(d).
 - (b) The allocation of the portion of the premiums that relate to the recovery of insurance acquisition cash flows (see paragraph AG125).

107. For insurance contracts other than those to which the premium allocation approach described in paragraphs 53–59 or 69–70A has been applied, an entity shall disclose the effect on the statement of financial position separately for insurance contracts issued and reinsurance contracts held that are initially recognised in the period, showing their effect at initial recognition on:
- (a) The estimates of the present value of future cash outflows, showing separately the amount of the insurance acquisition cash flows;
 - (b) The estimates of the present value of future cash inflows;
 - (c) The risk adjustment for non-financial risk; and
 - (d) The contractual service margin.
108. In the disclosures required by paragraph 107, an entity shall separately disclose amounts resulting from:
- (a) Contracts acquired from other entities in transfers of insurance contracts or PBE combinations; and
 - (b) Groups of contracts that are onerous.
109. For insurance contracts other than those to which the premium allocation approach described in paragraphs 53–59 or 69–70A has been applied, an entity shall disclose when it expects to recognise the contractual service margin remaining at the end of the reporting period in surplus or deficit quantitatively, in appropriate time bands. Such information shall be provided separately for insurance contracts issued and reinsurance contracts held.
- 109A An entity shall disclose quantitatively, in appropriate time bands, when it expects to derecognise an asset for insurance acquisition cash flows applying paragraph 28C.

Insurance Finance Revenue or Expenses

110. An entity shall disclose and explain the total amount of insurance finance revenue or expenses in the reporting period. In particular, an entity shall explain the relationship between insurance finance revenue or expenses and the investment return on its assets, to enable users of its financial statements to evaluate the sources of finance revenue or expenses recognised in surplus or deficit and other comprehensive revenue and expense.
111. For contracts with direct participation features, the entity shall describe the composition of the underlying items and disclose their fair value.
112. For contracts with direct participation features, if an entity chooses not to adjust the contractual service margin for some changes in the fulfilment cash flows, applying paragraph AG115, it shall disclose the effect of that choice on the adjustment to the contractual service margin in the current period.
113. For contracts with direct participation features, if an entity changes the basis of disaggregation of insurance finance revenue or expenses between surplus or deficit and other comprehensive revenue and expense, applying paragraph AG135, it shall disclose, in the period when the change in approach occurred:
- (a) The reason why the entity was required to change the basis of disaggregation;
 - (b) The amount of any adjustment for each financial statement line item affected; and
 - (c) The carrying amount of the group of insurance contracts to which the change applied at the date of the change.

Transition Amounts

114. An entity shall provide disclosures that enable users of financial statements to identify the effect of groups of insurance contracts measured at the transition date applying the modified transition approach (see paragraphs 132.6–132.19A) or the fair value transition approach (see paragraphs 132.20–132.24B) on the contractual service margin and insurance revenue in subsequent periods. Hence an entity shall

disclose the reconciliation of the contractual service margin applying paragraph 101(c), and the amount of insurance revenue applying paragraph 103(a), separately for:

- (a) Insurance contracts that existed at the transition date to which the entity has applied the modified transition approach;
 - (b) Insurance contracts that existed at the transition date to which the entity has applied the fair value transition approach; and
 - (c) All other insurance contracts.
115. For all periods in which disclosures are made applying paragraphs 114(a) or 114(b), to enable users of financial statements to understand the nature and significance of the methods used and judgements applied in determining the transition amounts, an entity shall explain how it determined the measurement of insurance contracts at the transition date.
116. An entity that chooses to disaggregate insurance finance revenue or expenses between surplus or deficit and other comprehensive revenue and expense applies paragraphs 132.18(b), 132.19(b), 132.24(b) and 132.24(c) to determine the cumulative difference between the insurance finance revenue or expenses that would have been recognised in surplus or deficit and the total insurance finance revenue or expenses at the transition date for the groups of insurance contracts to which the disaggregation applies. For all periods in which amounts determined applying these paragraphs exist, the entity shall disclose a reconciliation from the opening to the closing balance of the cumulative amounts included in other comprehensive revenue and expense for financial assets measured at fair value through other comprehensive revenue and expense related to the groups of insurance contracts. The reconciliation shall include, for example, gains or losses recognised in other comprehensive revenue and expense in the period and gains or losses previously recognised in other comprehensive revenue and expense in previous periods reclassified in the period to surplus or deficit.

Significant Judgements in Applying PBE IFRS 17

117. An entity shall disclose the significant judgements and changes in judgements made in applying PBE IFRS 17. Specifically, an entity shall disclose the inputs, assumptions and estimation techniques used, including:
- (a) The methods used to measure insurance contracts within the scope of PBE IFRS 17 and the processes for estimating the inputs to those methods. Unless impracticable, an entity shall also provide quantitative information about those inputs.
 - (b) Any changes in the methods and processes for estimating inputs used to measure contracts, the reason for each change, and the type of contracts affected.
 - (c) To the extent not covered in (a), the approach used:
 - (i) To distinguish changes in estimates of future cash flows arising from the exercise of discretion from other changes in estimates of future cash flows for contracts without direct participation features (see paragraph AG98);
 - (ii) To determine the risk adjustment for non-financial risk, including whether changes in the risk adjustment for non-financial risk are disaggregated into an insurance service component and an insurance finance component or are presented in full in the insurance service result;
 - (iii) To determine discount rates;
 - (iv) To determine investment components; and
 - (v) To determine the relative weighting of the benefits provided by insurance coverage and investment-return service or by insurance coverage and investment-related service (see paragraphs AG119–AG119B).
118. If, applying paragraph 88(b) or paragraph 89(b), an entity chooses to disaggregate insurance finance revenue or expenses into amounts presented in surplus or deficit and amounts presented in other comprehensive revenue and expense, the entity shall disclose an explanation of the methods used to determine the insurance finance revenue or expenses recognised in surplus or deficit.

119. An entity shall disclose the confidence level used to determine the risk adjustment for non-financial risk. If the entity uses a technique other than the confidence level technique for determining the risk adjustment for non-financial risk, it shall disclose the technique used and the confidence level corresponding to the results of that technique.
120. An entity shall disclose the yield curve (or range of yield curves) used to discount cash flows that do not vary based on the returns on underlying items, applying paragraph 36. When an entity provides this disclosure in aggregate for a number of groups of insurance contracts, it shall provide such disclosures in the form of weighted averages, or relatively narrow ranges.

Nature and Extent of Risks that arise from Contracts within the Scope of PBE IFRS 17

121. An entity shall disclose information that enables users of its financial statements to evaluate the nature, amount, timing and uncertainty of future cash flows that arise from contracts within the scope of PBE IFRS 17. Paragraphs 122–132 contain requirements for disclosures that would normally be necessary to meet this requirement.
122. These disclosures focus on the insurance and financial risks that arise from insurance contracts and how they have been managed. Financial risks typically include, but are not limited to, credit risk, liquidity risk and market risk.
123. If the information disclosed about an entity's exposure to risk at the end of the reporting period is not representative of its exposure to risk during the period, the entity shall disclose that fact, the reason why the period-end exposure is not representative, and further information that is representative of its risk exposure during the period.
124. For each type of risk arising from contracts within the scope of PBE IFRS 17, an entity shall disclose:
- (a) The exposures to risks and how they arise;
 - (b) The entity's objectives, policies and processes for managing the risks and the methods used to measure the risks; and
 - (c) Any changes in (a) or (b) from the previous period.
125. For each type of risk arising from contracts within the scope of PBE IFRS 17, an entity shall disclose:
- (a) Summary quantitative information about its exposure to that risk at the end of the reporting period. This disclosure shall be based on the information provided internally to the entity's key management personnel.
 - (b) The disclosures required by paragraphs 127–132, to the extent not provided applying (a) of this paragraph.
126. An entity shall disclose information about the effect of the regulatory frameworks in which it operates; for example, minimum capital requirements or required interest-rate guarantees. If an entity applies paragraph 20 in determining the groups of insurance contracts to which it applies the recognition and measurement requirements of PBE IFRS 17, it shall disclose that fact.

All Types of Risk—Concentrations of Risk

127. An entity shall disclose information about concentrations of risk arising from contracts within the scope of PBE IFRS 17, including a description of how the entity determines the concentrations, and a description of the shared characteristic that identifies each concentration (for example, the type of insured event, industry, geographical area, or currency). Concentrations of financial risk might arise, for example, from interest-rate guarantees that come into effect at the same level for a large number of contracts. Concentrations of financial risk might also arise from concentrations of non-financial risk; for example, if an entity provides product liability protection to pharmaceutical companies and also holds investments in those companies.

Insurance and Market Risks—Sensitivity Analysis

128. An entity shall disclose information about sensitivities to changes in risk variables arising from contracts within the scope of PBE IFRS 17. To comply with this requirement, an entity shall disclose:
- (a) A sensitivity analysis that shows how surplus or deficit and net assets/equity would have been affected by changes in risk variables that were reasonably possible at the end of the reporting period:
 - (i) For insurance risk—showing the effect for insurance contracts issued, before and after risk mitigation by reinsurance contracts held; and
 - (ii) For each type of market risk—in a way that explains the relationship between the sensitivities to changes in risk variables arising from insurance contracts and those arising from financial assets held by the entity.
 - (b) The methods and assumptions used in preparing the sensitivity analysis; and
 - (c) Changes from the previous period in the methods and assumptions used in preparing the sensitivity analysis, and the reasons for such changes.
129. If an entity prepares a sensitivity analysis that shows how amounts different from those specified in paragraph 128(a) are affected by changes in risk variables and uses that sensitivity analysis to manage risks arising from contracts within the scope of PBE IFRS 17, it may use that sensitivity analysis in place of the analysis specified in paragraph 128(a). The entity shall also disclose:
- (a) An explanation of the method used in preparing such a sensitivity analysis and of the main parameters and assumptions underlying the information provided; and
 - (b) An explanation of the objective of the method used and of any limitations that may result in the information provided.

Insurance Risk—Claims Development

130. An entity shall disclose actual claims compared with previous estimates of the undiscounted amount of the claims (i.e., claims development). The disclosure about claims development shall start with the period when the earliest material claim(s) arose and for which there is still uncertainty about the amount and timing of the claims payments at the end of the reporting period; but the disclosure is not required to start more than 10 years before the end of the reporting period. The entity is not required to disclose information about the development of claims for which uncertainty about the amount and timing of the claims payments is typically resolved within one year. An entity shall reconcile the disclosure about claims development with the aggregate carrying amount of the groups of insurance contracts, which the entity discloses applying paragraph 100(c).

Credit Risk—Other Information

131. For credit risk that arises from contracts within the scope of PBE IFRS 17, an entity shall disclose:
- (a) The amount that best represents its maximum exposure to credit risk at the end of the reporting period, separately for insurance contracts issued and reinsurance contracts held; and
 - (b) Information about the credit quality of reinsurance contracts held that are assets.

Liquidity Risk—Other Information

132. For liquidity risk arising from contracts within the scope of PBE IFRS 17, an entity shall disclose:
- (a) A description of how it manages the liquidity risk.
 - (b) Separate maturity analyses for portfolios of insurance contracts issued that are liabilities and portfolios of reinsurance contracts held that are liabilities that show, as a minimum, net cash flows of the portfolios for each of the first five years after the reporting date and in aggregate beyond the first five years. An entity is not required to include in these analyses liabilities for remaining coverage measured applying paragraphs 55–59 and paragraphs 69–70A. The analyses may take the form of:

- (i) An analysis, by estimated timing, of the remaining contractual undiscounted net cash flows; or
- (ii) An analysis, by estimated timing, of the estimates of the present value of the future cash flows.
- (c) The amounts that are payable on demand, explaining the relationship between such amounts and the carrying amount of the related portfolios of contracts, if not disclosed applying (b) of this paragraph.

Commencement and Application

132.1 A not-for-profit public benefit entity shall apply PBE IFRS 17 for annual financial statements covering periods beginning on or after 1 January 2023. If an entity applies PBE IFRS 17 earlier, it shall disclose that fact. Early application is permitted for entities that apply PBE IPSAS 41 on or before the date of initial application of PBE IFRS 17.

132.2 For the purposes of the transition requirements in paragraphs 132.1 and 132.3–132.33:

- (a) The date of initial application is the beginning of the annual reporting period in which an entity first applies PBE IFRS 17; and
- (b) The transition date is the beginning of the annual reporting period immediately preceding the date of initial application.

132.2A *Initial Application of PBE IFRS 17 and PBE IPSAS 41—Comparative Information*, issued in June 2022, added paragraphs 132.28A–132.28E and 132.33A. An entity that chooses to apply paragraphs 132.28A–132.28E and 132.33A shall apply them on initial application of PBE IFRS 17.

Insurance Contracts in the Public Sector

132.2B.1 The amending Standard *Insurance Contracts in the Public Sector*, issued in June 2023 broadened the scope of PBE IFRS 17 to include public sector public benefit entities. It amended paragraph 2.2 (previously numbered as paragraph 2.1) and added paragraphs 2.1, 6.1, 6.2, 14.1, 16.1, 22.1, 25.1, 34.1–34.4, 53.1, 69.1, 132.5A.1, AG64.1, AG121.1 and the Appendix E.

132.2B.2 An entity applying the amendments in this amending Standard shall provide comparative information in respect of the preceding accounting period.

132.2B.3 An entity shall apply these amendments in accordance with the commencement and application date provisions in paragraphs 132.2B.4 – 132.2B.6. An entity that applies these amendments to an ‘early adoption accounting period’ shall disclose that fact.

When the amending Standard takes effect (section 27 Financial Reporting Act 2013)

132.2B.4 The amending Standard takes effect on the 28th day after the date of its publication under the Legislation Act 2019. The amending Standard was published on 22 June 2023 and takes effect on 20 July 2023.

Accounting period in relation to which the amending Standard commences to apply (section 28 Financial Reporting Act 2013)

132.2B.5 The accounting periods in relation to which this amending Standard commences to apply are:

- (a) For an **early adopter**, those accounting periods following, and including, the **early adoption accounting period**.
- (b) For any other reporting entity, those accounting periods following, and including, the first accounting period for the entity that begins on or after the **mandatory date**.

132.2B.6 In paragraph 132.2B.5:

Early adopter means a reporting entity that applies this amending Standard for an early adoption accounting period.

Early adoption accounting period means an accounting period of the early adopter:

- (a) That begins before the mandatory date but has not ended or does not end before this amending Standard takes effect (and to avoid doubt, that period may have begun before this amending Standard takes effect); and
- (b) For which the early adopter:
 - (i) First applies this amending Standard in preparing its financial report; and
 - (ii) Discloses in its financial report for that accounting period that this amending Standard has been applied for that period.

Mandatory date means 1 January 2026.

Transition

Full Transition Approach¹

- 132.3 Unless it is impracticable to do so, or paragraph 132.5A applies, an entity shall apply PBE IFRS 17 as if it had always been applied, except that:
- (a) An entity is not required to present the quantitative information required by paragraph 33(f) of PBE IPSAS 3 *Accounting Policies, Changes in Accounting Estimates and Errors*; and
 - (b) An entity shall not apply the option in paragraph AG115 for periods before the transition date. An entity may apply the option in paragraph AG115 prospectively on or after the transition date if, and only if, the entity designates risk mitigation relationships at or before the date it applies the option.
- 132.4 To apply PBE IFRS 17 using the full transition approach, an entity shall at the transition date:
- (a) Identify, recognise and measure each group of insurance contracts as if PBE IFRS 17 had always applied;
 - (aa) Identify, recognise and measure any assets for insurance acquisition cash flows as if PBE IFRS 17 had always applied (except that an entity is not required to apply the recoverability assessment in paragraph 28E before the transition date);
 - (b) Derecognise any existing balances that would not exist had PBE IFRS 17 always applied; and
 - (c) Recognise any resulting net difference in net assets/equity.
- 132.5 If, and only if, it is impracticable for an entity to apply the full transition approach for a group of insurance contracts, an entity shall apply the following approaches instead of applying paragraph 132.4(a):
- (a) The modified transition approach in paragraphs 132.6–132.19A, subject to paragraph 132.6(a); or
 - (b) The fair value transition approach in paragraphs 132.20–132.24B.
- 132.5A Notwithstanding paragraph 132.5, an entity may choose to apply the fair value transition approach in paragraphs 132.20–132.24B for a group of insurance contracts with direct participation features to which it could apply PBE IFRS 17 using the full transition approach if, and only if:
- (a) The entity chooses to apply the risk mitigation option in paragraph AG115 to the group of insurance contracts prospectively from the transition date; and
 - (b) The entity has used derivatives, non-derivative financial instruments measured at fair value through surplus or deficit, or reinsurance contracts held to mitigate financial risk arising from the group of insurance contracts, as specified in paragraph AG115, before the transition date.
- 132.5A.1 Notwithstanding paragraph 132.5A, a public sector entity with an arrangement constituting a liability for settlement of claims incurred before the liability was acquired in a transfer shall:
- (a) classify the liability as a liability for incurred claims and apply PBE IFRS 17 when the entity has previously asserted explicitly that it regards the liability as an insurance liability; and

¹ 'Full Transition Approach' was previously referred to as 'retrospectively'. This terminology has been updated for alignment with the New Zealand legislative framework.

- (b) classify the liability as a provision and apply PBE IPSAS 19 when the entity has not previously asserted explicitly that it regards the liability as an insurance liability.

132.5B If, and only if, it is impracticable for an entity to apply paragraph 132.4(aa) for an asset for insurance acquisition cash flows, the entity shall apply the following approaches to measure the asset for insurance acquisition cash flows:

- (a) The modified transition approach in paragraphs 132.14B–132.14D and 132.17A, subject to paragraph 132.6(a); or
- (b) The fair value transition approach in paragraphs 132.24A–132.24B.

Modified Transition Approach²

132.6 The objective of the modified transition approach is to achieve the closest possible outcome to the full transition approach using reasonable and supportable information available without undue cost or effort. Accordingly, in applying this approach, an entity shall:

- (a) Use reasonable and supportable information. If the entity cannot obtain reasonable and supportable information necessary to apply the modified transition approach, it shall apply the fair value transition approach.
- (b) Maximise the use of information that would have been used to apply a full transition approach, but need only use information available without undue cost or effort.

132.7 Paragraphs 132.9–132.19A set out permitted modifications to application of the full transition approach in the following areas:

- (a) Assessments of insurance contracts or groups of insurance contracts that would have been made at the date of inception or initial recognition;
- (b) Amounts related to the contractual service margin or loss component for insurance contracts without direct participation features;
- (c) Amounts related to the contractual service margin or loss component for insurance contracts with direct participation features; and
- (d) Insurance finance revenue or expenses.

132.8 To achieve the objective of the modified transition approach, an entity is permitted to use each modification in paragraphs 132.9–132.19A only to the extent that an entity does not have reasonable and supportable information to apply the full transition approach.

Assessments at Inception or Initial Recognition

132.9 To the extent permitted by paragraph 132.8, an entity shall determine the following matters using information available at the transition date:

- (a) How to identify groups of insurance contracts, applying paragraphs 14–24;
- (b) Whether an insurance contract meets the definition of an insurance contract with direct participation features, applying paragraphs AG101–AG109;
- (c) How to identify discretionary cash flows for insurance contracts without direct participation features, applying paragraphs AG98–AG100; and
- (d) Whether an investment contract meets the definition of an investment contract with discretionary participation features within the scope of PBE IFRS 17, applying paragraph 71.

132.9A To the extent permitted by paragraph 132.8, an entity shall classify as a liability for incurred claims a liability for settlement of claims incurred before an insurance contract was acquired in a transfer of insurance contracts that do not form an operation or in a PBE combination within the scope of PBE IPSAS 40.

² ‘Modified Transition Approach’ was previously referred to as ‘Modified Retrospective Approach’. This terminology has been updated for alignment with the New Zealand legislative framework.

- 132.10 To the extent permitted by paragraph 132.8, an entity shall not apply paragraph 22 to divide groups into those that do not include contracts issued more than one year apart.

Determining the Contractual Service Margin or Loss Component for Groups of Insurance Contracts without Direct Participation Features

- 132.11 To the extent permitted by paragraph 132.8, for contracts without direct participation features, an entity shall determine the contractual service margin or loss component of the liability for remaining coverage (see paragraphs 49–52) at the transition date by applying paragraphs 132.12–132.16C.
- 132.12 To the extent permitted by paragraph 132.8, an entity shall estimate the future cash flows at the date of initial recognition of a group of insurance contracts as the amount of the future cash flows at the transition date (or earlier date, if the future cash flows at that earlier date can be determined, applying paragraph 132.4(a)), adjusted by the cash flows that are known to have occurred between the date of initial recognition of a group of insurance contracts and the transition date (or earlier date). The cash flows that are known to have occurred include cash flows resulting from contracts that ceased to exist before the transition date.
- 132.13 To the extent permitted by paragraph 132.8, an entity shall determine the discount rates that applied at the date of initial recognition of a group of insurance contracts (or subsequently):
- (a) Using an observable yield curve that, for at least three years immediately before the transition date, approximates the yield curve estimated applying paragraphs 36 and AG72–AG85, if such an observable yield curve exists.
 - (b) If the observable yield curve in paragraph (a) does not exist, estimate the discount rates that applied at the date of initial recognition (or subsequently) by determining an average spread between an observable yield curve and the yield curve estimated applying paragraphs 36 and AG72–AG85, and applying that spread to that observable yield curve. That spread shall be an average over at least three years immediately before the transition date.
- 132.14 To the extent permitted by paragraph 132.8, an entity shall determine the risk adjustment for non-financial risk at the date of initial recognition of a group of insurance contracts (or subsequently) by adjusting the risk adjustment for non-financial risk at the transition date by the expected release of risk before the transition date. The expected release of risk shall be determined by reference to the release of risk for similar insurance contracts that the entity issues at the transition date.
- 132.14A Applying paragraph AG137, an entity may choose not to change the treatment of accounting estimates made in previous interim financial statements. To the extent permitted by paragraph 132.8, such an entity shall determine the contractual service margin or loss component at the transition date as if the entity had not prepared interim financial statements before the transition date.
- 132.14B To the extent permitted by paragraph 132.8, an entity shall use the same systematic and rational method the entity expects to use after the transition date when applying paragraph 28A to allocate any insurance acquisition cash flows paid (or for which a liability has been recognised applying another Standard) before the transition date (excluding any amount relating to insurance contracts that ceased to exist before the transition date) to:
- (a) Groups of insurance contracts that are recognised at the transition date; and
 - (b) Groups of insurance contracts that are expected to be recognised after the transition date.
- 132.14C Insurance acquisition cash flows paid before the transition date that are allocated to a group of insurance contracts recognised at the transition date adjust the contractual service margin of that group, to the extent insurance contracts expected to be in the group have been recognised at that date (see paragraphs 28C and AG35C). Other insurance acquisition cash flows paid before the transition date, including those allocated to a group of insurance contracts expected to be recognised after the transition date, are recognised as an asset, applying paragraph 28B.
- 132.14D If an entity does not have reasonable and supportable information to apply paragraph 132.14B, the entity shall determine the following amounts to be nil at the transition date:
- (a) The adjustment to the contractual service margin of a group of insurance contracts recognised at the transition date and any asset for insurance acquisition cash flows relating to that group; and

- (b) The asset for insurance acquisition cash flows for groups of insurance contracts expected to be recognised after the transition date.
- 132.15 If applying paragraphs 132.12–132.14D results in a contractual service margin at the date of initial recognition, to determine the contractual service margin at the date of transition an entity shall:
- (a) If the entity applies paragraph 132.13 to estimate the discount rates that apply on initial recognition, use those rates to accrete interest on the contractual service margin; and
 - (b) To the extent permitted by paragraph 132.8, determine the amount of the contractual service margin recognised in surplus or deficit because of the transfer of services before the transition date, by comparing the remaining coverage units at that date with the coverage units provided under the group of contracts before the transition date (see paragraph AG119).
- 132.16 If applying paragraphs 132.12–132.14D results in a loss component of the liability for remaining coverage at the date of initial recognition, an entity shall determine any amounts allocated to the loss component before the transition date applying paragraphs 132.12–132.14 and using a systematic basis of allocation.
- 132.16A For a group of reinsurance contracts held that provides coverage for an onerous group of insurance contracts and was entered into before or at the same time that the insurance contracts were issued, an entity shall establish a loss-recovery component of the asset for remaining coverage at the transition date (see paragraphs 66A–66B). To the extent permitted by paragraph 132.8, an entity shall determine the loss-recovery component by multiplying:
- (a) The loss component of the liability for remaining coverage for the underlying insurance contracts at the transition date (see paragraphs 132.16 and 132.20); and
 - (b) The percentage of claims for the underlying insurance contracts the entity expects to recover from the group of reinsurance contracts held.
- 132.16B Applying paragraphs 14–22, at the transition date an entity might include in an onerous group of insurance contracts both onerous insurance contracts covered by a group of reinsurance contracts held and onerous insurance contracts not covered by the group of reinsurance contracts held. To apply paragraph 132.16A in such cases, an entity shall use a systematic and rational basis of allocation to determine the portion of the loss component of the group of insurance contracts that relates to insurance contracts covered by the group of reinsurance contracts held.
- 132.16C If an entity does not have reasonable and supportable information to apply paragraph 132.16A, the entity shall not identify a loss-recovery component for the group of reinsurance contracts held.

Determining the Contractual Service Margin or Loss Component for Groups of Insurance Contracts with Direct Participation Features

- 132.17 To the extent permitted by paragraph 132.8, for contracts with direct participation features an entity shall determine the contractual service margin or loss component of the liability for remaining coverage at the transition date as:
- (a) The total fair value of the underlying items at that date; minus
 - (b) The fulfilment cash flows at that date; plus or minus
 - (c) An adjustment for:
 - (i) Amounts charged by the entity to the policyholders (including amounts deducted from the underlying items) before that date.
 - (ii) Amounts paid before that date that would not have varied based on the underlying items.
 - (iii) The change in the risk adjustment for non-financial risk caused by the release from risk before that date. The entity shall estimate this amount by reference to the release of risk for similar insurance contracts that the entity issues at the transition date.
 - (iv) Insurance acquisition cash flows paid (or for which a liability has been recognised applying another Standard) before the transition date that are allocated to the group (see paragraph 132.17A).

- (d) If (a)–(c) result in a contractual service margin—minus the amount of the contractual service margin that relates to services provided before that date. The total of (a)–(c) is a proxy for the total contractual service margin for all services to be provided under the group of contracts, i.e., before any amounts that would have been recognised in surplus or deficit for services provided. The entity shall estimate the amounts that would have been recognised in surplus or deficit for services provided by comparing the remaining coverage units at the transition date with the coverage units provided under the group of contracts before the transition date; or
- (e) If (a)–(c) result in a loss component—adjust the loss component to nil and increase the liability for remaining coverage excluding the loss component by the same amount.

132.17A To the extent permitted by paragraph 132.8, an entity shall apply paragraphs 132.14B–132.14D to recognise an asset for insurance acquisition cash flows, and any adjustment to the contractual service margin of a group of insurance contracts with direct participation features for insurance acquisition cash flows (see paragraph 132.17(c)(iv)).

Insurance Finance Revenue or Expenses

132.18 For groups of insurance contracts that, applying paragraph 132.10, include contracts issued more than one year apart:

- (a) An entity is permitted to determine the discount rates at the date of initial recognition of a group specified in paragraphs AG72(b)–AG72(e)(ii) and the discount rates at the date of the incurred claim specified in paragraph AG72(e)(iii) at the transition date instead of at the date of initial recognition or incurred claim.
- (b) If an entity chooses to disaggregate insurance finance revenue or expenses between amounts included in surplus or deficit and amounts included in other comprehensive revenue and expense applying paragraphs 88(b) or 89(b), the entity needs to determine the cumulative amount of insurance finance revenue or expenses recognised in other comprehensive revenue and expense at the transition date to apply paragraph 91(a) in future periods. The entity is permitted to determine that cumulative amount either by applying paragraph 132.19(b) or:
 - (i) As nil, unless (ii) applies; and
 - (ii) For insurance contracts with direct participation features to which paragraph AG134 applies, as equal to the cumulative amount recognised in other comprehensive revenue and expense on the underlying items.

132.19 For groups of insurance contracts that do not include contracts issued more than one year apart:

- (a) If an entity applies paragraph 132.13 to estimate the discount rates that applied at initial recognition (or subsequently), it shall also determine the discount rates specified in paragraphs AG72(b)–AG72(e) applying paragraph 132.13; and
- (b) If an entity chooses to disaggregate insurance finance revenue or expenses between amounts included in surplus or deficit and amounts included in other comprehensive revenue and expense, applying paragraphs 88(b) or 89(b), the entity needs to determine the cumulative amount of insurance finance revenue or expenses recognised in other comprehensive revenue and expense at the transition date to apply paragraph 91(a) in future periods. The entity shall determine that cumulative amount:
 - (i) For insurance contracts for which an entity will apply the methods of systematic allocation set out in paragraph AG131—if the entity applies paragraph 132.13 to estimate the discount rates at initial recognition—using the discount rates that applied at the date of initial recognition, also applying paragraph 132.13;
 - (ii) For insurance contracts for which an entity will apply the methods of systematic allocation set out in paragraph AG132—on the basis that the assumptions that relate to financial risk that applied at the date of initial recognition are those that apply on the transition date, i.e., as nil;
 - (iii) For insurance contracts for which an entity will apply the methods of systematic allocation set out in paragraph AG133—if the entity applies paragraph 132.13 to estimate the

discount rates at initial recognition (or subsequently)—using the discount rates that applied at the date of the incurred claim, also applying paragraph 132.13; and

- (iv) For insurance contracts with direct participation features to which paragraph AG134 applies—as equal to the cumulative amount recognised in other comprehensive revenue and expense on the underlying items.

132.19A Applying paragraph AG137, an entity may choose not to change the treatment of accounting estimates made in previous interim financial statements. To the extent permitted by paragraph 132.8, such an entity shall determine amounts related to insurance finance revenue or expenses at the transition date as if it had not prepared interim financial statements before the transition date.

Fair Value Transition Approach³

132.20 To apply the fair value transition approach, an entity shall determine the contractual service margin or loss component of the liability for remaining coverage at the transition date as the difference between the fair value of a group of insurance contracts at that date and the fulfilment cash flows measured at that date.

132.20A For a group of reinsurance contracts held to which paragraphs 66A–66B apply (without the need to meet the condition set out in paragraph AG119C), an entity shall determine the loss-recovery component of the asset for remaining coverage at the transition date by multiplying:

- (a) The loss component of the liability for remaining coverage for the underlying insurance contracts at the transition date (see paragraphs 132.16 and 132.20); and
- (b) The percentage of claims for the underlying insurance contracts the entity expects to recover from the group of reinsurance contracts held.

132.20B Applying paragraphs 14–22, at the transition date an entity might include in an onerous group of insurance contracts both onerous insurance contracts covered by a group of reinsurance contracts held and onerous insurance contracts not covered by the group of reinsurance contracts held. To apply paragraph 132.20A in such cases, an entity shall use a systematic and rational basis of allocation to determine the portion of the loss component of the group of insurance contracts that relates to insurance contracts covered by the group of reinsurance contracts held.

132.21 In applying the fair value transition approach, an entity may apply paragraph 132.22 to determine:

- (a) How to identify groups of insurance contracts, applying paragraphs 14–24;
- (b) Whether an insurance contract meets the definition of an insurance contract with direct participation features, applying paragraphs AG101–AG109;
- (c) How to identify discretionary cash flows for insurance contracts without direct participation features, applying paragraphs AG98–AG100; and
- (d) Whether an investment contract meets the definition of an investment contract with discretionary participation features within the scope of PBE IFRS 17, applying paragraph 71.

132.22 An entity may choose to determine the matters in paragraph 132.21 using:

- (a) Reasonable and supportable information for what the entity would have determined given the terms of the contract and the market conditions at the date of inception or initial recognition, as appropriate; or
- (b) Reasonable and supportable information available at the transition date.

132.22A In applying the fair value transition approach, an entity may choose to classify as a liability for incurred claims a liability for settlement of claims incurred before an insurance contract was acquired in a transfer of insurance contracts that do not form an operation or in a PBE combination within the scope of PBE IPSAS 40.

132.23 In applying the fair value transition approach, an entity is not required to apply paragraph 22, and may include in a group contracts issued more than one year apart. An entity shall only divide groups into those

³ 'Fair Value Transition Approach' was previously referred as 'Fair Value Approach'. This terminology has been updated for consistency in light of updates to the terminology of other transition approaches.

including only contracts issued within a year (or less) if it has reasonable and supportable information to make the division. Whether or not an entity applies paragraph 22, it is permitted to determine the discount rates at the date of initial recognition of a group specified in paragraphs AG72(b)–AG72(e)(ii) and the discount rates at the date of the incurred claim specified in paragraph AG72(e)(iii) at the transition date instead of at the date of initial recognition or incurred claim.

- 132.24 In applying the fair value transition approach, if an entity chooses to disaggregate insurance finance revenue or expenses between surplus or deficit and other comprehensive revenue and expense, it is permitted to determine the cumulative amount of insurance finance revenue or expenses recognised in other comprehensive revenue and expense at the transition date:
- (a) As if the requirements had always been applied—but only if it has reasonable and supportable information to do so; or
 - (b) As nil—unless (c) applies; and
 - (c) For insurance contracts with direct participation features to which paragraph AG134 applies—as equal to the cumulative amount recognised in other comprehensive revenue and expense from the underlying items.

Asset for Insurance Acquisition Cash Flows

- 132.24A In applying the fair value transition approach for an asset for insurance acquisition cash flows (see paragraph 132.5B(b)), at the transition date, an entity shall determine an asset for insurance acquisition cash flows at an amount equal to the insurance acquisition cash flows the entity would incur at the transition date for the rights to obtain:
- (a) Recoveries of insurance acquisition cash flows from premiums of insurance contracts issued before the transition date but not recognised at the transition date;
 - (b) Future insurance contracts that are renewals of insurance contracts recognised at the transition date and insurance contracts described in (a); and
 - (c) Future insurance contracts, other than those in (b), after the transition date without paying again insurance acquisition cash flows the acquiree has already paid that are directly attributable to the related portfolio of insurance contracts.

- 132.24B At the transition date, the entity shall exclude from the measurement of any groups of insurance contracts the amount of any asset for insurance acquisition cash flows.

Comparative Information

- 132.25 Notwithstanding the reference to the annual reporting period immediately preceding the date of initial application in paragraph 132.2(b), an entity may also present adjusted comparative information applying PBE IFRS 17 for any earlier periods presented, but is not required to do so. If an entity does present adjusted comparative information for any earlier periods, the reference to ‘the beginning of the annual reporting period immediately preceding the date of initial application’ in paragraph 132.2(b) shall be read as ‘the beginning of the earliest adjusted comparative period presented’.
- 132.26 An entity is not required to provide the disclosures specified in paragraphs 93–132 for any period presented before the beginning of the annual reporting period immediately preceding the date of initial application.
- 132.27 If an entity presents unadjusted comparative information and disclosures for any earlier periods, it shall clearly identify the information that has not been adjusted, disclose that it has been prepared on a different basis, and explain that basis.
- 132.28 An entity need not disclose previously unpublished information about claims development that occurred earlier than five years before the end of the annual reporting period in which it first applies PBE IFRS 17. However, if an entity does not disclose that information, it shall disclose that fact.

Entities that First Apply PBE IFRS 17 and PBE IPSAS 41 at the same time

- 132.28A An entity that first applies PBE IFRS 17 and PBE IPSAS 41 at the same time is permitted to apply paragraphs 132.28B–132.28E (classification overlay) for the purpose of presenting comparative

information about a financial asset if the comparative information for that financial asset has not been restated for PBE IPSAS 41. Comparative information for a financial asset will not be restated for PBE IPSAS 41 if either the entity chooses not to restate prior periods (see paragraph 173 of PBE IPSAS 41), or the entity restates prior periods but the financial asset has been derecognised during those prior periods (see paragraph 158 of PBE IPSAS 41).

- 132.28B An entity applying the classification overlay to a financial asset shall present comparative information as if the classification and measurement requirements of PBE IPSAS 41 had been applied to that financial asset. The entity shall use reasonable and supportable information available at the transition date (see paragraph 132.2(b)) to determine how the entity expects the financial asset would be classified and measured on initial application of PBE IPSAS 41 (for example, an entity might use preliminary assessments performed to prepare for the initial application of PBE IPSAS 41).
- 132.28C In applying the classification overlay to a financial asset, an entity is not required to apply the impairment requirements in paragraphs 73–93 of PBE IPSAS 41. If, based on the classification determined applying paragraph 132.28B, the financial asset would be subject to the impairment requirements in paragraphs 73–93 of PBE IPSAS 41 but the entity does not apply those requirements in applying the classification overlay, the entity shall continue to present any amount recognised in respect of impairment in the prior period in accordance with PBE IPSAS 29 *Financial Instruments: Recognition and Measurement*. Otherwise, any such amounts shall be reversed.
- 132.28D Any difference between the previous carrying amount of a financial asset and the carrying amount at the transition date that results from applying paragraphs 132.28B–132.28C shall be recognised in opening accumulated comprehensive revenue and expense (or other component of net assets/equity, as appropriate) at the transition date.
- 132.28E An entity that applies paragraphs 132.28B–132.28D shall:
- (a) Disclose qualitative information that enables users of financial statements to understand:
 - (i) The extent to which the classification overlay has been applied (for example, whether it has been applied to all financial assets derecognised in the comparative period);
 - (ii) Whether and to what extent the impairment requirements in paragraphs 73–93 of PBE IPSAS 41 have been applied (see paragraph 132.28C);
 - (b) Only apply those paragraphs to comparative information for reporting periods between the transition date to PBE IFRS 17 and the date of initial application of PBE IFRS 17 (see paragraphs 132.2 and 132.25); and
 - (c) At the date of initial application of PBE IPSAS 41, apply the transition requirements in PBE IPSAS 41 (see paragraphs 157.1–184A of PBE IPSAS 41).

Redesignation of Financial Assets

- 132.29 At the date of initial application of PBE IFRS 17, an entity that had applied PBE IPSAS 41 to annual reporting periods before the initial application of PBE IFRS 17:
- (a) May reassess whether an eligible financial asset meets the condition in paragraph 40 or paragraph 41 of PBE IPSAS 41. A financial asset is eligible only if the financial asset is not held in respect of an activity that is unconnected with contracts within the scope of PBE IFRS 17. Examples of financial assets that would not be eligible for reassessment are financial assets held in respect of banking activities or financial assets held in funds relating to investment contracts that are outside the scope of PBE IFRS 17.
 - (b) Shall revoke its previous designation of a financial asset as measured at fair value through surplus or deficit if the condition in paragraph 44 of PBE IPSAS 41 is no longer met because of the application of PBE IFRS 17.
 - (c) May designate a financial asset as measured at fair value through surplus or deficit if the condition in paragraph 44 of PBE IPSAS 41 is met.
 - (d) May designate an investment in an equity instrument as at fair value through other comprehensive revenue and expense applying paragraph 106 of PBE IPSAS 41.

- (e) May revoke its previous designation of an investment in an equity instrument as at fair value through other comprehensive revenue and expense applying paragraph 106 of PBE IPSAS 41.
- 132.30 An entity shall apply paragraph 132.29 on the basis of the facts and circumstances that exist at the date of initial application of PBE IFRS 17. An entity shall apply those designations and classifications as if they had always been applied. In doing so, the entity shall apply the relevant transition requirements in PBE IPSAS 41. The date of initial application for that purpose shall be deemed to be the date of initial application of PBE IFRS 17.
- 132.31 An entity that applies paragraph 132.29 is not required to restate prior period comparative information to reflect such changes in designations or classifications. The entity may restate prior period comparative information only if it is possible without the use of hindsight. If an entity restates prior period comparative information, the restated financial statements must reflect all the requirements of PBE IPSAS 41 for those affected financial assets. If an entity does not restate prior period comparative information, the entity shall recognise, in the opening accumulated comprehensive revenue and expense (or other component of net assets/equity, as appropriate) at the date of initial application, any difference between:
- (a) The previous carrying amount of those financial assets; and
 - (b) The carrying amount of those financial assets at the date of initial application.
- 132.32 When an entity applies paragraph 132.29, it shall disclose in that annual reporting period for those financial assets by class:
- (a) If paragraph 132.29(a) applies—its basis for determining eligible financial assets;
 - (b) If any of paragraphs 132.29(a)–132.29(e) apply:
 - (i) The measurement category and carrying amount of the affected financial assets determined immediately before the date of initial application of PBE IFRS 17; and
 - (ii) The new measurement category and carrying amount of the affected financial assets determined after applying paragraph 132.29.
 - (c) If paragraph 132.29(b) applies—the carrying amount of financial assets in the statement of financial position that were previously designated as measured at fair value through surplus or deficit applying paragraph 44 of PBE IPSAS 41 that are no longer so designated.
- 132.33 When an entity applies paragraph 132.29, the entity shall disclose in that annual reporting period qualitative information that would enable users of financial statements to understand:
- (a) How it applied paragraph 132.29 to financial assets the classification of which has changed on initially applying PBE IFRS 17;
 - (b) The reasons for any designation or de-designation of financial assets as measured at fair value through surplus or deficit applying paragraph 44 of PBE IPSAS 41; and
 - (c) Why the entity came to any different conclusions in the new assessment applying paragraphs 40(a) or 41(a) of PBE IPSAS 41.
- 132.33A For a financial asset derecognised between the transition date and date of initial application of PBE IFRS 17, an entity may apply paragraphs 132.28B–132.28E (classification overlay) for the purpose of presenting comparative information as if paragraph 132.29 had been applied to that asset. Such an entity shall adapt the requirements of paragraphs 132.28B–132.28E so that the classification overlay is based on how the entity expects the financial asset would be designated applying paragraph 132.29 at the date of initial application of PBE IFRS 17.

Withdrawal and Replacement of PBE IFRS 4

- 132.34 PBE IFRS 17 supersedes PBE IFRS 4 *Insurance Contracts*.

Appendix A

Defined terms

[Not used]

Appendix B

Application Guidance

This Appendix is an integral part of PBE IFRS 17 Insurance Contracts

AG1. This appendix provides guidance on the following:

- (a) Definition of an insurance contract (see paragraphs AG2–AG30);
- (b) Separation of components from an insurance contract (see paragraphs AG31–AG35);
- (ba) Asset for reinsurance acquisition cash flows (see paragraphs AG35A–AG35D);
- (c) Measurement (see paragraphs AG36–AG119F);
- (d) Insurance revenue (see paragraphs AG120–AG127);
- (e) Insurance finance revenue or expenses (see paragraphs AG128–AG136); and
- (f) Interim financial statements (see paragraph AG137).

Definition of an Insurance Contract (paragraph 13.1)

AG2. This section provides guidance on the definition of an insurance contract as specified in paragraph 13.1. It addresses the following:

- (a) Uncertain future event (see paragraphs AG3–AG5);
- (b) Payments in kind (see paragraph AG6);
- (c) The distinction between insurance risk and other risks (see paragraphs AG7–AG16);
- (d) Significant insurance risk (see paragraphs AG17–AG23);
- (e) Changes in the level of insurance risk (see paragraphs AG24–AG25); and
- (f) Examples of insurance contracts (see paragraphs AG26–AG30).

Uncertain Future Event

AG3. Uncertainty (or risk) is the essence of an insurance contract. Accordingly, at least one of the following is uncertain at the inception of an insurance contract:

- (a) The probability of an insured event occurring;
- (b) When the insured event will occur; or
- (c) How much the entity will need to pay if the insured event occurs.

AG4. In some insurance contracts, the insured event is the discovery of a loss during the term of the contract, even if that loss arises from an event that occurred before the inception of the contract. In other insurance contracts, the insured event is an event that occurs during the term of the contract, even if the resulting loss is discovered after the end of the contract term.

AG5. Some insurance contracts cover events that have already occurred but the financial effect of which is still uncertain. An example is an insurance contract that provides insurance coverage against an adverse development of an event that has already occurred. In such contracts, the insured event is the determination of the ultimate cost of those claims.

Payments in Kind

AG6. Some insurance contracts require or permit payments to be made in kind. In such cases, the entity provides goods or services to the policyholder to settle the entity's obligation to compensate the policyholder for insured events. An example is when the entity replaces a stolen article instead of reimbursing the policyholder for the amount of its loss. Another example is when an entity uses its own hospitals and medical staff to provide medical services covered by the insurance contract. Such contracts are insurance contracts, even though the claims are settled in kind. Fixed-fee service contracts that meet

the conditions specified in paragraph 8 are also insurance contracts, but applying paragraph 8, an entity may choose to account for them applying either PBE IFRS 17 or PBE IPSAS 9 *Revenue from Exchange Transactions*.

The Distinction between Insurance Risk and Other Risks

- AG7. The definition of an insurance contract requires that one party accepts significant insurance risk from another party. PBE IFRS 17 defines insurance risk as ‘risk, other than financial risk, transferred from the holder of a contract to the issuer’. A contract that exposes the issuer to financial risk without significant insurance risk is not an insurance contract.
- AG8. The definition of financial risk in paragraph 13.1 refers to financial and non-financial variables. Examples of non-financial variables not specific to a party to the contract include an index of earthquake losses in a particular region or temperatures in a particular city. Financial risk excludes risk from non-financial variables that are specific to a party to the contract, such as the occurrence or non-occurrence of a fire that damages or destroys an asset of that party. Furthermore, the risk of changes in the fair value of a non-financial asset is not a financial risk if the fair value reflects changes in the market prices for such assets (i.e., a financial variable) and the condition of a specific non-financial asset held by a party to a contract (i.e., a non-financial variable). For example, if a guarantee of the residual value of a specific car in which the policyholder has an insurable interest exposes the guarantor to the risk of changes in the car’s physical condition, that risk is insurance risk, not financial risk.
- AG9. Some contracts expose the issuer to financial risk in addition to significant insurance risk. For example, many life insurance contracts guarantee a minimum rate of return to policyholders, creating financial risk, and at the same time promise death benefits that may significantly exceed the policyholder’s account balance, creating insurance risk in the form of mortality risk. Such contracts are insurance contracts.
- AG10. Under some contracts, an insured event triggers the payment of an amount linked to a price index. Such contracts are insurance contracts, provided that the payment contingent on the insured event could be significant. For example, a life-contingent annuity linked to a cost-of-living index transfers insurance risk because the payment is triggered by an uncertain future event—the survival of the person who receives the annuity. The link to the price index is a derivative, but it also transfers insurance risk because the number of payments to which the index applies depends on the survival of the annuitant. If the resulting transfer of insurance risk is significant, the derivative meets the definition of an insurance contract, in which case it shall not be separated from the host contract (see paragraph 11(a)).
- AG11. Insurance risk is the risk the entity accepts from the policyholder. This means the entity must accept, from the policyholder, a risk to which the policyholder was already exposed. Any new risk created by the contract for the entity or the policyholder is not insurance risk.
- AG12. The definition of an insurance contract refers to an adverse effect on the policyholder. This definition does not limit the payment by the entity to an amount equal to the financial effect of the adverse event. For example, the definition includes ‘new for old’ insurance coverage that pays the policyholder an amount that permits the replacement of a used and damaged asset with a new one. Similarly, the definition does not limit the payment under a life insurance contract to the financial loss suffered by the deceased’s dependants, nor does it exclude contracts that specify the payment of predetermined amounts to quantify the loss caused by death or an accident.
- AG13. Some contracts require a payment if a specified uncertain future event occurs, but do not require an adverse effect on the policyholder as a precondition for the payment. This type of contract is not an insurance contract even if the holder uses it to mitigate an underlying risk exposure. For example, if the holder uses a derivative to hedge an underlying financial or non-financial variable correlated with the cash flows from an asset of the entity, the derivative is not an insurance contract because the payment is not conditional on whether the holder is adversely affected by a reduction in the cash flows from the asset. The definition of an insurance contract refers to an uncertain future event for which an adverse effect on the policyholder is a contractual precondition for payment. A contractual precondition does not require the entity to investigate whether the event actually caused an adverse effect, but it does permit the entity to deny the payment if it is not satisfied that the event did cause an adverse effect.
- AG14. Lapse or persistency risk (the risk that the policyholder will cancel the contract earlier or later than the issuer had expected when pricing the contract) is not insurance risk because the resulting variability in the payment to the policyholder is not contingent on an uncertain future event that adversely affects the

policyholder. Similarly, expense risk (i.e., the risk of unexpected increases in the administrative costs associated with the servicing of a contract, rather than in the costs associated with insured events) is not insurance risk because an unexpected increase in such expenses does not adversely affect the policyholder.

- AG15. Consequently, a contract that exposes the entity to lapse risk, persistency risk or expense risk is not an insurance contract unless it also exposes the entity to significant insurance risk. However, if the entity mitigates its risk by using a second contract to transfer part of the non-insurance risk to another party, the second contract exposes the other party to insurance risk.
- AG16. An entity can accept significant insurance risk from the policyholder only if the entity is separate from the policyholder. In the case of a mutual entity, the mutual entity accepts risk from each policyholder and pools that risk. Although policyholders bear that pooled risk collectively because they hold the residual interest in the entity, the mutual entity is a separate entity that has accepted the risk.

Significant Insurance Risk

- AG17. A contract is an insurance contract only if it transfers significant insurance risk. Paragraphs AG7–AG16 discuss insurance risk. Paragraphs AG18–AG23 discuss the assessment of whether the insurance risk is significant.
- AG18. Insurance risk is significant if, and only if, an insured event could cause the issuer to pay additional amounts that are significant in any single scenario, excluding scenarios that have no commercial substance (i.e., no discernible effect on the economics of the transaction). If an insured event could mean significant additional amounts would be payable in any scenario that has commercial substance, the condition in the previous sentence can be met even if the insured event is extremely unlikely, or even if the expected (i.e., probability-weighted) present value of the contingent cash flows is a small proportion of the expected present value of the remaining cash flows from the insurance contract.
- AG19. In addition, a contract transfers significant insurance risk only if there is a scenario that has commercial substance in which the issuer has a possibility of a loss on a present value basis. However, even if a reinsurance contract does not expose the issuer to the possibility of a significant loss, that contract is deemed to transfer significant insurance risk if it transfers to the reinsurer substantially all the insurance risk relating to the reinsured portions of the underlying insurance contracts.
- AG20. The additional amounts described in paragraph AG18 are determined on a present-value basis. If an insurance contract requires payment when an event with uncertain timing occurs and if the payment is not adjusted for the time value of money, there may be scenarios in which the present value of the payment increases, even if its nominal value is fixed. An example is insurance that provides a fixed death benefit when the policyholder dies, with no expiry date for the cover (often referred to as whole-life insurance for a fixed amount). It is certain that the policyholder will die, but the date of death is uncertain. Payments may be made when an individual policyholder dies earlier than expected. Because those payments are not adjusted for the time value of money, significant insurance risk could exist even if there is no overall loss on the portfolio of contracts. Similarly, contractual terms that delay timely reimbursement to the policyholder can eliminate significant insurance risk. An entity shall use the discount rates required in paragraph 36 to determine the present value of the additional amounts.
- AG21. The additional amounts described in paragraph AG18 refer to the present value of amounts that exceed those that would be payable if no insured event had occurred (excluding scenarios that lack commercial substance). Those additional amounts include claims handling and assessment costs, but exclude:
- (a) The loss of the ability to charge the policyholder for future service. For example, in an investment-linked life insurance contract, the death of the policyholder means that the entity can no longer perform investment management services and collect a fee for doing so. However, this economic loss for the entity does not result from insurance risk, just as a mutual fund manager does not take on insurance risk in relation to the possible death of a client. Consequently, the potential loss of future investment management fees is not relevant when assessing how much insurance risk is transferred by a contract.
 - (b) A waiver, on death, of charges that would be made on cancellation or surrender. Because the contract brought those charges into existence, their waiver does not compensate the policyholder

for a pre-existing risk. Consequently, they are not relevant when assessing how much insurance risk is transferred by a contract.

- (c) A payment conditional on an event that does not cause a significant loss to the holder of the contract. For example, consider a contract that requires the issuer to pay CU1 million⁴ if an asset suffers physical damage that causes an insignificant economic loss of CU1 to the holder. In this contract, the holder transfers the insignificant risk of losing CU1 to the issuer. At the same time, the contract creates a non-insurance risk that the issuer will need to pay CU999,999 if the specified event occurs. Because there is no scenario in which an insured event causes a significant loss to the holder of the contract, the issuer does not accept significant insurance risk from the holder and this contract is not an insurance contract.
 - (d) Possible reinsurance recoveries. The entity accounts for these separately.
- AG22. An entity shall assess the significance of insurance risk contract by contract. Consequently, the insurance risk can be significant even if there is minimal probability of significant losses for a portfolio or group of contracts.
- AG23. It follows from paragraphs AG18–AG22 that, if a contract pays a death benefit that exceeds the amount payable on survival, the contract is an insurance contract unless the additional death benefit is not significant (judged by reference to the contract itself rather than to an entire portfolio of contracts). As noted in paragraph AG21(b), the waiver on death of cancellation or surrender charges is not included in this assessment if that waiver does not compensate the policyholder for a pre-existing risk. Similarly, an annuity contract that pays out regular sums for the rest of a policyholder's life is an insurance contract, unless the aggregate life-contingent payments are insignificant.

Changes in the Level of Insurance Risk

- AG24. For some contracts, the transfer of insurance risk to the issuer occurs after a period of time. For example, consider a contract that provides a specified investment return and includes an option for the policyholder to use the proceeds of the investment on maturity to buy a life-contingent annuity at the same rates the entity charges other new annuitants at the time the policyholder exercises that option. Such a contract transfers insurance risk to the issuer only after the option is exercised, because the entity remains free to price the annuity on a basis that reflects the insurance risk that will be transferred to the entity at that time. Consequently, the cash flows that would occur on the exercise of the option fall outside the boundary of the contract, and before exercise there are no insurance cash flows within the boundary of the contract. However, if the contract specifies the annuity rates (or a basis other than market rates for setting the annuity rates), the contract transfers insurance risk to the issuer because the issuer is exposed to the risk that the annuity rates will be unfavourable to the issuer when the policyholder exercises the option. In that case, the cash flows that would occur when the option is exercised are within the boundary of the contract.
- AG25. A contract that meets the definition of an insurance contract remains an insurance contract until all rights and obligations are extinguished (i.e., discharged, cancelled or expired), unless the contract is derecognised applying paragraphs 74–77, because of a contract modification.

Examples of Insurance Contracts

- AG26. The following are examples of contracts that are insurance contracts if the transfer of insurance risk is significant:
- (a) Insurance against theft or damage.
 - (b) Insurance against product liability, professional liability, civil liability or legal expenses.
 - (c) Life insurance and prepaid funeral plans (although death is certain, it is uncertain when death will occur or, for some types of life insurance, whether death will occur within the period covered by the insurance).
 - (d) Life-contingent annuities and pensions, i.e., contracts that provide compensation for the uncertain future event—the survival of the annuitant or pensioner—to provide the annuitant or pensioner

⁴ CU denotes currency unit.

with a level of income that would otherwise be adversely affected by his or her survival. (Employers' liabilities that arise from employee benefit plans and retirement benefit obligations reported by defined benefit retirement plans are outside the scope of PBE IFRS 17, applying paragraph 7(b)).

- (e) Insurance against disability and medical costs.
- (f) Surety bonds, fidelity bonds, performance bonds and bid bonds, i.e., contracts that compensate the holder if another party fails to perform a contractual obligation; for example, an obligation to construct a building.
- (g) Product warranties. Product warranties issued by another party for goods sold by a manufacturer, dealer or retailer are within the scope of PBE IFRS 17. However, product warranties issued directly by a manufacturer, dealer or retailer are outside the scope of PBE IFRS 17 applying paragraph 7(a), and are instead within the scope of PBE IPSAS 19 *Provisions, Contingent Liabilities and Contingent Assets*.
- (h) Title insurance (insurance against the discovery of defects in the title to land or buildings that were not apparent when the insurance contract was issued). In this case, the insured event is the discovery of a defect in the title, not the defect itself.
- (i) Travel insurance (compensation in cash or in kind to policyholders for losses suffered in advance of, or during, travel).
- (j) Catastrophe bonds that provide for reduced payments of principal, interest or both, if a specified event adversely affects the issuer of the bond (unless the specified event does not create significant insurance risk; for example, if the event is a change in an interest rate or a foreign exchange rate).
- (k) Insurance swaps and other contracts that require a payment depending on changes in climatic, geological or other physical variables that are specific to a party to the contract.

AG27. The following are examples of items that are not insurance contracts:

- (a) Investment contracts that have the legal form of an insurance contract but do not transfer significant insurance risk to the issuer. For example, life insurance contracts in which the entity bears no significant mortality or morbidity risk are not insurance contracts; such contracts are financial instruments or service contracts—see paragraph AG28. Investment contracts with discretionary participation features do not meet the definition of an insurance contract; however, they are within the scope of PBE IFRS 17 provided they are issued by an entity that also issues insurance contracts, applying paragraph 3(c).
- (b) Contracts that have the legal form of insurance, but return all significant insurance risk to the policyholder through non-cancellable and enforceable mechanisms that adjust future payments by the policyholder to the issuer as a direct result of insured losses. For example, some financial reinsurance contracts or some group contracts return all significant insurance risk to the policyholders; such contracts are normally financial instruments or service contracts (see paragraph AG28).
- (c) Self-insurance (i.e., retaining a risk that could have been covered by insurance). In such situations, there is no insurance contract because there is no agreement with another party. Thus, if an entity issues an insurance contract to its parent, subsidiary or fellow subsidiary, there is no insurance contract in the consolidated financial statements because there is no contract with another party. However, for the individual or separate financial statements of the issuer or holder, there is an insurance contract.
- (d) Contracts (such as gambling contracts) that require a payment if a specified uncertain future event occurs, but do not require, as a contractual precondition for payment, the event to adversely affect the policyholder. However, this does not exclude from the definition of an insurance contract contracts that specify a predetermined payout to quantify the loss caused by a specified event such as a death or an accident (see paragraph AG12).
- (e) Derivatives that expose a party to financial risk but not insurance risk, because the derivatives require that party to make (or give them the right to receive) payment solely based on the changes in one or more of a specified interest rate, a financial instrument price, a commodity price, a

foreign exchange rate, an index of prices or rates, a credit rating or a credit index or any other variable, provided that, in the case of a non-financial variable, the variable is not specific to a party to the contract.

- (f) Credit-related guarantees that require payments even if the holder has not incurred a loss on the failure of the debtor to make payments when due; such contracts are accounted for applying PBE IPSAS 41 *Financial Instruments* (see paragraph AG29).
- (g) Contracts that require a payment that depends on a climatic, geological or any other physical variable not specific to a party to the contract (commonly described as weather derivatives).
- (h) Contracts that provide for reduced payments of principal, interest or both, that depend on a climatic, geological or any other physical variable, the effect of which is not specific to a party to the contract (commonly referred to as catastrophe bonds).

AG28. An entity shall apply other applicable Standards, such as PBE IPSAS 41 and PBE IPSAS 9, to the contracts described in paragraph AG27.

AG29. The credit-related guarantees and credit insurance contracts discussed in paragraph AG27(f) can have various legal forms, such as that of a guarantee, some types of letters of credit, a credit default contract or an insurance contract. Those contracts are insurance contracts if they require the issuer to make specified payments to reimburse the holder for a loss that the holder incurs because a specified debtor fails to make payment when due to the policyholder applying the original or modified terms of a debt instrument. However, such insurance contracts are excluded from the scope of PBE IFRS 17 unless the issuer has previously asserted explicitly that it regards the contracts as insurance contracts and has used accounting applicable to insurance contracts (see paragraph 7(e)).

AG30. Credit-related guarantees and credit insurance contracts that require payment, even if the policyholder has not incurred a loss on the failure of the debtor to make payments when due, are outside the scope of PBE IFRS 17 because they do not transfer significant insurance risk. Such contracts include those that require payment:

- (a) Regardless of whether the counterparty holds the underlying debt instrument; or
- (b) On a change in the credit rating or the credit index, rather than on the failure of a specified debtor to make payments when due.

Separating Components from an Insurance Contract (paragraphs 10–13)

Investment Components (paragraph 11(b))

AG31. Paragraph 11(b) requires an entity to separate a distinct investment component from the host insurance contract. An investment component is distinct if, and only if, both the following conditions are met:

- (a) The investment component and the insurance component are not highly interrelated.
- (b) A contract with equivalent terms is sold, or could be sold, separately in the same market or the same jurisdiction, either by entities that issue insurance contracts or by other parties. The entity shall take into account all information reasonably available in making this determination. The entity is not required to undertake an exhaustive search to identify whether an investment component is sold separately.

AG32. An investment component and an insurance component are highly interrelated if, and only if:

- (a) The entity is unable to measure one component without considering the other. Thus, if the value of one component varies according to the value of the other, an entity shall apply PBE IFRS 17 to account for the combined investment and insurance component; or
- (b) The policyholder is unable to benefit from one component unless the other is also present. Thus, if the lapse or maturity of one component in a contract causes the lapse or maturity of the other, the entity shall apply PBE IFRS 17 to account for the combined investment component and insurance component.

Promises to Transfer Distinct Goods or Services other than Insurance Contract Services (paragraph 12)

- AG33. Paragraph 12 requires an entity to separate from an insurance contract a promise to transfer distinct goods or services other than insurance contract services to a policyholder. For the purpose of separation, an entity shall not consider activities that an entity must undertake to fulfil a contract unless the entity transfers a good or service other than insurance contract services to the policyholder as those activities occur. For example, an entity may need to perform various administrative tasks to set up a contract. The performance of those tasks does not transfer a service to the policyholder as the tasks are performed.
- AG34. A good or service other than insurance contract services promised to a policyholder is distinct if the policyholder can benefit from the good or service either on its own or together with other resources readily available to the policyholder. Readily available resources are goods or services that are sold separately (by the entity or by another entity), or resources that the policyholder has already got (from the entity or from other transactions or events).
- AG35. A good or service other than insurance contract services that is promised to the policyholder is not distinct if:
- (a) The cash flows and risks associated with the good or service are highly interrelated with the cash flows and risks associated with the insurance components in the contract; and
 - (b) The entity provides a significant service in integrating the good or service with the insurance components.

Insurance Acquisition Cash Flows (paragraphs 28A–28F)

AG35A To apply paragraph 28A, an entity shall use a systematic and rational method to allocate:

- (a) Insurance acquisition cash flows directly attributable to a group of insurance contracts:
 - (i) To that group; and
 - (ii) To groups that will include insurance contracts that are expected to arise from renewals of the insurance contracts in that group.
- (b) Insurance acquisition cash flows directly attributable to a portfolio of insurance contracts, other than those in (a), to groups of contracts in the portfolio.

AG35B At the end of each reporting period, an entity shall revise amounts allocated as specified in paragraph AG35A to reflect any changes in assumptions that determine the inputs to the method of allocation used. An entity shall not change amounts allocated to a group of insurance contracts after all contracts have been added to the group (see paragraph AG35C).

AG35C An entity might add insurance contracts to a group of insurance contracts across more than one reporting period (see paragraph 28). In those circumstances, an entity shall derecognise the portion of an asset for insurance acquisition cash flows that relates to insurance contracts added to the group in that period and continue to recognise an asset for insurance acquisition cash flows to the extent that the asset relates to insurance contracts expected to be added to the group in a future reporting period.

AG35D To apply paragraph 28E:

- (a) An entity shall recognise an impairment loss in surplus or deficit and reduce the carrying amount of an asset for insurance acquisition cash flows so that the carrying amount of the asset does not exceed the expected net cash inflow for the related group of insurance contracts, determined applying paragraph 32(a).
- (b) When an entity allocates insurance acquisition cash flows to groups of insurance contracts applying paragraph AG35A(a)(ii), the entity shall recognise an impairment loss in surplus or deficit and reduce the carrying amount of the related assets for insurance acquisition cash flows to the extent that:
 - (i) The entity expects those insurance acquisition cash flows to exceed the net cash inflow for the expected renewals, determined applying paragraph 32(a); and
 - (ii) The excess determined applying (b)(i) has not already been recognised as an impairment loss applying (a).

Measurement (paragraphs 29–71)

Estimates of Future Cash Flows (paragraphs 33–35)

AG36. This section addresses:

- (a) Unbiased use of all reasonable and supportable information available without undue cost or effort (see paragraphs AG37–AG41);
- (b) Market variables and non-market variables (see paragraphs AG42–AG53);
- (c) Using current estimates (see paragraphs AG54–AG60); and
- (d) Cash flows within the contract boundary (see paragraphs AG61–AG71).

Unbiased Use of all Reasonable and Supportable Information Available Without Undue Cost or Effort (paragraph 33(a))

- AG37. The objective of estimating future cash flows is to determine the expected value, or probability-weighted mean, of the full range of possible outcomes, considering all reasonable and supportable information available at the reporting date without undue cost or effort. Reasonable and supportable information available at the reporting date without undue cost or effort includes information about past events and current conditions, and forecasts of future conditions (see paragraph AG41). Information available from an entity's own information systems is considered to be available without undue cost or effort.
- AG38. The starting point for an estimate of the cash flows is a range of scenarios that reflects the full range of possible outcomes. Each scenario specifies the amount and timing of the cash flows for a particular outcome, and the estimated probability of that outcome. The cash flows from each scenario are discounted and weighted by the estimated probability of that outcome to derive an expected present value. Consequently, the objective is not to develop a most likely outcome, or a more-likely-than-not outcome, for future cash flows.
- AG39. When considering the full range of possible outcomes, the objective is to incorporate all reasonable and supportable information available without undue cost or effort in an unbiased way, rather than to identify every possible scenario. In practice, developing explicit scenarios is unnecessary if the resulting estimate is consistent with the measurement objective of considering all reasonable and supportable information available without undue cost or effort when determining the mean. For example, if an entity estimates that the probability distribution of outcomes is broadly consistent with a probability distribution that can be described completely with a small number of parameters, it will be sufficient to estimate the smaller number of parameters. Similarly, in some cases, relatively simple modelling may give an answer within an acceptable range of precision, without the need for many detailed simulations. However, in some cases, the cash flows may be driven by complex underlying factors and may respond in a non-linear fashion to changes in economic conditions. This may happen if, for example, the cash flows reflect a series of interrelated options that are implicit or explicit. In such cases, more sophisticated stochastic modelling is likely to be necessary to satisfy the measurement objective.
- AG40. The scenarios developed shall include unbiased estimates of the probability of catastrophic losses under existing contracts. Those scenarios exclude possible claims under possible future contracts.
- AG41. An entity shall estimate the probabilities and amounts of future payments under existing contracts on the basis of information obtained including:
- (a) Information about claims already reported by policyholders.
 - (b) Other information about the known or estimated characteristics of the insurance contracts.
 - (c) Historical data about the entity's own experience, supplemented when necessary with historical data from other sources. Historical data is adjusted to reflect current conditions, for example, if:
 - (i) The characteristics of the insured population differ (or will differ, for example, because of adverse selection) from those of the population that has been used as a basis for the historical data;

- (ii) There are indications that historical trends will not continue, that new trends will emerge or that economic, demographic and other changes may affect the cash flows that arise from the existing insurance contracts; or
- (iii) There have been changes in items such as underwriting procedures and claims management procedures that may affect the relevance of historical data to the insurance contracts.
- (d) Current price information, if available, for reinsurance contracts and other financial instruments (if any) covering similar risks, such as catastrophe bonds and weather derivatives, and recent market prices for transfers of insurance contracts. This information shall be adjusted to reflect the differences between the cash flows that arise from those reinsurance contracts or other financial instruments, and the cash flows that would arise as the entity fulfils the underlying contracts with the policyholder.

Market Variables and Non-Market Variables

AG42. PBE IFRS 17 identifies two types of variables:

- (a) Market variables—variables that can be observed in, or derived directly from, markets (for example, prices of publicly traded securities and interest rates); and
- (b) Non-market variables—all other variables (for example, the frequency and severity of insurance claims and mortality).

AG43. Market variables will generally give rise to financial risk (for example, observable interest rates) and non-market variables will generally give rise to non-financial risk (for example, mortality rates). However, this will not always be the case. For example, there may be assumptions that relate to financial risks for which variables cannot be observed in, or derived directly from, markets (for example, interest rates that cannot be observed in, or derived directly from, markets).

Market Variables (paragraph 33(b))

AG44. Estimates of market variables shall be consistent with observable market prices at the measurement date. An entity shall maximise the use of observable inputs and shall not substitute its own estimates for observable market data. If variables need to be derived (for example, because no observable market variables exist) they shall be as consistent as possible with observable market variables.

AG45. Market prices blend a range of views about possible future outcomes and also reflect the risk preferences of market participants. Consequently, they are not a single-point forecast of the future outcome. If the actual outcome differs from the previous market price, this does not mean that the market price was ‘wrong’.

AG46. An important application of market variables is the notion of a replicating asset or a replicating portfolio of assets. A replicating asset is one whose cash flows *exactly* match, in all scenarios, the contractual cash flows of a group of insurance contracts in amount, timing and uncertainty. In some cases, a replicating asset may exist for some of the cash flows that arise from a group of insurance contracts. The fair value of that asset reflects both the expected present value of the cash flows from the asset and the risk associated with those cash flows. If a replicating portfolio of assets exists for some of the cash flows that arise from a group of insurance contracts, the entity can use the fair value of those assets to measure the relevant fulfilment cash flows instead of explicitly estimating the cash flows and discount rate.

AG47. PBE IFRS 17 does not require an entity to use a replicating portfolio technique. However, if a replicating asset or portfolio does exist for some of the cash flows that arise from insurance contracts and an entity chooses to use a different technique, the entity shall satisfy itself that a replicating portfolio technique would be unlikely to lead to a materially different measurement of those cash flows.

AG48. Techniques other than a replicating portfolio technique, such as stochastic modelling techniques, may be more robust or easier to implement if there are significant interdependencies between cash flows that vary based on returns on assets and other cash flows. Judgement is required to determine the technique that best meets the objective of consistency with observable market variables in specific circumstances. In particular, the technique used must result in the measurement of any options and guarantees included in the insurance contracts being consistent with observable market prices (if any) for such options and guarantees.

Non-Market Variables

- AG49. Estimates of non-market variables shall reflect all reasonable and supportable evidence available without undue cost or effort, both external and internal.
- AG50. Non-market external data (for example, national mortality statistics) may have more or less relevance than internal data (for example, internally developed mortality statistics), depending on the circumstances. For example, an entity that issues life insurance contracts shall not rely solely on national mortality statistics, but shall consider all other reasonable and supportable internal and external sources of information available without undue cost or effort when developing unbiased estimates of probabilities for mortality scenarios for its insurance contracts. In developing those probabilities, an entity shall give more weight to the more persuasive information. For example:
- (a) Internal mortality statistics may be more persuasive than national mortality data if national data is derived from a large population that is not representative of the insured population. This might be because, for example, the demographic characteristics of the insured population could significantly differ from those of the national population, meaning that an entity would need to place more weight on the internal data and less weight on the national statistics.
 - (b) Conversely, if the internal statistics are derived from a small population with characteristics that are believed to be close to those of the national population, and the national statistics are current, an entity shall place more weight on the national statistics.
- AG51. Estimated probabilities for non-market variables shall not contradict observable market variables. For example, estimated probabilities for future inflation rate scenarios shall be as consistent as possible with probabilities implied by market interest rates.
- AG52. In some cases, an entity may conclude that market variables vary independently of non-market variables. If so, the entity shall consider scenarios that reflect the range of outcomes for the non-market variables, with each scenario using the same observed value of the market variable.
- AG53. In other cases, market variables and non-market variables may be correlated. For example, there may be evidence that lapse rates (a non-market variable) are correlated with interest rates (a market variable). Similarly, there may be evidence that claim levels for house or car insurance are correlated with economic cycles and therefore with interest rates and expense amounts. The entity shall ensure that the probabilities for the scenarios and the risk adjustments for the non-financial risk that relates to the market variables are consistent with the observed market prices that depend on those market variables.

Using Current Estimates (paragraph 33(c))

- AG54. In estimating each cash flow scenario and its probability, an entity shall use all reasonable and supportable information available without undue cost or effort. An entity shall review the estimates that it made at the end of the previous reporting period and update them. In doing so, an entity shall consider whether:
- (a) The updated estimates faithfully represent the conditions at the end of the reporting period.
 - (b) The changes in estimates faithfully represent the changes in conditions during the period. For example, suppose that estimates were at one end of a reasonable range at the beginning of the period. If the conditions have not changed, shifting the estimates to the other end of the range at the end of the period would not faithfully represent what has happened during the period. If an entity's most recent estimates are different from its previous estimates, but conditions have not changed, it shall assess whether the new probabilities assigned to each scenario are justified. In updating its estimates of those probabilities, the entity shall consider both the evidence that supported its previous estimates and all newly available evidence, giving more weight to the more persuasive evidence.
- AG55. The probability assigned to each scenario shall reflect the conditions at the end of the reporting period. Consequently, applying PBE IPSAS 14 *Events after the Reporting Date*, an event occurring after the end of the reporting period that resolves an uncertainty that existed at the end of the reporting period does not provide evidence of the conditions that existed at that date. For example, there may be a 20 percent probability at the end of the reporting period that a major storm will strike during the remaining six months of an insurance contract. After the end of the reporting period but before the financial

statements are authorised for issue, a major storm strikes. The fulfilment cash flows under that contract shall not reflect the storm that, with hindsight, is known to have occurred. Instead, the cash flows included in the measurement include the 20 per cent probability apparent at the end of the reporting period (with disclosure applying PBE IPSAS 14 that a non-adjusting event occurred after the end of the reporting period).

- AG56. Current estimates of expected cash flows are not necessarily identical to the most recent actual experience. For example, suppose that mortality experience in the reporting period was 20 per cent worse than the previous mortality experience and previous expectations of mortality experience. Several factors could have caused the sudden change in experience, including:
- (a) Lasting changes in mortality;
 - (b) Changes in the characteristics of the insured population (for example, changes in underwriting or distribution, or selective lapses by policyholders in unusually good health);
 - (c) Random fluctuations; or
 - (d) Identifiable non-recurring causes.
- AG57. An entity shall investigate the reasons for the change in experience and develop new estimates of cash flows and probabilities in the light of the most recent experience, the earlier experience and other information. The result for the example in paragraph AG56 would typically be that the expected present value of death benefits changes, but not by as much as 20 per cent. In the example in paragraph AG56, if mortality rates continue to be significantly higher than the previous estimates for reasons that are expected to continue, the estimated probability assigned to the high-mortality scenarios will increase.
- AG58. Estimates of non-market variables shall include information about the current level of insured events and information about trends. For example, mortality rates have consistently declined over long periods in many countries. The determination of the fulfilment cash flows reflects the probabilities that would be assigned to each possible trend scenario, taking account of all reasonable and supportable information available without undue cost or effort.
- AG59. Similarly, if cash flows allocated to a group of insurance contracts are sensitive to inflation, the determination of the fulfilment cash flows shall reflect current estimates of possible future inflation rates. Because inflation rates are likely to be correlated with interest rates, the measurement of fulfilment cash flows shall reflect the probabilities for each inflation scenario in a way that is consistent with the probabilities implied by the market interest rates used in estimating the discount rate (see paragraph AG51).
- AG60. When estimating the cash flows, an entity shall take into account current expectations of future events that might affect those cash flows. The entity shall develop cash flow scenarios that reflect those future events, as well as unbiased estimates of the probability of each scenario. However, an entity shall not take into account current expectations of future changes in legislation that would change or discharge the present obligation or create new obligations under the existing insurance contract until the change in legislation is substantively enacted.

Cash Flows within the Contract Boundary (paragraph 34)

- AG61. 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.
- AG62. 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.

AG63. 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.

AG64. 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 service. 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.

AG64.1 Public sector entities often operate within a broad government policy framework that takes into account general economic circumstances and community needs and not only the circumstances specific to the entity and its policyholders. For example, there may be cases when the entity's management, including relevant government Minister(s), deliberately phase in price increases or decreases or benefit adjustments over a long period to help individuals or businesses manage through an economic cycle. Although the phasing-in process might notionally take into account risks relating to a number of coverage periods, this is not the motivating factor. The broader policy objectives are the motivating factor. Therefore, in the context of PBE IFRS 17 paragraph 34(b)(ii), the public sector entity would not be regarded as taking into account the risks that relate to periods after the reassessment date due to broader policy objectives influencing the phasing in of price increases or decreases or benefit adjustments.

AG65. Cash flows within the boundary of an insurance contract are those that relate directly to the fulfilment of the contract, including cash flows for which the entity has discretion over the amount or timing. The cash flows within the boundary include:

- (a) Premiums (including premium adjustments and instalment premiums) from a policyholder and any additional cash flows that result from those premiums.
- (b) Payments to (or on behalf of) a policyholder, including claims that have already been reported but have not yet been paid (i.e., reported claims), incurred claims for events that have occurred but for which claims have not been reported and all future claims for which the entity has a substantive obligation (see paragraph 34).
- (c) Payments to (or on behalf of) a policyholder that vary depending on returns on underlying items.
- (d) Payments to (or on behalf of) a policyholder resulting from derivatives, for example, options and guarantees embedded in the contract, to the extent that those options and guarantees are not separated from the insurance contract (see paragraph 11(a)).
- (e) An allocation of insurance acquisition cash flows attributable to the portfolio to which the contract belongs.
- (f) Claim handling costs (i.e., the costs the entity will incur in investigating, processing and resolving claims under existing insurance contracts, including legal and loss-adjusters' fees and internal costs of investigating claims and processing claim payments).
- (g) Costs the entity will incur in providing contractual benefits paid in kind.
- (h) Policy administration and maintenance costs, such as costs of premium billing and handling policy changes (for example, conversions and reinstatements). Such costs also include recurring

commissions that are expected to be paid to intermediaries if a particular policyholder continues to pay the premiums within the boundary of the insurance contract.

- (i) Transaction-based taxes (such as premium taxes, value added taxes and goods and services taxes) and levies (such as fire service levies and guarantee fund assessments) that arise directly from existing insurance contracts, or that can be attributed to them on a reasonable and consistent basis.
- (j) Payments by the insurer in a fiduciary capacity to meet tax obligations incurred by the policyholder, and related receipts.
- (k) Potential cash inflows from recoveries (such as salvage and subrogation) on future claims covered by existing insurance contracts and, to the extent that they do not qualify for recognition as separate assets, potential cash inflows from recoveries on past claims.
- (ka) Costs the entity will incur:
 - (i) Performing investment activity, to the extent the entity performs that activity to enhance benefits from insurance coverage for policyholders. Investment activities enhance benefits from insurance coverage if the entity performs those activities expecting to generate an investment return from which policyholders will benefit if an insured event occurs.
 - (ii) Providing investment-return services to policyholders of insurance contracts without direct participation features (see paragraph AG119B).
 - (iii) Providing investment-related service to policyholders of insurance contracts with direct participation features.
- (l) An allocation of fixed and variable overheads (such as the costs of accounting, human resources, information technology and support, building depreciation, rent, and maintenance and utilities) directly attributable to fulfilling insurance contracts. Such overheads are allocated to groups of contracts using methods that are systematic and rational, and are consistently applied to all costs that have similar characteristics.
- (m) Any other costs specifically chargeable to the policyholder under the terms of the contract.

AG66. The following cash flows shall not be included when estimating the cash flows that will arise as the entity fulfils an existing insurance contract:

- (a) Investment returns. Investments are recognised, measured and presented separately.
- (b) Cash flows (payments or receipts) that arise under reinsurance contracts held. Reinsurance contracts held are recognised, measured and presented separately.
- (c) Cash flows that may arise from future insurance contracts, i.e., cash flows outside the boundary of existing contracts (see paragraphs 34–35).
- (d) Cash flows relating to costs that cannot be directly attributed to the portfolio of insurance contracts that contain the contract, such as some product development and training costs. Such costs are recognised in surplus or deficit when incurred.
- (e) Cash flows that arise from abnormal amounts of wasted labour or other resources that are used to fulfil the contract. Such costs are recognised in surplus or deficit when incurred.
- (f) Income tax payments and receipts the insurer does not pay or receive in a fiduciary capacity or that are not specifically chargeable to the policyholder under the terms of the contract.
- (g) Cash flows between different components of the reporting entity, such as policyholder funds and shareholder funds, if those cash flows do not change the amount that will be paid to the policyholders.
- (h) Cash flows arising from components separated from the insurance contract and accounted for using other applicable PBE Standards (see paragraphs 10–13).

AG66A Before the recognition of a group of insurance contracts, an entity might be required to recognise an asset or liability for cash flows related to the group of insurance contracts other than insurance acquisition cash flows either because of the occurrence of the cash flows or because of the requirements of another Standard. Cash flows are related to the group of insurance contracts if those cash flows would have been

included in the fulfilment cash flows at the date of initial recognition of the group had they been paid or received after that date. To apply paragraph 38(c)(ii) an entity shall derecognise such an asset or liability to the extent that the asset or liability would not be recognised separately from the group of insurance contracts if the cash flow or the application of the Standard occurred at the date of initial recognition of the group of insurance contracts.

Contracts with Cash Flows that Affect or are Affected by Cash Flows to Policyholders of Other Contracts

- AG67. Some insurance contracts affect 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; and
 - (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.
- AG68. Sometimes, such contracts will affect the cash flows to policyholders of contracts in other groups. The fulfilment cash flows of each group 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 to policyholders in another group. Hence the fulfilment cash flows for a group:
- (a) Include payments arising from the terms of existing contracts to policyholders of contracts in other groups, regardless of whether those payments are expected to be made to current or future policyholders; and
 - (b) Exclude payments to policyholders in the group that, applying (a), have been included in the fulfilment cash flows of another group.
- AG69. For example, to the extent that payments to policyholders in one group are reduced from a share in the returns on underlying items of CU350 to CU250 because of payments of a guaranteed amount to policyholders in another group, the fulfilment cash flows of the first group would include the payments of CU100 (i.e., would be CU350) and the fulfilment cash flows of the second group would exclude CU100 of the guaranteed amount.
- AG70. Different practical approaches can be used to determine the fulfilment cash flows of groups of contracts that affect or are affected by cash flows to policyholders of contracts in other groups. In some cases, an entity might be able to identify the change in the underlying items and resulting change in the cash flows only at a higher level of aggregation than the groups. In such cases, the entity shall allocate the effect of the change in the underlying items to each group on a systematic and rational basis.
- AG71. After all insurance contract services have been provided to the contracts in a group, the fulfilment cash flows may still include payments expected to be made to current policyholders in other groups or future policyholders. An entity is not required to continue to allocate such fulfilment cash flows to specific groups but can instead recognise and measure a liability for such fulfilment cash flows arising from all groups.

Discount Rates (paragraph 36)

- AG72. An entity shall use the following discount rates in applying PBE IFRS 17:
- (a) To measure the fulfilment cash flows—current discount rates applying paragraph 36;
 - (b) To determine the interest to accrete on the contractual service margin applying paragraph 44(b) for insurance contracts without direct participation features—discount rates determined at the date of initial recognition of a group of contracts, applying paragraph 36 to nominal cash flows that do not vary based on the returns on any underlying items;

- (c) To measure the changes to the contractual service margin applying paragraphs AG96(a)–AG96(b) and AG96(d) for insurance contracts without direct participation features—discount rates applying paragraph 36 determined on initial recognition;
 - (d) For groups of contracts applying the premium allocation approach that have a significant financing component, to adjust the carrying amount of the liability for remaining coverage applying paragraph 56—discount rates applying paragraph 36 determined on initial recognition;
 - (e) If an entity chooses to disaggregate insurance finance revenue or expenses between surplus or deficit and other comprehensive revenue and expense (see paragraph 88), to determine the amount of the insurance finance revenue or expenses included in surplus or deficit:
 - (i) For groups 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, applying paragraph AG131—discount rates determined at the date of initial recognition of a group of contracts, applying paragraph 36 to nominal cash flows that do not vary based on the returns on any underlying items;
 - (ii) For groups of insurance contracts for which changes in assumptions that relate to financial risk have a substantial effect on the amounts paid to policyholders, applying paragraph AG132(a)(i)—discount rates that allocate the remaining revised expected finance revenue or expenses over the remaining duration of the group of contracts at a constant rate; and
 - (iii) For groups of contracts applying the premium allocation approach applying paragraphs 59(b) and AG133—discount rates determined at the date of the incurred claim, applying paragraph 36 to nominal cash flows that do not vary based on the returns on any underlying items.
- AG73. To determine the discount rates at the date of initial recognition of a group of contracts described in paragraphs AG72(b)–AG72(e), an entity may use weighted-average discount rates over the period that contracts in the group are issued, which applying paragraph 22 cannot exceed one year.
- AG74. Estimates of discount rates shall be consistent with other estimates used to measure insurance contracts to avoid double counting or omissions; for example:
- (a) Cash flows that do not vary based on the returns on any underlying items shall be discounted at rates that do not reflect any such variability;
 - (b) Cash flows that vary based on the returns on any financial underlying items shall be:
 - (i) Discounted using rates that reflect that variability; or
 - (ii) Adjusted for the effect of that variability and discounted at a rate that reflects the adjustment made.
 - (c) Nominal cash flows (i.e., those that include the effect of inflation) shall be discounted at rates that include the effect of inflation; and
 - (d) Real cash flows (i.e., those that exclude the effect of inflation) shall be discounted at rates that exclude the effect of inflation.
- AG75. Paragraph AG74(b) requires cash flows that vary based on the returns on underlying items to be discounted using rates that reflect that variability, or to be adjusted for the effect of that variability and discounted at a rate that reflects the adjustment made. The variability is a relevant factor regardless of whether it arises because of contractual terms or because the entity exercises discretion, and regardless of whether the entity holds the underlying items.
- AG76. Cash flows that vary with returns on underlying items with variable returns, but that are subject to a guarantee of a minimum return, do not vary solely based on the returns on the underlying items, even when the guaranteed amount is lower than the expected return on the underlying items. Hence, an entity shall adjust the rate that reflects the variability of the returns on the underlying items for the effect of the guarantee, even when the guaranteed amount is lower than the expected return on the underlying items.
- AG77. PBE IFRS 17 does not require an entity to divide estimated cash flows into those that vary based on the returns on underlying items and those that do not. If an entity does not divide the estimated cash flows in

this way, the entity shall apply discount rates appropriate for the estimated cash flows as a whole; for example, using stochastic modelling techniques or risk-neutral measurement techniques.

- AG78. Discount rates shall include only relevant factors, i.e., factors that arise from the time value of money, the characteristics of the cash flows and the liquidity characteristics of the insurance contracts. Such discount rates may not be directly observable in the market. Hence, when observable market rates for an instrument with the same characteristics are not available, or observable market rates for similar instruments are available but do not separately identify the factors that distinguish the instrument from the insurance contracts, an entity shall estimate the appropriate rates. PBE IFRS 17 does not require a particular estimation technique for determining discount rates. In applying an estimation technique, an entity shall:
- (a) Maximise the use of observable inputs (see paragraph AG44) and reflect all reasonable and supportable information on non-market variables available without undue cost or effort, both external and internal (see paragraph AG49). In particular, the discount rates used shall not contradict any available and relevant market data, and any non-market variables used shall not contradict observable market variables.
 - (b) Reflect current market conditions from the perspective of a market participant.
 - (c) Exercise judgement to assess the degree of similarity between the features of the insurance contracts being measured and the features of the instrument for which observable market prices are available and adjust those prices to reflect the differences between them.
- AG79. For cash flows of insurance contracts that do not vary based on the returns on underlying items, the discount rate reflects the yield curve in the appropriate currency for instruments that expose the holder to no or negligible credit risk, adjusted to reflect the liquidity characteristics of the group of insurance contracts. That adjustment shall reflect the difference between the liquidity characteristics of the group of insurance contracts and the liquidity characteristics of the assets used to determine the yield curve. Yield curves reflect assets traded in active markets that the holder can typically sell readily at any time without incurring significant costs. In contrast, under some insurance contracts the entity cannot be forced to make payments earlier than the occurrence of insured events, or dates specified in the contracts.
- AG80. Hence, for cash flows of insurance contracts that do not vary based on the returns on underlying items, an entity may determine discount rates by adjusting a liquid risk-free yield curve to reflect the differences between the liquidity characteristics of the financial instruments that underlie the rates observed in the market and the liquidity characteristics of the insurance contracts (a bottom-up approach).
- AG81. Alternatively, an entity may determine the appropriate discount rates for insurance contracts based on a yield curve that reflects the current market rates of return implicit in a fair value measurement of a reference portfolio of assets (a top-down approach). An entity shall adjust that yield curve to eliminate any factors that are not relevant to the insurance contracts, but is not required to adjust the yield curve for differences in liquidity characteristics of the insurance contracts and the reference portfolio.
- AG82. In estimating the yield curve described in paragraph AG81:
- (a) If there are observable market prices in active markets for assets in the reference portfolio, an entity shall use those prices.
 - (b) If a market is not active, an entity shall adjust observable market prices for similar assets to make them comparable to market prices for the assets being measured.
 - (c) If there is no market for assets in the reference portfolio, an entity shall apply an estimation technique. For such assets an entity shall:
 - (i) Develop unobservable inputs using the best information available in the circumstances. Such inputs might include the entity's own data and, in the context of PBE IFRS 17, the entity might place more weight on long-term estimates than on short-term fluctuations; and
 - (ii) Adjust those data to reflect all information about market participant assumptions that is reasonably available.
- AG83. In adjusting the yield curve, an entity shall adjust market rates observed in recent transactions in instruments with similar characteristics for movements in market factors since the transaction date, and shall adjust observed market rates to reflect the degree of dissimilarity between the instrument being

measured and the instrument for which transaction prices are observable. For cash flows of insurance contracts that do not vary based on the returns on the assets in the reference portfolio, such adjustments include:

- (a) Adjusting for differences between the amount, timing and uncertainty of the cash flows of the assets in the portfolio and the amount, timing and uncertainty of the cash flows of the insurance contracts; and
- (b) Excluding market risk premiums for credit risk, which are relevant only to the assets included in the reference portfolio.

AG84. In principle, for cash flows of insurance contracts that do not vary based on the returns of the assets in the reference portfolio, there should be a single illiquid risk-free yield curve that eliminates all uncertainty about the amount and timing of cash flows. However, in practice the top-down approach and the bottom-up approach may result in different yield curves, even in the same currency. This is because of the inherent limitations in estimating the adjustments made under each approach, and the possible lack of an adjustment for different liquidity characteristics in the top-down approach. An entity is not required to reconcile the discount rate determined under its chosen approach with the discount rate that would have been determined under the other approach.

AG85. PBE IFRS 17 does not specify restrictions on the reference portfolio of assets used in applying paragraph AG81. However, fewer adjustments would be required to eliminate factors that are not relevant to the insurance contracts when the reference portfolio of assets has similar characteristics. For example, if the cash flows from the insurance contracts do not vary based on the returns on underlying items, fewer adjustments would be required if an entity used debt instruments as a starting point rather than equity instruments. For debt instruments, the objective would be to eliminate from the total bond yield the effect of credit risk and other factors that are not relevant to the insurance contracts. One way to estimate the effect of credit risk is to use the market price of a credit derivative as a reference point.

Risk Adjustment for Non-Financial Risk (paragraph 37)

AG86. The risk adjustment for non-financial risk relates to risk arising from insurance contracts other than financial risk. Financial risk is included in the estimates of the future cash flows or the discount rate used to adjust the cash flows. The risks covered by the risk adjustment for non-financial risk are insurance risk and other non-financial risks such as lapse risk and expense risk (see paragraph AG14).

AG87. The risk adjustment for non-financial risk for insurance contracts measures the compensation that the entity would require to make the entity indifferent between:

- (a) Fulfilling a liability that has a range of possible outcomes arising from non-financial risk; and
- (b) Fulfilling a liability that will generate fixed cash flows with the same expected present value as the insurance contracts.

For example, the risk adjustment for non-financial risk would measure the compensation the entity would require to make it indifferent between fulfilling a liability that—because of non-financial risk—has a 50 per cent probability of being CU90 and a 50 per cent probability of being CU110, and fulfilling a liability that is fixed at CU100. As a result, 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.

AG88. Because the risk adjustment for non-financial risk reflects the compensation the entity would require for bearing the 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; and
- (b) Both favourable and unfavourable outcomes, in a way that reflects the entity's degree of risk aversion.

AG89. The purpose of the risk adjustment for non-financial risk is to measure the effect of uncertainty in the cash flows that arise from insurance contracts, other than uncertainty arising from financial risk. Consequently, the risk adjustment for non-financial risk shall reflect all non-financial risks associated

with the insurance contracts. It shall not reflect the risks that do not arise from the insurance contracts, such as general operational risk.

- AG90. The risk adjustment for non-financial risk shall be included in the measurement in an explicit way. The risk adjustment for non-financial risk is conceptually separate from the estimates of future cash flows and the discount rates that adjust those cash flows. The entity shall not double-count the risk adjustment for non-financial risk by, for example, also including the risk adjustment for non-financial risk implicitly when determining the estimates of future cash flows or the discount rates. The discount rates that are disclosed to comply with paragraph 120 shall not include any implicit adjustments for non-financial risk.
- AG91. PBE IFRS 17 does not specify the estimation technique(s) used to determine the risk adjustment for non-financial risk. However, to reflect the compensation the entity would require for bearing the non-financial risk, the risk adjustment for non-financial risk shall have the following characteristics:
- (a) Risks with low frequency and high severity will result in higher risk adjustments for non-financial risk than risks with high frequency and low severity;
 - (b) For similar risks, contracts with a longer duration will result in higher risk adjustments for non-financial risk than contracts with a shorter duration;
 - (c) Risks with a wider probability distribution will result in higher risk adjustments for non-financial risk than risks with a narrower distribution;
 - (d) The less that is known about the current estimate and its trend, the higher will be the risk adjustment for non-financial risk; and
 - (e) To the extent that emerging experience reduces uncertainty about the amount and timing of cash flows, risk adjustments for non-financial risk will decrease and vice versa.
- AG92. An entity shall apply judgement when determining an appropriate estimation technique for the risk adjustment for non-financial risk. When applying that judgement, an entity shall also consider whether the technique provides concise and informative disclosure so that users of financial statements can benchmark the entity's performance against the performance of other entities. Paragraph 119 requires an entity that uses a technique other than the confidence level technique for determining the risk adjustment for non-financial risk to disclose the technique used and the confidence level corresponding to the results of that technique.

Initial Recognition of Transfers of Insurance Contracts and PBE Combinations (paragraph 39)

- AG93. When an entity acquires insurance contracts issued or reinsurance contracts held in a transfer of insurance contracts that do not form an operation or in a PBE combination within the scope of PBE IPSAS 40, the entity shall apply paragraphs 14–24 to identify the groups of contracts acquired, as if it had entered into the contracts on the date of the transaction.
- AG94. An entity shall use the consideration received or paid for the contracts as a proxy for the premiums received. The consideration received or paid for the contracts excludes the consideration received or paid for any other assets and liabilities acquired in the same transaction. In a PBE combination within the scope of PBE IPSAS 40, the consideration received or paid is the fair value of the contracts at that date.
- AG95. Unless the premium allocation approach for the liability for remaining coverage in paragraphs 55–59 and 69–70A applies, on initial recognition the contractual service margin is calculated applying paragraph 38 for acquired insurance contracts issued and paragraph 65 for acquired reinsurance contracts held using the consideration received or paid for the contracts as a proxy for the premiums received or paid at the date of initial recognition.
- AG95A. If acquired insurance contracts issued are onerous, applying paragraph 47, the entity shall recognise the excess of the fulfilment cash flows over the consideration paid or received as part of goodwill or gain on a bargain purchase for contracts acquired in a PBE combination within the scope of PBE IPSAS 40 or as a loss in surplus or deficit for contracts acquired in a transfer. The entity shall establish a loss component of the liability for remaining coverage for that excess, and apply paragraphs 49–52 to allocate subsequent changes in fulfilment cash flows to that loss component.

AG95B For a group of reinsurance contracts held to which paragraphs 66A–66B apply, an entity shall determine the loss-recovery component of the asset for remaining coverage at the date of the transaction by multiplying:

- (a) The loss component of the liability for remaining coverage of the underlying insurance contracts at the date of the transaction; and
- (b) The percentage of claims on the underlying insurance contracts the entity expects at the date of the transaction to recover from the group of reinsurance contracts held.

AG95C The entity shall recognise the amount of the loss-recovery component determined applying paragraph AG95B as part of goodwill or gain on a bargain purchase for reinsurance contracts held acquired in a PBE combination within the scope of PBE IPSAS 40, or as revenue in surplus or deficit for contracts acquired in a transfer.

AG95D Applying paragraphs 14–22, at the date of the transaction an entity might include in an onerous group of insurance contracts both onerous insurance contracts covered by a group of reinsurance contracts held and onerous contracts not covered by the group of reinsurance contracts held. To apply paragraph AG95B in such cases, an entity shall use a systematic and rational basis of allocation to determine the portion of the loss component of the group of insurance contracts that relates to insurance contracts covered by the group of reinsurance contracts held.

Asset for Insurance Acquisition Cash Flows

AG95E When an entity acquires insurance contracts issued in a transfer of insurance contracts that do not form an operation or in a PBE combination within the scope of PBE IPSAS 40, the entity shall recognise an asset for insurance acquisition cash flows at fair value at the date of the transaction for the rights to obtain:

- (a) Future insurance contracts that are renewals of insurance contracts recognised at the date of the transaction; and
- (b) Future insurance contracts, other than those in (a), after the date of the transaction without paying again insurance acquisition cash flows the acquiree has already paid that are directly attributable to the related portfolio of insurance contracts.

AG95F At the date of the transaction, the amount of any asset for insurance acquisition cash flows shall not be included in the measurement of the acquired group of insurance contracts applying paragraphs AG93–AG95A.

Changes in the Carrying Amount of the Contractual Service Margin for Insurance Contracts without Direct Participation Features (paragraph 44)

AG96. For insurance contracts without direct participation features, paragraph 44(c) requires an adjustment to the contractual service margin of a group of insurance contracts for changes in fulfilment cash flows that relate to future service. These changes comprise:

- (a) Experience adjustments arising from premiums received in the period that relate to future service, and related cash flows such as insurance acquisition cash flows and premium-based taxes, measured at the discount rates specified in paragraph AG72(c).
- (b) Changes in estimates of the present value of the future cash flows in the liability for remaining coverage, except those described in paragraph AG97(a), measured at the discount rates specified in paragraph AG72(c).
- (c) Differences between any investment component expected to become payable in the period and the actual investment component that becomes payable in the period. Those differences are determined by comparing (i) the actual investment component that becomes payable in the period with (ii) the payment in the period that was expected at the start of the period plus any insurance finance revenue, or expenses related to that expected payment before it becomes payable.
- (ca) Differences between any loan to a policyholder expected to become repayable in the period and the actual loan to a policyholder that becomes repayable in the period. Those differences are determined by comparing (i) the actual loan to a policyholder that becomes repayable in the period with (ii) the repayment in the period that was expected at the start of the period plus any insurance finance revenue or expenses related to that expected repayment before it becomes repayable.

- (d) Changes in the risk adjustment for non-financial risk that relate to future service. An entity is not required to disaggregate the change in the risk adjustment for non-financial risk between (i) a change related to non-financial risk and (ii) the effect of the time value of money and changes in the time value of money. If an entity makes such a disaggregation, it shall adjust the contractual service margin for the change related to non-financial risk, measured at the discount rates specified in paragraph AG72(c).
- AG97. An entity shall not adjust the contractual service margin for a group of insurance contracts without direct participation features for the following changes in fulfilment cash flows because they do not relate to future service:
- (a) The effect of the time value of money and changes in the time value of money and the effect of financial risk and changes in financial risk. These effects comprise:
 - (i) The effect, if any, on estimated future cash flows;
 - (ii) The effect, if disaggregated, on the risk adjustment for non-financial risk; and
 - (iii) The effect of a change in discount rate.
 - (b) Changes in estimates of fulfilment cash flows in the liability for incurred claims.
 - (c) Experience adjustments, except those described in paragraph AG96(a).
- AG98. The terms of some insurance contracts without direct participation features give an entity discretion over the cash flows to be paid to policyholders. A change in the discretionary cash flows is regarded as relating to future service, and accordingly adjusts the contractual service margin. To determine how to identify a change in discretionary cash flows, an entity shall specify at inception of the contract the basis on which it expects to determine its commitment under the contract; for example, based on a fixed interest rate, or on returns that vary based on specified asset returns.
- AG99. An entity shall use that specification to distinguish between the effect of changes in assumptions that relate to financial risk on that commitment (which do not adjust the contractual service margin) and the effect of discretionary changes to that commitment (which adjust the contractual service margin).
- AG100. If an entity cannot specify at inception of the contract what it regards as its commitment under the contract and what it regards as discretionary, it shall regard its commitment to be the return implicit in the estimate of the fulfilment cash flows at inception of the contract, updated to reflect current assumptions that relate to financial risk.

Changes in the Carrying Amount of the Contractual Service Margin for Insurance Contracts with Direct Participation Features (paragraph 45)

- AG101. Insurance contracts with direct participation features are insurance contracts that are substantially investment-related service contracts under which an entity promises an investment return based on underlying items. Hence, they are defined as insurance contracts for which:
- (a) The contractual terms specify that the policyholder participates in a share of a clearly identified pool of underlying items (see paragraphs AG105–AG106);
 - (b) The entity expects to pay to the policyholder an amount equal to a substantial share of the fair value returns on the underlying items (see paragraph AG107); and
 - (c) The entity expects a substantial proportion of any change in the amounts to be paid to the policyholder to vary with the change in fair value of the underlying items (see paragraph AG107).
- AG102. An entity shall assess whether the conditions in paragraph AG101 are met using its expectations at inception of the contract and shall not reassess the conditions afterwards, unless the contract is modified, applying paragraph 72.
- AG103. To the extent that insurance contracts in a group affect the cash flows to policyholders of contracts in other groups (see paragraphs AG67–AG71), an entity shall assess whether the conditions in paragraph AG101 are met by considering the cash flows that the entity expects to pay the policyholders determined applying paragraphs AG68–AG70.

AG104. The conditions in paragraph AG101 ensure that insurance contracts with direct participation features are contracts under which the entity's obligation to the policyholder is the net of:

- (a) The obligation to pay the policyholder an amount equal to the fair value of the underlying items; and
- (b) A variable fee (see paragraphs AG110–AG118) that the entity will deduct from (a) in exchange for the future service provided by the insurance contract, comprising:
 - (i) The amount of the entity's share of the fair value of the underlying items; less
 - (ii) Fulfilment cash flows that do not vary based on the returns on underlying items.

AG105. A share referred to in paragraph AG101(a) does not preclude the existence of the entity's discretion to vary the amounts paid to the policyholder. However, the link to the underlying items must be enforceable (see paragraph 2).

AG106. The pool of underlying items referred to in paragraph AG101(a) can comprise any items, for example a reference portfolio of assets, the net assets of the entity, or a specified subset of the net assets of the entity, as long as they are clearly identified by the contract. An entity need not hold the identified pool of underlying items. However, a clearly identified pool of underlying items does not exist when:

- (a) An entity can change the underlying items that determine the amount of the entity's obligation with retrospective effect; or
- (b) There are no underlying items identified, even if the policyholder could be provided with a return that generally reflects the entity's overall performance and expectations, or the performance and expectations of a subset of assets the entity holds. An example of such a return is a crediting rate or dividend payment set at the end of the period to which it relates. In this case, the obligation to the policyholder reflects the crediting rate or dividend amounts the entity has set, and does not reflect identified underlying items.

AG107. Paragraph AG101(b) requires that the entity expects a substantial share of the fair value returns on the underlying items will be paid to the policyholder and paragraph AG101(c) requires that the entity expects a substantial proportion of any change in the amounts to be paid to the policyholder to vary with the change in fair value of the underlying items. An entity shall:

- (a) Interpret the term 'substantial' in both paragraphs in the context of the objective of insurance contracts with direct participation features being contracts under which the entity provides investment-related services and is compensated for the services by a fee that is determined by reference to the underlying items; and
- (b) Assess the variability in the amounts in paragraphs AG101(b) and AG101(c):
 - (i) Over the duration of the insurance contract; and
 - (ii) On a present value probability-weighted average basis, not a best or worst outcome basis (see paragraphs AG37–AG38).

AG108. For example, if the entity expects to pay a substantial share of the fair value returns on underlying items, subject to a guarantee of a minimum return, there will be scenarios in which:

- (a) The cash flows that the entity expects to pay to the policyholder vary with the changes in the fair value of the underlying items because the guaranteed return and other cash flows that do not vary based on the returns on underlying items do not exceed the fair value return on the underlying items; and
- (b) The cash flows that the entity expects to pay to the policyholder do not vary with the changes in the fair value of the underlying items because the guaranteed return and other cash flows that do not vary based on the returns on underlying items exceed the fair value return on the underlying items.

The entity's assessment of the variability in paragraph AG101(c) for this example will reflect a present value probability-weighted average of all these scenarios.

AG109. Reinsurance contracts issued and reinsurance contracts held cannot be insurance contracts with direct participation features for the purposes of PBE IFRS 17.

- AG110. For insurance contracts with direct participation features, the contractual service margin is adjusted to reflect the variable nature of the fee. Hence, changes in the amounts set out in paragraph AG104 are treated as set out in paragraphs AG111–AG114.
- AG111. Changes in the obligation to pay the policyholder an amount equal to the fair value of the underlying items (paragraph AG104(a)) do not relate to future service and do not adjust the contractual service margin.
- AG112. Changes in the amount of the entity's share of the fair value of the underlying items (paragraph AG104(b)(i)) relate to future service and adjust the contractual service margin, applying paragraph 45(b).
- AG113. Changes in the fulfilment cash flows that do not vary based on the returns on underlying items (paragraph AG104(b)(ii)) comprise:
- (a) Changes in the fulfilment cash flows other than those specified in (b). An entity shall apply paragraphs AG96–AG97, consistent with insurance contracts without direct participation features, to determine to what extent they relate to future service and, applying paragraph 45(c), adjust the contractual service margin. All the adjustments are measured using current discount rates.
 - (b) The change in the effect of the time value of money and financial risks not arising from the underlying items; for example, the effect of financial guarantees. These relate to future service and, applying paragraph 45(c), adjust the contractual service margin, except to the extent that paragraph AG115 applies.
- AG114. An entity is not required to identify the adjustments to the contractual service margin required by paragraphs AG112 and AG113 separately. Instead, a combined amount may be determined for some or all of the adjustments.

Risk Mitigation

- AG115. To the extent that an entity meets the conditions in paragraph AG116, it may choose not to recognise a change in the contractual service margin to reflect some or all of the changes in the effect of the time value of money and financial risk on:
- (a) The amount of the entity's share of the underlying items (see paragraph AG112) if the entity mitigates the effect of financial risk on that amount using derivatives or reinsurance contracts held; and
 - (b) The fulfilment cash flows set out in paragraph AG113(b) if the entity mitigates the effect of financial risk on those fulfilment cash flows using derivatives, non-derivative financial instruments measured at fair value through surplus or deficit, or reinsurance contracts held.
- AG116. To apply paragraph AG115, an entity must have a previously documented risk-management objective and strategy for mitigating financial risk as described in paragraph AG115. In applying that objective and strategy:
- (a) An economic offset exists between the insurance contracts and the derivative, non-derivative financial instrument measured at fair value through surplus or deficit, or reinsurance contract held (i.e., the values of the insurance contracts and those risk-mitigating items generally move in opposite directions because they respond in a similar way to the changes in the risk being mitigated). An entity shall not consider accounting measurement differences in assessing the economic offset.
 - (b) Credit risk does not dominate the economic offset.
- AG117. The entity shall determine the fulfilment cash flows in a group to which paragraph AG115 applies in a consistent manner in each reporting period.
- AG117A If the entity mitigates the effect of financial risk using derivatives or non-derivative financial instruments measured at fair value through surplus or deficit, it shall include insurance finance revenue or expenses for the period arising from the application of paragraph AG115 in surplus or deficit. If the entity mitigates the effect of financial risk using reinsurance contracts held, it shall apply the same accounting policy for the presentation of insurance finance revenue or expenses arising from the

application of paragraph AG115 as the entity applies to the reinsurance contracts held applying paragraphs 88 and 90.

AG118. If, and only if, any of the conditions in paragraph AG116 cease to be met, an entity shall cease to apply paragraph AG115 from that date. An entity shall not make any adjustment for changes previously recognised in surplus or deficit.

Recognition of the Contractual Service Margin in Surplus or Deficit

AG119. An amount of the contractual service margin for a group of insurance contracts is recognised in surplus or deficit in each period to reflect the insurance contract 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 insurance contract services 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 period.
- (b) Allocating the contractual service margin at the end of the period (before recognising any amounts in surplus or deficit to reflect the insurance contract 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 surplus or deficit the amount allocated to coverage units provided in the period.

AG119A To apply paragraph AG119, the period of investment-return service or investment-related service ends at or before the date that all amounts due to current policyholders relating to those services have been paid, without considering payments to future policyholders included in the fulfilment cash flows applying paragraph AG68.

AG119B Insurance contracts without direct participation features may provide an investment-return service if, and only if:

- (a) An investment component exists, or the policyholder has a right to withdraw an amount;
- (b) The entity expects the investment component or amount the policyholder has a right to withdraw to include an investment return (an investment return could be below zero, for example, in a negative interest rate environment); and
- (c) The entity expects to perform investment activity to generate that investment return.

Reinsurance Contracts Held—Recognition of Recovery of Losses on Underlying Insurance Contracts (paragraphs 66A–66B)

AG119C Paragraph 66A applies if, and only if, the reinsurance contract held is entered into before or at the same time as the onerous underlying insurance contracts are recognised.

AG119D To apply paragraph 66A, an entity shall determine the adjustment to the contractual service margin of a group of reinsurance contracts held and the resulting revenue by multiplying:

- (a) The loss recognised on the underlying insurance contracts; and
- (b) The percentage of claims on the underlying insurance contracts the entity expects to recover from the group of reinsurance contracts held.

AG119E Applying paragraphs 14–22, an entity might include in an onerous group of insurance contracts both onerous insurance contracts covered by a group of reinsurance contracts held and onerous insurance contracts not covered by the group of reinsurance contracts held. To apply paragraphs 66(c)(i)–(ii) and paragraph 66A in such cases, the entity shall apply a systematic and rational method of allocation to determine the portion of losses recognised on the group of insurance contracts that relates to insurance contracts covered by the group of reinsurance contracts held.

AG119F After an entity has established a loss-recovery component applying paragraph 66B, the entity shall adjust the loss-recovery component to reflect changes in the loss component of an onerous group of underlying insurance contracts (see paragraphs 50–52). The carrying amount of the loss-recovery component shall not exceed the portion of the carrying amount of the loss component of the onerous

group of underlying insurance contracts that the entity expects to recover from the group of reinsurance contracts held.

Insurance Revenue (paragraphs 83 and 85)

AG120. The total insurance revenue for a group of insurance contracts is the consideration for the contracts, i.e., the amount of premiums paid to the entity:

- (a) Adjusted for a financing effect; and
- (b) Excluding any investment components.

AG121. Paragraph 83 requires the amount of insurance revenue recognised in a period to depict the transfer of promised services at an amount that reflects the consideration to which the entity expects to be entitled in exchange for those services. The total consideration for a group of contracts covers the following amounts:

- (a) Amounts related to the provision of services, comprising:
 - (i) Insurance service expenses, excluding any amounts relating to the risk adjustment for non-financial risk included in (ii) and any amounts allocated to the loss component of the liability for remaining coverage;
 - (ia) Amounts related to income tax that are specifically chargeable to the policyholder;
 - (ii) The risk adjustment for non-financial risk, excluding any amounts allocated to the loss component of the liability for remaining coverage; and
 - (iii) The contractual service margin.
 - (b) Amounts related to insurance acquisition cash flows.

AG121.1 For a public sector entity, consistent with paragraph 83 and the guidance on identifying coverage periods in paragraphs E13–E17, revenue collected to provide insurance coverage is recognised over the relevant coverage periods. For example:

- (a) when coverage is determinable from the period(s) over which coverage is provided under insurance contracts issued by private sector insurers, the public sector entity recognises insurance revenue based on the coverage period determined from the private sector insurance contracts. If the public sector entity does not have a detailed knowledge from the private sector insurers about the coverage periods, those periods would need to be estimated from the available information; and
- (b) when a coverage period coincides with the public sector entity's annual reporting period, revenue is recognised over the annual reporting period. This may be the case, for example, when arrangements are funded from a levy on the insurance contracts issued by private sector insurers in a particular period and the levy is intended to meet claims for benefits arising from events during the reporting period, rather than from events during the private sector insurance contract coverage periods. In this example, the period over which levies are collected would not necessarily need to be the same as the coverage period.

All the revenue collected to provide insurance coverage is recognised over the relevant coverage period, which may sometimes include funds from sources other than premiums or levies received from participants, for example, top-up funding from sources such as general taxation received from time to time.

AG122. Insurance revenue for a period relating to the amounts described in paragraph AG121(a) is determined as set out in paragraphs AG123–AG124. Insurance revenue for a period relating to the amounts described in paragraph AG121(b) is determined as set out in paragraph AG125.

AG123. When an entity provides services in a period, it reduces the liability for remaining coverage for the services provided and recognises insurance revenue. The reduction in the liability for remaining coverage that gives rise to insurance revenue excludes changes in the liability that do not relate to services expected to be covered by the consideration received by the entity. Those changes are:

- (a) Changes that do not relate to services provided in the period, for example:
 - (i) Changes resulting from cash inflows from premiums received;
 - (ii) Changes that relate to investment components in the period;
 - (ia) Changes resulting from cash flows from loans to policyholders;
 - (iii) Changes that relate to transaction-based taxes collected on behalf of third parties (such as premium taxes, value added taxes and goods and services taxes) (see paragraph AG65(i));
 - (iv) Insurance finance revenue or expenses;
 - (v) Insurance acquisition cash flows (see paragraph AG125); and
 - (vi) Derecognition of liabilities transferred to a third party.
- (b) Changes that relate to services, but for which the entity does not expect consideration, i.e., increases and decreases in the loss component of the liability for remaining coverage (see paragraphs 47–52).

AG123A To the extent that an entity derecognises an asset for cash flows other than insurance acquisition cash flows at the date of initial recognition of a group of insurance contracts (see paragraphs 38(c)(ii) and B66A), it shall recognise insurance revenue and expenses for the amount derecognised at that date.

AG124. Consequently, insurance revenue for the period can also be analysed as the total of the changes in the liability for remaining coverage in the period that relates to services for which the entity expects to receive consideration. Those changes are:

- (a) Insurance service expenses incurred in the period (measured at the amounts expected at the beginning of the period), excluding:
 - (i) Amounts allocated to the loss component of the liability for remaining coverage applying paragraph 51(a);
 - (ii) Repayments of investment components;
 - (iii) Amounts that relate to transaction-based taxes collected on behalf of third parties (such as premium taxes, value added taxes and goods and services taxes) (see paragraph AG65(i));
 - (iv) Insurance acquisition expenses (see paragraph AG125); and
 - (v) The amount related to the risk adjustment for non-financial risk (see (b)).
- (b) The change in the risk adjustment for non-financial risk, excluding:
 - (i) Changes included in insurance finance revenue or expenses applying paragraph 87;
 - (ii) Changes that adjust the contractual service margin because they relate to future service applying paragraphs 44(c) and 45(c); and
 - (iii) Amounts allocated to the loss component of the liability for remaining coverage applying paragraph 51(b).
- (c) The amount of the contractual service margin recognised in surplus or deficit in the period, applying paragraphs 44(e) and 45(e).
- (d) Other amounts, if any, for example, experience adjustments for premium receipts other than those that relate to future service (see paragraph AG96(a)).

AG125. An entity shall determine insurance revenue related to insurance acquisition cash flows by allocating the portion of the premiums that relate to recovering those cash flows to each reporting period in a systematic way on the basis of the passage of time. An entity shall recognise the same amount as insurance service expenses.

AG126. When an entity applies the premium allocation approach in paragraphs 55–58, insurance revenue for the period is the amount of expected premium receipts (excluding any investment component and adjusted to reflect the time value of money and the effect of financial risk, if applicable, applying paragraph 56) allocated to the period. The entity shall allocate the expected premium receipts to each period of insurance contract service:

- (a) On the basis of the passage of time; but
- (b) If the expected pattern of release of risk during the coverage period differs significantly from the passage of time, then on the basis of the expected timing of incurred insurance service expenses.

AG127. An entity shall change the basis of allocation between paragraphs AG126(a) and AG126(b) as necessary if facts and circumstances change.

Insurance Finance Revenue or Expenses (paragraphs 87–92)

AG128. Paragraph 87 requires an entity to include in insurance finance revenue or expenses the effect of the time value of money and financial risk and changes therein. For the purposes of PBE IFRS 17:

- (a) Assumptions about inflation based on an index of prices or rates or on prices of assets with inflation-linked returns are assumptions that relate to financial risk;
- (b) Assumptions about inflation based on an entity's expectation of specific price changes are not assumptions that relate to financial risk; and
- (c) Changes in the measurement of a group of insurance contracts caused by changes in the value of underlying items (excluding additions and withdrawals) are changes arising from the effect of the time value of money and financial risk and changes therein.

AG129. Paragraphs 88–89 require an entity to make an accounting policy choice as to whether to disaggregate insurance finance revenue or expenses for the period between surplus or deficit and other comprehensive revenue and expense. An entity shall apply its choice of accounting policy to portfolios of insurance contracts. In assessing the appropriate accounting policy for a portfolio of insurance contracts, applying paragraph 16 of PBE IPSAS 3 *Accounting Policies, Changes in Accounting Estimates and Errors*, the entity shall consider for each portfolio the assets that the entity holds and how it accounts for those assets.

AG130. If paragraph 88(b) applies, an entity shall include in surplus or deficit an amount determined by a systematic allocation of the expected total finance revenue or expenses over the duration of the group of insurance contracts. In this context, a systematic allocation is an allocation of the total expected finance revenue or expenses of a group of insurance contracts over the duration of the group that:

- (a) Is based on characteristics of the contracts, without reference to factors that do not affect the cash flows expected to arise under the contracts. For example, the allocation of the finance revenue or expenses shall not be based on expected recognised returns on assets if those expected recognised returns do not affect the cash flows of the contracts in the group.
- (b) Results in the amounts recognised in other comprehensive revenue and expense over the duration of the group of contracts totalling zero. The cumulative amount recognised in other comprehensive revenue and expense at any date is the difference between the carrying amount of the group of contracts and the amount that the group would be measured at when applying the systematic allocation.

AG131. For groups of insurance contracts for which changes in assumptions that relate to financial risk do not have a substantial effect on the amounts paid to the policyholder, the systematic allocation is determined using the discount rates specified in paragraph AG72(e)(i).

AG132. For groups of insurance contracts for which changes in assumptions that relate to financial risk have a substantial effect on the amounts paid to the policyholders:

- (a) A systematic allocation for the finance revenue or expenses arising from the estimates of future cash flows can be determined in one of the following ways:
 - (i) Using a rate that allocates the remaining revised expected finance revenue or expenses over the remaining duration of the group of contracts at a constant rate; or
 - (ii) For contracts that use a crediting rate to determine amounts due to the policyholders—using an allocation that is based on the amounts credited in the period and expected to be credited in future periods.
- (b) A systematic allocation for the finance revenue or expenses arising from the risk adjustment for non-financial risk, if separately disaggregated from other changes in the risk adjustment for non-

financial risk applying paragraph 81, is determined using an allocation consistent with that used for the allocation for the finance revenue or expenses arising from the future cash flows.

- (c) A systematic allocation for the finance revenue or expenses arising from the contractual service margin is determined:
 - (i) For insurance contracts that do not have direct participation features, using the discount rates specified in paragraph AG72(b); and
 - (ii) For insurance contracts with direct participation features, using an allocation consistent with that used for the allocation for the finance revenue or expenses arising from the future cash flows.

AG133. In applying the premium allocation approach to insurance contracts described in paragraphs 53–59, an entity may be required, or may choose, to discount the liability for incurred claims. In such cases, it may choose to disaggregate the insurance finance revenue or expenses applying paragraph 88(b). If the entity makes this choice, it shall determine the insurance finance revenue or expenses in surplus or deficit using the discount rate specified in paragraph AG72(e)(iii).

AG134. Paragraph 89 applies if an entity, either by choice or because it is required to, holds the underlying items for insurance contracts with direct participation features. If an entity chooses to disaggregate insurance finance revenue or expenses applying paragraph 89(b), it shall include in surplus or deficit expenses or revenue that exactly match the revenue or expenses included in surplus or deficit for the underlying items, resulting in the net of the separately presented items being nil.

AG135. An entity may qualify for the accounting policy choice in paragraph 89 in some periods but not in others because of a change in whether it holds the underlying items. If such a change occurs, the accounting policy choice available to the entity changes from that set out in paragraph 88 to that set out in paragraph 89, or vice versa. Hence, an entity might change its accounting policy between that set out in paragraph 88(b) and that set out in paragraph 89(b). In making such a change an entity shall:

- (a) Include the accumulated amount previously included in other comprehensive revenue and expense by the date of the change as a reclassification adjustment in surplus or deficit in the period of change and in future periods, as follows:
 - (i) If the entity had previously applied paragraph 88(b)—the entity shall include in surplus or deficit the accumulated amount included in other comprehensive revenue and expense before the change as if the entity were continuing the approach in paragraph 88(b) based on the assumptions that applied immediately before the change; and
 - (ii) If the entity had previously applied paragraph 89(b)—the entity shall include in surplus or deficit the accumulated amount included in other comprehensive revenue and expense before the change as if the entity were continuing the approach in paragraph 89(b) based on the assumptions that applied immediately before the change.
- (b) Not restate prior period comparative information.

AG136. When applying paragraph AG135(a), an entity shall not recalculate the accumulated amount previously included in other comprehensive revenue and expense as if the new disaggregation had always applied; and the assumptions used for the reclassification in future periods shall not be updated after the date of the change.

The Effect of Accounting Estimates Made in Interim Financial Statements

AG137 If an entity prepares interim financial statements applying PBE IAS 34 *Interim Financial Reporting*, the entity shall make an accounting policy choice as to whether to change the treatment of accounting estimates made in previous interim financial statements when applying PBE IFRS 17 in subsequent interim financial statements and in the annual reporting period. The entity shall apply its choice of accounting policy to all groups of insurance contracts it issues and groups of reinsurance contracts it holds.

Appendix C

Effective Date and Transition

[Not used]

Appendix D

Amendments to other Standards

The amendments contained in this appendix when this Standard was issued in 2019 have been incorporated into the text of the relevant pronouncements.

Appendix E

Implementation Guidance for Public Sector Public Benefit Entities

This Appendix is an integral part of PBE IFRS 17 Insurance Contracts. It describes the application of paragraphs 6.1 and 6.2. The Appendix applies only to public sector public benefit entities and does not affect the application of PBE IFRS 17 by not-for-profit public benefit entities.

Introduction

- E1. PBE IFRS 17 *Insurance Contracts* incorporates IFRS 17 *Insurance Contracts*, issued by the International Accounting Standards Board. Consequently, the text of PBE IFRS 17 is generally expressed from the perspective of private sector entities. The NZASB prepared this Appendix to explain and illustrate the application of the principles of paragraphs 6.1 and 6.2 of the Standard by public sector public benefit entities in relation to identifying public sector arrangements that give rise to insurance contracts that fall within the scope of PBE IFRS 17.
- E2. Judgement needs to be exercised in applying the pre-requisites, indicators and other considerations based on each entity's circumstances.
- E3. For the purposes of this Appendix, in some cases relatively generic terms are used, rather than the more specific defined terms in PBE IFRS 17, because the guidance is focused on identifying the public sector activities to which PBE IFRS 17 applies. For example, this Appendix uses the term:
 - (a) 'Arrangement' on the basis that some public sector arrangements will fall within the scope of PBE IFRS 17 and be insurance contracts, but some will not; and
 - (b) 'Participant' on the basis that participants in arrangements that are insurance contracts will be policyholders, but participants in public sector arrangements that do not will fall within the scope of PBE IFRS 17 will not be policyholders.
- E4. The guidance in paragraphs AG7–AG16 of the Application Guidance on distinguishing between insurance risks and other risks applies equally to public sector entities. However, because public sector entities often undertake a wider range of risk-bearing activities than private sector entities, additional guidance is needed to identify insurance contracts in a public sector context.
- E5. Governments often arrange to provide support as a result of events that affect individuals and communities. Some of these arrangements involve transactions that are best accounted for as insurance contracts, while many of these arrangements relate to a government's role in providing services such as social benefits, universal health care and disaster relief. In determining which of these types of arrangements give rise to insurance contracts that fall within the scope of PBE IFRS 17, an entity considers the pre-requisites, indicators and the other considerations outlined in paragraphs E6–E36.

Identifying Insurance Contracts in a Public Sector Context (paragraphs 6.1 and 6.2)

Applying the Pre-requisites, Indicators and Other Considerations

- E6. In accordance with paragraph 6.1, a public sector entity would need to consider whether PBE IFRS 17 applies to an arrangement if, and only if, both of the following pre-requisites are established:
 - (a) The arrangement is enforceable – refer to guidance in paragraphs E9–E12; and
 - (b) The arrangement has an identifiable coverage period – refer to guidance in paragraphs E13–E17.
- E7. When both of the pre-requisites in paragraph E6 are established in respect of an arrangement, subject to paragraphs 8 and 8A an entity applies the following indicators on a collective basis to determine whether the arrangement gives rise to insurance contracts that fall within the scope of PBE IFRS 17:
 - (a) The source and extent of funding – refer to guidance in paragraphs E18–E22; and
 - (b) The similarity of risks covered and benefits provided – refer to guidance in paragraphs E23–E30.
- E8. When applying the indicators in paragraph E7 does not definitively determine whether an arrangement gives rise to insurance contracts that fall within the scope of PBE IFRS 17, a public sector entity applies

the following other considerations on a collective basis to determine whether the arrangement gives rise to insurance contracts that fall within the scope of PBE IFRS 17:

- (a) The management practices and assessment of financial performance applied – refer to guidance in paragraphs E31–E33; and
- (b) The existence of a separate fund, or earmarked assets, that are restricted to being used to meet benefits – refer to guidance in paragraphs E34–E36.

Pre-requisite: Enforceable Nature of Arrangement

- E9. An insurance contract is a contract under which one party (the insurer) accepts significant insurance risk from another party (the insured) by agreeing to compensate the insured if a specified future event adversely affects the insured. Under New Zealand Accounting Standards, a contract is an agreement between two or more parties that creates enforceable rights and obligations. When there is not an enforceable contract in respect of a public sector arrangement, that arrangement is not within the scope of PBE IFRS 17.
- E10. In determining whether there is an enforceable contract, the following matters are relevant:
 - (a) When a public sector entity or its controlling government does not have the practical ability under existing or substantively enacted legislation to deny or change promised benefits or amounts based on agreed parameters, it is indicative of an enforceable contract; and
 - (b) When an individual or entity can identify promised amounts or amounts based on agreed parameters that they will receive from the public sector entity on the occurrence of specified events, it is indicative of an enforceable contract.
- E11. When a public sector entity or its controlling government has the practical ability under existing or substantively enacted legislation to retrospectively deny or substantively change promised benefits or compensation, the policyholder does not have enforceable rights under the arrangement and the public sector entity does not have enforceable obligations for promised amounts or for amounts based on agreed parameters. For example, if an entity can retrospectively make a substantive change to the amount of benefits, such as by curtailing compensation being paid to a beneficiary in relation to a past event under existing legislation, this indicates the arrangement is not enforceable.
- E12. An arrangement that involves a public sector entity issuing documentation to another party, similar to an insurance contract issued by a private sector insurer, would be indicative of an agreement that creates enforceable rights and obligations. However, having some or all of the substantive rights and obligations for an insurance arrangement being set out in law or regulation would not necessarily mean that the arrangement is unsuitable to be accounted for as an insurance contract. In common with the private sector, arrangements need to be interpreted within a regulatory framework and, consistent with paragraphs 2 and 2.1, an entity is required to consider its substantive rights and obligations, whether they arise from a contract, law or regulation.

Pre-requisite: Identifiable Coverage Period

- E13. An insurance contract has an identifiable coverage period – either the period during which insured events occur (losses-occurring coverage) or the period during which claims become known (claims-made coverage).
- E14. In determining whether there is an identifiable coverage period for a public sector arrangement, the following factors may be relevant:
 - (a) There is documentation agreed between the public sector entity and a participant in an arrangement that identifies a period over which coverage is to be provided;
 - (b) Funding, for example from participant premiums or levies, is associated with coverage for an identifiable period that may, for example, be set out in law or regulation; and
 - (c) A public sector arrangement is an adjunct, for example based on law or regulation, to an insurance contract issued by another entity (e.g., a private sector insurer) and a coverage period for the public sector arrangement can be determined by reference to the insurance contract of the other entity.
- E15. In relation to paragraph E14(b), in some circumstances a public sector entity may be able to determine coverage periods for its arrangements based on the coverage periods identified when it sets premiums

and benefits. For example, an arrangement may have a coverage period aligned with the entity's annual reporting period on the basis that it sets premiums and benefits with the objective of raising funds from the arrangements in place in that year that are estimated to be sufficient to meet all the benefits, including future benefits, expected to arise from events that occur in that year.

- E16. In relation to paragraph E14(c), in some cases the period over which claims for benefits might arise under a public sector arrangement would be determinable from the period over which coverage is provided under an insurance contract issued by a private sector insurer. This may be the case when, for example, the public sector entity's arrangements are funded from a levy on the insurance contracts issued by private sector insurers and the levy is intended to meet claims for benefits arising from events that occur during the private sector insurance contract coverage periods. In other cases, the period over which claims for benefits might arise under a public sector arrangement may not be determinable from the period over which coverage is provided under an insurance contract issued by a private sector insurer. This may be the case when, for example, the public sector entity's arrangements are funded from a levy on the insurance contracts issued by private sector insurers in a particular period and the levy is intended to meet claims for benefits arising from events in that period, rather than from events during the private sector insurance contract coverage periods.
- E17. The following are examples of circumstances that would be indicative of an arrangement without an identifiable coverage period:
- (a) A public sector entity has an open-ended arrangement to provide benefits based on eligibility criteria that relate to an individual's inherent status, for example, age or disability;
 - (b) Those who stand to benefit from an arrangement are eligible for compensation based only on suffering loss from a specified natural disaster; and
 - (c) A public sector entity's policy is to raise funds from levies or by other means to meet claims from current and/or prior periods on a pay-as-you-go basis. Entities operating on a pay-as-you-go basis are focused on meeting net cash outflows expected to occur in the current period, rather than on meeting net cash outflows related to events that arise in a particular coverage period that may involve fund outflows expected to occur in both the current and future periods.

Indicator: Source and Extent of Funding

- E18. Under an insurance contract, a policyholder usually pays premiums to an insurer. In most cases, the premiums are the primary source of funding the payment of any claims and the costs of operating the insurance business.
- E19. When a public sector entity receives premiums or levies under an arrangement in exchange for accepting risks from those who stand to benefit, it is an indication that an arrangement gives rise to insurance contracts within the scope of PBE IFRS 17. The greater the extent to which the participant who stands to benefit from an arrangement is providing the funding, the more indicative this would be of a policyholder-insurer relationship and an arrangement that gives rise to insurance contracts that fall within the scope of PBE IFRS 17.
- E20. The individual or entity from which the public sector entity receives premiums does not need to be a direct beneficiary of the arrangement. Instead, they may be an indirect beneficiary. For example, when a public sector entity receives levies from the participant for the purpose of compensating other parties that might be damaged by the participant's actions, the benefit to the participant would often be that the damaged parties cannot seek additional compensation from them by other means.
- E21. When all of a public sector entity's funding to meet benefits is received in exchange for accepting risks from those who stand to benefit, this is highly indicative of an arrangement that gives rise to insurance contracts that fall within the scope of PBE IFRS 17. The lower the proportion of a public sector entity's funding to meet benefits in exchange for accepting risks from those who stand to benefit, the less likely it is that those arrangements would be accounted for as insurance contracts. For example, a co-payment from a beneficiary that is intended to help ration services and is not intended to fully fund services is unlikely to indicate an arrangement that gives rise to insurance contracts that fall within the scope of PBE IFRS 17. When a public sector entity receives a significant portion of funding from sources such as general taxation, this would indicate that an arrangement does not give rise to insurance contracts that fall within the scope of PBE IFRS 17.

- E22. Under most general insurance contracts issued by private sector insurers, in the event that a policyholder cancels its coverage prior to the end of the coverage period, the policyholder would ordinarily receive a pro rata premium refund, possibly adjusted for administrative costs. Although not all contracts issued by private sector insurers allow for refunds, the practice is indicative of insurance contracts. Accordingly, a public sector entity arrangement that allows for a refund of premium when the policyholder terminates the arrangement early is indicative of an arrangement that gives rise to insurance contracts that fall within the scope of PBE IFRS 17.

Indicator: Similarity of Risks Covered and Benefits Provided

- E23. Under an insurance contract, significant insurance risk is transferred from an insured to an insurer. Private sector insurers accept a wide range of risks. These include risks relating to, for example, property loss, loss of income, professional and trade indemnity, public and legal liability, medical costs, mortality and disability. In the event that an insured event occurs, to the extent required under a general insurance contract the insurer would typically provide a benefit commensurate with the loss.
- E24. It is an indicator that a public sector entity arrangement gives rise to insurance contracts within the scope of PBE IFRS 17 when it involves accepting risks and providing benefits that are the same as, or similar to, those offered by private sector insurers. In some cases, public sector entities operate alongside private sector insurers to accept risks and provide benefits that are the same, for example in respect of employer liability for workers' compensation risks.
- E25. In some cases, public sector entities are monopolies in their jurisdictions and there are no relevant counterpart arrangements of private sector entities to consider. In these cases, consideration is given to whether a public sector entity's arrangements involve accepting risks and providing benefits that are the same as, or are similar to, those offered by private sector insurers in other, similar jurisdictions. In relation to other jurisdictions, only information that is readily available need be considered. That is, public sector entities need not conduct an exhaustive search for counterpart arrangements.
- E26. The greater the level of similarity between the risks accepted and benefits provided by a public sector entity and those offered by any relevant counterpart private sector insurer, the more likely it would be that an arrangement gives rise to insurance contracts that fall within the scope of PBE IFRS 17.
- E27. In some cases, there will be a clear similarity between the risks being accepted and the benefits being provided by a public sector entity and private sector insurers, and this is highly indicative of an arrangement that gives rise to insurance contracts that fall within the scope of PBE IFRS 17.
- E28. Public sector entities often fill gaps in a market left by the private sector because they pose the greatest risks and might generally be unprofitable or unsustainable for the private sector to cover. Of itself, the level of riskiness generally is not relevant to determining whether there is similarity between the risks covered and the benefits provided by public sector entities and private sector insurers. The similarity of the nature of the risks covered and benefits provided is the key focus. Accordingly, the nature of a risk covered by a public sector entity and private sector insurers could be the same, even though the level of risk borne by the public sector entity is more extreme.
- E29. Many of the risks covered by private sector insurers are also the subject of social benefits provided by governments. Accordingly, while in some cases, the similarity of risks covered and benefits provided by a public sector arrangement to the risks and benefits under a social benefit program may help indicate whether that arrangement would be excluded from the scope of PBE IFRS 17, in many cases it may not.
- E30. It would be indicative of providing benefits that are the same as, or similar to, those offered by private sector insurers when an entity manages claims in order to provide benefits commensurate with participants' losses, rather than simply dispensing a fixed amount of compensation based on participants meeting specified eligibility criteria.

Other Consideration: Management Practices and Assessment of Financial Performance

- E31. Consideration is given to the extent to which a public sector entity has objectives, policies and processes for managing risks associated with its arrangements and has its financial performance assessed against those objectives and how successfully it applies those policies and processes in determining whether an arrangement gives rise to insurance contracts that fall within the scope of PBE IFRS 17. In that context, an entity that has insurance contracts would be expected to conduct the following activities (either itself or via outsourcing):

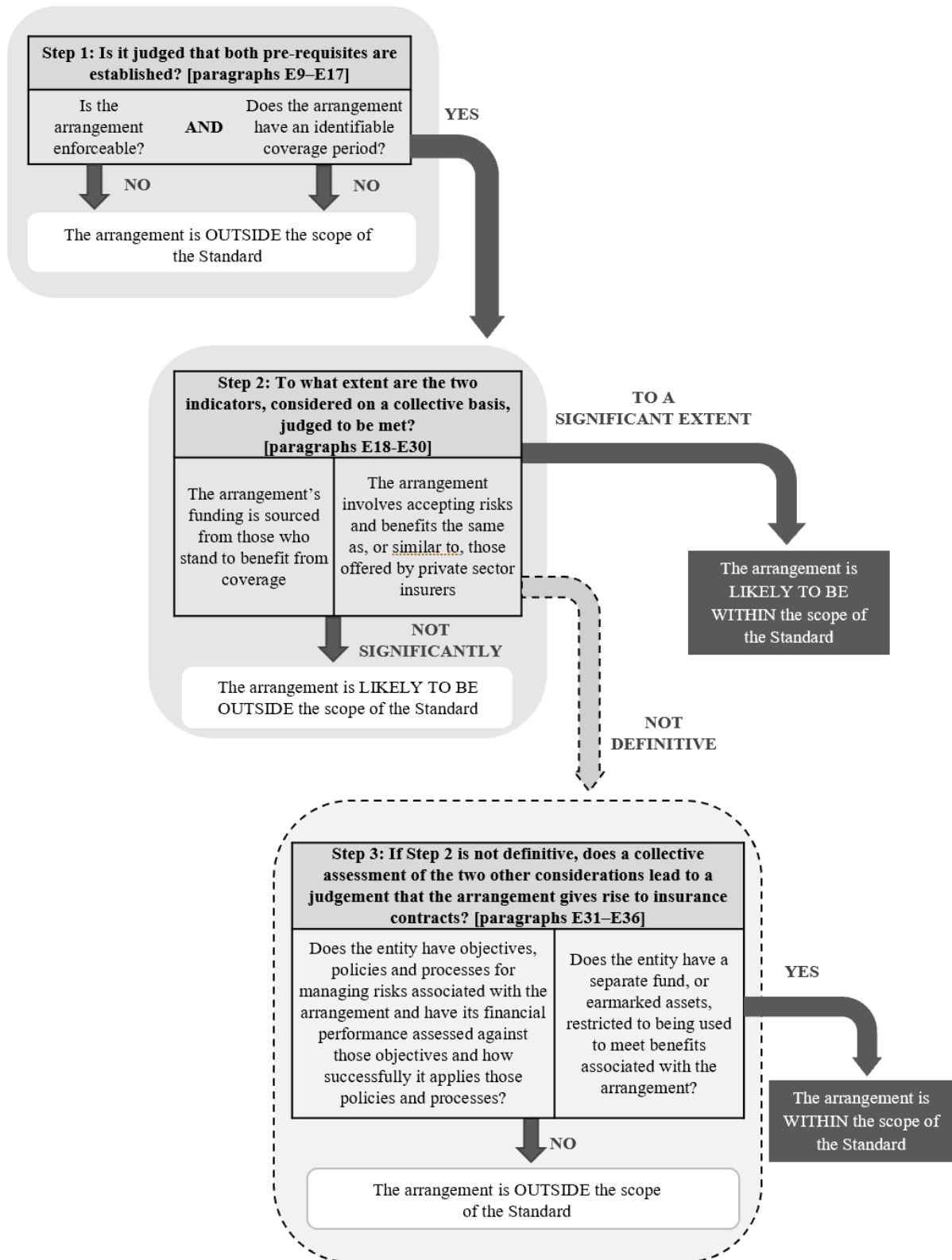
- (a) Underwriting and risk assessment;
 - (b) Managing the entity's capital based on the measurement of risks and uncertainties relating to coverage and incurred claims and their potential future impacts; and
 - (c) Fair and prudent claims management.
- E32. In general, any public sector entity that is responsible for dispensing compensation (as an insurer or non-insurer) would be expected to have sound practices in respect of risk assessment, managing capital and managing claims. However, these features of some public sector arrangements are still regarded as a relevant consideration, in conjunction with the indicators identified in paragraph E7 and the other consideration identified in paragraph E8(b), to determine whether an arrangement gives rise to insurance contracts that fall within the scope of PBE IFRS 17, when the indicators are not definitive.
- E33. In particular, it may imply that an arrangement gives rise to insurance contracts that fall within the scope of PBE IFRS 17 when an entity assesses the relative riskiness of participants and prices coverage based on those assessments. This does not mean an arrangement that involves an entity charging a standard amount to all participants, regardless of risk, is necessarily outside the scope of PBE IFRS 17, because some entities (even in the private sector) are subject to regulatory constraints on pricing (as acknowledged in paragraph 20), such as community-rated pricing.

Other Consideration: Assets Held to Meet Benefits

- E34. Consideration is given to whether there is a separate fund, or earmarked assets, that are restricted to being used to meet benefits in determining whether an arrangement gives rise to insurance contracts that fall within the scope of PBE IFRS 17.
- E35. The existence of a separate fund, or earmarked assets, that are restricted to being used to meet benefits is a feature of many types of public sector arrangements. However, the feature is still regarded as a relevant consideration, in conjunction with the indicators identified in paragraph E7 and the other consideration identified in paragraph E8(a), to determine whether an arrangement gives rise to insurance contracts that fall within the scope of PBE IFRS 17, when the indicators are not definitive.
- E36. To be relevant, the separate fund or earmarked assets need not be managed by the public sector entity itself. It is the existence of a separate fund or earmarked assets that is considered, not the performance of investing activities.

Diagram – Applying the Pre-requisites, Indicators and Other Considerations

- E37. The diagram below illustrates the application of paragraphs 6.1, 6.2 and E6–E8 relevant to public sector entities for identifying arrangements that give rise to insurance contracts that fall within the scope of PBE IFRS 17. The diagram should be read in conjunction with the guidance set out in paragraphs E9–E36, as referenced in the diagram.



Basis for Conclusions

This Basis for Conclusions accompanies, but is not part of, PBE IFRS 17.

- BC1. At the date of issuing PBE IFRS 17 *Insurance Contracts* the International Public Sector Accounting Standards Board (IPSASB) had not developed, nor had any plans of developing, an IPSAS for accounting for insurance contracts.
- BC2. When the PBE Standards were developed, the New Zealand Accounting Standards Board (NZASB) included PBE IFRS 4 *Insurance Contracts*, which was based on NZ IFRS 4 *Insurance Contracts*. Although NZ IFRS 4 included the requirements of IFRS 4 *Insurance Contracts*, it also included appendices that carried forward the accounting for insurance contracts that was applicable in New Zealand before the adoption of IFRS® Standards.
- BC3. In August 2017 the NZASB approved NZ IFRS 17 *Insurance Contracts*, which is identical to IFRS 17 *Insurance Contracts* except for a New Zealand-specific scope paragraph. On adoption, NZ IFRS 17 supersedes NZ IFRS 4 and its appendices.
- BC4. In December 2018 the NZASB issued NZASB ED 2018-7 PBE IFRS 17 *Insurance Contracts* (ED 2018-7). ED 2018-7 was based on NZ IFRS 17. The NZASB proposed no modifications to the recognition, measurement, presentation or disclosure requirements in NZ IFRS 17 for application by Tier 1 and Tier 2 public benefit entities (PBEs). However, the NZASB proposed a scope modification and limited changes to align terminology and ensure coherence with the suite of PBE Standards.
- BC5. When developing ED 2018-7 the NZASB observed that some public sector PBEs were applying the requirements of PBE IFRS 4 for ‘insurance-like’ activities that arose from statute rather than contract. The NZASB considered PBEs, specifically public sector PBEs, with such ‘insurance-like’ activities that would be outside the scope of NZ IFRS 17 should be captured within the scope of a PBE Standard based on NZ IFRS 17. ED 2018-7 proposed a modified scope to capture schemes that are eligible to apply the ‘insurance approach’ under IPSAS 42 *Social Benefits* and included related application guidance.
- BC6. Feedback from respondents on ED 2018-7 raised concerns with the proposals for public sector entities with ‘insurance-like’ activities funded through levies and emphasised that further consideration was needed to address public sector-specific issues. The NZASB did not receive any formal submissions from not-for-profit PBEs. However, informal feedback received did not indicate any concerns with the requirements in ED 2018-7 for not-for-profit PBEs.
- BC7. At the time of developing ED 2018-7 the NZASB was aware of several not-for-profit PBEs that carried out insurance activities in New Zealand and were required to be licensed by the Reserve Bank of New Zealand and subject to regulation. The NZASB was mindful that it is desirable for all licensed insurers to apply the same requirements when preparing general purpose financial reports.
- BC8. Considering the feedback received on ED 2018-7 and the desire for all licensed insurers to apply the same requirements, the NZASB agreed to issue PBE IFRS 17 *Insurance Contracts* for application by Tier 1 and Tier 2 not-for-profit PBEs only and undertake further work on public sector issues raised by respondents.

Amendments to PBE IFRS 17 (August 2020)

- BC9. In June 2019, the International Accounting Standard Board (IASB) issued for comment IASB ED/2019/4 *Amendments to IFRS 17* (ED/2019/4). The aim of the proposed amendments was to ease the implementation of IFRS 17 by reducing implementation costs and making it easier for entities to explain the results of applying IFRS 17 to investors and others. ED/2019/4 also included a proposal to defer the effective date of IFRS 17 by one year. ED/2019/4 was issued for comment in New Zealand.
- BC10. In August 2019, the NZASB issued for comment NZASB ED 2019-3 *Amendments to PBE IFRS 17* (ED 2019-3), which proposed equivalent amendments to PBE IFRS 17. However, ED 2019-3 did not propose to defer the effective date of PBE IFRS 17 because PBE IFRS 17 was originally issued with an effective date of 1 January 2022, which was the date the IASB proposed in ED/2019/4.
- BC11. During its redeliberations on ED/2019/4, the IASB decided to defer the effective date of IFRS 17 by two years, that is, from 1 January 2021 to 1 January 2023. Therefore, to ensure that the effective date of PBE IFRS 17 remained aligned with that of NZ IFRS 17, in June 2020 the NZASB issued

NZASB ED 2020-4 *PBE IFRS 17 – Deferral of Effective Date*. That ED proposed to defer the effective date of PBE IFRS 17 by a further year (from 1 January 2022 to 1 January 2023).

- BC12. In August 2020 the NZASB issued *Amendments to PBE IFRS 17*. This amending standard finalised the proposals in ED 2019-3 and ED 2020-4 and was aligned with *Amendments to NZ IFRS 17* issued in August 2020.

Public Sector Amendments June 2023

- BC13 This Basis for Conclusions summarises the Australian Accounting Standards Board's and the New Zealand Accounting Standards Board's considerations in reaching the conclusions on public sector modifications to AASB 17 *Insurance Contracts* and PBE IFRS 17 *Insurance Contracts*. It sets out the reasons why the Boards developed the modifications, the approach taken to developing those modifications and the bases for the key decisions made. In making decisions, individual Board members gave greater weight to some factors than to others.

Reasons for Making Public Sector Modifications

- BC14 AASB 17 and PBE IFRS 17, as first issued in 2017, have a mandatory application date of annual reporting periods beginning on or after 1 January 2023.
- BC15 IFRS 17 *Insurance Contracts*, which is incorporated into AASB 17/PBE IFRS 17, has been developed largely for the for-profit private sector, and to a relevant extent for a mutual entity context [AASB 17.B16/PBE IFRS 17.AG16]. IFRS 17 has not been designed to cater for the public sector context. Accordingly, the AASB and the NZASB undertook a joint project to consider the need for modifications in AASB 17/PBE IFRS 17 to suit the public sector context in Australia and New Zealand.
- BC16 There are important differences between the public sector and private sector contexts that can affect the manner in which IFRS 17 applies.
- BC17 While mutual entities may be not-for-profit entities in the sense that members share in any surpluses, they nonetheless would typically need to build and maintain reserves to remain in business by generating surpluses. Accordingly, the users of financial statements of private sector entities (including mutual entities) when compared with public sector entities can have very different perspectives on the significance of onerous contracts, compensation needed for bearing risk, and the need to hold capital. Key drivers of these different perspectives in the public sector can include monopoly powers, access to government guarantees and taxpayer funding and a focus on public policy objectives.
- BC18 Accordingly, there is a strong conceptual underpinning for having modifications to AASB 17/PBE IFRS 17 that are applicable only to public sector entities.
- BC19 In addition, there may be existing inconsistencies in Australia in the application of Standards as some Australian public sector entities with similar arrangements have been applying AASB 1023 *General Insurance Contracts* and others have been applying AASB 137 *Provisions, Contingent Liabilities and Contingent Assets*. The project is intended to help achieve a greater level of consistency of reporting across the Australian public sector.

Joint Project between the AASB and the NZASB

- BC20 In 2020, the AASB and the NZASB decided to work jointly to progress the project on insurance contracts in the public sector with the following background and objectives.⁵
- BC21 Both Boards maintain different tiers of reporting, which, among other things, use the 'public accountability' distinction developed by the IASB. Entities that hold assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses are identified as having public accountability. Both Boards generally regard entities engaged in insurance activities as having public accountability and needing to prepare Tier 1 general purpose financial statements.
- BC22 Some of the public sector entities in Australia that conduct insurance activities have self-identified as for-profit entities – most have self-identified as not-for-profit entities. In principle, Tier 1 for-profit public sector entities apply Australian Accounting Standards incorporating IFRS Standards without

⁵ At the time of undertaking the public sector modification project, the NZASB had already issued PBE IFRS 17 for not-for-profit public benefit entities. However, this Standard was not regarded as applying to arrangements of public sector public benefit entities.

modification. The *AASB Not-for-Profit Entity Standard-Setting Framework* notes the Financial Reporting Council's broad strategic direction that the AASB applies the principle of transaction neutrality (modified as necessary) in setting standards for not-for-profit and public sector entities. This Framework notes (emphasis added):

22 IFRS Standards (including Interpretations) are appropriate as a base for the following reasons: ...

- (d) **IFRS Standards can be modified appropriately for NFP-specific issues**, as demonstrated by the International Public Sector Accounting Standards Board (IPSASB) using IFRS Standards as a base for their corresponding Standards, **departing only to the extent appropriate for public sector issues**.

BC23 The following background applies for the NZASB.

(a) The *New Zealand Accounting Standards Framework* notes (emphasis added):

28. The accounting standards applying to the PBE tiers are as follows: ...

- PBE Tier 1: Tier 1 PBE Accounting Requirements – These are the requirements in the accounting standards (referred to as PBE Standards) and applicable authoritative notices.

They comprise International Public Sector Accounting Standards (IPSAS), **modified as appropriate for New Zealand circumstances** (for either public sector or NFP entities), together with additional standards as necessary and applicable authoritative notices.

- (b) Additional Accounting Standards for PBEs include IFRS Accounting Standards for which there is no equivalent IPSAS (for example, PBE IFRS 4) and domestic Accounting Standards.
- (c) In February 2018, the NZASB considered the application of the *Policy Approach to Developing the Suite of PBE Standards* (PBE Policy Approach) and decided to develop PBE IFRS 17. The trigger in the PBE Policy Approach for developing PBE IFRS 17 is the change to an IFRS Standard (IFRS 4 is superseded by IFRS 17) that has been used as the basis for a PBE Standard.
- (d) A further motivation for developing PBE IFRS 17 was to address arrangements that are eligible to apply the insurance approach as permitted under IPSAS 42 *Social Benefits* [PBE IFRS 17.BC5].⁶ (The insurance approach would involve applying IFRS 17 [IPSAS 42.AG19].)

Consistency in Financial Reporting – within and between Jurisdictions

BC24 The proposals in AASB Discussion Paper *Australian-specific Insurance Issues – Regulatory Disclosures and Public Sector Entities* (2017) identified as an objective “to achieve greater consistency of financial reporting across the public sector among entities engaging in insurance activities for the benefit of users of that information” [page 6]. While the NZASB has fewer public sector stakeholders with arrangements that might be accounted for as insurance contracts, consistency remains a key issue.

BC25 Although there is no binding agreement in place regarding public sector entities, to the extent feasible the Boards consider it would be desirable to have the same insurance Accounting Standards applying in Australia and New Zealand. This is because, for example, there can be useful benchmarking of financial position and performance of public sector entities between the two jurisdictions. Accordingly, the Boards consider that it is beneficial to have achieved a consistent outcome in the two jurisdictions such that AASB 17 and PBE IFRS 17 contain the same public sector modifications.

BC26 The public sector modifications to AASB 17/PBE IFRS 17 resulted from a wide-ranging due process that included:

⁶ IPSAS 42 does not require an entity that meets the criteria to apply the insurance approach – only that the entity is eligible to apply that approach.

- (a) the AASB and NZASB issuing AASB ED 319 *Insurance Contracts in the Public Sector* and NZASB ED 2022-3 *Insurance Contracts in the Public Sector* in March 2022, which had the same technical content;
- (b) the AASB and NZASB issuing a Draft Standard of the amendments to AASB 17/PBE IFRS 17 (and, in the case of the AASB only, AASB 1050 *Administered Items*) in October 2022 for fatal flaw comment;
- (c) direct stakeholder outreach, including consulting the Public Sector Focus Group, a sub-group of the Transition Resource Group for AASB 17 *Insurance Contracts*, which includes members from both jurisdictions;
- (d) the AASB issuing Discussion Paper *Australian-specific Insurance Issues – Regulatory Disclosures and Public Sector Entities* in 2017; and
- (e) the NZASB issuing Exposure Draft ED 2018-7 *PBE IFRS 17 Insurance Contracts* in 2018.

Both Boards have considered respondents' feedback from all of the above consultations.

BC27 The main focus of this Basis for Conclusions is on the most recent due process. The AASB project summary contains a summary of the project history, including the earlier due process stages of the project.

BC28 At the time of preparing this Basis for Conclusions, the IPSASB was not considering the development of an insurance Accounting Standard based on IFRS 17.

Sub-grouping of Contracts (Modifications to Paragraphs 14, 16 and 22)

Requirements under (Superseded) AASB 1023/PBE IFRS 4

BC29 The Boards observed that, under AASB 1023/PBE IFRS 4, the liability for remaining coverage is measured as the amount of premium received and/or receivable for the contract period that remains unearned. An insurer is required to apply a Liability Adequacy Test to the carrying amount of the liability for remaining coverage (represented by 'unearned premium') when there is an indication that the liability may be inadequate [AASB 1023.9.1/PBE IFRS 4 (Appendix D.9.1)]. The Liability Adequacy Test is applied at a portfolio of contracts level. The Boards noted that, in the case of some public sector entities, there is only one portfolio of contracts and, for those entities, the Liability Adequacy Test is effectively conducted at the whole-of-entity level.

BC30 The Liability Adequacy Test involves comparing:

- (a) the amount of the liability for remaining coverage recognised on the statement of financial position; with
- (b) current estimates of the present value of the expected future cash flows relating to future claims arising from existing insurance contracts, plus a risk margin that reflects the inherent uncertainty in the central estimate.

There is a deficiency if (a) is less than (b), in which case an additional 'unexpired risk liability' is recognised for the deficiency,⁷ which is also recognised immediately as a loss.⁸

Requirements in AASB 17/PBE IFRS 17: Sub-grouping of Onerous versus Non-onerous Contracts

BC31 AASB 17/PBE IFRS 17 has a much greater emphasis (than AASB 1023/PBE IFRS 4) on identifying onerous contracts and their identification has fundamental impacts on a wide range of accounting outcomes. In particular, at initial recognition, insurance contracts within each portfolio of contracts must be sub-grouped as:

- (a) contracts that are onerous at initial recognition, if any;

⁷ Because a deficiency is not represented by 'unearned premium' in the context of AASB 1023/PBE IFRS 4, the deficiency is separately recognised as an 'unexpired risk liability'.

⁸ An entity with deferred acquisition costs and intangible assets related to insurance contracts would write those off before recognising any remaining deficiency [AASB 1023.9.1/PBE IFRS 4 (Appendix D.9.1)]; however, public sector entities do not ordinarily have material deferred acquisition costs or intangible assets.

- (b) contracts that have no significant possibility of becoming onerous subsequently, if any; and
- (c) other (non-onerous) contracts [AASB 17/PBE IFRS 17.16].

BC32 The Boards noted the following:

- (a) In the private for-profit sector,⁹ the presumption is that insurers issue insurance contracts that are intended to be profitable. In practice, the profit component should act as a ‘buffer’ to any liability inadequacy and private for-profit sector insurers only occasionally need to test for liability inadequacy and few entities need to recognise an unexpired risk liability under AASB 1023/PBE IFRS 4.
- (b) In contrast, for most public sector entities applying AASB 1023/PBE IFRS 4, the liability for remaining coverage based on unearned premium is routinely inadequate because they price to break even on a best-estimate basis after taking into account projected investment returns.¹⁰ That is, the amounts collected in levies/premiums are typically inadequate to meet expected claims. Accordingly, many public sector entities routinely recognise unexpired risk liabilities under AASB 1023/PBE IFRS 4.

The Boards highlighted this as a key distinguishing factor among public sector entities compared with private sector for-profit entities.

BC33 The Boards acknowledged that there are no public-sector-specific modifications to AASB 1023/PBE IFRS 4 based on this key distinguishing factor and that the routine recognition of unexpired risk liabilities, which are typically offset by investment income/gains, is an accepted practice. However, the Boards noted that the AASB 17/PBE IFRS 17 requirement to sub-group contracts based on whether they are onerous versus non-onerous raises further potential accounting complications. In particular, the Boards observed that:

- (a) accounting for a whole portfolio that is onerous is likely to be relatively simple compared with having to identify some (possibly) non-onerous contracts from within a largely onerous portfolio of contracts and account for them separately;
- (b) the level of interest among public sector entities and their users in knowing about profitable sub-groups of contracts that might exist within a wider loss-making portfolio, would be lower than the level of interest among private sector insurers and their users in knowing about loss-making sub-groups of contracts that might exist within a wider profitable portfolio; and
- (c) any interest among users of public sector entities’ financial statements in knowing about cross-subsidisation among different classes of policyholders would probably be best met through disclosures (rather than disaggregation that affects recognition and measurement).

Analysis on Sub-grouping by Onerous versus Non-onerous Contracts

BC34 The Boards noted that:

- (a) there is no impact on the long-run overall results from taking different approaches to onerous contract units of account and annual cohorts of contracts versus a portfolio unit of account; and
- (b) the main impact of AASB 17/PBE IFRS 17 (relative to AASB 1023/PBE IFRS 4) would be to recognise losses up-front that would otherwise have been recognised over the coverage period. The Boards thought that, since most of the coverage periods are typically one year, the timing of loss recognition would typically not be very different as between AASB 17/PBE IFRS 17 and AASB 1023/PBE IFRS 4.

BC35 The Boards observed that the IASB decided on the requirements in AASB 17/PBE IFRS 17.16 to divide each portfolio of contracts into sub-groups because it regards information about onerous contracts to be useful information about an entity’s decisions on pricing contracts and about future cash flows, and wants this information to be reported on a timely basis. The IASB does not want this information to be obscured by offsetting onerous contracts in one group with profitable contracts in another group

⁹ As noted in paragraphs BC15 and BC17, this is also generally the case for mutual entities in the private sector.

¹⁰ The expected investment returns are ordinarily higher than the discount rates (for time value) applied to measure insurance liabilities.

[IFRS 17.BC119].¹¹ The Boards acknowledged that the up-front recognition of losses may be particularly useful in a private sector for-profit context.

- BC36 The Boards observed that the impact of AASB 17/PBE IFRS 17 would depend on the nature of the arrangements and how they have been priced and they considered the following examples by way of illustration.
- (a) Worker's compensation insurance contracts are typically priced for the expected actual risks by employer and/or industry. At initial recognition, unless a deliberate decision has been taken to under-price for risk on some contracts and over-price others, ordinarily there would not be onerous and non-onerous sub-groups. Typically, in a public sector context (of break-even pricing after taking into account investment earnings), the portfolio would be expected to comprise only one group of onerous contracts.
 - (b) Transport accident insurance contracts are typically priced for the expected actual risks over the whole portfolio. However, the public sector entity might have relatively granular information available about policyholders by risk profile. For example, it may be known that drivers living in particular geographic regions are likely, on average, to give rise to fewer claims and are largely profitable. In such a case there may be onerous and non-onerous groups of contracts based on geographic regions.
- BC37 The Boards noted that AASB 17/PBE IFRS 17.20 provides relief from sub-grouping as onerous versus non-onerous contracts when contracts within a portfolio would fall into different groups only because law or regulation specifically constrains the entity's practical ability to set a different price or level of benefits for policyholders with different characteristics. Accordingly, in the transport accident case noted above, if the pricing constraints on the entity are the cause of overpricing for low-claim geographic regions, they need not be separately accounted for (as a non-onerous contract group). However, the Boards remained concerned that this relief may be difficult to apply in some cases due to possible ambiguity about where price/levy/benefit decision-making power may reside – with the entity itself, or with the government, for example, the relevant Minister(s).
- BC38 The Boards considered feedback received from stakeholders on sub-grouping of contracts in response to consultation that preceded AASB ED 319/NZASB ED 2022-3.
- BC39 NZASB ED 2018-7 proposed no changes to PBE IFRS 17 in respect of onerous contracts; however, it specifically sought feedback from stakeholders on the requirements in PBE IFRS 17.16. The responses to NZASB ED 2018-7 generally argued for public-sector-specific modifications based on a view that the requirements in PBE IFRS 17.16 are not relevant to the circumstances of public sector insurers in New Zealand. The responses included the following:
- (a) pricing decisions and the resulting onerous contracts will often be a consequence of broader policy decisions of government;
 - (b) the level of aggregation should be the same as the level used for setting levies;
 - (c) while for-profit insurers use granular information to improve profitability and avoid adverse selection by policyholders – this is not relevant to public sector entities, which typically deliberately cross-subsidise across communities;
 - (d) public sector entities do not choose their customers or seek to market their services to particular customers, and risks are usually community rated – accordingly, grouping by onerous/non-onerous arrangements is not relevant.
- BC40 The AASB Discussion Paper (2017) did not specifically request input on this topic and there were no comments from stakeholders on onerous contract groups. However, the topic was raised in stakeholder outreach in Australia and New Zealand conducted in 2020-21 and the following matters were raised.
- (a) In any given year, all contracts in a portfolio are likely to be onerous at initial recognition because the entity relies on investment returns to break even. That is, amounts raised from the levies/premiums charged are inadequate relative to expected claims and there will be a negative insurance service result (negative underwriting result). Accordingly, unless there is sound

¹¹ The IASB chose groups of contracts as a way of striking a compromise between accounting on an individual contract basis (that would be particularly burdensome) and accounting at the portfolio level of aggregation [IFRS 17.BC123 & BC124].

evidence of a non-onerous group of contracts there would be no disaggregation of the portfolio under AASB 17/PBE IFRS 17.

- (b) Given that some entities do not price differentially based on policyholder-specific risks, they do not monitor (and may not possess) the information necessary to differentiate between onerous versus non-onerous contracts at initial recognition. For example, some entities are not permitted to hold information on gender or age; however, if available, gender and/or age-related information would enable the entity to identify onerous versus non-onerous contracts.
- (c) Ordinarily, all of a public sector entity's onerous contracts and non-onerous contracts would be the result of regulatory impediments that are covered by the relief in AASB 17/PBE IFRS 17.20; however, there may be exceptions.
- (d) The entity takes a long-term view to avoid volatility in premiums/levies – periodically, there may be profitable or onerous contracts that depend on whether, for example, there are deficits to be 'rectified' or surpluses to be 'used up'.

BC41 The Boards considered a number of possible approaches to addressing the sub-grouping of contracts in a public sector context, including the following.

- (a) All public sector entities should be exempted from AASB 17/PBE IFRS 17.16, on the basis that:
 - (i) timely information on profitability is not relevant to most public sector entities; and
 - (ii) whether public sector entities have portfolios of onerous contracts and sub-groups of onerous contracts;

are not relevant. However, it was acknowledged that information on sub-groups of onerous contracts might be useful in helping to inform users about cross-subsidies between different classes of policyholders.
- (b) Only not-for-profit public sector entities (which is the majority of the relevant entities) should be exempted from AASB 17/PBE IFRS 17.16 for the reasons noted in (a) above.
- (c) All public sector entities should be exempted from AASB 17/PBE IFRS 17.16; however, require disclosure about the nature of the pricing process, including constraints under which an entity operates to cross-subsidise different policyholder cohorts, that can lead to some groups of contracts being onerous. This might provide additional relevant information about the impact of price constraints on each entity. However, it was acknowledged that the additional disclosure could be a burden and may already be readily available from other sources (although the burden might be mitigated by permitting disclosure by cross-reference).
- (d) AASB 17/PBE IFRS 17.16 should apply to public sector entities and guidance should be provided for the public sector context on the manner in which AASB 17/PBE IFRS 17.20 would provide relief from the need to sub-group contracts.

Sub-grouping Onerous versus Non-onerous Contracts – Proposals for AASB ED 319/NZASB ED 2022-3

BC42 Based on the above deliberations, the Boards decided to propose an exemption for all public sector entities from applying the requirements in AASB 17/PBE IFRS 17.16. That is, public sector entities would not be required to sub-group contracts based on whether, at initial recognition, they are:

- (a) onerous;
- (b) have no significant possibility of becoming onerous subsequently, or
- (c) are neither (a) nor (b).

BC43 The Boards consider this exemption is justified for the following reasons.

- (a) The motivation behind the AASB 17/PBE IFRS 17 requirements for information about onerous contracts is useful information about an entity's decisions on pricing contracts, which is not as relevant in the public sector context (relative to the private sector). This is particularly the case for not-for-profit entities. However, even public sector entities that are identified as for-profit entities are typically not able to underwrite risks in the manner available to private sector insurers

and, therefore, disaggregating onerous versus non-onerous contracts would not provide useful information for assessing a public sector entity's financial position or performance.

- (b) Public sector entities' information systems are often geared to identifying, at a broad level, high-risk groups of policyholders for strategic and government policy decision-making (for example, to conduct safety campaigns), but not necessarily for identifying separate groups of contracts that give rise to accounting profits or losses. The managements of public sector entities (whether for-profit or not-for-profit) typically do not seek to financially remediate groups of onerous contracts or seek to attract more profitable customers in the same manner as private sector insurers. And, unlike private sector insurers, public sector entities do not ordinarily choose the customers to which they market their products. Accordingly, the costs for public sector entities of disaggregating onerous versus non-onerous groups of contracts would exceed any likely benefits.
- (c) If public sector entities are subject to AASB 17/PBE IFRS 17.16, it would be necessary to explain how the relief in AASB 17/PBE IFRS 17.20 could be applied in a public sector context. That would mean explaining whether the constraints identified in AASB 17/PBE IFRS 17.20 would be constraints imposed only on the entity itself or on the entity and its controlling government, including any relevant Minister(s). In the context of AASB 17/PBE IFRS 17, there is the potential for ambiguity in considering whether:
 - (i) a public sector entity's practical ability to fully price for risks or benefits includes the ability of its controlling government, and any relevant Minister(s), to decide on pricing or benefits in their capacity as managers of the public sector entity; versus
 - (ii) overall pricing constraints relevant to AASB 17/PBE IFRS 17.20 in respect of government policy more broadly.

- BC44 The Boards also considered that the differences (from the private sector) in the accountability/regulatory, governance and financial management frameworks in general among public sector insurers might also justify an exemption for all public sector entities from applying the requirements in AASB 17/PBE IFRS 17.16.¹²
- BC45 The Boards decided to propose requiring additional disclosures about the nature of the pricing process; including information about the manner in which pricing/benefits are determined, the timeframes for which they are typically determined, and any other relevant constraints under which an entity operates that result in, for example, cross-subsidising different classes of policyholders. The Boards noted that this information may already be publicly available from other sources and that the proposed requirement could be met by cross-reference to relevant authoritative sources available to users of the financial statements on the same terms as the financial statements and at the same time.
- BC46 The Boards acknowledged that, in general, Accounting Standards do not require disclosures around pricing decisions and whether they involve cross-subsidisation among customers. However, the Boards considered proposing this additional disclosure is justified due to the likely significance of the manner in which pricing/benefits are determined on the performance and financial position of public sector entities that bear insurance risk.

Sub-grouping of Contracts Issued no more than a Year Apart

- BC47 The Boards observed that portfolios of contracts might include contracts entered into over successive years, and that AASB 17/PBE IFRS 17 requires entities to divide each portfolio of contracts into sub-groups of contracts issued no more than a year apart [AASB 17/PBE IFRS 17.22]. The effect of this requirement is to reveal cases of onerous contracts issued in a particular year without them being obscured by profitable contracts issued in other years. This is mainly an issue when there are contracts with multi-year coverage periods.
- BC48 The Boards noted that, given the monopoly position of many public sector entities, they may phase in increases and decreases to levies/premiums and the extent to which arrangements might be onerous or non-onerous for any given annual cohort of contracts is likely to be less relevant than for a private sector for-profit insurer.

¹² In that context, the Boards noted: paragraph 30(g) of the [AASB Not-for-Profit Entity Standard-Setting Framework](#); and, to some extent, paragraph 62 of the [New Zealand Accounting Standards Framework](#).

- BC49 The Boards noted that some of the responses to NZASB ED 2018-7 argued for a public sector modification based on the view that the requirement in PBE IFRS 17.22 is not relevant to the circumstances of some public sector insurers that take a long view on pricing. That is, for example, grouping by annual cohort is irrelevant when the insured risk is for highly uncertain and infrequent events where the entity is a monopoly provider (and cannot withdraw from the market).

Analysis of Sub-grouping of Contracts Issued no more than a Year Apart

- BC50 The Boards noted that the IASB decided to require sub-grouping of contracts issued no more than a year apart because it considers annual grouping by the underwriting year to be important to ensure that trends in the profitability of a portfolio of contracts are reflected in the financial statements on a timely basis [IFRS 17.BC136].
- BC51 In the context of the Australian and New Zealand public sectors, the Boards observed the following.
- (a) Many public sector entities would only issue contracts with one year of coverage and the difference between the portfolio perspective versus sub-grouping by annual cohort would not be particularly relevant. However, some public sector entities issue contracts that provide multi-year coverage – for example, in respect of domestic building risk coverage arrangements, and there may exist onerous versus non-onerous annual cohorts of contracts.
 - (b) When relevant, the requirement in AASB 17/PBE IFRS 17.22 to identify separate groups of contracts by their year of issue is expected to result in insurers identifying their reporting period as the relevant period. Australian and New Zealand public sector entities have 1 July to 30 June reporting periods and, if they were to comply with AASB 17/PBE IFRS 17.22, would be expected to regard all contracts issued between 1 July and 30 June as being within one group of contracts.
- BC52 The Boards noted that the AASB 17/PBE IFRS 17.22 requirement to determine groups of contracts based on the underwriting year as the unit of account for the liability for remaining coverage could have flow-on consequences for the information that needs to be produced to manage the liability for incurred claims (unless insurers operate two parallel systems). This might be the case for the following reasons.
- (a) Claims are usually monitored in the context of the related levies/premiums ‘earned’, and premium ‘earning’ under AASB 17/PBE IFRS 17 would be based on the underwriting year used for the liability for remaining coverage under AASB 17/PBE IFRS 17.22.
 - (b) Many public sector entities tend to manage claims on an accident year basis because claims management plays such a prominent role for public sector entities, rather than profitability and underwriting performance.¹³ Under an accident year basis, all claims arising from incidents/accidents within a particular annual period are tracked over time and compared year-on-year with levies/premiums earned in that year for the related contracts, regardless of when those contracts were issued/underwritten.
 - (c) For some public sector entities, the underwriting year and the accident year are the same due to most (or all) contracts being issued with coverage that coincides with the annual reporting period. However, for other public sector entities they are different.
- BC53 The Boards also noted that some insurance risks relate to providing coverage for highly uncertain infrequent events. While the coverage period for contracts for these risks are often only one year, the insured events might be expected to occur many years apart. Accordingly, in years when there are no relevant events, the contracts are highly profitable; while in years when a relevant event occurs, the contracts result in large losses. The Boards observed that:
- (a) from the perspective of a private sector insurer that can choose to engage in these contracts or withdraw from the market, sub-grouping contracts by their year of issue (underwriting year) based on AASB 17/PBE IFRS 17.22 might help track this profit or loss volatility; while
 - (b) from the perspective of a public sector entity that is a monopoly and cannot choose to withdraw from the market, sub-grouping contracts by their year of issue (underwriting year) based on

¹³ The liability for incurred claims is also the focus of management attention for most public sector entities because their liabilities for incurred claims are usually much larger than their liabilities for remaining coverage.

AASB 17/PBE IFRS 17.22 seems much less relevant. For these entities, tracking sub-groups of contracts by the year in which the infrequent events occur (accident year) might be more relevant.

Sub-grouping of Contracts Issued no more than a Year Apart – Proposals for AASB ED 319/NZASB ED 2022-3

- BC54 Based on the above deliberations, the Boards decided to propose an exemption for all public sector entities from applying the requirements in AASB 17/PBE IFRS 17.22. The Boards consider this exemption is justified for the following reasons:
- (a) The IASB's reasoning behind the requirements (annual groupings by issue date are important to ensure that trends in the profitability of a portfolio of contracts are reflected in the financial statements on a timely basis) is generally less crucial (or is unimportant) to public sector entities.
 - (b) The main focus of interest among public sector entities is on claims experience rather than profitability or underwriting performance. Some of those entities would track and manage claims on an accident year basis (not an underwriting year). Others use an underwriting year basis. Some entities track claims on both bases. Managements are likely to continue their existing tracking focus (which they have found to be effective) even if the external reporting requirements changed to groups based on the date when contracts are issued. The costs for some entities of operating a parallel tracking system (based on the underwriting year) to facilitate external reporting would not justify any benefits that might arise from applying AASB 17/NZ IFRS 17.22.
 - (c) The requirement in AASB 17/PBE IFRS 17.57 to compare the liability for remaining coverage¹⁴ with the fulfilment cash flows that relate to remaining coverage when facts and circumstances indicate a group of insurance contracts is onerous could be applied at the portfolio level.¹⁵ Given that, for most public sector entities, the liability for remaining coverage is routinely inadequate because they price to break even after taking into account projected investment returns, exempting public sector entities from applying the requirements in AASB 17/PBE IFRS 17.22 would rarely (if ever) result in delayed recognition of onerous contracts.

Sub-grouping Contracts – AASB ED 319/NZASB ED 2022-3 Feedback and Board Conclusions

- BC55 All respondents to AASB ED 319/NZASB ED 2022-3 who commented on the proposal to exempt public sector entities from sub-grouping between onerous and non-onerous contracts were supportive. Their support was based substantively on the reasons outlined in paragraphs BC43 and BC44. Some respondents particularly noted:
- (a) the monopoly and community-wide nature of many public sector arrangements makes them unsuitable for sub-grouping based on profitability;
 - (b) there is no loss-leading in public sector arrangements that users might find interesting in a commercial context;
 - (c) performance at the portfolio level is generally a more relevant benchmark for public sector entities.
- BC56 All respondents to AASB ED 319/NZASB ED 2022-3 who commented on the proposal to exempt public sector entities from sub-grouping contracts issued no more than a year apart were supportive. Their support was largely based on the reasons provided by the Boards in paragraphs BC52 and BC53.
- BC57 Based on the feedback received from stakeholders and the reasoning applied by the Boards in determining their proposals, the Boards concluded that paragraphs 16 and 22 would be modified so that public sector entities would be exempted from the requirements of these two paragraphs.
- BC58 The Boards noted that the practical impact of these exemptions is that public sector entities would be permitted to have a basic unit of account that is a portfolio (also see the discussion above on groups of contracts issued no more than a year apart). Accordingly, their liabilities for remaining coverage and liabilities for incurred claims would be permitted to be measured for each portfolio as a whole (and, for

¹⁴ Calculated using the premium allocation approach, which public sector entities may choose to apply under AASB 17/PBE IFRS 17.

¹⁵ This is the level at which the Liability Adequacy Test is currently applied under AASB 1023.9.1/PBE IFRS 4 (Appendix D.9.1).

those entities with only one portfolio, effectively at the whole-of-entity level). The Boards concluded that paragraph 14 would be modified to clarify this point.

Terminology

- BC59 The Boards are conscious that most of the requirements in AASB 17/PBE IFRS 17 make reference to ‘group(s) of contracts’, ‘group(s) of insurance contracts’, and ‘same group’ because it has been drafted for private sector entities that would typically have groups of insurance contracts as their main unit of account. However, public sector entities applying the exemption from sub-grouping would read, for example, the reference in AASB 17/PBE IFRS 17.57 to: “If at any time during the coverage period, facts and circumstances indicate that a **group of insurance contracts** is onerous, ...” as requiring: “If at any time during the coverage period, facts and circumstances indicate that a **portfolio of insurance contracts** is onerous, ...”.
- BC60 The Boards also note that entities are generally expected to read the requirements of AASB 17/PBE IFRS 17 based on their own circumstances. For example, when relevant, entities are required to regard references in AASB 17/PBE IFRS 17 to ‘insurance contracts’ as applying to ‘reinsurance contracts held’ in accordance with AASB 17/PBE IFRS 17.4. Therefore, the Boards concluded that public sector entities should be capable of reading AASB 17/PBE IFRS 17, when relevant, as applying to a portfolio unit of account and decided that no public-sector specific terminology modifications are needed regarding the terms ‘group(s)’ and ‘portfolio(s)’.

Initial Recognition when Contracts are Onerous (Modification to Paragraph 25)

- BC61 In general, the following applies under AASB 1023/PBE IFRS 4.
- (a) An insurance liability is recognised when premium is received or receivable, because the measurement model simply defers unearned premiums received or receivable on the balance sheet. Premiums might be received before coverage begins, on the day coverage begins or after coverage begins.
 - (b) An unexpired risk liability (onerous contract loss) is recognised based on whether unearned premiums are adequate to meet expected future claims and other relevant costs. Accordingly, loss recognition is dependent on when unearned premiums are recognised on the balance sheet.
- BC62 In contrast, AASB 17/PBE IFRS 17.25 requires a group of insurance contracts an entity issues to be recognised from the earliest of the following:
- (a) the beginning of the coverage period of the group of contracts;
 - (b) the date when the first payment from a policyholder in the group becomes due; and
 - (c) for a group of onerous contracts, when the group becomes onerous.
- BC63 The Boards observed that, for the onerous contract trigger in AASB 17/PBE IFRS 17.25(c) to be the earliest date, the insurer would have already accepted the insured’s risk before coverage commences and before premiums are due and there are facts and circumstances indicating a group of insurance contracts is onerous.¹⁶ Accordingly, there would need to be up-front loss recognition for any onerous contracts that have been entered into as at the balance date, even though the coverage period may only commence in the subsequent reporting period. This reflects the emphasis in AASB 17/PBE IFRS 17 on the early recognition of onerous contract losses.
- BC64 The Boards observed that the differing circumstances of public sector entities compared with their private sector counterparts would potentially mean that applying AASB 17/PBE IFRS 17.25(c) would have unhelpful accounting consequences.
- (a) Private sector for-profit insurers would typically only by exception knowingly issue onerous contracts [see the perspective in IFRS 17.BC135]. However, most public sector entities routinely issue onerous contracts (because levies/premiums charged are inadequate to cover expected claims).

¹⁶ Based on IFRS 17.BC140 to BC144.

- (b) Private sector insurers will typically have contracts commencing throughout their reporting period and, therefore, only a relatively small portion of contracts that commence in the following year would typically be enforceable on the entity at any given reporting date. However, some public sector entities have a large portion of their contracts covering periods that coincide with their reporting period. Accordingly, for these entities, all or most of next year's contracts could be enforceable on the entity at each reporting date.

The Boards noted that, for an entity that has enforceable arrangements in the weeks before year end for the following 1 July to 30 June coverage period, applying AASB 17/PBE IFRS 17.25(c) would mean all of the onerous contract losses associated with next year's arrangements would need to be included in the current year's results. While this may not have a major impact year-on-year, the Boards thought it would be a counter-intuitive outcome.

Initial Recognition when Contracts are Onerous – Proposals for AASB ED 319/NZASB ED 2022-3

BC65 Based on the above deliberations, the Boards decided to propose an exemption for all public sector entities from applying the requirements in AASB 17/PBE IFRS 17.25(c). The Boards considered this exemption is justified for the following reasons.

- (a) The consequences of applying AASB 17/PBE IFRS 17.25(c) to some public sector insurers would be potentially burdensome from a practical viewpoint, since their systems are not currently set up to capture this information, and would lead to information that is not useful for users of the financial statements. This is because, for some public sector entities, on an ongoing basis, the results for the current period would include the onerous contract losses of all or most of the following year's contracts.
- (b) AASB 17/PBE IFRS 17.25(c) was conceived in the context of private sector for-profit insurers for which, in theory, onerous contracts would be the exception and for which enforceable contracts as at the reporting date that relate to the following year of coverage would be a relatively small proportion of total contracts.

Initial Recognition when Contracts are Onerous – AASB ED 319/NZASB ED 2022-3 Feedback and Board Conclusions

BC66 All respondents to AASB ED 319/NZASB ED 2022-3 who commented on the proposal to exempt public sector entities from applying the requirements in AASB 17/PBE IFRS 17.25(c) were supportive. Their support was based substantively on the reasons outlined in paragraph BC65. Some respondents particularly noted that, without the exemption, there could be an adverse impact on the usefulness of the information in financial statements to users, in particular for some workers compensation and public indemnity insurers that have coverage periods aligned to annual reporting periods which would result in the recognition of future year onerous contracts late in the current year.

BC67 Based on the feedback received from stakeholders and the reasoning applied by the Boards in determining their proposals, the Boards concluded that paragraph 25 would be modified so that public sector entities would be required to recognise insurance contracts an entity issues from the earliest of:

- (a) the beginning of the coverage period of the group of contracts; and
- (b) the date when the first payment from a policyholder in the group becomes due.

Determining Contract Boundaries, Coverage Periods and Eligibility for the Premium Allocation Approach (Modifications to Paragraph 34)

BC68 The Boards noted that contract boundaries and coverage periods under AASB 17/PBE IFRS 17 are crucial for two main reasons:

- (a) identifying the cash flows used to measure liabilities for remaining coverage for in-force arrangements; and
- (b) determining whether liabilities for remaining coverage for in-force arrangements are eligible to be measured by applying the premium allocation approach.

Contract Boundaries and Coverage Periods of Public Sector Arrangements

- BC69 The Boards noted that, of the public sector arrangements that might fall within the scope of AASB 17/PBE IFRS 17:
- (a) most have ‘stated’ coverage periods of one year; however
 - (b) a minority of arrangements have coverage periods longer than a year, including:
 - (i) for example, arrangements issued in respect of construction and home building risks; and
 - (ii) some reinsurance contracts held.
- BC70 Arrangements between public sector entities and their policyholders ordinarily include an identified period that is presumed to be the coverage period for the purposes of applying AASB 1023/PBE IFRS 4. For example, the stated period of cover for arrangements relating to transport accidents or workers’ compensation would usually be one year and the liabilities and revenues are recognised on this basis.
- BC71 The Boards acknowledged that AASB 17/PBE IFRS 17 does not make this same presumption. Under AASB 17/PBE IFRS 17, the coverage period might be different from the stated period in a contract or arrangement because it is determined, in large part, based on identifying the cash flows that are within the contract boundary. In that context, the Boards noted that cash flows are regarded as being within the boundary of an insurance contract to the extent that the entity can compel the policyholder to pay premiums or the entity has a substantive obligation to provide the policyholder with insurance contract services [AASB 17/PBE IFRS 17.34].
- BC72 The Boards further noted that, an entity’s substantive obligation to provide insurance contract 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 [AASB 17/PBE IFRS 17.34(a)]; 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 up to the date when the risks are reassessed does not take into account the risks that relate to periods after the reassessment date [AASB 17/PBE IFRS 17.34(b)].
- BC73 The Boards observed the following.
- (a) Criterion (a) relating to individual policyholders, would usually only be applicable for large risks that are individually underwritten. This might, for example, be relevant for large construction risk arrangements entered into by some public sector entities.
 - (b) The vast majority of the public sector arrangements that might fall within the scope of AASB 17/PBE IFRS 17 would be priced at a level higher than individual contracts and the criteria in AASB 17/PBE IFRS 17.34(b) would be relevant.
- BC74 The Boards acknowledged that these criteria mean a coverage period could be either longer or shorter than the contractually-stated term, and noted the following examples.
- (a) A contract with a stated term of one year and a \$100 premium is accompanied by an option for a second year of coverage for another \$100 premium. The initial contract would be regarded as a contract for two years of coverage because the insurer does not have the practical ability to fully reprice the risk/benefits for the second year.
 - (b) A contract with a stated term of ten years involves ten annual premiums that the insurer can reset each year to reflect current expected risks/benefits as if that contract were a new contract with the same characteristics as the existing contract issued on that date. Although the insurer is obliged to keep accepting premiums and providing coverage for ten years, each year (up to a possible ten

years) would be regarded as a separate coverage period because the insurer has the practical ability to reprice risk/benefits each year.

- BC75 The Boards observed that the criteria in AASB 17/PBE IFRS 17.34 are based on the existence of the insurer's practical ability to fully price for risks/benefits, not the manner in which the insurer might choose to use that ability. Accordingly, the fact that an entity might have the practical ability to fully price for risks/benefits but choose not to use that ability, is not relevant to determining the cash flows within the boundary of an insurance arrangement.
- BC76 In relation to the contract boundary criteria, the Boards noted there may be issues specific to the public sector that were not necessarily considered in the development of IFRS 17, which they might need to specifically address in AASB 17/PBE IFRS 17. In particular, those issues include:
- (a) whether a public sector entity (itself) would be regarded as having the practical ability to set prices and benefits, or whether that power lies more broadly with government, including for example, the relevant Minister(s); and
 - (b) assessing the practical ability to set prices and benefits for a monopoly provider that cannot cease insuring risks by withdrawing from the market.

Practical Ability

- BC77 The Boards observed that the levy/premium and benefit decision-making power may reside with the public sector entity itself, or more commonly, resides with the government, for example, the relevant Minister(s) or regulatory pricing supervisor.
- BC78 The Boards noted that a typical public sector model involves:
- (a) benefits largely being determined by reference to regulation or legislation, which would be the product of consultation and review; and
 - (b) levies/premiums being set under a process where the public sector entity makes recommendations to a government regulatory pricing supervisor or Minister for approval. The recommendations may be approved with or without alterations.
- BC79 In these circumstances, literally, the public sector entity (itself) does not have the practical ability to set prices/levies and benefits. A strict interpretation of AASB 17/PBE IFRS 17.34 might mean that the public sector entity's arrangements are open-ended and coverage is virtually perpetual. The Boards noted a flow on consequence of this would be that, under AASB 17/PBE IFRS 17, a public sector entity may need to account for arrangements as if they were issuing very long-term multi-year contracts with the need to estimate cash flows over long forecast periods.
- BC80 The Boards considered the main alternative perspective to be that the entity and its controlling government,¹⁷ including any relevant Minister(s) or regulatory pricing supervisor, would be regarded collectively as having the practical ability to fully price for risks/benefits. The Boards noted a flow on consequence of this perspective is that, under AASB 17/PBE IFRS 17, a public sector entity's arrangements would be regarded as having contract boundaries based on the timing (often annual) of pricing/benefit reviews by government, rather than being open-ended.
- BC81 The Boards also considered whether the practical ability of a government or public sector entity should be affected by constraints imposed by the political and economic environment. However, they noted that:
- (a) all entities face political and/or economic constraints of some kind; including, for example, competitive pressures facing private sector insurers; and
 - (b) the practical ability benchmark needs to be applied in the context of AASB 17.B64/PBE IFRS 17.AG64, which says (in part): "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 ...".
- BC82 Accordingly, provided the constraints (political or commercial) apply to new (current) arrangements as well as existing arrangements, they are not regarded as constraints that affect an insurer's practical ability

¹⁷ Under existing (or substantively enacted) legislation.

to fully price for risks/benefits in relation to the existing arrangements. The Boards considered that, instead, the focus should be on the constraints operating under existing and substantively enacted legislation.

Practical Ability – Proposal for AASB ED 319/NZASB ED 2022-3

BC83 The Boards decided, for the avoidance of doubt, to propose including guidance in AASB 17/PBE IFRS 17 to the effect that an entity's practical ability to fully price for risks/benefits also includes the ability of its controlling government, including any relevant Minister(s) and/or regulatory pricing supervisor, under existing and/or substantively enacted legislation to decide on pricing and benefits. The Boards considered this guidance to be supportable for the following reasons.

- (a) The approach seems reasonable given that the government owns and controls the public sector entity and users of the financial statements would know, when relevant, that the ultimate decision-making power lies with the government.
- (b) Without guidance, entities might need to engage in costly analysis in consultation with their auditors to determine how long-run pricing affects the entity's practical ability; and inconsistent determinations about 'practical ability' might be made by different entities in similar circumstances.

Contract Boundaries and Coverage Periods of Public Sector Arrangements – AASB ED 319/NZASB ED 2022-3 Feedback and Board Conclusions

BC84 All respondents to AASB ED 319/NZASB ED 2022-3 who commented on the proposed guidance were supportive. Their support was based substantively on the reasons outlined in paragraphs BC81–BC83.

BC85 Some respondents also sought additional guidance on the following matters.

- (a) In the public sector there can be situations in which there is an established practice of, or regulatory requirement for, periodic pricing reviews, such as every five years, which may appear to give rise to multi-year coverage periods, but do not in fact remove the practical ability to re-price for risk on a more frequent basis.
- (b) The meaning of coverage may not be clear when public sector arrangements are essentially statutory and are linked to an underlying insurance contract sold by a commercial insurer. There was a concern about possible confusion over whether the coverage would be regarded as: (i) the same as the underlying insurance contract; or (ii) the period over which claims are expected to be settled.

BC86 Based on the feedback received from stakeholders and the reasoning applied by the Boards in determining their proposals, the Boards concluded that the proposed guidance on coverage periods and practical ability would be included in AASB 17/PBE IFRS 17. They also concluded that additional guidance should be provided along the following lines.

- (a) Public sector entities would need to consider whether multi-year pricing reviews removed the practical ability to reprice more frequently or whether, in substance, it remains feasible for an entity to re-price for risk on a more frequent basis.
- (b) In some cases, the period over which claims for benefits might arise under a public sector arrangement would be determinable from the period over which coverage is provided under an insurance contract issued by a private sector insurer. This may be the case when, for example, the public sector entity's arrangements are funded from a levy on the insurance contracts issued by a private sector insurer and the levy is intended to meet claims for benefits arising from events that occur during the private sector insurance contract coverage periods.
- (c) In other cases, the period over which claims for benefits might arise under a public sector arrangement may not be determinable from the period over which coverage is provided under an insurance contract issued by a private sector insurer. This may be the case when, for example, the public sector entity's arrangements are funded from a levy on the insurance contracts issued by a private sector insurer in a particular period (say, 1 July to 30 June) and the levy is intended to meet claims for benefits arising from events in that period, rather than from events during the private sector insurance contract coverage periods (which may be for years commencing on any day of the year).

BC87 The Boards concluded that this additional guidance is particularly important in providing many public sector entities with a basis for determining when they have an identifiable coverage period, being one of the pre-requisites for applying AASB 17/PBE IFRS 17.

Contract Boundaries and Coverage Periods – Impact of Monopoly and Standing Ready over the Long-run

BC88 The Boards observed that:

- (a) the IASB presumably developed IFRS 17 largely with competitive markets in mind [IFRS 17.BC167 & BC168(a)]; and
- (b) most of the public sector entities that are the subject of the joint AASB/NZASB project are monopolies or near monopolies,¹⁸ and are not able to withdraw from the market(s) they serve without a change of legislation.

BC89 The Boards also observed that, for a public sector entity, a monopoly position can mean:

- (a) the power to charge above-market levies/premiums; but
- (b) the responsibility to keep providing insurance services to a community of policyholders in perpetuity, or at least until there is legislative change and/or structural changes to the markets served.

BC90 The Boards considered whether the responsibility to keep providing insurance services to a community of policyholders might have consequences for the contract boundary; and the coverage period of a public sector entity's arrangements and noted the following possible views.

- (a) The responsibility to keep providing insurance services to a community of policyholders means the contract boundary (and coverage period) extends over multiple years, even though the contractually-stated coverage period might be, for example, one year.
- (b) An alternative view is that this year's policyholders may or may not continue to be policyholders next year and, accordingly, the responsibility to keep providing insurance services to a community of policyholders over the long term is not relevant to determining coverage periods.

Contract Boundaries and Coverage Periods – Monopolies and Standing Ready over the Long-run – Proposal for AASB ED 319/NZASB ED 2022-3

BC91 The Boards decided, for the avoidance of doubt, to propose including guidance in AASB 17/PBE IFRS 17 to the effect that an entity's monopoly status (and the possible inference that there is a legislative obligation to stand-ready to insure future policyholders), of itself, does not affect an entity's practical ability to fully price for risks/benefits and, therefore, would not affect the coverage period of an insurance contract. The Boards consider this guidance to be supportable for the following reasons.

- (a) The monopoly or near monopoly status of public sector entities, coupled with their inability to withdraw from the markets they serve without a change of legislation, is a set of circumstances unique to the public sector. The Boards consider that providing some direction to the affected public sector entities could have a cost-beneficial impact on the application of AASB 17/PBE IFRS 17.34(b)(ii). Accordingly, to the extent guidance is provided that these circumstances do not, of themselves affect an entity's practical ability to fully price for risks/benefits is a 'modification' of IFRS 17, it would be justified under the Boards' frameworks for setting standards for public sector entities.
- (b) If the monopoly status of a public sector entity was to be regarded as leading to multi-year coverage periods, the entity would need to estimate the number of years of coverage. It seems highly likely that the entity's estimates would prove to be different from the actual number of periods over which participants continue their coverage. If the difference between the originally-determined coverage periods and the actual coverage period is significant, this would result in 'a modification of an insurance contract' under AASB 17/PBE IFRS 17.72 and 73. The existing contract would be derecognised and a new (modified) contract would be recognised. This process

¹⁸ The reference to 'near monopolies' relates mainly to arrangements such as the workers' compensation arrangements that operate in most Australian states, from which 'approved' large employers can be excluded on meeting certain conditions.

has the potential to involve complex and costly tracking of information and it seems unlikely this is a scenario that was contemplated in developing IFRS 17.

- (c) The guidance could be regarded as reasonable under the principles in AASB 17/PBE IFRS 17 given that typically there is turnover among policyholders over successive years, even though it may be limited. For example, in respect of compulsory third party (personal injury) insurance, at the margin, some motor vehicles registered and insured in the current year may be deregistered and uninsured in the following year.
- (d) Without guidance, entities might need to engage in costly analysis in consultation with their auditors to determine how monopoly status affects the entity's practical ability to fully price for risks/benefits; and inconsistent determinations about practical ability to fully price for risks/benefits might be made by different entities in similar circumstances.

Contract Boundaries and Coverage Periods – Impact of Monopoly and Long-run Pricing

- BC92 The Boards observed that the pricing of levies/premiums for many public sector entities is based on achieving a break even result over the long-term. Accordingly, in some cases, the actual amounts charged in any given period might be regarded as being the result, in part, of taking into account the risks that relate to periods after the current contract period. In these cases, the criterion in AASB 17/PBE IFRS 17.34(b)(ii) would not be met and the arrangements would be regarded as, for example, involving a multi-year coverage period, even though the contractually-stated coverage period might be one year.
- BC93 The Boards noted that the long-run focus of pricing for many public sector entities might be based solely on past experience and not be influenced by projections of risk relating to future periods. This is likely to be the case for entities providing coverage for risks that evolve only slowly over time in their nature and level of severity. For example, typically this might be expected to apply for workers' compensation and transport accident risks. The long-run focus of pricing for other public sector entities might be based, at least in part, on projections of risk relating to future periods. For example, this might be the case for entities providing coverage for risks that are scheduled to change, and possibly when an entity insures for losses arising from infrequent severe events such as earthquakes.
- BC94 The Boards noted the following possible scenarios:
- (a) A legislative change has been made to significantly increase benefits relating to certain types of injuries that occur after July 20X1. Based on government policy, the entity is gradually increasing levies/premiums over the 20X2 to 20X7 financial years in order to establish reserves to help fund the higher benefits. In this case, the current-year pricing is taking into account risks that relate to periods after the current period. Accordingly, the contract boundary (and coverage period) could be determined as extending from 20X2 until 20X7 and possibly beyond.
 - (b) An entity insures against losses from what is projected to be a one-in-20-year event and charges levies/premiums for one-year contracts each year over a 20-year period that are designed to meet the expected benefits that will need to be paid. In a competitive (private sector) market context, the entity would not be regarded as taking into account the risks that relate to periods after the current contract period because the entity would be viewed as considering the risk of loss for each one-year period. Policyholders could obtain the same coverage from a different insurer in a subsequent year. Accordingly, in the private sector context, the contract boundary (and coverage period) would be determined as being one year. In a monopoly public sector context, the current-year pricing could be regarded as taking into account risks that relate to periods after the current period. Accordingly, the contract boundary (and coverage period) could be determined as being 20 years.
- BC95 The Boards observed that applying AASB 17/PBE IFRS 17 unmodified might have a range of related implications. This could include public sector entities having to estimate the average time that a policyholder is expected to keep participating in the arrangement to determine a coverage period for the purposes of AASB 17/PBE IFRS 17. This could have flow-on consequences for uncertainty around the estimated length of coverage periods and the volatility of cash flows.

Contract Boundaries and Coverage Periods – Impact of Monopoly and Long-run Pricing – Proposal for AASB ED 319/NZASB ED 2022-3

- BC96 The Boards decided, for the avoidance of doubt, to propose including guidance in AASB 17/PBE IFRS 17 that a public sector entity would not fail to meet the criterion that pricing up to the date when the risks are reassessed does not take into account risks for periods after the reassessment date simply because it has a deliberate policy of setting prices and benefits based on a medium- to long-term view.
- BC97 The Boards considered the guidance is justified on the basis that public sector entities are more likely than their private sector counterparts to have overriding public policy objectives imposed upon them that would necessitate medium- to long-term pricing and benefits approaches. The Boards were also concerned that, without guidance, entities might need to engage in costly analysis in consultation with their auditors to determine how medium- to long-term pricing and benefits would affect their ability to meet the criterion in AASB 17/PBE IFRS 17.34(b)(ii).
- BC98 The Boards also noted that, in principle, such pricing policies are unlikely to mean that the entity has lost its practical ability to price its arrangements based on risks and benefits for the relevant (current) periods of coverage. They simply mean the entity, together with its controlling government, Minister(s) and/or regulatory pricing supervisor, has chosen to take a longer-term perspective.

Contract Boundaries and Coverage Periods – Impact of Monopoly and Standing Ready over the Long-run – AASB ED 319/NZASB ED 2022-3 Feedback and Board Conclusions

- BC99 All respondents to AASB ED 319/NZASB ED 2022-3 who commented on the proposed guidance were supportive. Their support was based substantively on the reasons outlined in paragraphs BC96–BC98.
- BC100 Based on the feedback received from stakeholders and the reasoning applied by the Boards in determining their proposals, the Boards concluded, for the avoidance of doubt, to modify paragraph 34 to include guidance in AASB 17/PBE IFRS 17 to the effect that:
- (a) an entity’s monopoly status (and the possible inference that there is a legislative obligation to stand-ready to insure future policyholders), of itself, does not affect an entity’s practical ability to fully price for risks/benefits and, therefore, would not affect the coverage period of an insurance contract;
 - (b) a public sector entity would not fail to meet the criterion that pricing up to the date when the risks are reassessed does not take into account risks for periods after the reassessment date simply because it has a deliberate policy of setting prices and benefits based on a medium- to long-term view; and
 - (c) any legislated obligation for a public sector entity to stand-ready to insure future policyholders, of itself, is not an obligation that would affect the practical ability to fully price for risks or benefits.

Disclosure and Long-run Pricing (Modification to Paragraph 34)

- BC101 The Boards considered that, given the impact on public sector entities of medium- to long-term pricing and benefits approaches on the application of the requirements of AASB 17/PBE IFRS 17.34, where those approaches exist, they should be the subject of disclosure. This is because the disclosure could provide useful context for users of the financial statements.
- BC102 The Boards observed that the pricing and benefit approaches of public sector entities might be the subject of transparent public processes and, therefore, adequate disclosures might already be made outside the financial statements.

Disclosure and Long-run Pricing – Proposal for AASB ED 319/NZASB ED 2022-3

- BC103 For the reasons noted immediately above, the Boards decided to propose that, when a public sector entity takes into account risks that relate to periods after the reassessment date based on having a policy of determining prices and benefits over a period longer than a single coverage period, it should be required to disclose information about the manner in which pricing/benefits are determined and the timeframes for which they are typically determined. The Boards decided to propose that the disclosure could be made either directly in the notes to the financial statements or by reference to an authoritative source, provided

that source is available to users of the financial statements on the same terms as the financial statements and at the same time.

Disclosure and Long-run Pricing – AASB ED 319/NZASB ED 2022-3 Feedback and Board Conclusions

- BC104 Those respondents to AASB ED 319/NZASB ED 2022-3 who commented on the proposed disclosure requirement expressed concerns about:
- (a) the potential need to disclose commercially sensitive information;
 - (b) the information being of little value to users; and
 - (c) audit and other related cost ramifications of cross-referencing to information in external materials, which may also need to be reviewed.
- BC105 The Boards consider that information about the manner in which a public sector entity sets its prices and benefits is important because it can be driven by a range of regulations and laws. Accordingly, the Board concluded that a form of disclosure should be required.
- BC106 To address the concerns in the feedback received, the Boards concluded that they should simplify the disclosure to require information on the timeframes for which prices are typically determined and identification of the relevant government regulations or laws under which prices and benefits are set, without the need for any further explanation. The Boards noted the simplified disclosure would be required of all public sector entities applying AASB 17/PBE IFRS 17, not only those taking into account risks that relate to periods after the reassessment date based on having a policy of determining prices and benefits over a period longer than a single coverage period. The Boards considered that requiring the disclosure of all public sector entities applying AASB 17/PBE IFRS 17 avoids entities having to identify whether their pricing policy would be regarded as involving determining prices and benefits over a period longer than a single coverage period. The Boards also noted that the audit of external materials would be expected to be limited to confirming that the references to government regulations or laws are relevant to determining the manner in which a public sector entity sets its prices and benefits.
- BC107 In concluding on the simpler form of disclosure, the Boards noted that they would expect the information provided to be brief and that it would involve naming the relevant authoritative sources from which users can gain a broad understanding of the processes for setting the entity's insurance contract prices and benefits.

Premium Allocation Approach (Modifications to Paragraphs 53 and 69)

- BC108 AASB 17/PBE IFRS 17 includes two approaches to measuring liabilities for remaining coverage:
- (a) a general measurement model that involves discounting fulfilment cash flows and, when relevant, recognising a contractual service margin (deferred profit/loss); and
 - (b) the premium allocation approach, which is a simplified approach and typically much less burdensome to apply than the general measurement model.
- BC109 The Boards noted that eligibility for the premium allocation approach is available on a group-of-contracts basis¹⁹ – that is, an entity might apply the general measurement model to some groups of contracts and the premium allocation approach to other (eligible) groups of contracts. However, they further noted that creating an accounting system capable of implementing the general measurement model, of itself, could involve significant costs, even if it only needs to be applied to some of an entity's arrangements.
- BC110 The Boards observed that, for most public sector entities currently applying AASB 1023/PBE IFRS 4, the liability for incurred claims²⁰ is typically much larger than the liability for remaining coverage.²¹ Nonetheless, the liability for remaining coverage would be expected to be a material amount for many public sector entities with arrangements that would be scoped into AASB 17/PBE IFRS 17. Accordingly, eligibility to apply the premium allocation approach is a key issue for public sector stakeholders.

¹⁹ Although the Boards proposed that, effectively, the basic unit of account for public sector entities would be portfolios, in which case the test would apply at the portfolio level.

²⁰ Generally referred to as the 'outstanding claims liability' under AASB 1023/PBE IFRS 4.

²¹ Akin to the 'unearned premium liability' referred to in AASB 1023/PBE IFRS 4.

BC111 The Boards noted the two bases on which arrangements might be eligible for the premium allocation approach under AASB 17/PBE IFRS 17.53 – at inception:

- (a) the entity reasonably expects the premium allocation approach would produce a measurement of the liability for remaining coverage that would not differ materially from the one that would be produced applying the general measurement model: or
- (b) the coverage period of each contract in the group is one year or less (determined at that date applying AASB 17/PBE IFRS 17.34).

The Boards observed that the same criteria apply in respect of reinsurance contracts held under AASB 17/PBE IFRS 17.69. They also observed that, when there are contracts with coverage periods longer than a year, criterion (a) would involve creating a system to periodically test for material differences that, of itself, could involve significant costs.

BC112 In general, the Boards expected that, with the proposed guidance on determining coverage periods, most public sector arrangements that would fall within the scope of AASB 17/PBE IFRS 17 seemed likely to be eligible to apply the premium allocation approach. This was on the basis that, in most cases, the coverage periods are expected to be up to a year in duration for insurance contracts issued and one to three years for reinsurance contracts held.

BC113 The Board noted that, while some public sector arrangements may still not qualify for the premium allocation approach, in principle it would be reasonable for the general measurement model to apply in these cases.

Premium Allocation Approach – AASB ED 319/NZASB ED 2022-3 Feedback and Board Conclusions

BC114 Some respondents expressed concern that there are public sector arrangements which involve multi-year coverage and may not be eligible to measure their liabilities for remaining coverage applying the premium allocation approach. In particular, they noted that domestic building risks and some construction and engineering risks associated with government infrastructure projects would typically have coverage periods of six or more years. These respondents considered the cost of maintaining the relevant systems for applying the general measurement model would outweigh the potential value of the information generated.

BC115 The Boards redeliberated on:

- (a) whether having public sector entities applying the premium allocation approach when a strict application of AASB 17/PBE IFRS 17 would otherwise require the entity to apply the general measurement model would deprive users of useful information;
- (b) whether any benefits a user may enjoy from having an entity apply the general measurement model instead of the premium allocation approach would justify the additional costs; and
- (c) the possible extent of costs associated with testing for eligibility for the premium allocation approach even when the general measurement model is not eventually applied.

BC116 The Boards reflected on the factors relevant to determining whether the general measurement model is suitable for application by public sector entities, including the following.

- (a) The modifications relating to sub-grouping, which mean a portfolio of contracts is expected to be the main unit of account for public sector entities.
- (b) The key difference between the general measurement model and premium allocation approach is the contractual service margin that represents unearned profit at contract inception – yet most public sector insurance arrangements are break even or loss making. The contractual service margin accretes interest over time based on the initial recognition date discount rate, whereas, other cash flows are discounted at current rates.
- (c) For public sector arrangements, there would typically be a loss component under the general measurement model, not a contractual service margin. A loss component would need to be tracked so that changes in cash flows can be allocated systematically between the loss component and the liability for remaining coverage excluding the loss component. However, this would be done on a portfolio basis and, unless, the whole portfolio became profitable, all cash flows would be discounted at current rates.

- (d) Similar losses would typically still be recognised using the premium allocation approach because the deferred premiums received would need to be compared with an up-to-date assessment of expected cash flows, which is essentially the same as the existing accounting under the AASB 1023/PBE IFRS 4 Liability Adequacy Test. There would typically be only a small likelihood of a whole portfolio being profitable and, therefore, a different pattern of profit and loss recognition emerging under the general measurement model compared with the premium allocation approach.
- (e) In the atypical case that contracts issued by public sector entities would generate a contractual service margin under the general measurement model, the entity would need to determine a pattern of coverage to allocate the margin, which may be different from the pattern of release from risk and two components of revenue (coverage and release of risk) that need to be tracked. It seems unlikely that the users of the public sector entities' financial statements would place much value on having two separate patterns for revenue recognition. That is, it seems likely that users would be satisfied with all revenue being recognised based on the passage of time or, if significantly different from the passage of time, based on the pattern of risk, which is the basis that applies under the premium allocation approach.

BC117 The Boards acknowledged that some of the same factors might be relevant to private sector not-for-profit entities; however, they noted there are important distinctions between the public and private sectors that provide a conceptual underpinning for a differential approach between the two sectors, including the following.

- (a) Public sector entities typically seek to break even in conducting insurance activities. Not-for-profit entities (outside the public sector) would typically need to rely on their own resources to maintain solvency, which could involve building (and, when necessary, re-building) reserves, by including a profit margin into the pricing of their services. That is, even though these entities may not seek to make a profit from their activities, they would often still generate reserves that are subsequently re-distributed to customers/members. Accordingly, the recognition of a contractual service margin under the general measurement model is likely to be more relevant in a private sector not-for-profit entity context.
- (b) All private sector entities that issue insurance contracts in Australia and/or New Zealand, including for-profit and not-for-profit private sector entities, would need to be registered as insurers and would face prudential regulation and need to hold risk-weighted regulatory capital and maintain the potential to generate profits to remain solvent. Public sector entities may have their own self-imposed prudential measures, but are not typically compelled to consider profits as a source of capital on an ongoing basis.

BC118 The Boards concluded that paragraphs 53 and 69 would be modified to provide public sector entities with an accounting policy choice to always apply the premium allocation approach to measure liabilities/assets for remaining coverage, without the need to consider the eligibility criteria in AASB 17/PBE IFRS 17 paragraphs 53 and 69 on the basis that:

- (a) the practical differences between the accounting outcomes of applying the premium allocation approach or the general measurement model are expected not to be material in a public sector context in most cases;
- (b) the possible difference between the pattern of recognition of any contractual service margin component of the liability for remaining coverage is unlikely to influence users' decision making in a public sector context;
- (c) the costs of establishing and operating a system to produce information that might be needed in applying the general measurement model to every possible scenario that might arise would probably be considerable, and is unlikely to be used by public sector entities for management purposes; and
- (d) few public sector insurance arrangements are likely to be ineligible for the premium allocation approach, yet the process of justifying eligibility for any contracts with coverage period of more than a year can, of itself, be resource intensive and may need to be periodically repeated.

Risk Adjustments

Background

BC119 The Boards noted that:

- (a) under AASB 17/PBE IFRS 17, a risk adjustment is: “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”; while
- (b) under AASB 1023/PBE IFRS 4, a risk margin relates to the inherent uncertainty in the central estimate of the present value of the expected future payments.

BC120 The Boards noted that the notion of a risk adjustment in AASB 17/PBE IFRS 17 is the compensation the entity would require to make it indifferent between fulfilling a liability of fixed amount and a liability of uncertain amount that has a central estimate equivalent to the fixed liability [AASB 17.B87/PBE IFRS 17.AG87]. It is designed to convey information to users of financial statements about the amount charged by the entity for the uncertainty arising from non-financial risk associated with the amount and timing of cash flows.

BC121 The Boards noted that AASB 1023/PBE IFRS 4 has no equivalent to the AASB 17/PBE IFRS 17 notion of compensation – instead, the risks are regarded as being inherent in the cash flows.

BC122 The Boards noted that, under AASB 17/PBE IFRS 17:

- (a) there is a presumption that for-profit private sector entities would need to be compensated for bearing risk and, as risk is released, revenue would be recognised; and
- (b) public sector entities may have a different perspective and not need to be compensated for bearing risk on the basis that:
 - (i) they are often monopolies and there may be the opportunity to increase premiums/levies to meet future claims; and
 - (ii) they have explicit or implicit government guarantees of financial support.

Industry Benchmarks and Current Practices

BC123 The Boards noted that neither Standard requires a particular technique to be used to measure risk adjustments; however, currently entities typically use a confidence level (probability of adequacy) approach. The Boards also noted that:

- (a) under AASB 1023/PBE IFRS 4, many entities benchmark to a 75% confidence level (indicating the liability for incurred claims would be adequate to meet actual claims three years in four); and
- (b) under AASB 17/PBE IFRS 17, when an approach other than the confidence level technique is used, an entity must disclose the technique used and the confidence level corresponding to the results of that technique [AASB 17/PBE IFRS 17.119].

BC124 The Boards observed that the 75% confidence level benchmark originally arose from a minimum prudential reporting benchmark and has become a widely used reference point in Australia and New Zealand and more broadly in other jurisdictions. Additionally, although other methods (such as cost of capital techniques) may be used to measure risk adjustments, they are often only permitted by regulators subject to achieving a minimum confidence level.

BC125 The Boards observed that most of the public sector entities applying AASB 1023/PBE IFRS 4 recognise risk margins at a 75% confidence level, or some level close to that benchmark. The Boards also observed that some of the Australian public sector entities applying AASB 137 also recognise risk margins at a 75% confidence level, or some level close to that benchmark. In outreach conducted in 2021-21, some stakeholders indicated that information about uncertainties in the cash flows are important to them, even in measuring provisions (under AASB 137).

Previous Public Sector Proposals and Stakeholder Feedback

BC126 The Boards noted that the AASB Discussion Paper (2017) and NZASB ED 2018-7 did not propose any modifications in respect of the risk adjustment requirements in AASB 17/PBE IFRS 17. However, they

noted that the AASB Discussion Paper Basis for Conclusions [AASB DP.BC8 to BC13] raised the possibility of a risk adjustment of zero based on a case of a public sector entity with a government guarantee and/or a monopoly position in which it can recoup current and past losses from its controlling government or via future contracts. However, the AASB Discussion Paper put the view that, while the risk adjustment might differ from a for-profit private sector entity, it is unlikely to be nil because:

- (a) the uncertainties associated with outstanding claims cash flows in respect of past transactions, that would be reflected in a risk adjustment are a characteristic of the claims liability; and
- (b) in respect of the current (usually annual coverage) transactions, the entity is bearing risk for that period and an entity's monopoly position is not relevant [AASB DP.BC10].

BC127 The Boards noted that, in response to the AASB Discussion Paper (2017) proposals:

- (a) some respondents considered that there would be risk adjustments (above zero) and also noted various considerations, including:
 - (i) disclosures around the techniques used to determine risk adjustments should be required to help ensure transparency;
 - (ii) if the AASB expects risk adjustments to be different from those in the private sector, the implication is that they would be lower (compared with the private sector) and guidance would be needed to help entities make those calculations; and
 - (iii) whether it is appropriate to imply that risk adjustments in the public and private sectors should be aligned;
- (b) other respondents considered that there would be circumstances in which a risk adjustment could be zero, such as when:
 - (i) there is absolute certainty around the government backing of the best estimate liability; and
 - (ii) the liability cash flows are so long term that the volatility is mitigated by long-term investment returns.

BC128 The Boards noted that some respondents to NZASB ED 2018-7 considered that risk adjustments would not be relevant to many public sector entities and, if they were to be required:

- (a) explicit guidance on determining risk adjustments in the public sector would be needed; and/or
- (b) the Standard should specify that risk adjustments are zero for public sector entities.

BC129 The Boards noted the comments of respondents to NZASB ED 2018-7, which included the following:

- (a) risk adjustments are predicated on the liability being an estimated amount a third party would likely want to be paid to assume the risk of settling claims, which is akin to an exit price; however, the liabilities will be settled by the entity itself;
- (b) if the entity seeks to fund a liability that includes a risk adjustment, in order to report a break-even result, the entity would need to set levies and other forms of income at amounts that (on average) would be higher than necessary; and
- (c) if the entity is funded to meet a best estimate liability, including a risk adjustment in the liability would automatically result in reported losses, which may never eventuate.

BC130 The Boards also noted the following feedback received from stakeholder outreach conducted in 2020-21.

- (a) AASB 1023/PBE IFRS 4 is regarded as requiring a risk margin to be included in measuring liabilities for outstanding claims, while AASB 137/PBE IPSAS 19 is generally regarded as not requiring a risk margin to be included in measuring provisions, but can be interpreted as permitting a risk/prudential margin to be included.
- (b) A key reason for some stakeholders choosing to apply AASB 137/PBE IPSAS 19 (rather than AASB 1023/PBE IFRS 4) is that they do not regard risk margins as appropriate to their circumstances.

- (c) Some stakeholders had assumed that their risk adjustments under AASB 17/PBE IFRS 17 would be the same as their risk margins under AASB 1023/PBE IFRS 4, while others had yet to consider whether they would have a risk adjustment under AASB 17/PBE IFRS 17 and, if they did, whether it would be more or less than any risk margin they currently apply.

Alternative Approaches Considered by the Boards

BC131 The Boards considered the following possible approaches regarding the risk adjustments requirement:

- (a) Approach 1: require public sector entities to apply AASB 17/PBE IFRS 17 with no modifications or guidance;
- (b) Approach 2: require public sector entities to have a zero risk adjustment; and
- (c) Approach 3: require a particular confidence level for determining risk adjustments for liabilities for incurred claims for all public sector entities.

Approach 1: Apply AASB 17/PBE IFRS 17 with no Modifications or Guidance

BC132 The Boards considered the possible advantages of applying AASB 17/PBE IFRS 17 with no modifications or guidance.

- (a) It could be considered consistent with the principle of only making modifications to the IFRS Standards if there is a strong case based on substantive differences in circumstances of public sector entities (compared with the entities for which IFRS Accounting Standards are developed).
- (b) It would allow for different risk adjustments to be recognised to suit the nature of each entity's claims liabilities, which would be helpful since different public sector entities hold claim liabilities with different characteristics. For example, very long-tail, relatively predictable claims (such as regular income support payments), would result in a relatively small risk adjustment. In contrast, claims subject to future legal judgements might result in a relatively large risk adjustment.
- (c) Different public sector entities hold different views on whether they should have a risk adjustment above zero in measuring their claim liabilities based on their circumstances. Each entity would be able to determine its position consistent with its own facts and circumstances, including its objectives, management philosophy, and level of risk aversion.
- (d) A for-profit public sector entity could recognise a risk adjustment on the basis that it expects to profit from bearing risk, while a not-for-profit entity might not recognise a risk adjustment because it does not seek to profit from bearing risk.

BC133 The Boards considered the possible disadvantages of applying AASB 17/PBE IFRS 17 with no modifications or guidance.

- (a) IFRS 17 was designed to be applied by private sector entities. The public sector context is often different; in particular, due to entities holding a monopoly position and being driven by public policy objectives.
- (b) Different public sector entities may determine different outcomes even though they have similar operations. Accordingly, their reported financial position and financial performance would not be comparable.
- (c) Public sector entities might expend a disproportionate amount of time and resources determining the compensation they might notionally require for bearing the uncertainty about the amount and timing of the cash flows that arises from non-financial risk as the entity fulfils its arrangements. There may be little or no additional information value achieved for users of the financial statements through this process.

Approach 2: Require Public Sector Entities to have a Zero Risk Adjustment (Confidence Level of 50%)

BC134 The Boards noted that opinions differ about whether, in concept, an entity can have a risk adjustment of zero and still claim to have contracts that transfer insurance risk. For the purposes of discussion, the Boards assumed that, in particular circumstances, a zero risk adjustment is compatible with the transfer of insurance risk and noted the example of a mutual risk-pooling arrangement that involves accepting risk from each policyholder and sharing the risk with other policyholders. Although a public sector entity

might be regarded as simply an administrator of such a pooling arrangement, it could nevertheless also be seen as bearing risk for the current in-force arrangements because the risk is typically pooled over a number of coverage periods.

BC135 The Boards considered the possible advantages of requiring public sector entities to have a zero risk adjustment.

- (a) All public sector entities would have a consistent approach (based on best estimate claim liabilities).
- (b) Best estimates (with no risk adjustment) are typically relevant to user decision making because they ordinarily provide a basis for determining how much levies or other charges need to be generated to sustain the entity in the long term.
- (c) Most of the relevant public sector entities are monopolies and/or have the power to adjust future levies and charges to meet any shortfalls in funding the existing claim liabilities. Accordingly, risk adjustments may not be relevant because these entities have no reason to be risk averse.
- (d) Zero risk adjustments (and, therefore, zero changes from period to period in risk adjustments) would avoid misleading impacts on the income statement, since risk adjustments tend to create short term losses and longer-term gains as actual claims revert to the best estimate over the long term.
- (e) Zero risk adjustments would reduce report preparation costs by removing the need for management (and auditors) to determine (and assess) risk adjustments and to make disclosures about risk adjustments.

BC136 The Boards considered the possible disadvantages of requiring public sector entities to have a zero risk adjustment.

- (a) Many public sector entities hold strong views on the need to show their users that claim liabilities carry a level of uncertainty as to timing and amount, and consistency does not necessarily lead to comparability. All entities are risk averse to varying degrees.
- (b) There would be no changes in risk adjustments to provide useful information about changes in the levels of uncertainty among cash flows over time.
- (c) There are often obstacles to exercising monopoly and other powers. For example, it might not currently be feasible to increase levies in either the short to medium term to meet shortfalls in a timely manner. The risks that exist within in-force arrangements should not be regarded as being able to be offset by possible future transactions.
- (d) It is normal commercial practice to determine risk adjustments and many public sector entities, particularly those with independent boards of management, would wish to have a risk adjustment for financial reporting purposes to match their risk management activities (and management reporting).

Approach 3: Require a Particular Confidence Level (above 50%) for Determining Risk Adjustments for Liabilities for Incurred Claims for all Public Sector Entities

BC137 The Boards considered the possible advantages of requiring a particular confidence level (above 50%) for determining risk adjustments for liabilities for incurred claims for all public sector entities.

- (a) All public sector entities would have a consistent approach (based on a common confidence level).
- (b) A common confidence level would reduce report preparation costs by removing the need for management (and auditors) to determine (and assess) risk adjustments. In particular, this requirement would be generally consistent with prevailing current practice (which is long-standing) and be readily understood by all relevant stakeholders.
- (c) Relative to having a zero risk adjustment, the common confidence level approach would show, from period to period, the impacts of any changes in risk adjustments, which provides useful information about changing levels of uncertainty on the amount and timing of cash flows over time.

BC138 The Boards considered the possible disadvantages of requiring a particular confidence level for liabilities for incurred claims for determining risk adjustments for all public sector entities.

- (a) It would be inconsistent with principle-based standard setting to set an arbitrary benchmark such as a 75% confidence level.²²
- (b) The approach prevents entities from determining risk adjustments appropriate to their particular circumstances. Requiring a percentage confidence level also presumes that this is the best technique for determining risk adjustments in all circumstances; however, an entity might consider that another technique (e.g. a ‘cost of capital’ technique) is more appropriate.
- (c) Consistency does not necessarily lead to comparability.
- (d) If there is a general shift in expectations about the uncertainty surrounding the amount and timing of cash flows, the required confidence level might need to be updated by the Boards.

Disclosures

BC139 The Boards considered that each of the three approaches outlined above could be supplemented with disclosures such as the following.

- (a) If Approach 1 is adopted (no modifications), the entity could also be required to disclose a risk adjustment for benchmark confidence level (such as 75%) to provide a point of reference for comparison.
- (b) If Approach 2 is adopted (zero risk adjustment), the entity could also be required to disclose what the risk adjustment would have been if AASB 17/PBE IFRS 17 were applied unmodified.
- (c) If Approach 3 is adopted and each public sector entity recognises a risk adjustment for a standardised confidence level (such as 75%), the entity could also be required to disclose what its risk adjustment would have been if AASB 17/PBE IFRS 17 were applied unmodified.

BC140 The Boards also considered whether, if Approach 3 were proposed as a rebuttable presumption, disclosure should be proposed of the basis for any rebuttal. However, they observed that this would go beyond counterpart disclosures already required in AASB 17/PBE IFRS 17. For example, they noted that AASB 17/PBE IFRS 17.119 requires that an entity using a technique other than the confidence level technique for determining the risk adjustment need only disclose the technique used and the confidence level corresponding to the results of that technique.

Analysis of Approaches by the Boards

BC141 The Boards analysed the basis for the IASB’s decisions on requiring a risk adjustment and reflected on how each of the benefits the IASB identified might still be met in a public sector context under each of the approaches (no modifications, a mandated zero risk adjustment, or a mandated confidence level such as 75%).

BC142 The Boards noted that requiring a risk adjustment is intended to provide a clear insight into the insurance contracts and distinguishes them from risk-free liabilities [IFRS 17.BC211(a)]. The Boards thought this reasoning seems as relevant in the public sector as it is for private sector insurers, but that it does not necessarily suggest that requiring a zero risk adjustment would be inappropriate because a public sector might conceivably be ambivalent between an insurance contract liability with a range of possible outcomes arising from insurance risk and fulfilling a liability that would generate fixed cash flows with the same expected present value.

BC143 The Boards noted that requiring a risk adjustment results in a profit recognition pattern that reflects both the profit recognised by bearing risk and the profit recognised by providing services [IFRS 17.BC211(b)]. The Boards considered this reasoning would be less relevant in respect of public sector entities that are not seeking to profit from bearing risk. However, on balance, the Boards thought that this reasoning could also be applied to revenue recognition and be relevant to a public sector entity, and would probably best

²² The Boards noted that some Australian public sector entities are required (via regulation imposed in that jurisdiction) to benchmark to Australian Prudential Regulation Authority (APRA) prudential requirements, which include a minimum risk margin.

support the view that the risk adjustment requirements of AASB 17/PBE IFRS 17 should be applied unmodified.

- BC144 The Boards noted that requiring a risk adjustment can be necessary to faithfully represent circumstances in which the entity has charged insufficient premiums for bearing the risk that the claims might ultimately exceed expected premiums [IFRS 17.BC211(c)]. The Boards thought this reasoning may not always be as relevant in the public sector as it is for private sector insurers because a public sector entity may have the capacity to aim for a break-even result over the medium to long term while private sector insurers may not.
- BC145 The Boards noted that requiring a risk adjustment should result in changes in estimates of risk being reported promptly and in an understandable way [IFRS 17.BC211(d)]. The Boards thought this reasoning seems as relevant in the public sector as it is for private sector insurers and would suggest that requiring a zero risk adjustment might be inappropriate.
- BC146 The Boards also analysed the following criticisms of risk adjustments considered by the IASB in developing IFRS 17 and reflected on whether they might be more relevant in the public sector and, therefore, justify a different outcome from the requirements in AASB 17/PBE IFRS 17.
- (a) Currently, there is no single well-defined measurement approach to risk adjustments that would necessarily provide consistency and comparability of results [IFRS 17.BC210(a)]. This criticism is no more relevant, in a general sense, in the public sector than it is for private sector insurers.
 - (b) Some measurement techniques for risk adjustments are difficult to explain to users of financial statements [IFRS 17.BC210(b)]. This criticism may be more relevant in the public sector than it is for private sector insurers because the public sector users might be relatively less familiar with actuarial techniques. The NZASB in particular thought that this criticism might imply that mandating a widely-understood basis of measurement (such as a confidence level of 75%) could be useful in a public sector context.
 - (c) It is impossible to subsequently assess whether a particular adjustment was reasonable, including whether (for example) a decision to set a confidence level at a particular percentile was appropriate [IFRS 17.BC210(c)]. This criticism is no more relevant in the public sector than it is for private sector insurers.
 - (d) Developing systems to determine risk adjustments will involve costs that are not justified by the benefits [IFRS 17.BC210(d)]. This criticism may be more relevant in the public sector than it is for private sector insurers because the public sector entities may not otherwise have to determine risk adjustments for management or prudential reporting purposes and typically do not price arrangements to be compensated for risk. The NZASB in particular, at the time it was preparing and issuing NZASB ED 2022-3, thought that this criticism might imply that it would be inappropriate to simply leave public sector entities to apply the risk adjustment requirements of AASB 17/PBE IFRS 17 unaided.
 - (e) Including a risk adjustment in identifying any loss on initial recognition is inconsistent with IFRS 15 (on revenue) [IFRS 17.BC210(e)]. This criticism is no more relevant (and possibly less relevant given the infrequent application of AASB 15 *Revenue from Contracts with Customers*) in the public sector than it is for private sector insurers.
 - (f) If including a risk adjustment results in a loss, that loss will reverse in later periods as the entity is released from that risk, which may confuse some users of financial statements [IFRS 17.BC210(f)]. This criticism may be more relevant in the public sector than it is for private sector insurers because many public sector entities would be aiming to break even over the long term, rather than earn profits or incur losses. In contrast, private sector entities would typically aim to profit from bearing risk. However, the Boards also acknowledged that any tendency of risk adjustments to create short term losses and longer-term gains would generally be a ‘once-off’ impact and would not usually affect ongoing reported financial performance unless the volumes of transactions are volatile year-on-year.
 - (g) A risk adjustment could be used to introduce bias into the measurement of insurance contracts [IFRS 17.BC210(g)]. This criticism is no more relevant in the public sector than it is for private sector insurers.

Risk Adjustment Measurement Proposal in AASB ED 319

BC147 The AASB observed that:

- (a) most public sector entities do not seek to profit from bearing insurance risk;
- (b) under AASB 17, public sector entities might determine a zero risk adjustment on the basis that they are monopolies and can adjust future prices to make up for higher-than-expected past claims;
- (c) under AASB 17, public sector entities might determine a risk adjustment based on a particular level of adequacy based on their facts and circumstances; and
- (d) providing a benchmark confidence level, even as a rebuttable presumption, is not consistent with principle-based standard setting.

BC148 Accordingly, the AASB decided on Approach 1 and to propose not making public-sector-specific modifications to the requirement to include a risk adjustment in measuring liabilities for incurred claims.

Risk Adjustment Measurement Proposal in NZASB ED 2022-3

BC149 A primary concern for the NZASB was that entities, their advisors and auditors might expend considerable effort to identify and measure a relevant compensation-based risk adjustment for little benefit to users.

BC150 The NZASB observed that existing practice under AASB 1023/PBE IFRS 4 has developed over many years and most public sector entities applying these standards benchmark to a 75% confidence level. The benchmark seems to have become widely accepted (including outside Australia and New Zealand) because it is:

- (a) relatively easy (and low cost) to measure;²³
- (b) relatively easy to understand; and
- (c) financial statement users and entity managements have found it informative.

BC151 The NZASB considered that the 75% benchmark has been an effective and low-cost way for public sector entities to measure risk margins under AASB 1023/PBE IFRS 4. Nevertheless, the NZASB also acknowledged that there may be circumstances in which a benchmark other than a 75% confidence level is more relevant and that entities should be able to rebut the 75% benchmark.

BC152 Accordingly, the NZASB decided on Approach 3 and to propose a public-sector-specific modification of a rebuttable presumption that risk adjustments are measured at an amount that achieves a 75% confidence level in respect of liabilities for incurred claims.

BC153 While acknowledging that providing a benchmark confidence level is not consistent with principle-based standard setting, the NZASB considered it justifiable to propose the modification because:

- (a) the cost-saving benefits of using the benchmark would exceed any loss of information value; and
- (b) the rebuttable presumption would still allow for flexibility in circumstances in which a 75% confidence level may not be appropriate.

Boards' Disclosure Proposal for AASB ED 319/NZASB ED 2022-3 about Risk Adjustments in a Public Sector Context

BC154 The Boards noted that there are comprehensive disclosure requirements in AASB 17/NZ IFRS 17 about risk adjustments, particularly in the requirements for reconciliations of insurance liabilities.

BC155 Both Boards decided that it would be inappropriate to propose to require more disclosure of public sector entities than is required of other entities applying AASB 17/NZ IFRS 17 about risk adjustments in general.

²³ The Boards observed that, of itself, very little additional actuarial effort is likely to be needed to determine a risk adjustment – most of the relevant work is performed to determine the best estimate.

Feedback on AASB ED 319/NZASB ED 2022-3

BC156 Some respondents expressed the view that the NZASB's proposed 75% rebuttable presumption would be straightforward to implement and avoid debate about how the risk adjustment requirements should apply. Some respondents also noted the view that it would also help achieve consistency across public sector entities with the rebuttable presumption of a 75% confidence level.

BC157 Most respondents, however, supported not having an explicit modification to AASB 17/PBE IFRS 17 for the following reasons:

- (a) consistency with principle-based standard setting;
- (b) many public sector entities would need to rebut the 75% confidence level because it would not be consistent with their existing pricing policies;
- (c) a rebuttable 75% confidence level could be viewed as more onerous than the requirements for the private sector; and
- (d) consistency across public sector entities might be able to be achieved without the need for a rebuttable presumption.

BC158 Some respondents also supported the Boards providing some form of application guidance, including:

- (a) to explain how the risk adjustment requirements differ from the existing risk margin requirements;
- (b) on the basis that the risk adjustment requirement in AASB 17/PBE IFRS 17 is simply an expression of compensation required due to the uncertainty in fulfilling the liability – additional application guidance should be provided to assist entities that do not require compensation;
- (c) to explain whether a public sector entity can have a zero risk adjustment and the circumstances when this may be appropriate; and
- (d) to assist entities to determine when an estimate other than the central estimate would need to be used; that is, when other than a zero risk adjustment would be needed,²⁴ assuming a public sector entity can have a zero risk adjustment.

Boards' Redeliberations on Risk Adjustments

BC159 The Boards noted the following lines of thinking on the AASB 17/PBE IFRS 17 risk adjustment requirements.

- (a) A strict application of the AASB 17/PBE IFRS 17 definition of 'risk adjustment for non-financial risk' to an entity that does not seek to be compensated for bearing risk would seem to result in a zero risk adjustment. Since almost all public sector entities do not seek to be compensated in their pricing of levies/premiums for bearing risk, it could reasonably be expected (based on the definition alone) that they would determine zero risk adjustments (a liability with a confidence level of 50%);
- (b) Based on AASB 17.B87/PBE IFRS 17.AG87, some public sector entities that do not price for bearing risk, nonetheless, would not be indifferent between;
 - (i) fulfilling a liability that has a range of possible outcomes arising from non-financial risk; and
 - (ii) fulfilling a liability that will generate fixed cash flows with the same expected present value as the insurance contracts; and

would, therefore, have a risk adjustment above zero. And some stakeholders consulted by the Boards expressed the view that a zero risk adjustment does not seem realistic in respect of insurance liabilities and the uncertainty associated with them.
- (c) A public sector entity that does not price for risk could validly have no risk adjustment included in its liability for remaining coverage, but have a risk adjustment included in its liability for incurred claims on the basis that it is not indifferent to the variability associated with the expected

²⁴ The Boards noted that, in principle, a central estimate is not the same as having a zero risk adjustment because a zero risk adjustment could be re-measured to something above zero; whereas, a central estimate is always a central estimate.

cash flows estimated to settle claims. Accordingly, it is feasible that the confidence level for measuring a liability for remaining coverage could be different from the confidence level applied to the liability for incurred claims because the actual pricing structure does not necessarily reflect the risk appetite of the entity.

BC160 In respect of the circumstances of a public sector entity, the Boards considered the following.

- (a) Pricing decisions can be based on a range of factors and, for example, complications can arise, when entities include a margin in levies for capital management purposes. By way of illustration, a public sector entity may need to build up its capital in preparation for enhancing future benefits or to make up for previous under-reserving because claims experience has been worse than expected.
- (b) It may be reasonable to distinguish cases of ‘capital management’ and ‘capital repair’ from cases when an entity is pricing with a view to being compensated for risk. That is, there may be cases when entities price above break even for reasons other than seeking to be compensated for risk, which should be acknowledged. An ongoing policy of break-even pricing would be generally indicative of a public sector entity that is not seeking to be compensated for bearing risk.

Boards’ Conclusions on Risk Adjustments

BC161 The Boards concluded that they would not make modifications to the risk adjustment requirements of AASB 17/PBE IFRS 17 for application by public sector entities, that is Approach 1 described in paragraphs BC132 and BC133.

BC162 The Boards consider that the risk adjustment requirements of AASB 17/PBE IFRS 17 were designed to be applied to reflect the circumstances of each entity and public sector entities, by applying the unmodified requirements, would be able to reflect the impacts of their circumstances and their perspectives on insurance risk in their financial reporting. Accordingly, the Boards concluded that the amount of a risk adjustment a particular public sector entity includes in either their liabilities for remaining coverage or liabilities for incurred claims would depend on that entity’s circumstances.

BC163 In forming their conclusions, the Boards noted the following matters.

- (a) For the avoidance of doubt, the ‘compensation’ approach to risk adjustments in AASB 17/PBE IFRS 17 is different from the approach to risk margins under the superseded Standards (AASB 1023 and AASB 4/PBE IFRS 4), which were based on the inherent uncertainty within the estimates of expected cash flows. That is, the risk margins under the superseded Standards needed to be recognised when inherent uncertainty existed, regardless of an entity’s perspective on the extent to which it needed to be compensated for that uncertainty. In contrast, the recognition and measurement of a risk adjustment under AASB 17/PBE IFRS 17 relates to the compensation the entity requires for bearing the uncertainty about the amount and timing of cash flows that arises from non-financial risk. Accordingly, the risk adjustment depends on both the inherent uncertainty within the estimates of expected cash flows and each entity’s own facts and circumstances, including its objectives, management philosophy, and level of risk aversion.
- (b) In the private sector, there would generally be expected to be some, at least broad, connection between the compensation charged for bearing risk included in setting premiums and the extent to which the insurer is indifferent between the two sets of cash flows referenced in AASB 17.B87/PBE IFRS 17.AG87. This broad connection would be expected given that private sector insurers are required to remain solvent from a prudential reporting perspective and endeavour to remain profitable, particularly when they are for-profit entities. However, that same perspective does not necessarily apply to public sector entities.
- (c) There may be public sector entities that have circumstances which would lead them to recognising and measuring their liabilities for remaining coverage and/or their liabilities for incurred claims and those insurance liabilities with a zero risk adjustment.
- (d) There may be public sector entities that have circumstances which would lead them to having a zero risk adjustment in recognising and measuring their liabilities for remaining coverage, but having a risk adjustment above zero in recognising and measuring their liabilities for incurred claims. The Boards observed that this situation might arise, for example, when claims are related

to infrequent large-scale events and the uncertainties around the amounts and timing of cash flows from those events are particularly difficult to estimate.

- (e) Break-even pricing may be indicative of public sector entities that do not seek to be compensated for risk and do not include risk adjustments in recognising and measuring their liabilities for remaining coverage and/or their liabilities for incurred claims.
- (f) The availability of risk mitigation factors, such as access to government guarantees and, potentially funding from general taxation, and a monopoly market position, could be significant factors in determining whether, and to what extent, some public sector entities might need to be compensated for bearing risk. Therefore, those factors may influence public sector entities' level of indifference between fulfilling a liability that has a range of possible outcomes arising from insurance risk and fulfilling a liability that would generate fixed cash flows with the same expected present value. Accordingly, those factors may impact on the amounts of risk adjustments included in recognising and measuring their liabilities for remaining coverage and/or liabilities for incurred claims.
- (g) The extent to which a public sector entity might seek to be compensated for bearing risk, and the significance of the risk mitigation measures such as government guarantees, could depend on the extent to which the entity and its management is treated as operating independently from its controlling government. A relatively independent entity might, for example, be responsible for entering into its own risk mitigation measures, such as a reinsurance program, or maintaining a particular funding-to-liabilities ratio, and may not be expected to rely on measures such as government guarantees.

Identifying Public Sector Arrangements that fall within the Scope of AASB 17/PBE IFRS 17 (Modifications to Paragraph 6 and Addition of Appendix E)

BC164 In developing their proposals for identifying which arrangements in the public sector would be accounted for as insurance contracts, the Boards' general approach was based on:

- (a) considering the definitions and guidance on 'insurance contracts', 'insurance contract services' and 'insurance risk' in AASB 17/PBE IFRS 17; and
- (b) identifying a range of indicators that would be considered collectively, along with related guidance.

BC165 The Boards took the view that a collective consideration of the proposed indicators discussed below in paragraphs BC168–BC228 would mean that:

- (a) the existence of a particular indicator would not necessarily result in AASB 17/PBE IFRS 17 being applicable; and
- (b) the absence of a particular indicator would not necessarily result in AASB 17/PBE IFRS 17 being inapplicable.

BC166 In developing the proposed indicators, the Boards noted that the main alternative requirements applicable to liabilities of public sector entities are set out in AASB 137/PBE IPSAS 19 *Provisions, Contingent Liabilities and Contingent Assets*. Accordingly, the Boards were mindful of the key differences between the requirements of AASB 17/PBE IFRS 17 and AASB 137/PBE IPSAS 19, which include different discount rate requirements for present valuing cash flows and the specific requirement in AASB 17/PBE IFRS 17 for a risk adjustment.

BC167 Paragraphs BC168 to BC245 outline the Boards' deliberations in identifying proposed indicators for determining when AASB 17/PBE IFRS 17 would be applied. This includes deliberations on indicators that were considered and rejected, discussed below in paragraphs BC229–BC245.

Similarity of Risks Covered and Benefits Provided

BC168 The AASB Discussion Paper (2017) proposals identified, as a suggested criterion for determining whether activities relate to insurance, that the transactions or arrangements entered into have similar characteristics and relate to a similar level of insurance risk as those entered into by for-profit private sector entities that are accounted for as insurance contracts [AASB DP.E14(c)]. This is not a factor

explicitly identified in NZASB ED 2018-7, although it can be argued that it was proposed implicitly via other proposed indicators.

- BC169 The Boards observed that some public sector arrangements have direct counterparts with private sector insurance contracts, including for example, workers' compensation contracts. In the context of a transaction neutral approach to accounting standard setting, the Boards regard this as a useful indicator that some types of arrangements in the public sector would be accounted for by applying AASB 17/PBE IFRS 17.
- BC170 The Boards noted that an arrangement in the public sector might provide a combination of types of coverage and benefits that are not matched by a private sector insurance contract, but that components of the arrangement might be directly comparable to a private sector insurance contract. For example, in Australia, compulsory third-party motor insurance arrangements provided by a public sector entity includes coverage for serious or catastrophic injuries; whereas, the counterpart private sector insurance contracts typically do not. That serious or catastrophic injury coverage is often provided under a separate public sector arrangement.
- BC171 Accordingly, the Boards acknowledge the limitations in some circumstances of using the similarity of risks covered and benefits provided as an indicator of whether AASB 17/PBE IFRS 17 would apply because directly comparable forms of coverage may not be identifiable. However, the Boards note that considering the similarity of risks covered and benefits provided would involve a broader analysis than simply assessing whether directly comparable forms of coverage exist. Also refer to the Boards' conclusions in paragraph BC263 regarding the similarity between the risks and the benefits themselves and not the level of riskiness.
- BC172 The field testing conducted in 2021-22 on the indicators revealed mixed views. Some stakeholders considered similarity of risks covered and benefits provided to be one of the most significant indicators. Other stakeholders considered that it is not a useful indicator either because:
- (a) there are examples of similar risks and benefits being addressed via insurance arrangements and (non-insurance) compensation schemes; or
 - (b) there are some arrangements that are clearly insurance contracts, but are currently exclusively issued in Australia by public sector entities.
- BC173 The field testing also revealed that the perspectives of some stakeholders about what constitutes a 'similar risk' can vary depending on whether the participants/policyholders are third parties or other public sector entities within the same government (see the discussion on 'captive' insurer at paragraphs BC272 to BC287). The Boards noted that the similarity of risks relates to the risks (or the amount and timing of cash flows) transferred and would not depend on the identity of the participants/policyholders. From the perspective of the public sector entity in its stand-alone general purpose financial statements, related-party participants/policyholders are nevertheless third parties.

Boards' Proposal on Similarity of Risks Covered and Benefits as an Indicator in AASB ED 319/NZASB ED 2022-3

- BC174 Based on the above deliberations, the Boards decided to propose as an indicator of public sector arrangements to be accounted for as insurance contracts, the similarity of risks covered and benefits provided due to the fact that the transfer of insurance risk is central to the definition of 'insurance contract'.
- BC175 The Boards considered how widely entities would be expected to search for counterpart insurance contracts and concluded it would be reasonable for entities to consider counterpart contracts both within and outside Australia and New Zealand, using information that is readily available. That is, public sector entities would not need to conduct an exhaustive global search for counterpart contracts.

Identifiable Coverage Period

- BC176 A key feature of an insurance contract in the context of AASB 17/PBE IFRS 17 is the existence of an identifiable coverage period, which is defined as 'the period during which the entity provides insurance contract services'. The coverage period provides the basis for determining the cash flows to include in measuring insurance contracts.

- (a) Most insurance contracts provide protection for events that occur during the coverage period – for example, coverage for claims that might arise from an incident over a one-year contract period. The claims may not come to light until after the coverage period has ended. These are sometimes referred to as ‘claims incurred’ contracts because the time when the event occurs is crucial to identifying valid claims.
- (b) Some insurance contracts provide protection for claims that arise during the coverage period, regardless of when the incidents that gave rise to the claims have occurred. These are sometimes referred to as ‘claims made’ contracts because the time when the claim emerges is crucial to identifying valid claims.

BC177 The Boards observed that, instead of having an identifiable coverage period, social benefit type schemes tend to be open-ended and depend on participants continuing to meet eligibility criteria, which might include, for example, being unemployed, being a student, or being above a certain age. In that context, IPSAS 42.5 defines ‘social benefit’ as:

cash transfers provided to:

- (a) specific individuals and/or households who meet eligibility criteria;
- (b) mitigate the effect of social risks; and
- (c) address the needs of society as a whole.

The social benefit eligibility criteria relate to someone’s inherent status, rather than relating to an uncertain future event that occurs within a particular coverage period.

BC178 The field testing revealed that some stakeholders consider having an identifiable coverage period is an essential feature for arrangements to be accounted for as insurance contracts on the basis that:

- (a) without a coverage period, an entity would be unable to determine the relevant fulfilment cash flows to include in measuring insurance liabilities; and
- (b) having an identifiable coverage period contrasts with open-ended compensation schemes that provide benefits based on meeting eligibility criteria (and would not be accounted for as insurance contracts).

BC179 With the benefit of feedback from field testing the indicators, the Boards noted that there is a distinction between a period being identified for the purposes of raising levies to fund a compensation scheme and the notion that an amount is collected to cover events that occur over a particular coverage period.

Boards’ Proposal on Coverage Period as an Indicator in AASB ED 319/NZASB ED 2022-3

BC180 Based on the above deliberations, the Boards decided to propose as an indicator of public sector arrangements to be accounted for as insurance contracts, the existence of an identifiable coverage period.

Enforceable Nature of Arrangement

BC181 The Boards noted that an indicative criterion in IPSAS 42 for being eligible to apply the insurance approach (and apply IFRS 17) is that the arrangements between the entity and its participants are enforceable in a similar manner to an insurer being required to act in accordance with an insurance contract [IPSAS 42.AG25(a)]. Both the AASB Discussion Paper (2017) [AASB DP.E13(b)] and NZASB ED 2018-7 [ED 2018-7.AG1.6] proposed a similar indicator. The AASB Discussion Paper proposal identified as a key criterion that a participant’s beneficial rights from an arrangement cannot be altered without a specific change in legislation or relevant governing measures and cannot be retrospectively amended.

BC182 The Boards observed that, in a for-profit private sector setting, an insurer is required to act in accordance with the terms of the contract with a policyholder in terms of the types of risks covered and what constitutes insured events and, therefore, could be the subject of a valid claim. The actual amounts of compensation paid in respect of claims are determined by reference to the terms of the contract. Typically, those terms would be based on:

- (a) the extent of loss; and

- (b) the extent to which the policyholder or another party is responsible for the events that led to the loss (that is, which party is at fault), including failure to take reasonable steps to avoid the loss.

However, in some cases, there is an identified insured amount (for example, an agreed value for motor vehicle write-off) and sometimes the amount is a function of a number of factors and possibly negotiation.

- BC183 Nevertheless, the extent of a claim in a for-profit private sector setting would need to be determined in the context of the insurance contract terms – there would ordinarily not be an opportunity for an insurer to arbitrarily change those terms under an existing contract.
- BC184 This is in contrast with a scheme under which participants are promised a benefit, but the public sector entity retains the capacity to change the benefits payable to scheme participants. This is potentially a distinguishing feature of some public sector schemes (relative to the enforceable nature of contracts in the for-profit private sector). However, the significance of this capacity may be mitigated by the extent to which benefits could be changed for existing participants under arrangements in place at the reporting date.
- BC185 The Boards considered three examples to help illustrate the relevance of this capacity. Assume a public sector arrangement has a liability for providing income support for permanently disabled motor accident victims based on paying 50% of Average Weekly Earnings (AWE).
- (a) Example A: The entity has the power to change the rate of benefits to future participants to less than 50% of AWE. However, the entity has an enforceable commitment to paying 50% of AWE to existing participants, for example, by way of settlements.
 - (b) Example B1: The entity (or the government that controls the entity) has the power to change the rate of benefits to existing participants to less than 50% of AWE but only after obtaining a change to existing legislation.
 - (c) Example B2: The entity (or the government that controls the entity) has the unilateral power to change the rate of benefits to existing participants to less than 50% of AWE, for example, based on projected budget priorities.
- BC186 The Boards noted that:
- (a) the terms in Example A are like those under most insurance contracts issued by private sector entities;
 - (b) the terms in Example B1 are unlike those under most insurance contracts issued by private sector entities; however, the fact that a legislative change would be needed to change the benefits is significant; and
 - (c) the terms in Example B2 are unlike insurance contracts issued by private sector entities because these entities would not be able to arbitrarily change benefits.
- BC187 The Boards identified that the enforceable nature of an arrangement is consistent with the basis for the accounting in AASB 17/PBE IFRS 17. Accordingly, the Boards considered that the extent to which the existing benefits under an arrangement are enforceable on the relevant public sector entity is an indicator for determining when that arrangement is accounted for as an insurance contract. Correspondingly, the Boards also considered that cases when an entity would be able to arbitrarily change benefits seems indicative of a conventional social benefit arrangement.
- BC188 The Boards observed that, relative to private sector insurers, governments are in a unique position to be able to legislate, which is relevant to Example B1 above. Having established an arrangement that provides benefits to participants, in theory, the government subsequently has the power to take those benefits away or at least adjust the amount of benefits.
- BC189 The Boards also observed that AASB 17/PBE IFRS 17 relies on the notion of an insurer having a ‘practical ability’ for the purposes of, for example:
- (a) determining the boundary of an insurance contract (practical ability to set a new price or new benefits [AASB 17/PBE IFRS 17.34(a)]); and
 - (b) relief from recognising a separate onerous contract group (when contracts within a portfolio would fall into different groups only because law or regulation specifically constrains the entity’s practical ability to set a different price or level of benefits [AASB 17/PBE IFRS 17.20]).

- BC190 The Boards identified that the notion of ‘practical ability’ could be used to help distinguish those cases when a public sector arrangement should be regarded as enforceable from cases when an arrangement is not enforceable. That is, an indicator that it is relevant to account for public sector arrangements as insurance contracts would be that the entity (or its controlling government) does not have the practical ability to change a benefit retrospectively.
- BC191 The Boards noted that some insurance contracts include features in their original terms that enable policyholders to take actions that change the amount, timing, nature or uncertainty of the amounts they will receive and AASB 17.B62/PBE IFRS 17.AG62 requires an insurer to determine the probabilities of those options being exercised in measuring insurance liabilities. When expectations are different from actual events, the insurer recognises ‘experience adjustments’ and remeasures insurance liabilities based on updated expectations. However, these contract options are at the discretion of the insured and are different from changes to existing contract terms made by an issuer.

Contract versus Statute

- BC192 The Boards noted that the AASB Discussion Paper (2017) proposals included the following [page 5].

The AASB’s view is that although AASB 17 applies only to contracts, the *Framework for the Preparation and Presentation of Financial Statements* (Conceptual Framework) does not limit liability recognition to that arising from contracts, and specifically indicates that obligations may arise from statute. In applying its principle of transaction neutrality, the AASB considers that public sector entities with insurance risk created by statute, that are in substance similar to public and private sector entities with insurance risk created by contracts, should account for insurance risk in the same way.

The respondents to the Discussion Paper either explicitly or implicitly accepted the view that AASB 17 could apply when there is an insurance arrangement based on statute (and not contracts).

- BC193 The Boards also noted PBE IFRS 17.BC5 explains that, when developing NZASB ED 2018-7, the NZASB observed some public sector PBEs were applying the requirements of PBE IFRS 4 for ‘insurance-like’ activities that arose from statute rather than contract.
- BC194 The Boards observed that the stakeholder outreach conducted in 2020-21 and the field testing of the indicators conducted in 2021-22 identified three broad types of response from stakeholders.
- (a) The manner in which the arrangement has been established (contract versus statute) is a matter of form rather than substance. These stakeholders have observed that:
 - (i) virtually identical forms of coverage are provided under either statutory or private sector (contractual) arrangements (such as comprehensive third-party motor coverage) – accordingly, the insurance Accounting Standards would apply by analogy to statutory arrangements under the accounting policy hierarchy;²⁵
 - (ii) the purpose of having a statutory (rather than contractual) arrangement is generally to mandate that people obtain coverage from the one entity (usually a public sector entity); and
 - (iii) individuals and entities are required by statute to pay for some types of insurance coverage from private sector insurers (such as workers’ compensation coverage) and the arrangements are effectively a combination of contractual and statutory terms.
 - (b) Literally, the insurance Accounting Standards are considered to apply only to contracts, and entities’ activities in respect of relationships based only on statute are (strictly interpreted) not within the scope of the insurance Accounting Standards. These stakeholders have observed that: AASB 15/NZ IFRS 15 and AASB 16/NZ IFRS 16 *Leases* provide clear definitions and descriptions of contracts that can be used as a bright line.
 - (c) For some types of risks (such as workers’ compensation coverage), the existence of documentation that includes substantive information about risks and benefits (well beyond the detail in any relevant enabling legislation or regulations), is an indication of an insurance contract.

²⁵ AASB 108/PBE IPSAS 3 *Accounting Policies, Changes in Accounting Estimates and Errors* [paragraphs 10 and 11/paragraphs 12 and 14].

BC195 The Boards noted that, under AASB 17/PBE IFRS 17, the description of the rights and obligations that would be accounted for under insurance contracts is broad (and go beyond the contract). AASB 17/PBE IFRS 17.2 says (emphasis added):

- 2 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.^[26] 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 (i.e., 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).

BC196 Stakeholders have requested the Boards to clarify whether an arrangement where a public sector entity is required by statute or other regulation alone, without separate documentation evidencing agreements directly with participants, could indicate a contract exists for the purposes of AASB 17/PBE IFRS 17. The Boards observed, for arrangements that would be accounted for as insurance contracts, it would generally be expected that some form of documentation, in addition to statutory requirements, would exist to evidence rights and obligations of participants and the relevant public sector entity. However, the Boards considered that there may be circumstances in which there is only limited documentation in addition to statutory requirements, and that limited documentation, within the statutory environment, could still be regarded as comprising, in combination with the statutory requirements, a contract.

Boards' Proposal on the Enforceable Nature of Arrangement as an Indicator in AASB ED 319/NZASB ED 2022-3

BC197 Based on the above deliberations, the Boards decided to propose as an indicator of public sector arrangements to be accounted for as insurance contracts, the absence of a practical ability to retrospectively change coverage or benefits. The Boards also decided to propose the 'practical ability' is linked to existing or substantively enacted legislative powers. The Boards noted that, otherwise, in a public sector context, an assessment of 'practical ability' would probably need to take into account a range of factors, including whether the entity (or its controlling government) has sufficient political capital to make a change that reduces a benefit, which would not be workable.

BC198 The Boards also decided that the existence or otherwise of 'contracts' versus legislative requirements is not, of itself, likely to be a useful indicator of arrangements that would be accounted for as insurance contracts. Instead, the Boards consider the enforceable nature of the arrangements (the absence of a practical ability to retrospectively change coverage or benefits) is the most relevant focus, not the form of the documentation of the arrangements.

Source and Extent of Funding

Fully Funded

BC199 One of the criteria in IPSAS 42 for being eligible to apply the insurance approach is that an arrangement is intended to be fully funded from contributions and levies. NZASB ED 2018-7 proposed using the 'fully-funded' criterion for determining whether PBE IFRS 17 would apply [ED 2018-7.AG1.1 to AG1.4].

BC200 IPSAS 42.AG20 explains 'fully funded' as follows.

AG20 A social benefit scheme is intended to be fully funded from contributions when:

- (a) The legislation or other arrangement governing the social benefit scheme provides for the scheme to be funded by contributions or levies paid by or on behalf of either the potential beneficiaries or those whose activities create or exacerbate the social risks

²⁶ The second sentence of AASB 17.2/PBE IFRS 17.2 is the same as the definition for 'contract' used more generally in Accounting Standards (including: AASB 15/NZ IFRS 15 *Revenue from Contracts with Customers*).

which are mitigated by the social benefit scheme, together with investment returns arising from the contributions or levies; and

- (b) One or both of the following indicators (individually or in combination) is satisfied:
 - (i) Contribution rates or levy rates are reviewed (and, where appropriate, adjusted in line with the scheme's funding policy), either on a regular basis or when specified criteria are met, with the aim of ensuring that the revenue from contributions or levies will be sufficient to fully fund the social benefit scheme; and/or
 - (ii) Social benefit levels are reviewed (and, where appropriate, adjusted in line with the scheme's funding policy), either on a regular basis or when specified criteria are met, with the aim of ensuring that the levels of social benefits provided will not exceed the level of funding available from contributions or levies.

BC201 Some respondents to NZASB ED 2018-7 commented that the meaning of 'fully funded' is not necessarily clear for entities that aim to be self-funded over the long term, but that in any given year might be:

- (a) overpricing to make up for past deficits;
- (b) underpricing to use up past surpluses; or
- (c) underpricing to suit current economic conditions.

Substantially Self-funded

BC202 The AASB was also mindful of the IPSASB's work on social benefits in preparing its Discussion Paper (2017) proposals, but considered that 'fully funded' would be too much of a bright line [AASB DP.BC28(b)(ii)].

BC203 Instead, one of the non-mandatory criteria proposed in the AASB Discussion Paper for determining whether AASB 17 should apply in the public sector was that the arrangement be 'substantially self-funded' [AASB DP.E14(a)]. Under the proposal, there were two aspects to self-funding:

- (a) the source of funding should be those who stand to benefit from the arrangement or those who exacerbate the risks to potential beneficiaries; and
- (b) the revenue being sufficient and/or the benefit levels being managed such that the arrangement is self-sustaining.

BC204 There was a limited response to the proposal of a 'substantially self-funded' criterion. Those who did respond generally supported using the criterion.

Beneficiary Pays

BC205 The Boards observed that all of the public sector entities in Australia and New Zealand that are currently applying the insurance Standards, or have contemplated applying the insurance Standards, receive contributions from arrangement participants either directly or indirectly via premiums or levies. In general, most or all of the funding for these entities is sourced from arrangement participants, who stand to benefit from the coverage.

BC206 The Boards also observed that some of the public sector entities in Australia that are currently not applying the insurance Standards also source most or all of their funding from those who stand to benefit from the coverage.

BC207 The Boards noted that, if this indicator were applied, it would at least have the benefit of immediately ruling out the application of the insurance Standards to a range of social benefits such as aged pensions or universal healthcare activities and disability support. The Boards also noted a possible complication is that schemes such as Medicare in Australia, at least notionally, have dedicated funding through the Medicare levy on taxpayers. However, the Boards considered the Medicare levy to probably be sufficiently like a tax to be regarded as not being a beneficiary pays model as intended under this indicator. Accordingly, the Boards considered whether it might also be helpful to explain that the significance of the indicator would be on a spectrum relating to the extent to which premiums or levies represented a beneficiary-pays model.

- BC208 The Boards observed that a payment/contribution to the insurer from a policyholder is not a part of the insurance contract definition in AASB 17/PBE IFRS 17. However, they noted that some type of funding from an arrangement participant is probably a reasonable indicator of the relevance of applying AASB 17/PBE IFRS 17 in the sense that it helps to establish an enforceable contract-like relationship between the entity providing the coverage and the arrangement participants.
- BC209 The Boards observed that the practice of refunding pro rata amounts of payments/contributions in the event that an arrangement participant cancels its coverage prior to the end of the coverage period would be further evidence of an enforceable contract-like relationship between the entity providing the coverage and an arrangement participant. The Boards noted that this is a widespread practice in the private sector general insurance industry.

Capitalising/Recapitalising

- BC210 The Boards noted that some public sector entities might need funding sourced from general taxation from time to time to help capitalise or recapitalise a public sector arrangement. These might be regarded as equity injections in some cases, rather than a source of routine funding. Accordingly, the Boards observed that periodic injections of funding from general taxation to capitalise or recapitalise a public sector arrangement would not be in conflict with a self-funding or beneficiary-pays model of funding, for the purpose of determining whether an arrangement should be accounted for under AASB 17/PBE IFRS 17.

Administrative Convenience

- BC211 The Boards noted that some public sector arrangements involve sourcing funds by way of levies on transactions between participants and private sector entities (which may be insurers). The Boards noted that, while there may not be a direct cash transaction between the public sector entity and participants in terms of the collection of funds, this is often due to the need for administrative convenience, which would not affect an assessment of the extent to which funds are sourced from participants.

Boards' Proposal on the Source and Extent of Funding as an Indicator in AASB ED 319/NZASB ED 2022-3

- BC212 Based on the above considerations, the Boards decided to propose as an indicator of public sector arrangements to be accounted for as insurance contracts, the extent to which an arrangement participant is responsible for paying a contribution. This is on that basis that it provides evidence of a contract-like relationship between an arrangement participant and the public sector entity. The Boards decided that references to 'fully-funded' and 'substantially self-funded' are probably not useful because they are difficult to interpret, but that relevant contributions would be expected to be more than, for example, a relatively small co-payment.
- BC213 Consistent with this perspective, the Boards also decided that the extent to which a contribution from an arrangement participant is an indicator of public sector arrangements to be accounted for as insurance contracts is dependent on:
- (a) the strength of the association between the contribution and the risks covered – for example, a motor vehicle owner (arrangement participant) contributes in return for being covered for risks associated with road use; and
 - (b) the extent to which the contribution is substantive relative to the risks being transferred.
- BC214 The Boards also noted the level of contributions from arrangement participants that might be sought in any given period could be affected by the extent to which the public sector entity is currently fully funded. That is, contributions might be higher or lower in any given period to either make up for earlier funding shortfalls or use up existing surpluses.²⁷ Accordingly, a medium-term view (rather than a year-by-year view) might need to be taken when assessing whether contributions from participants are substantive relative to the risks being transferred in any given period.

²⁷ Public sector entities often occupy a monopoly position and are able to raise or lower contributions to either make up for earlier funding shortfalls or use up existing surpluses.

Management Practices and Assessing Financial Performance

Assessing Financial Performance (in general)

- BC215 The Boards noted that an indicative criterion in IPSAS 42 for being eligible to apply the insurance approach is that the entity assesses its financial performance and financial position of an arrangement on a regular basis where it is required to report internally on the financial performance of the arrangement, and, where necessary, to take action to address any under-performance by the arrangement [IPSAS 42.AG25(d)].
- BC216 The Boards noted that NZASB ED 2018-7 included a proposed indicator similar to this indicative criterion in IPSAS 42 [ED 2018-7.AG1.6(d)]. The Boards also noted that the AASB Discussion Paper (2017) included a proposed indicator similar to this indicative criterion in IPSAS 42, but that the Discussion Paper proposal placed an emphasis on the assessment of claims performance [AASB DP.E14(b)].
- BC217 The Boards observed that there was little feedback on this proposal in response to NZASB ED 2018-7 and a mixed response to the AASB Discussion Paper proposal, with most respondents saying the criterion was not helpful in distinguishing insurance activities from other types of activities. In general, respondents considered there are accountability and performance mechanisms across the spectrum of social benefit and insurance arrangements in most jurisdictions.

Management Focus of the Entity (more specifically)

- BC218 The Boards noted that, in stakeholder outreach conducted in 2020-21, there was more interest in discussing the ways in which they managed their particular activities, rather than the more general matter of assessing financial performance.
- (a) Most of the stakeholders from entities that are currently applying AASB 1023/PBE IFRS 4 expressed the view that they have been established to manage an area of risk and effectively provided with seed capital and a licence to charge levies/premiums in order to operate with relative financial independence. They are generally expected to be self-funding with a view to not making further calls on government funding and consider themselves to be operating an insurance-like business on a long-term sustainable basis. Within the constraints imposed upon them, they price risk based on commercial principles and manage claims fairly and prudently.
 - (b) Most of the Australian stakeholders from entities that are currently applying AASB 137 expressed the view that they are operating a compensation scheme based on terms that have largely been dictated to them (for example, through their enabling legislation) and do not have the scope to manage the risks in the manner of a private sector insurer.
 - (c) A small number of Australian stakeholders indicated that they consider the way their entities are currently managed would be better reflected in a change to their existing accounting – some from AASB 1023 to AASB 137 and some from AASB 137 to AASB 1023/AASB 17.
- BC219 The Boards considered that, the manner in which an entity is managed is, in principle, an important indicator of which Standards should be applied on the basis that faithfully reflecting the business model in financial statements is something that Standards ordinarily aim to achieve. However, this type of indicator is likely to be subject to wide interpretation unless it is associated with specific insurance liability management practices. In that context, the Boards considered those insurance liability management practices could include the following.
- (a) *Underwriting and pricing specific types of risks:* although few (if any) public sector entities are completely unconstrained in their ability to differentially price their services, many of them are able to price risk based on an arrangement participant's characteristics (for example, industry of employment, claims experience or type of vehicle).
 - (b) *Use of reinsurance contracts to manage capital:* this is not to say that the existence of a reinsurance contract, of itself, is indicative. However, in association with other factors, such as a policy of protecting its own capital base (rather than relying on the taxpayer) for its continuing operation, the existence of a reinsurance contract can indicate that the entity is expected to manage its liabilities prudently in a manner consistent with a private sector insurer.

- (c) *Fair and prudent management of claims and remediation of significant claims risks*: although fair and prudent claims management would typically be a feature of a broad range of compensation schemes, it is a particularly significant feature of managing insurance risk, especially when coupled with possible remediation activities. Remediation will necessarily be different in a monopoly context compared with a typical commercial context. In a commercial context, remediation will often include resetting underwriting terms to exclude certain types of (high-risk) customers; whereas, monopoly public sector entities are not generally able to filter their participant base. Accordingly, for public sector entities, remediation would usually take other forms, such as interventions with risk management education programs or safety campaigns. The Boards acknowledged that, while public sector entities do not have the same imperatives commercial insurers might have on managing claims in a manner that permits them to keep trading, they are required to act fairly and would typically be required to act prudently. Accordingly, while the need to act fairly and prudently might be important in identifying arrangements that would be accounted for as insurance contracts, its presence could also be indicative of a broader range of compensation arrangements.

Boards' Proposal on Management Practices and Assessing Financial Performance as an Indicator in AASB ED 319/NZASB ED 2022-3

- BC220 The Boards decided that general practices of assessing an arrangement's financial performance and financial position on a regular basis, reporting internally on financial performance and, where necessary, taking action to address any under-performance is not a potentially useful indicator of public sector arrangements to be accounted for as insurance contracts. The Boards consider the inference that social benefit schemes versus insurance arrangements are less likely to monitor performance in this way is probably not supportable.
- BC221 Instead, the Boards decided to propose as an indicator of public sector arrangements to be accounted for as insurance contracts that the entity has objectives, policies and processes for managing risks associated with those arrangements and for its financial performance to be assessed based on how the entity meets those objectives and how successfully it applies those policies and processes. The Boards decided that, in this context, the public sector entity would be expected to conduct the following activities (either itself or via outsourcing):
- (a) underwriting and risk assessment;
 - (b) the measurement of risks and uncertainties and their impacts; and
 - (c) fair and prudent claims management and, when relevant, engage in remediation work.
- BC222 The Boards decided that the presence of all three of these factors would be an indicator of public sector arrangements to be accounted for as insurance contracts; and, conversely, the fewer of these three factors that are present, the less likely it would be for arrangements to be accounted for as insurance contracts.

Assets Held to Meet Benefits

- BC223 IPSAS 42 identifies the existence of assets being held in a separate fund, or otherwise earmarked, and restricted to being used to provide benefits as being an indicator of insurance contracts [IPSAS 42.AG25(b)]. Similarly, the AASB Discussion Paper (2017) proposals identified that assets and liabilities arising from the arrangements being held in a separate fund, or otherwise specifically identified as used solely to provide benefits to beneficiaries as indicating an insurance arrangement [AASB DP.E14(d)]. However, the AASB Discussion Paper proposals also noted that the absence of separately allocated assets is not necessarily an indicator the arrangement is not insurance.
- BC224 The Boards noted that there is a link between the indicator on 'Source and extent of funding' (discussed above) and 'Assets held to meet benefits' because funds that are sourced from an arrangement's participants are more likely to be set aside in an arrangement fund than would be the case for funds sourced from general taxation.
- BC225 The Boards also noted that there is a link with the indicator on 'Management practices and assessing financial performance' (discussed above) because public sector entities that manage their own assets intended to meet claims would be more likely to have management practices that more generally mirror those of private sector insurers. The Boards observed that this perspective is supported by feedback received in recent stakeholder outreach, with many public sector entities having been established to be

self-sustaining and having responsibility for overseeing an area of risk while achieving a breakeven result from all of their activities, including investment performance. This is a characteristic of private sector insurers, some of which routinely operate on a long-term sustainable basis by generating underwriting losses that are more than offset by investment returns.

- BC226 The Boards acknowledged that the existence of assets being held in a separate fund, or otherwise earmarked, and restricted to being used to provide benefits is a feature that can also apply to arrangements which are not in the nature of insurance. For example, a compensation scheme might be established for the victims of a recent disaster and be funded from general taxation, public appeals, or levies on certain suppliers or consumers that are pooled and invested and subsequently applied to help fund recovery efforts. Nonetheless, the Boards considered that this feature is a potentially important indicator because its absence might be indicative of arrangements that should not be accounted for as insurance contracts.
- BC227 The Boards noted that some public sector entities have assets set aside for benefits, but are not actively involved in the management of the underlying investments, which is handled centrally, for example, by a government agency established for this purpose. The public sector entity's role might be limited to advising that agency about its liquidity needs. The Boards consider the existence of assets set aside to meet benefits to be the crucial factor, and do not regard the extent of a public sector entity's active involvement in the management of its underlying investments as affecting the validity of this indicator.

Boards' Proposal on Assets Held to Meet Benefits as an Indicator in AASB ED 319/NZASB ED 2022-3

- BC228 Based on the above considerations, the Boards decided to propose as an indicator of public sector arrangements to be accounted for as insurance contracts, the existence of assets being held in a separate fund, or an entity having access to earmarked assets, that are restricted to being used to provide benefits to an arrangement's participants.

Profit Seeking

Australian Entities

- BC229 Most of the Australian public sector entities currently applying AASB 4 and AASB 1023 classify themselves as not-for-profit entities, with some classifying themselves as for-profit entities.
- BC230 The AASB Discussion Paper (2017) proposed that the amendments to AASB 17 for public sector entities should apply to both for-profit and not-for-profit public sector entities and the respondents who directly commented on this issue agreed with the AASB's proposal.
- BC231 In the stakeholder outreach conducted in 2020–21, there was virtually no support for excluding a public sector entity from applying AASB 17 on the basis that it is a not-for-profit entity. For the few stakeholders who supported automatically including a public sector entity within the scope of AASB 17 on the basis that it is a for-profit entity, their support hinged on a view that a for-profit entity is more likely to be seeking to profit from the service of bearing risk. These stakeholders viewed this as consistent with AASB 17 requiring a risk adjustment in measuring insurance liabilities and recognising revenue from bearing risk in a pattern based on the release from risk.
- BC232 The AASB observed that the differing classifications (for-profit versus not-for-profit) across Australian jurisdictions seem to be driven largely by the funding structure and, for example, whether the entity's enabling legislation allows for the entity to pay dividends to government in recognition of the cost of government capital deployed to the entity.

New Zealand Entities

- BC233 All New Zealand public sector entities currently applying PBE IFRS 4 classify themselves as not seeking to profit from their activities.²⁸
- BC234 NZASB ED 2018-7 did not include any proposals relating to the profit-seeking motive.

²⁸ Public benefit entities (PBEs) are reporting entities whose primary objective is to provide goods or services for community or social benefit and where any equity has been provided with a view to supporting that primary objective rather than for a financial return to equity holders (paragraph 6 of XRB A1 *Application of the Accounting Standards Framework*). PBEs comprise not-for-profit entities and public sector entities.

Boards' Proposal on Profit Seeking not being an Indicator in AASB ED 319/NZASB ED 2022-3

BC235 The Boards noted that the IASB did not regard the not-for-profit nature of mutual insurance entities to be a factor that would cause IFRS 17 to be inapplicable. The IFRS 17 Basis for Conclusions makes it clear that, in the IASB's view, IFRS 17 can be applied consistently to for-profit entities and mutual entities [IFRS 17.BC264 to BC269]. For-profit insurance entities and mutual insurance entities often compete for customers in the same markets.

BC236 Based on the above deliberations, the Boards decided to propose that the not-for-profit nature of an entity should not be a barrier to public sector arrangements being accounted for as insurance contracts, and this was not proposed as an indicator. However, the Boards also noted that the classification (as for-profit versus not-for-profit) would be a part of the context in which the proposed indicators are considered and, therefore, could impact on the outcome of a collective assessment of those indicators.

Scoping out Social Benefits or Specific Entities

BC237 The Boards noted that IPSAS 42.5 includes a definition of 'social risks', which mentions events or circumstances that are intended to give rise to distinct benefits from the causes of other forms of aid, such as benefits provided as the result of a disaster [IPSAS 42.AG10]. The IPSAS 42 definition is:

Social risks are events or circumstances that:

- (a) relate to the characteristics of individuals and/or households – for example, age, health, poverty and employment status; and
- (b) may adversely affect the welfare of individuals and/or households, either by imposing additional demands on their resources or by reducing their income.

BC238 The Boards observed that social risks identified in the definition are indicative, rather than implying that the same risks might not also be the subject of insurance contracts. They further noted that most, if not all, the classes of social risks mentioned in the definition could be the subject of insurance contracts sold by private sector entities, such as: annuities (age-related); health insurance (health-related); and income protection (related to health, poverty and/or employment status). Accordingly, the Boards concluded that it would not be productive to propose scoping out benefits relating to social risks using the definition in IPSAS 42.

BC239 The Boards also considered whether it might be feasible to identify particular entities or activities that would not fall within the scope of AASB 17/PBE IFRS 17. For example, whether entities such as those closely associated with the hospital/health system, as a way of automatically excluding them and removing the need for an analysis of indicators to determine whether they need to apply AASB 17/PBE IFRS 17. In that context, the Boards noted that AASB 17/PBE IFRS 17 sets a precedent by specifically scoping out particular types of transactions conducted by particular types of entities that would otherwise probably need to be accounted for as insurance contracts. These transactions include, for example, warranties provided by a manufacturer, dealer or retailer in connection with the sale of its goods or services to a customer [AASB 17/PBE IFRS 17.7(a)].

Boards' Proposal on Scoping out Social Benefits or Specific Entities not being an Indicator in AASB ED 319/NZASB ED 2022-3

BC240 The Boards decided that, while it would provide certainty for some entities, they are generally opposed to specifically identifying public sector arrangements that are not within the scope of AASB 17/PBE IFRS 17 because it is typically not the role of the Boards to identify specific entities that should, or should not, apply particular Standards.

BC241 The Boards also decided that while there may be some merit in proposing that specifically identified types of activities are not within the scope of AASB 17/PBE IFRS 17:

- (a) this could be problematic due to the potential interface between, for example, the public health system and the medical nature of many claims that might be the subject of arrangements that would be accounted for as insurance contracts; and
- (b) the relevant types of excluded activities should be able to be identified based on applying other proposed indicators.

Fault-based Nature of an Arrangement

- BC242 In respect of many classes of risk, private sector insurers attribute fault in determining whether claims are valid or the amount of those claims. For example, a policyholder that is negligent may receive a lower claim benefit than a policyholder who is not at fault, which is designed to avoid moral hazard issues. Accordingly, it could be argued that fault-based arrangements are more likely to result in insurance activities.
- BC243 The Boards noted that public sector arrangements vary across jurisdictions. For example, some of the Australian Compulsory Third Party motor insurance arrangements for non-serious injury are fault-based, while all the Compulsory Third Party motor insurance arrangements that include serious injury are no-fault arrangements. Currently, Australian stakeholders' application of either AASB 4 and AASB 1023 or AASB 137 has not reflected the fault status of the arrangements. That is, some public sector entities operating no-fault arrangements are applying AASB 4 and AASB 1023, while others have been applying AASB 137. However, the Boards are not aware of any public sector entities operating fault-based arrangements that are applying AASB 137.
- BC244 The Boards also observed that, while no-fault arrangements are more prevalent in the public sector, many classes of risk covered by for-profit private sector insurers do not involve attributing fault in determining whether claims are valid or the amount of those claims. For example, insurance contracts for risks such as health/disease and longevity are typically no-fault contracts.

Boards' Proposal on Fault-based Nature of Arrangement not being an Indicator in AASB ED 319/NZASB ED 2022-3

- BC245 Based on the above deliberations, the Boards decided that the no-fault versus fault-based nature of public sector arrangements would not be helpful in indicating whether the arrangements are to be accounted for as insurance contracts and this distinction was not proposed as an indicator.

Relative Significance of the Indicators

- BC246 The Boards considered whether some indicators should be:
- (a) separately identified as being pre-requisites for applying AASB 17/PBE IFRS 17 (that is, their absence means AASB 17/PBE IFRS 17 would not apply); or
 - (b) separately identified as being determinative in applying AASB 17/PBE IFRS 17 (that is, their presence means AASB 17/PBE IFRS 17 would apply); or
 - (b) otherwise ranked in some manner based on their significance in determining arrangements that should be accounted for by applying AASB 17/PBE IFRS 17.
- BC247 The field testing conducted in 2021-22 on the proposed indicators revealed a range of views. Some stakeholders noted a preference for ranking the indicators in some manner, although there was no consensus among those stakeholders for a particular ranking of the indicators. However, many of those seeking some form of ranking typically identified the most significant indicators as being:
- (a) an identifiable coverage period – on the basis that it contrasts with an open-ended compensation scheme that provides benefits based on meeting eligibility criteria; and
 - (b) the enforceable nature of the arrangement – on the basis that it means there is a binding arrangement between the public sector entity and a participant similar to that found in an insurance contract issued by a private sector insurer.
- BC248 In contrast, the field testing also revealed that many of those seeking some form of ranking typically identified the least significant indicators as being:
- (a) management practices and assessing financial performance – on the basis that there are many sound management and reporting practices that are routinely practiced both by insurers and by those responsible for compensation schemes; and
 - (b) the existence of a separate fund or earmarked assets held to meet benefits – on the basis that funds are often set aside within compensation schemes.

Boards' Proposal on not Assigning a Relative Significance to the Indicators in AASB ED 319/NZASB ED 2022-3

- BC249 The Boards decided that they would not propose assigning a relative significance to each of the indicators on the basis that this is generally inconsistent with principle-based standard setting and with the notion of making a collective assessment and applying judgement based on the relevant circumstances. Instead, the Boards responded to the field test feedback by trying to better explain the relevant aspects of the indicators considered by some to be the least significant.
- BC250 The Boards also decided to include a specific question in AASB ED 319/NZASB ED 2022-3 on whether the indicators should be ranked in some manner and, if so, how they should be ranked and the reasons for that ranking.

Identifying Public Sector Arrangements Scoped into AASB 17/PBE IFRS 17 – AASB ED 319/NZASB ED 2022-3 Feedback

- BC251 Most respondents to AASB ED 319/NZASB ED 2022-3 supported using indicators to determine whether public sector arrangements fall within the scope of AASB 17/PBE IFRS 17.
- BC252 While many respondents considered some indicators to be more relevant than others, most were in favour of retaining all the proposed indicators.
- BC253 Some respondents suggested additional or alternative indicators for arrangements being identified as insurance contracts, and others suggested indicators for arrangements that should not be identified as insurance contracts, including, for example, having a government guarantee to support the arrangements. There were mixed views on whether the fact that some public sector entities fill gaps in the private sector insurance market for the same risks as being insured by private sector insurers is indicative or non-indicative of insurance contracts.
- BC254 Some respondents also suggested amending the 'insurance contract' definition to cater more specifically for public sector circumstances, in particular, in cases when the arrangements depend largely on a regulatory framework rather than separate contracts.
- BC255 Respondents also provided the following feedback on the specific proposed indicators.
- (a) **Similarity of risks covered and benefits provided:** Most respondents considered this to be an important indicator because it is intuitive that a public sector arrangement which addresses similar risks and benefits to insurance contracts in the private sector would be a good candidate to fall within the scope of AASB 17/PBE IFRS 17 and is consistent with the notion of transaction neutrality. Some respondents considered that there could be two elements to this indicator: (i) similarity or comparability between the risks and the benefits themselves; and (ii) similarity with the level of riskiness when compared with private sector insurance contracts, because public sector entities are often filling a gap in the market relating to insuring the more catastrophic risks.
 - (b) **Identifiable coverage period:** All respondents supported this indicator and many considered that it should rank above most of the other indicators, with some suggesting that it should be a pre-requisite for applying AASB 17/PBE IFRS 17. Some of these respondents noted that, without an identifiable coverage period, it would not be feasible to determine the fulfilment cash flows that should be used to measure insurance liabilities and, accordingly, it is an essential feature of an insurance contract both in principle and in practical terms. Some respondents also commented that having an identifiable coverage period can be regarded as the direct opposite of a (non-insurance) compensation scheme under which individuals or entities are eligible for benefits simply because of the inherent characteristics or status they possess at a particular time.
 - (c) **Enforceable nature of arrangement:** All respondents supported this indicator and many considered that it should rank above most of the other indicators, with some suggesting that it should be a pre-requisite for applying AASB 17/PBE IFRS 17. Many of these respondents considered that enforceability is essential to there being a contract, consistent with other AASB Standards applied in the public sector that relate to contracts on revenue recognition and leases.
 - (d) **Source and extent of funding:** All respondents supported this indicator, including that there greater the extent of funding by the insured/beneficiary, the more likely it is an arrangement that would be suitable to be accounted for as giving rise to insurance contracts. Some respondents

acknowledged that there is no particular tipping point in respect of the extent of funding. Some respondents considered that it is at least as relevant to focus on how an amount of funding is calculated, rather than only its source being, for example, general taxation and suggested an actuarially calculated appropriation could be indicative of insurance.

- (e) **Management practices and assessing financial performance:** Most respondents supported this indicator, but many considered that it should rank below most of the other indicators. Some respondents did not favour the indicator because they considered that most arrangements operated by government would be expected to possess this attribute to meet relevant governance standards. Some respondents considered that the focus should be on management practices more specific to the insurance industry, including underwriting and risk management.
- (f) **Assets held to meet benefits:** Most respondents supported this indicator, but many considered that it should rank below most of the other indicators. Some respondents did not favour the indicator because they considered that many compensation schemes operated by government hold assets to meet the expected benefit payments.

BC256 Some respondents favoured a collective assessment of all the proposed indicators without ranking them. However, most respondents favoured ranking the indicators and/or identifying some indicators as pre-requisites, for a range of reasons, including on the basis that they considered it would:

- (a) tend to result in a greater level of consistency in application and, therefore, in more consistent outcomes;
- (b) make the assessment easier compared with the potential burden of making a collective assessment of six indicators.

BC257 Those respondents who favoured ranking the indicators and/or identifying some indicators as pre-requisites had varied views on which of the indicators should be ranked most highly. However, balancing all the feedback received, the Boards noted that:

- (a) having an identifiable coverage period and the enforceable nature of an arrangement were generally regarded as the most crucial of the indicators;
- (b) the similarity of risks covered and benefits provided and the source and extent of funding from those who stand to benefit from an arrangement were generally regarded as relatively important indicators; and
- (c) having management practices and assessing financial performance in a manner consistent with insurance industry practices and the existence of assets being held in a separate fund, or an entity having access to earmarked assets, that are restricted to being used to meet benefits to an arrangement's participants were generally regarded as the least important of the indicators.

BC258 There was no specific feedback from respondents to AASB ED 319/NZASB ED 2022-3 on the Boards' rejecting the following factors in determining whether an arrangement would be within the scope of AASB 17/PBE IFRS 17:

- (a) the for-profit versus not-for-profit status of the entity;
- (b) scoping out social benefits or specific entities; and
- (c) the fault-based nature of the arrangement.

Boards' Conclusions on Identifying Public Sector Arrangements Scoped into the AASB 17/PBE IFRS 17

BC259 The Boards reflected on their reasons for proposing a collective assessment of the six proposed indicators and the feedback received and concluded that, in determining when a public sector arrangement should fall within the scope of AASB 17/PBE IFRS 17:

- (a) the six proposed indicators are all potentially relevant;
- (b) no other indicators should be applied; and
- (c) it would be beneficial to provide a more structured approach to applying the indicators, rather than the proposed collective assessment approach.

BC260 Instead of identifying six indicators, the Board concluded that:

- (a) two of the proposed indicators should instead be pre-requisites for applying AASB 17/PBE IFRS 17;
- (b) two of the proposed indicators should remain as indicators to be assessed collectively; and
- (c) two of the proposed indicators should instead be ranked lower than indicators and be ‘other considerations’ to be assessed collectively.

The Boards considered that this would provide a more rigorous approach to determining public sector arrangements that should fall within the scope of AASB 17/PBE IFRS 17. However, they noted that judgement would still need to be exercised in applying the pre-requisites, indicators and other considerations based on each entity’s circumstances.

BC261 More specifically, the Boards concluded the following.

- (a) The existence of an identifiable coverage period for a public sector arrangement is a pre-requisite for applying AASB 17/PBE IFRS 17 on the basis that the coverage period is crucial for determining the fulfilment cash flows to include when measuring insurance liabilities and for determining the timing of insurance revenues and expenses.
- (b) The enforceable nature of a public sector arrangement is a pre-requisite for applying AASB 17/PBE IFRS 17 on the basis that a key feature of any contract is its enforceability and public sector arrangements that lack enforceability are more in the nature of social benefits.
- (c) The similarity of risks covered and benefits provided with those offered by a relevant counterpart private sector insurer is an indicator to be applied to determine whether arrangements fall within the scope of AASB 17/PBE IFRS 17 on the basis that this is consistent with a transaction neutral approach to standard-setting. The greater the level of similarity between the risks accepted and benefits provided by a public sector entity and those offered by a relevant counterpart private sector insurer, the more likely it would be that the public sector entity’s arrangements would be accounted for as insurance contracts.
- (d) The source and extent of funding from those who stand to benefit from an arrangement is an indicator to be applied to determine whether arrangements fall within the scope of AASB 17/PBE IFRS 17 on the basis that a user-pays arrangement is consistent with a commercial arrangement for the transfer of insurance risk. The greater the extent of funding from those who stand to benefit from an arrangement, the more likely it would be that the public sector entity’s arrangements would be accounted for as insurance contracts. A user-pays arrangement is typically distinguishable from a social benefit scheme or (non-insurance) compensation scheme.
- (e) In the event that the indicators in paragraphs (c) and (d) are not collectively definitive in determining whether arrangements fall within the scope of AASB 17/PBE IFRS 17, collective consideration is given to whether, in respect of the relevant arrangements:
 - (i) the entity has management practices and assesses financial performance in a manner consistent with insurance industry practices; and
 - (ii) there is a separate fund, or earmarked assets, that are restricted to being used to meet benefits to participants in the arrangement;

in order to determine whether arrangements fall within the scope of AASB 17/PBE IFRS 17.

BC262 In respect of the pre-requisite for an identifiable coverage period, the Boards concluded that additional guidance would be helpful to explain that a person’s inherent status in meeting eligibility criteria for participation in a scheme, stands in contrast to the existence of an identifiable coverage period.

BC263 In relation to the indicator ‘similarity of risks covered and benefits provided’ with those offered by any relevant counterpart private sector insurer, the Boards concluded that the similarity between the risks and the benefits themselves is the focus, not the level of riskiness. While some ‘last resort’ risks or ‘protection gaps’ might be peculiar to the public sector in terms of their level of riskiness, they concluded this would not preclude them from being within the scope of AASB 17/PBE IFRS 17. The Boards observed that, under AASB 17/PBE IFRS 17, insurance contracts are identified on the basis that they involve the transfer insurance risks – there is no limit on the level of insurance risk that might be transferred in an insurance contract or the level of riskiness.

- BC264 In relation to the source and extent of funding from those who stand to benefit from an arrangement, the Boards concluded this could still be indicative of an arrangement that would fall within the scope of AASB 17/PBE IFRS 17 even though the relevant public sector entity may receive top-up funding from sources such as general taxation from time to time.

Application Date of the Standard

- BC265 The mandatory application date of AASB 17/PBE IFRS 17 for entities other than public sector entities is periods beginning on or after 1 January 2023.
- BC266 The Boards noted that they typically provide at least a one-year gap between the time a new or revised Standard is issued and the beginning of the comparative reporting period to which it applies. This is designed to allow stakeholders to adequately prepare for any changes to processes for preparing and auditing financial statements.
- BC267 Accordingly, the AASB decided to propose that public sector entities falling within the scope of AASB 17 be required to apply it for annual reporting periods beginning on or after 1 July 2025 and the NZASB decided it would propose that public sector entities falling within the scope of PBE IFRS 17 apply it to annual periods beginning on or after 1 January 2025. The difference in date reflects different administrative procedures; however, the impact would be the same under both proposed dates because public sector entities typically have July to June reporting periods and would first be required to apply AASB 17/PBE IFRS 17 for the period 1 July 2025 to 30 June 2026, with comparative information for the period 1 July 2024 to 30 June 2025.
- BC268 Consistent with existing practice, the Boards also decided to propose that entities would be permitted to apply AASB 17/PBE IFRS 17 for ‘early adoption accounting periods’, i.e. periods that begin before the mandatory date and, if an entity does apply the Standard for an ‘early adoption accounting period’, it must disclose this fact. For PBE IFRS 17, an ‘early adoption accounting period’ is a period that begins before the mandatory date but that has not ended before the Standard takes effect.

Application Date of the Standard – AASB ED 319/NZASB ED 2022-3 Feedback and Boards’ Conclusions

- BC269 Most respondents to AASB ED 319/NZASB ED 2022-3 supported the proposed application date, provided the Boards meet the planned timetable of having an Amending Standard issued by the end of December 2022. Entities that had the greatest concerns about the proposed mandatory application date(s) were either currently applying AASB 137²⁹ or were also facing other substantive regulatory changes in the near term.
- BC270 The Boards noted that, in responding to the Draft Standard of the amendments to AASB 17/PBE IFRS 17 issued in October 2022 for fatal-flaw review comment, some stakeholders expressed the view that the mandatory application date should be extended for a further year. In order to gauge views on the mandatory application date, the Boards conducted informal outreach with key constituents in November 2022 on whether the mandatory application date should be extended for a year. While most respondents had no specific preference for either a 2025 or 2026 transition date, some stakeholders considered that the additional time would be of great value to facilitate:
- (a) the update of information systems and data collection processes for arrangements falling within the scope of AASB 17/PBE IFRS 17 that currently classify their liabilities as provisions and, in some cases, when coverage periods need to be determined based on contracts issued by private sector insurers; and
 - (b) the ability to engage with key users of their financial information on the changes to their financial statements from transitioning to AASB 17/PBE IFRS 17, including in terms of budgetary processes.
- BC271 On balance, the AASB concluded that the mandatory application date should be annual reporting periods beginning on or after 1 July 2026 and the NZASB concluded it should be annual periods beginning on or after 1 January 2026, which will result in the Standard being applicable for the same annual reporting periods in both jurisdictions. The Boards consider it is appropriate to extend the mandatory application date on the basis that:

²⁹ AASB 137 only (and not PBE IFRS 19) because the relevant entities are Australian.

- (a) although the 2025 mandatory application date would have provided approximately 18 months between the issue of the Amending Standard and the beginning of the comparative period to which AASB 17/PBE IFRS 17 would apply mandatorily, the transition effort will be much greater for some public sector entities than for others; and
- (b) although a number of the public sector modifications made to AASB 17/PBE IFRS 17 are expected to help facilitate the transition process, some public sector entities may need the additional time to inform key users of the changes to their financial statements.

The Boards also noted that harmonisation across the two jurisdictions is desirable both in terms of the requirements and the practical application date.

Captive Insurers (Amendments to AASB 1050 *Administered Items*)

BC272 The Boards noted that large consolidated group entities sometimes establish a ‘captive insurer’ subsidiary to coordinate risk management for all (or most) entities within the group.³⁰ The subsidiary typically charges premiums to other entities in the group and pays them valid claims in respect of insured events, and ordinarily (re)insures some or all of the risks with one or more third-party (re)insurer(s). Australian or New Zealand-based private sector captive insurers would need to be registered as insurers and, therefore, required to prepare general purpose financial statements and meet relevant regulatory and prudential requirements.

BC273 The Boards noted that governments also create captive insurers and the key motivations are typically to:

- (a) centralise the administration of insurable risks across a complex group of entities and coordinate risk management policies and processes;
- (b) charge premiums to other government agencies and, thereby, create incentives for them to manage risks; and
- (c) in some cases, coordinate in a cost-beneficial manner the acquisition of insurance/reinsurance coverage from an external insurer/reinsurer.

BC274 The Boards observed that, at the whole-of-government level:

- (a) transactions between the captive insurer and other government agencies are eliminated;
- (b) any (re)insurance contracts between the captive and third-party insurers are treated as insurance contracts in which the government is a policyholder; and
- (c) any remaining liabilities to third parties (for example, to government employees for workplace injuries) would be accounted for by applying AASB 137/PBE IPSAS 19.

BC275 The Boards considered whether they should:

- (a) in the context of the requirements imposed on private sector Australian-based and New Zealand-based captive insurers, explicitly require public sector captive insurers that prepare general purpose financial statements to apply AASB 17/PBE IFRS 17; or
- (b) given the eliminations at the whole-of-government level, explicitly scope public sector captive insurers out of applying AASB 17/PBE IFRS 17.

BC276 The Boards noted the following in respect of the AASB Discussion Paper (2017).

- (a) It was proposed that public sector captive insurers should be permitted an optional exemption to not apply AASB 17 on the basis that:
 - (i) some captive public sector entities do not currently apply insurance accounting to their insurance transactions; and
 - (ii) the cost of doing so is likely to be greater than the benefits given the accounting would be reversed on consolidation. (In the consolidated entity, since insurance risk has not been transferred to a party outside the group, any claim liabilities would probably be accounted for as provisions by applying AASB 137).

³⁰ For a consolidated group that is not an insurer, the captive insurer would typically organise the group’s insurance coverage. For a consolidated group that is an insurer, the captive insurer would typically organise the group’s reinsurance coverage.

- (b) It was also proposed that, in the event there is a public sector entity that accepts insurance risk from both related and unrelated parties, the optional exemption from applying AASB 17 would apply only to transactions with related parties.
- (c) Respondents expressed mixed views, including:
 - (i) support for captive insurers being scoped out of AASB 17;
 - (ii) support for the optional exemption;
 - (iii) strong disagreement with the proposals based on a view they would create complexity for some entities within a group reporting structure that are required to use two different measurement bases; and
 - (iv) when there are no users dependent upon the financial statements of a captive insurer, it would be at the discretion of the relevant government to exempt the entity from preparing general purpose financial statements.

BC277 The Boards noted that NZASB ED 2018-7 did not raise the issue of captive insurers and nor did any of the respondents to the ED.

BC278 The Boards also noted that more recent stakeholder consultation revealed a variety of reasons for different practices among Australian governments in terms of whether separate general purpose financial statements are presented for captive insurers.

- (a) Various accountability mechanisms and reporting requirements apply across the public sector and captive insurers either report separately (or not) based on those general requirements. For example, an entity may be regarded as being primarily engaged in providing claims management services to other areas of government rather than bearing insurance risk, which may lead a jurisdiction to conclude that:
 - (i) separate general purpose financial statements are not needed; or
 - (ii) if separate general purpose financial statements are needed, they would be prepared on the basis that the entity is a service provider for managing the claims process, rather than bearing insurance risk, and would not apply insurance contract accounting.
- (b) Historical responsibilities for bearing risks have been allocated to the entity, which were accompanied by particular (usually legislated) accountability mechanisms and reporting requirements.
- (c) A deliberate policy has been adopted to impose accountability mechanisms and reporting requirements on a captive insurer, consistent with (for example) having an independent board of directors. Entities with independent boards of directors/management might be particularly keen to demonstrate accountability and prepare separate financial statements. Some stakeholders consider the fact that their customers are related entities makes it all the more important that they prepare separate general purpose financial statements.

Boards' Position on Captive Insurers in AASB ED 319/NZASB ED 2022-3

BC279 The Boards considered that the issues surrounding captive insurers are essentially reporting entity issues, that could affect the application of Accounting Standards more generally, rather than being issues of particular relevance to the insurance project. The Boards observed that governments which regard their captive insurer(s) as needing to prepare general purpose financial statements would have to determine whether they have:

- (a) insurance contracts and need to apply insurance contract accounting; or
- (b) are only service providers, akin to insurance brokers that are intermediaries between policyholders and insurers, that would apply, for example, AASB 15 *Revenue from Contracts with Customers*/PBE IPSAS 9 *Revenue from Exchange Transactions*.

The Boards also observed that governments which regard their captive insurer(s) as not needing to prepare general purpose financial statements, might seek to have them prepare a type of segment information, for example, for management purposes.

BC280 Accordingly, the Boards decided not to propose public sector modifications in respect of captive insurers because wider issues regarding the identification of reporting entities are at stake that are not specific to this project. They noted, if a jurisdiction determines that an entity should prepare general purpose financial statements, provided the entity's activities fall within the scope of AASB 17/PBE IFRS 17, that Standard should be applied. The Boards considered it would be inappropriate, for example, to exempt public sector captive insurers from applying AASB 17/PBE IFRS 17 in their separate financial statements.

Captive Insurers – AASB ED 319 feedback and the AASB's Conclusions

BC281 Some Australian respondents to AASB ED 319 expressed the following concerns about not providing any specific relief from applying AASB 17 to captive insurers and noted the following issues and perspectives.

- (a) The user of captive insurer financial statements is the controlling government, and the application of AASB 17 would provide no additional information to that user.
- (b) The costs of preparing individual captive entity financial statements in accordance with AASB 17, only to eliminate this treatment on consolidation, would exceed the potential benefit.
- (c) Issues could arise when an entity that does not prepare general purpose financial statements has insurance arrangements which are administered by a government department. Under AASB 1050, the government department may need to apply AASB 17 to prepare its administered items disclosure note in its general purpose financial statements. However, at the Whole of Government level, those arrangements are recognised under AASB 137.
- (d) A similar issue arises for the General Government Sector (GGS) financial statements where AASB 17 accounting would need to be applied in relation to captive insurance activities conducted by Public Financial Corporations (PFC)³¹ that are eliminated on consolidation in the Whole of Government financial statements.

There were no comments from New Zealand stakeholders on captive insurers.

BC282 The AASB noted it would be consistent with paragraph 24 of AASB 1050 *Administered Items*, although not the only possible interpretation, for a government department administering an arrangement that falls within the scope of AASB 17 to prepare administered item disclosures based on applying AASB 17. This is because it is not self-insurance from the perspectives of the administered entity or of the administering government department.

BC283 The AASB also noted that the issue of effectively preparing two sets of financial statements using different accounting policies is not new because there are current instances of reporting AASB 1023 *General Insurance Contracts* information for insurance activities conducted between public sector entities controlled by the same government. Therefore, currently, two sets of financial information are sometimes prepared.

BC284 The AASB noted that, for the reasons outlined in paragraph BC278, current reporting practices for captive insurance arrangements in the public sector³² vary widely in terms of the type of reporting and the accounting policies applied and the formats include the following:

- (a) separate stand-alone general purpose financial statements, presumably on the basis the arrangements are deemed to be a reporting entity;
- (b) as a segment of the general purpose financial statements of an entity that also includes other (non-captive) insurance arrangements; and
- (c) financial information disclosures presented in the notes to the general purpose financial statements of another entity, such as the responsible government department, whether as part of an administered items note or presented in some other way.

³¹ A captive insurer seems most likely to be classified as a PFC, although it's possible there may be captives that are classified as a public non-financial corporation (PNFC).

³² Private sector captive insurers in Australia and New Zealand must prepare stand-alone financial statements because they are registered insurance companies – accordingly, similar debates about the form of reporting generally do not arise.

BC285 The AASB considered four possible alternative approaches.

- (a) Approach 1: Allow captive insurers a free choice to apply AASB 17 or AASB 137 regardless of whether the activities would fall within the scope of AASB 17 based on the pre-requisites, indicators and other considerations, which would avoid governments being forced to apply different forms of accounting at the entity and consolidated levels. Entities currently applying AASB 137 would not be at risk of having to change their reporting to applying AASB 17 and some entities currently applying AASB 1023 may change their reporting to apply AASB 137, rather than AASB 17. However, the AASB considered the principle that each entity should apply Standards based on its own perspective and circumstances, not those of its parent, and the free choice might be seen as inconsistent with this principle.
- (b) Approach 2: Require captive insurers to apply AASB 137, whether controlled or administered, which would avoid governments being forced to apply different forms of accounting at the entity and consolidated levels (unless applying AASB 17 met management reporting needs) and would remove any element of doubt about which Standards to apply. Entities currently applying AASB 1023 would be required to change their reporting to apply AASB 137, rather than AASB 17. It would help achieve consistent reporting of information about self-insurance activities across all forms of reporting. However, the AASB considered this approach may result in a loss of useful information, in particular disclosures about claims, and would be inconsistent with the principle that each entity applies Standards based on its own perspective and circumstances. In addition, it would force some entities to transition from insurance accounting under AASB 1023 to AASB 137, when transitioning to AASB 17 may be preferred for cost-benefit reasons.
- (c) Approach 3: Require captive insurers to apply AASB 17, whether insurance activities are controlled or administered. This is effectively the position proposed in AASB ED 319/NZASB ED 2022-3, which would avoid governments being forced to apply different forms of accounting at the entity and consolidated levels (unless applying AASB 137 met management reporting needs) and remove doubt about which Standards to apply. Entities currently applying AASB 137 would be required to change their reporting to apply AASB 17, but only when the activities would fall within the scope of AASB 17 based on the pre-requisites, indicators and other considerations. It would help achieve consistent reporting of information about self-insurance activities across all forms of reporting. However, the AASB noted constituent concerns about having some entities transition from accounting under AASB 137 to AASB 17, which would have cost implications.
- (d) Approach 4: No modifications to the application of AASB 17 when the activities would fall within the scope of AASB 17 based on the pre-requisites, indicators and other considerations when an entity controls the insurance activities and prepares stand-alone general purpose financial statements. However, permit a free choice for government departments to apply either AASB 17 or AASB 137 to prepare administered item information on captive insurers that do not prepare stand-alone general purpose financial statements. This would avoid governments being forced to apply different forms of accounting at the entity and consolidated levels, but not necessarily when there are stand-alone general purpose financial statements as well. This is consistent with the principle that each entity applies Standards based on its own perspective and circumstances in the context of stand-alone general purpose financial statements, but not in an administered items context.

BC286 The AASB concluded that Approach 4 should be implemented by amending AASB 1050 for the following reasons.

- (a) The AASB considers that the decision of a jurisdiction to require an entity to prepare stand-alone general purpose financial statements when that entity, from a whole of government perspective, conducts self-insurance activities, should trigger the need to apply Accounting Standards based on that entity's perspective. As a stand-alone entity, its insurance activities³³ would not be self-insurance and, if the activities fall within the scope of AASB 17 based on the pre-requisites,

³³ This could be all the entity's activities or only a portion of its activities.

indicators and other considerations, the captive insurer should apply AASB 17 in its general purpose financial statements.

- (b) It is reasonable from a cost-benefit perspective to avoid the potential for different accounting policies having to be applied in reporting administered item information in Departmental general purpose financial statements and consolidated information in Whole of Government general purpose financial statements.
- (c) Approach 4 seems consistent with the basis on which AASB 1050 was created. AASB 1050 emerged from a restructuring of Accounting Standards applicable to government entities that included withdrawing AAS 29 *Financial Reporting by Government Departments*, which, among other things, addressed administered item disclosure requirements. In this process, the AASB made a limited number of amendments and acknowledged inadequacies in AAS 29 are retained, including the lack of extensive guidance for identifying administered items and the potential inadequate prominence given to administered items in a complete set of financial statements – refer to paragraph BC13 of AASB 1050. The AASB noted that one possible inadequacy appears to be that the basis of accounting for administered items may differ from the basis that would be used in a government department’s own financial statements in respect of controlled items – refer to paragraph BC18 of AASB 1050.

The Boards noted that supportive feedback was received for Approach 4, which was included in the Draft Standard of the amendments to AASB 17/PBE IFRS 17 (and, in the case of the AASB only, AASB 1050 *Administered Items*) issued in October 2022 for fatal flaw comment.

- BC287 The AASB noted that the decision to take Approach 4 in this project, including permitting a choice of Standard to apply to determine administered item disclosures, should not be viewed as setting a precedent for how any future AASB work on administered item disclosures might evolve.

Other Modifications Considered but not Included

Discounting and Inflating

- BC288 Based on public sector arrangements that seem likely to fall within the scope of AASB 17/PBE IFRS 17 and the Boards’ proposals on contract boundaries and coverage periods (modifications to paragraphs 34 and B64/AG64), the Boards noted that:

- (a) most coverage periods are one year or less; and
- (b) levies/premiums are typically received either shortly before coverage commences or early in the coverage period.

- BC289 Accordingly, the Boards observed that the discounting requirements in AASB 17/PBE IFRS 17 (such as in AASB 17/PBE IFRS 17.36 and 56):

- (a) would not be expected to be relevant in measuring levies/premiums and in measuring most liabilities for remaining coverage;
- (b) might be relevant in the unlikely event that the general measurement model would need to be applied to measure liabilities for remaining coverage for arrangements that provide multi-year coverage.

- BC290 However, the Boards observed that public sector arrangements which seem likely to fall within the scope of AASB 17/PBE IFRS 17 often involve claims that are settled over long periods – sometimes many decades – and that discounting and inflating is usually an important aspect of measuring liabilities for incurred claims.

- BC291 The Boards noted that, under AASB 1023/PBE IFRS 4, expected future cash flows are:

- (a) discounted for the time value of money at a risk-free rate based on current observable, objective rates that relate to the nature, structure and term of the future obligations;
- (b) may need to be inflated because the ultimate cost of settlement will be affected by inflationary factors likely to occur during the period to settlement; and
- (c) not expected to be either discounted or inflated when they are settled within a year.

- BC292 The Boards noted that, under AASB 17/PBE IFRS 17, essentially the same notions of discounting and inflating cash flows apply, but that the discount rate relates to a current time value of money and the liquidity characteristics of the insurance contracts. That is, all other things being equal, the discount rates under AASB 17/PBE IFRS 17 would be expected to be higher than under AASB 1023/PBE IFRS 4 due to the adjustment for illiquidity.
- BC293 The Boards noted the various sources of guidance and requirements (outside the Standards) for determining discount rates and inflation rates, including:
- (a) Australian and New Zealand actuarial guidance on valuation of general insurance claims;
 - (b) Australian Prudential Regulation Authority prudential requirements on insurance liability valuation;
 - (c) the risk-free discount rates and consumer price index (CPI) assumptions published by the New Zealand Treasury that must be used for the purpose of preparing the financial statements of government reporting entities submitting valuations to Treasury for measuring insurance claims liabilities under PBE IFRS 4.
- BC294 The Boards noted that, in respect of discount rates, all the various sources of guidance have a common starting point of sovereign bond yields for durations that match the relevant claims liabilities, with extrapolation when needed.

Illiquidity Premium

- BC295 The Boards observed that, in concept, the size of an illiquidity premium would be positively correlated with:
- (a) the length of time over which claims (cash flows) are expected to be paid; and
 - (b) the predictability of the cash flows.

Accordingly, the longer the time to expected settlement and the more predictable are the cash flows, the less liquid is the liability and the larger is the illiquidity premium.

- BC296 The Boards noted that, in general, private sector insurers have yet to settle on their approach to determining an illiquidity premium under AASB 17/PBE IFRS 17 and that there are, as yet, no readily-available and widely-accepted benchmarks that can be applied. However, the Boards expect that an industry practice will emerge that public sector entities could apply.
- BC297 The Boards considered whether there might be a need for public sector specific guidance on determining an illiquidity premium, but concluded that the issues for public sector entities are no different from those that need to be addressed by other entities applying AASB 17/PBE IFRS 17.

Investment Rates of Return and Discount Rate Volatility

- BC298 The Boards noted that:
- (a) most public sector entities set premiums/levies with a view to breaking even, after taking into account any relevant projected investment earnings; and
 - (b) the rate of projected investment returns assumed is typically above the time value of money rate applied to measure liabilities for incurred claims.

Accordingly, public sector entities ordinarily recognise unexpired risk liabilities (onerous contract losses) due, in part, to the gap between the rates.

- BC299 The Boards also noted that, for many public sector entities, the liability for incurred claims is by far the largest liability and small changes in discount rates can create liability changes from period to period that create the largest expense or revenue item in the income statement. Based on consultation with stakeholders when undertaking this project, yields on government bonds that are typically used to determine risk-free rates had been at historical lows, and small changes in rates have been having a larger than usual impact.
- BC300 The Boards noted that, based on stakeholder outreach conducted in 2020-21, there is a widespread awareness that:

- (a) the gap between discount rates leads to up-front loss recognition;
- (b) changes in discount rates lead to volatility; and
- (c) some stakeholders find the up-front loss recognition and volatility potentially misleading.

BC301 The Boards noted some stakeholders consider that long-run investment rates of return should be applied to discount cash flows in measuring liabilities for incurred claims, which may generally remove the up-front loss recognition and mitigate the volatility in liabilities for incurred claims.

BC302 The Boards considered whether there might be a need for public sector-specific guidance or modifications in respect of the discount rate requirements in AASB 17/PBE IFRS 17 (such as in AASB 17/PBE IFRS 17.36 and 56) on the basis that:

- (a) for-profit private sector insurers typically have a profit 'buffer' that (in most cases) avoids the need to recognise an up-front loss relating to the impact of the gap between risk-free and investment rates; and
- (b) the gap between the risk-free and investment rates can be larger for public sector entities relative to their regulated private sector counterparts. This is because regulated private sector insurers typically hold investments with an overall lower risk/return profile than their public sector counterparts, which do not face the same regulatory disincentives to investing in higher risk/return asset classes.

Rates in Other Standards

BC303 The Boards noted that some Australian public sector entities have arrangements that give rise to claims settled over long periods and these arrangements are currently accounted for as provisions by applying AASB 137. They noted that discount rates required for measuring provisions reflect current market assessments of the time value of money and the risks specific to the liability.

BC304 The Boards noted that, based on stakeholder outreach conducted in 2020-21, there are differing views on the rates required by AASB 137/PBE IPSAS 19.

- (a) Some stakeholders interpret the AASB 137/PBE IPSAS 19 requirements as being the same or similar to the discounting requirements in AASB 1023/PBE IFRS 4 and AASB 17/PBE IFRS 17.
- (b) Some stakeholders regard the AASB 137/PBE IPSAS 19 requirements as being different from the discounting requirements in AASB 1023/PBE IFRS 4 and AASB 17/PBE IFRS 17. They see a key potential difference being the focus of AASB 1023/PBE IFRS 4 (and AASB 17/PBE IFRS 17) on an entity perspective because an insurer is expected to fulfil its insurance liabilities. In contrast, they see the focus of AASB 137/PBE IPSAS 19 as being on settlement, which could be with a third party and be measured at more or less than face value.

Presentation

BC305 The Boards observed that:

- (a) under AASB 1023/PBE IFRS 4, both the initial and subsequent impacts of discounting and inflating fulfilment cash flows are presented within the 'underwriting result'; however,
- (b) under AASB 17/PBE IFRS 17:
 - (i) only the initial impacts of discounting fulfilment cash flows are presented within the 'insurance service result';
 - (ii) the impacts of subsequent discount rate changes are presented in 'insurance finance income or expenses', including the impact on insurance liabilities of the unwinding of the discount as time passes and the impact of discount rate changes under AASB 17/PBE IFRS 17.87; and
 - (iii) some of the subsequent impacts of inflation rate changes are presented in 'insurance service result' and others in 'insurance finance income or expenses' under AASB 17.B128/PBE IFRS 17.AG128.

- BC306 The Boards noted that at least some of the volatility currently presented as a part of the underwriting result would be separately presented under AASB 17/PBE IFRS 17 as finance income or expense, which may help facilitate explaining the impacts of changing discount rates to users of the financial statements.
- BC307 The Boards also noted that the distinction between the subsequent impacts of inflation rate changes that are presented in ‘insurance service result’ versus ‘insurance finance income or expenses’ has yet to be clarified in practice, but the issues are the same for both private and public sector entities. Accordingly, the Boards expect that an industry practice will emerge that public sector entities could apply.

Boards’ Position on Discounting and Inflating in AASB ED 319/NZASB ED 2022-3

- BC308 The Boards considered whether there might be a need for public sector-specific modifications to the discount rate requirements of AASB 17/PBE IFRS 17 to address concerns about up-front loss recognition and volatility.
- BC309 The Boards decided that they would not propose any modifications on discounting fulfilment cash flows for the following reasons.
- (a) The same discounting issues which arise for public sector entities also arise for private sector entities, while acknowledging those issues can have a more significant impact for public sector entities.
 - (b) The issues of volatility of liabilities due to discount rate changes from period to period are also a feature of the discount rate requirements in other Standards (such as AASB 119/PBE IPSAS 39 *Employee Benefits*), and that any efforts to address these issues would need to involve a broad-based project that goes beyond a project on insurance arrangements in the public sector.
 - (c) Any project on discount rates might involve a broader consideration of measurement issues more generally.
- BC310 Specifically in relation to the possible application of long-run investment returns as the basis for discount rates, the Boards noted that, conventionally, assets and liabilities are measured independently. That is, for example, the measurement of a liability is based on the liability’s inherent characteristics, not on the characteristics of any assets that might be available to settle the liability. Accordingly, the Boards concluded that any consideration of overturning long-standing conventions of this nature would need to involve a review of principles that go beyond a project on insurance arrangements in the public sector.

Discounting and Inflating – AASB ED 319/NZASB ED 2022-3 Feedback and Boards’ Conclusion

- BC311 There was no specific feedback from respondents to AASB ED 319/NZASB ED 2022-3 on discounting and inflating. The Boards concluded that it is not appropriate to have public sector modifications on discounting and/or inflating fulfilment cash flows in the context of AASB 17/PBE IFRS 17.

Measurement of Investments Backing Insurance Liabilities

- BC312 When it is feasible under Accounting Standards to measure an investment that backs insurance liabilities at fair value through profit or loss, AASB 1023/PBE IFRS 4 requires an entity to apply fair value through profit or loss accounting. This includes applying accounting policy choices/designations within Accounting Standards to use fair value through profit or loss accounting for: financial instruments; investment property; and, in relation to separate financial statements, investments in subsidiaries, joint ventures and associates.
- BC313 The Boards acknowledged that the AASB 1023/PBE IFRS 4 requirements were based on a view that fair value accounting for investments would provide the greatest level of balance sheet and income statement consistency with the measurement of insurance liabilities, which is largely a current value basis.
- BC314 The Boards noted that, unlike AASB 1023/PBE IFRS 4, IFRS 17 is a global Standard, and asset measurement and reporting practices (other than fair value through profit or loss) may emerge within the insurance industry globally, which Australian and New Zealand insurers should be able to follow.
- BC315 The Boards noted that, in stakeholder consultation conducted for this project in 2020-21, the following themes emerged.

- (a) Most public sector entities do not determine their own accounting policies, particularly in relation to policies for transactions that are common across the public sector – those policies are determined by the Treasury office of their jurisdiction.
- (b) The established practice is to apply fair value through profit or loss accounting to assets when feasible and this shows no sign of changing.
- (c) Many public sector entity investments are managed separately by a specialist public sector funds management entity. Those funds management entities ordinarily hold assets for trading and apply fair value through profit or loss accounting. Most funds management entities typically only supply fair value information to their unitholders.

Boards' Position on Measurement of Investments Backing Insurance Liabilities in AASB ED 319/NZASB ED 2022-3

BC316 The Boards considered that:

- (a) in practical terms, there are strong existing incentives for public sector entities to apply fair value through profit or loss accounting;
- (b) in broad terms, the general application of fair value through profit or loss accounting to investments backing insurance liabilities is probably the most useful approach to meet the needs of public sector users of the financial statements; and
- (c) all the relevant public sector entities are likely to voluntarily continue applying fair value through profit or loss accounting.

BC317 The Boards decided that they would not propose carrying forward into AASB 17/PBE IFRS 17 the modifications on investment measurement from AASB 1023/PBE IFRS 4 for public sector entities.

Measurement of Investments Backing Insurance Liabilities – AASB ED 319/NZASB ED 2022-3 Feedback and Boards' Conclusion

BC318 There was no specific feedback from respondents to AASB ED 319/NZASB ED 2022-3 on measurement of investments backing insurance liabilities. The Boards concluded that it is not appropriate to have public sector modifications on the measurement of investments backing insurance liabilities in the context of AASB 17/PBE IFRS 17.

BC319 The Boards noted informal feedback suggesting public sector entities with arrangements that might fall within the scope of AASB 17/PBE IFRS 17 would typically be applying a fair value through profit or loss approach to recognise and measure investments, when available under the Accounting Standards. In many cases, this is due to the government-wide accounting policy framework and/or because many entities have their investments in the custody of central agencies that only provide information for financial reporting purposes on a fair value through profit or loss basis.

Risk Mitigation Program and Other Similar Costs

BC320 The Boards noted that most entities that conduct insurance business undertake risk mitigation activities, which are not directly related to particular insurance arrangements. They could include, for example:

- (a) risk assessments of a customer's premises that are to be insured; and/or
- (b) education programs among policyholders regarding safe work practices.

BC321 The Boards observed that, for private sector for-profit insurers, these activities would be expected to typically be closely associated with underwriting or claims management and to be attributable to particular contracts or groups of contracts.

BC322 The Boards also observed that the same types of activities are conducted by public sector entities; however, they would often have a broader community focus, including for example:

- (a) road safety campaigns;
- (b) research into medical practices in public hospitals; and/or
- (c) research into rehabilitation techniques to improve return to work experience.

- BC323 The Boards noted that, compared with AASB 1023/PBE IFRS 4, AASB 17/PBE IFRS 17 has more specific requirements around the types of costs that are to be accounted for as a part of insurance contract liabilities and more specific presentation requirements around the income statement line items that make up the ‘insurance service result’. In particular, they noted that costs which might currently be accounted for as a part of the ‘underwriting result’ under AASB 1023/PBE IFRS 4 may not be sufficiently attributable to the fulfilment of particular groups of contracts to be accounted for within the ‘insurance service result’ under AASB 17/PBE IFRS 17.
- BC324 This led the Boards to consider whether there is a need for public-sector-specific modifications in respect of costs associated with risk mitigation activities that might not be attributable to particular groups of contracts. This is particularly since these costs may be more significant in a public sector context (compared with private sector for-profit entities).
- BC325 The Boards noted the following feedback received from stakeholder outreach conducted in 2020-21.
- (a) Some public sector entities that provide risk coverage for policyholders also have a separate (sometimes legislated) objective of educating communities about safety or investing in infrastructure that promotes safe outcomes.
 - (b) Public sector entities are typically separately accountable for costs associated with risk mitigation and they are usually readily identifiable.

Boards’ Position on Risk Mitigation Program and Other Similar Costs in AASB ED 319/NZASB ED 2022

- BC326 Based on the above considerations, the Boards decided that there is no need to propose any public sector modifications in respect of risk mitigation program and other similar costs.
- BC327 The Boards considered that:
- (a) public sector entities would have little difficulty identifying risk mitigation program costs and classifying them in accordance with AASB 17/PBE IFRS 17; and
 - (b) presenting these costs separately from the insurance service result would be useful in a public sector context since they usually relate to a separate and identifiable organisational objective.

Risk Mitigation Program and Other Similar Costs – AASB ED 319/NZASB ED 2022-3 Feedback and Boards’ Conclusion

- BC328 There was no specific feedback from respondents to AASB ED 319/NZASB ED 2022-3 on risk mitigation program and other similar costs. The Boards concluded that it is not appropriate to have public sector modifications on the classification or presentation of risk mitigation program and other similar costs in the context of AASB 17/PBE IFRS 17.

Other Matters Raised in Feedback on AASB ED 319/NZASB ED 2022-3

- BC329 Respondents to AASB ED 319/NZASB ED 2022-3, either in their formal submissions, or in follow-up discussions, raised the following matters:
- (a) accounting for insurance contracts that provide adverse development coverage; and
 - (b) accounting for non-distinct investment components.

Adverse Development Coverage

- BC330 In respect of insurance contracts that provide adverse development coverage, the Boards noted that the coverage period relates to the time over which the amount of claims is expected to remain uncertain, which would often be up to the time of settlement, which is potentially a long period. Accordingly, the insurer would recognise any compensation received or receivable for accepting adverse development risk over that potentially long coverage period and may never recognise a liability for incurred claims, even though the liability is managed as a claims liability. The Boards considered whether public sector entities, in particular, might have insurance contracts that provide adverse development coverage and whether there are any public sector specific reasons for modifying AASB 17/PBE IFRS 17 in accounting for such coverage.
- BC331 The Boards concluded that there is no need for public sector modifications in respect of adverse development coverage on the basis that:

- (a) while a public sector entity might have contracts providing adverse development coverage that, for example, might arise from a government restructuring of administrative arrangements, that form of coverage is not expected to be common in the public sector and possibly less common than in the private sector;
- (b) while there may be concerns that the accounting does not reflect the manner in which the contracts are managed, the same issues arise in the private sector; and
- (c) the potentially long coverage period would not affect eligibility for applying the premium allocation approach given that the Boards concluded public sector entities would have an accounting policy choice to apply that approach.

BC332 However, the Boards also noted that the transition provision in AASB 17.C9A/PBE IFRS 17. 132.9A applies to an entity using a modified transition approach in accordance with AASB 17.C8/PBE IFRS 17.132.8 and involves classifying as a liability for incurred claims a liability for settlement of claims incurred before an insurance contract was acquired in a transfer of insurance contracts. Such a transfer may not form a business or may be in a business combination within the scope of AASB 3 *Business Combinations* /PBE IPSAS 40 *PBE Combinations*. The Boards observed that there is an additional dimension to such transfers in a public sector context because some liabilities acquired by public sector entities in their claims settlement stage are being accounted for under AASB 137/PBE IPSAS 19. The existing AASB 17/PBE IFRS 17 transition provision requires the continued use of claims liability accounting under AASB 17/PBE IFRS 17, but would not enable the continued use of AASB 137/PBE IPSAS 19.

BC333 Given that the arrangements concerned are in their settlement phase, the Boards considered that any benefit to users of a public sector entity changing its accounting to apply AASB 17/PBE IFRS 17 rather than AASB 137/PBE IPSAS 19 in the event that the relevant arrangement was within the scope of AASB 17/PBE IFRS 17³⁴ would be likely to be outweighed by the costs. Accordingly, the Boards concluded that, on transition to AASB 17/PBE IFRS 17, in respect of an arrangement that constitutes a liability for settlement of claims incurred before the liability was acquired in a transfer, a public sector entity would be required to:

- (a) classify the liability as a liability for incurred claims and apply AASB 17/PBE IFRS 17 when the entity has previously asserted explicitly that it regards the liability as an insurance liability; and
- (b) classify the liability as a provision and apply AASB 137/PBE IPSAS 19 when the entity has not previously asserted explicitly that it regards the liability as an insurance liability.

The Boards noted that supportive feedback was received for the above transition provision, which was included in the Draft Standard of the amendments to AASB 17/PBE IFRS 17 (and, in the case of the AASB only, AASB 1050 *Administered Items*) issued in October 2022 for fatal flaw comment.

Non-distinct Investment Components

BC334 The Boards noted that non-distinct investment components arise when, in all circumstances, there is a return of premium/levies from the insurer to the policyholder and that this can arise, for example, when the final amount of premiums/levies depends on the extent of claims. They noted that this sometimes arises for Workers' Compensation insurance, which is conducted by both private and public sector entities. The Boards considered whether there are any public sector specific reasons for modifying AASB 17/PBE IFRS 17 in accounting for non-distinct investment components.

BC335 The Boards concluded that there is no need for public sector modifications in respect of non-distinct investment components on the basis that:

- (a) the nature of the non-distinct investment components that arise in the public sector appear to be no different from those that arise in the private sector; and
- (b) based on informal consultation with key stakeholders, the incidence of non-distinct investment components in the public sector is no more prevalent, and possibly less prevalent, than in the private sector.

³⁴ Although there would be no current coverage, a past coverage period may be determinable in some cases.

Summary of Project History 2017 to 2020

AASB

BC336 The table below outlines a brief history of the AASB's project between 2017–2020.

<i>Time</i>	<i>Milestone</i>	<i>Remarks</i>
July 2017	AASB makes AASB 17 Insurance Contracts , which incorporates IFRS 17 <i>Insurance Contracts</i> (May 2017) applicable to annual reporting periods beginning on or after 2021	The AASB was aware of key concerns from the NFP public sector in particular that need further consideration before a decision is made about whether those entities should be subject to AASB 17 without amendment. Chiefly among those concerns was AASB 17 applicability to statutory obligations such as Medicare, the National Disability Insurance Scheme or worker's compensation insurance. The AASB acknowledged those concerns and decided to temporarily exclude NFP public sector entities from the scope of AASB 17 pending the outcome of its separate project to address these issues. Until such time as the NFP public sector issues are addressed, those affected entities continue to be subject to AASB 4, AASB 1023 and AASB 1038 (and, potentially, Interpretation 1047).
Nov 2017	Discussion Paper Australian-specific Insurance Issues – Regulatory Disclosures and Public Sector Entities	For comment by 28 February 2018 The DP notes in the introduction: The AASB's view is that although AASB 17 applies only to contracts, the <i>Framework for the Preparation and Presentation of Financial Statements</i> (Conceptual Framework) does not limit liability recognition to that arising from contracts, and specifically indicates that obligations may arise from statute. In applying its principle of transaction neutrality, the AASB considers that public sector entities with insurance risk created by statute, that are in substance similar to public and private sector entities with insurance risk created by contracts, should account for insurance risk in the same way. The DP specifically sought feedback on: • applying AASB 17 to 'insurance-like' arrangements in the public sector • applying the requirements for a risk adjustment (to insurance liabilities) • determining the contract boundary • captive insurance arrangements
Sep 2018	AASB considers a summary of constituent feedback on the Discussion Paper	The minutes record the AASB decided to: - conduct further field testing of the 'insurance-like' criteria - based on the field testing, consider whether clarifications of the 'insurance-like' criteria are required, particularly the 'funding' criteria - consider the assumptions used in determining discount rates for public sector entities - consider the assumptions used in determining risk margins for public sector entities. Six formal responses to the DP were received (including from HoTARAC and ACAG).

<i>Time</i>	<i>Milestone</i>	<i>Remarks</i>
Jun 2019	Exposure Draft of proposed amendments to AASB 17	AASB ED 292 incorporated amendments to IFRS 17 proposed by the IASB. For comment to AASB by 30 August 2019 and to the IASB by 25 September 2019
Jul 2020	AASB makes AASB 2020-5 Amendments to Australian Accounting Standards – Insurance Contracts	AASB 2020-5 amends AASB 17 to be in line with an amended IFRS 17 issued by the IASB in June 2020. Key amendments to AASB 17 and IFRS 17 are: • a revised mandatory application date of annual reporting periods beginning on or after 1 January 2023 • requiring separate presentation of insurance assets and liabilities by ‘portfolio’ rather than ‘group of contracts’ • permitting the recognition of a separate acquisition costs asset in particular circumstances • recognising reinsurance contract held gains relating to onerous underlying contract losses in particular circumstances • entities preparing interim financial statements can choose to apply the ‘year-to-date’ measurement principle in AASB 134 / IAS 34 <i>Interim Financial Reporting</i>

NZASB

BC337 The table below outlines a brief history of the NZASB’s project between 2017–2020.

<i>Time</i>	<i>Milestone</i>	<i>Remarks</i>
Aug 2017	NZASB issues NZ IFRS 17 Insurance Contracts , which incorporates IFRS 17 <i>Insurance Contracts</i> (May 2017) applicable to annual reporting periods beginning on or after 2021	NZ IFRS 17 applies only to for-profit entities.
Feb 2018	NZASB agrees to develop a PBE Standard based on IFRS 17	
Dec 2018	NZASB ED 2018-7 PBE IFRS 17 Insurance Contracts	For comment by 17 May 2019 NZASB ED 2018-7 proposed amending the scope of PBE IFRS 17 to capture schemes that are eligible to apply the insurance approach under IPSAS 42 <i>Social Benefits</i> (i.e. intended to be fully funded from contributions and levies; and there is evidence the entity manages the scheme in the same way as an issuer of insurance contracts, including assessing the financial performance and financial position of the arrangement on a regular basis). NZASB ED 2018-7 sought feedback on • appropriateness of a risk adjustment for certain PBEs

<i>Time</i>	<i>Milestone</i>	<i>Remarks</i>
		• whether the ‘contract boundary’ is clear for entities funded through levies • whether ‘portfolios’ and ‘onerous contract groups’ are appropriate for PBEs • relevant discount rates for PBEs.
June 2019	NZASB considers constituent feedback on NZASB ED 2018-7	Six formal responses to the ED were received. The Board: (a) NOTED the feedback received on NZASB ED 2018-7 PBE IFRS 17 <i>Insurance Contracts</i>; and (b) AGREED to: (i) add a public sector-specific PBE insurance project to its workplan to consider the public sector-specific issues raised by respondents; and (ii) proceed to issue PBE IFRS 17 <i>Insurance Contracts</i> with a proposed scope modification to limit its application to Tier 1 and Tier 2 not-for-profit PBEs.
Aug 2019	NZASB ED 2019-3 Proposed amendments to PBE IFRS 17	NZASB ED 2019-3 proposed to incorporate into PBE IFRS 17 the amendments to IFRS 17 proposed by the IASB in June 2019. Comments were due to the NZASB by 19 November 2019.
Aug 2020	NZASB issues Amendments to NZ IFRS 17 and Amendments to PBE IFRS 17	Key amendments to NZ IFRS 17, PBE IFRS 17 and IFRS 17 are: • a revised mandatory application date of annual reporting periods beginning on or after 1 January 2023 • requiring separate presentation of insurance assets and liabilities by ‘portfolio’ rather than ‘group of contracts’ • permitting the recognition of a separate acquisition costs asset in particular circumstances • recognising reinsurance contract held gains relating to onerous underlying contract losses in particular circumstances • entities preparing interim financial statements can choose to apply the ‘year-to-date’ measurement principle in AASB 134/IAS 34 <i>Interim Financial Reporting</i>

History of Amendments

PBE IFRS 17 *Insurance Contracts* was issued in July 2019.

This table lists the pronouncements establishing and substantially amending PBE IFRS 17. The table is based on amendments issued as at 22 June 2023.

Pronouncements	Date issued	Early operative date	Mandatory date (annual reporting periods... on or after ...)
PBE IFRS 17 <i>Insurance Contracts</i>	July 2019	Early application is permitted	1 Jan 2022 ³⁵
<i>Amendments to PBE IFRS 17</i>	Aug 2020	Early application is permitted as long as PBE IPSAS 41 has been applied on or before the date of initial application of PBE IFRS 17	1 Jan 2023
<i>Initial Application of PBE IFRS 17 and PBE IPSAS 41—Comparative Information</i>	June 2022	Early application is permitted	1 Jan 2023
<i>Insurance Contracts in the Public Sector</i>	June 2023	Application to an earlier accounting period is permitted for accounting periods that end after this Standard takes effect.	1 Jan 2026

Table of Amended Paragraphs in PBE IFRS 17		
Paragraph affected	How affected	By ... [date]
Paragraph 2.1	Added	<i>Insurance Contracts in the Public Sector</i> [Jun 23]
Paragraph 2.2	Amended and renumbered (originally numbered as paragraph 2.1)	<i>Insurance Contracts in the Public Sector</i> [Jun 23]
Paragraph 4	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 5	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraphs 6.1-6.2	Added	<i>Insurance Contracts in the Public Sector</i> [Jun 23]
Paragraph 7	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 8A	Added	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 10	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 11	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 12	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]

³⁵ *Amendments to PBE IFRS 17*, issued in August 2020, subsequently deferred the mandatory date to 1 January 2023.

Table of Amended Paragraphs in PBE IFRS 17		
Paragraph affected	How affected	By ... [date]
Paragraph 13.1: definition of contractual service margin	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 13.1: definition of coverage period	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 13.1: definition of group of insurance contracts	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 13.1: definition of insurance acquisition cash flows	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 13.1: definition of insurance contract services	Added	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 13.1: definition of investment component	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 13.1: definition of liability for incurred claims	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 13.1: definition of liability for remaining coverage	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 14.1	Added	<i>Insurance Contracts in the Public Sector</i> [Jun 23]
Paragraph 16.1	Added	<i>Insurance Contracts in the Public Sector</i> [Jun 23]
Paragraph 19	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 22.1	Added	<i>Insurance Contracts in the Public Sector</i> [Jun 23]
Paragraph 24	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 25.1	Added	<i>Insurance Contracts in the Public Sector</i> [Jun 23]
Paragraph 27	Deleted	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 28	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraphs 28A–28F and preceding heading	Added	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 29 and preceding heading	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Heading preceding paragraph 32	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 34	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraphs 34.1–34.4	Added	<i>Insurance Contracts in the Public Sector</i> [Jun 23]
Paragraph 38	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 39	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 44 and preceding heading	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 45	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]

Table of Amended Paragraphs in PBE IFRS 17		
Paragraph affected	How affected	By ... [date]
Paragraph 47	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 48	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 50	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 53	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 53.1	Added	<i>Insurance Contracts in the Public Sector</i> [Jun 23]
Paragraph 55	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 56	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 60	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 62	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 62A	Added	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 65	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 65A	Added	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 66	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 66A	Added	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 66B	Added	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 69	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 69.1	Added	<i>Insurance Contracts in the Public Sector</i> [Jun 23]
Paragraph 70A	Added	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 71	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 72	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 76	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 78	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 79	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 83	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 86	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 87A	Added	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 88	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 89	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 97	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 99	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 100	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 101	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 103	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 104	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 105	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 105A	Added	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 105B	Added	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 106	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 107	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]

Table of Amended Paragraphs in PBE IFRS 17		
Paragraph affected	How affected	By ... [date]
Paragraph 108	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 109	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 109A	Added	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 114	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 117	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 128	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 132	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 132.1	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 132.2A	Added	<i>Initial Application of PBE IFRS 17 and PBE IPSAS 41—Comparative Information</i> [June 2022]
Paragraphs 132.2B.1-132.2B.6	Added	<i>Insurance Contracts in the Public Sector</i> [Jun 23]
Paragraph 132.3	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 132.4	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 132.5	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 132.5A	Added	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 132.5A.1	Added	<i>Insurance Contracts in the Public Sector</i> [Jun 23]
Paragraph 132.5B	Added	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 132.7	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 132.8	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 132.9	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 132.9A	Added	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 132.11	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 132.14A–132.14D	Added	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 132.15	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 132.16	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 132.16A–132.16C	Added	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 132.17	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 132.17A	Added	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 132.19A	Added	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 132.20A–132.20B	Added	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 132.21	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 132.22A	Added	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 132.24A–132.24B and preceding heading	Added	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 132.28A–132.28E and preceding heading	Added	<i>Initial Application of PBE IFRS 17 and PBE IPSAS 41—Comparative Information</i> [June 2022]

Table of Amended Paragraphs in PBE IFRS 17		
Paragraph affected	How affected	By ... [date]
Paragraph 132.31	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph 132.33A	Added	<i>Initial Application of PBE IFRS 17 and PBE IPSAS 41—Comparative Information</i> [June 2022]
Paragraph AG1	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph AG5	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph AG12	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph AG33 and preceding heading	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph AG34	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph AG35	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraphs AG35A–AG35D and preceding heading	Added	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph AG64	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph AG64.1	Added	<i>Insurance Contracts in the Public Sector</i> [Jun 23]
Paragraph AG65	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph AG66	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph AG66A	Added	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph AG71	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph AG72	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph AG93	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph AG94	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph AG95	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraphs AG95A–AG95D	Added	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraphs AG95E–AG95F and the preceding heading	Added	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph AG96	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph AG97	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph AG104	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph AG107	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph AG112	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph AG115	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph AG116	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph AG117A	Added	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph AG118	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph AG119	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph AG119A	Added	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph AG119B	Added	<i>Amendments to PBE IFRS 17</i> [Aug 2020]

Table of Amended Paragraphs in PBE IFRS 17		
Paragraph affected	How affected	By ... [date]
Paragraphs AG119C–AG119F and preceding heading	Added	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph AG121	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph AG121.1	Added	<i>Insurance Contracts in the Public Sector</i> [Jun 23]
Paragraph AG123	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph AG123A	Added	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph AG124	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph AG126	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph AG128	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph AG134	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]
Paragraph AG137 and preceding heading	Amended	<i>Amendments to PBE IFRS 17</i> [Aug 2020]