

Recognising the contractual service margin in profit or loss

Basic overview

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IFRS 17 webcasts

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This webcast

March 2018 Recognising the contractual service margin in profit or loss

Previous webcasts

May 2017 Introducing IFRS 17
May 2017 Understanding IFRS 17
June 2017 Core requirements: scope of IFRS 17
July 2017 Core requirements: measurement essentials of IFRS 17
August 2017 Simplified accounting for contracts with short coverage periods
September 2017 Reinsurance contracts held
November 2017 Core requirements: Recognition and derecognition
December 2017 Transition to IFRS 17
January 2018 Level of aggregation



Further information:

go.ifrs.org/IFRS-17-implementation and
IFRS 17 webcasts YouTube playlist:

<https://www.youtube.com/playlist?list=PLrLeeuMbuaUeLNX7Qoqlq7Oh3csegFwYn>

Basic overview

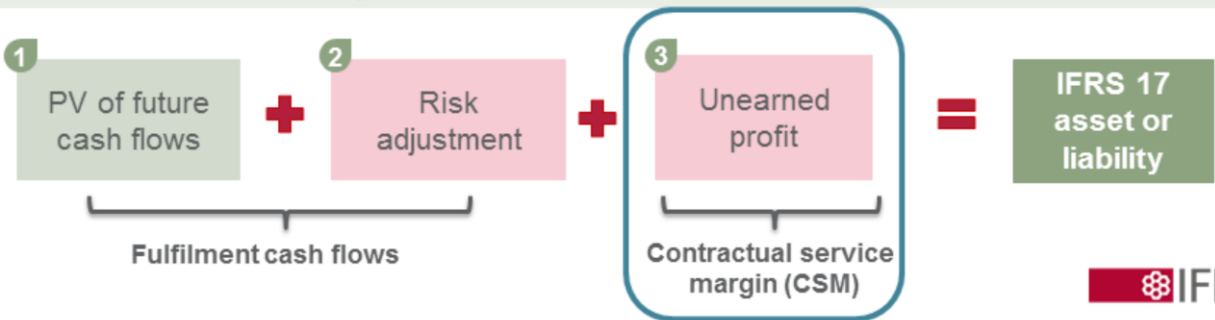
- The objective of the allocation of the contractual service margin
- Allocating the contractual service margin
- Other topics
 - Considering the time value of money when allocating the contractual service margin (CSM)

The objective of the allocation of the contractual service margin

Reminder: IFRS 17 core requirements

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



Further information:

IFRS 17 paragraph 32

IFRS 17 Appendix A definitions:

- Contractual service margin
- Risk adjustment for non-financial risk
- Fulfilment cash flows
- Financial risk

Basis for Conclusions on IFRS 17 paragraphs BC16-BC21

Webcast *Core requirements: measurement essentials of IFRS 17*

at go.ifrs.org/IFRS-17-implementation and IFRS 17 youtube playlist:

https://www.youtube.com/playlist?list=PLrLeeuMbuUeLNX7Qoqlq7Oh_3csegFwYn

Reminder: Insurance service result = CSM + risk adjustment

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Statement of profit or loss
Insurance revenue
Incurred claims and expenses
Insurance service result
Investment income
Insurance finance expenses
Net financial result
Profit or loss

CSM

- Reflects service provided during current period
- Systematic allocation to P&L

Risk adjustment

- Reflects the bearing of risk during the current period for liability for remaining overage and liability for incurred claims
- Explicitly measured



Further information:

IFRS 17 paragraphs 83-85 and B120-B124

Basis for Conclusions on IFRS 17 paragraphs BC35-BC37, BC222-BC223 and BC279(a)

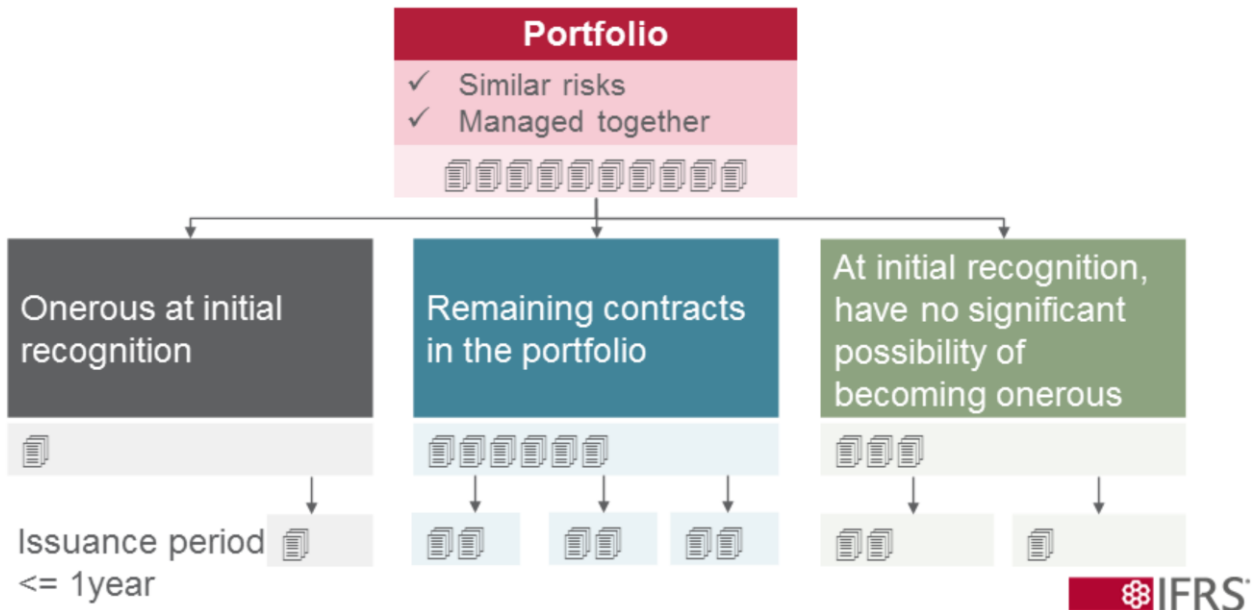
Webcast *Core requirements: measurement essentials of IFRS 17*

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Reminder: Grouping of insurance contracts

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Further information:

IFRS 17 paragraphs 14-24

Basis for Conclusions on IFRS 17 paragraphs BC115-BC139

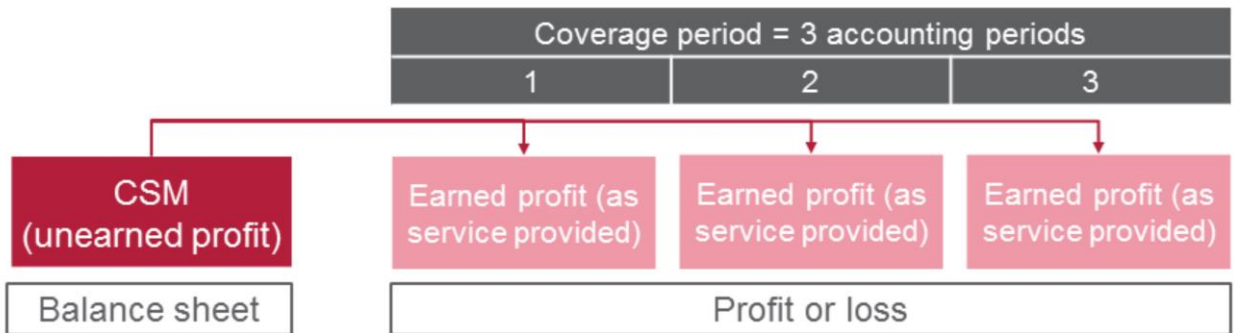
Webcast IFRS 17 *Level of Aggregation (Part 1)* at [go.ifrs.org/IFRS-17-implementation](https://www.ifrs.org/IFRS-17-implementation) and IFRS 17 YouTube playlist

<https://www.youtube.com/playlist?list=PLrLeeuMbuUeLNX7Qoqlq7Oh3csegFwYn>

Allocation of profit for a group of contracts

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- Grouping contracts means profit is not identified with each individual contract
- Coverage units provides basis for systematic allocation of unearned profit of a group to each period that represents service provided



Further information:

IFRS 17 paragraphs 43, 44(e), 45(e) and B119

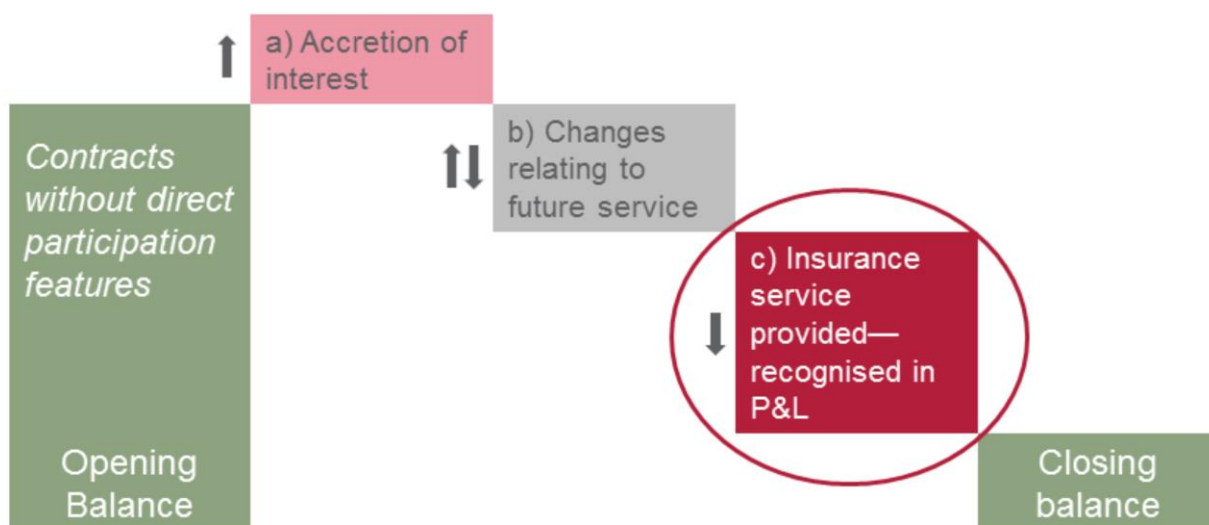
Basis for Conclusions on IFRS 17 paragraphs BC118, BC120 and BC279 – BC283

Allocating the contractual service margin

Reminder: Contractual Service Margin

Subsequent measurement

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For simplicity, foreign currency differences and adjustments relating to contracts joining the group are not illustrated



Further information:

IFRS 17 paragraphs 43-44 and B96-B100

Basis for Conclusions on IFRS 17 paragraphs BC22-BC24 and BC220-BC224

Webcast *Core requirements: measurement essentials of IFRS 17*

at go.ifrs.org/IFRS-17-implementation and IFRS 17 youtube playlist:

https://www.youtube.com/playlist?list=PLrLeeuMbuaUeLNX7Qoqlq7Oh_3csegFwYn

Recognising CSM in profit or loss

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- An amount of CSM for a group of insurance contracts is recognised in profit or loss (P/L) in each accounting period:
 1. **Determine** the amount of the CSM to be allocated
 2. **Recognise** the amount of CSM in P/L determined by allocation
 - Identify number of coverage units over the current and expected remaining coverage period
 - Allocate the CSM balance equally to each coverage unit
 - Recognise in P/L the amount of CSM allocated to coverage units provided in that period



Further information:

IFRS 17 paragraphs 44(e), 45(e) and B119

Basis for Conclusions of IFRS 17 paragraphs BC220, BC221 and BC279-BC283

Identify the number of coverage units

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- The total number of coverage units of a group is the quantity of coverage provided by contracts in the group over the expected coverage period
- Coverage units are determined based on*:
 - a) quantity of benefits provided by contracts in the group
 - b) expected coverage duration of contracts in the group
 - c) likelihood of insured events occurring only *to extent that they affect expected duration of contracts in the group*

* discussed at February 2018 meeting of the TRG for IFRS 17



Further information:

IFRS 17 paragraph B119

Basis for Conclusions on IFRS 17 paragraphs BC279, BC282 and BC283

Discussed at the February 2018 meeting of the Transition Resource Group on IFRS 17 *Insurance Contracts* - Agenda Paper 5 <http://www.ifrs.org/groups/transition-resource-group-for-insurance-contracts/#meetings>

- Coverage units are assessed
 - at each reporting period
 - prospectively
- Accordingly, an entity shall assess for contracts in the group:
 - expected coverage duration
 - quantity of benefit provided
- During the period, coverage units may be impacted by:
 - new contracts joining the group
 - derecognised contracts

Further information:

IFRS 17 paragraph B119

Basis for Conclusions on IFRS 17 paragraph BC279

Webcast IFRS 17 *Core requirements: Recognition and derecognition* at

go.ifrs.org/IFRS-17-implementation and IFRS 17 youtube playlist:

<https://www.youtube.com/playlist?list=PLrLeeuMbuaUeLNX7Qoqlq7Oh3csegFwYn>

Discussed at the February 2018 meeting of the Transition Resource Group on IFRS 17 *Insurance Contracts* - Agenda Paper 5 <http://www.ifrs.org/groups/transition-resource-group-for-insurance-contracts/#meetings>

Simplified base example

- Recognition at the end of period 1
 - A group with expected duration of 3 coverage periods
 - Identical quantity of benefit in each period
 - Day 1 CSM of CU150

	Period 1	Period 2	Period 3
Coverage units	10	10	10
CSM in P/L	CU50		
CSM in B/S	CU150	CU100	

- 10/30 (current/(current + remaining) coverage units)
- Recognise 1/3 x CU150 CSM in profit or loss



Assumptions: interest is accreted on the CSM at 0% and no changes occur

Further information:

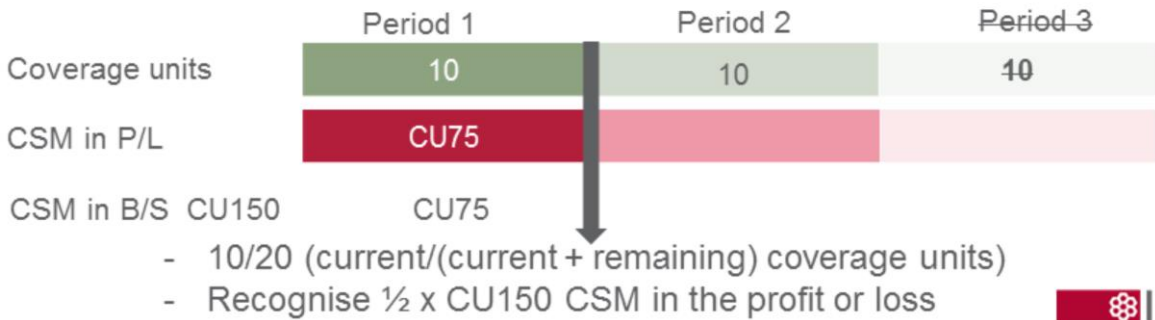
IFRS 17 paragraph B119

Basis for Conclusions on IFRS 17 paragraphs BC279, BC282 and BC283

Example – decrease in coverage duration

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- Recognition at the end of period 1
 - Same scenario as basic example (slide 14), except that in period 1 coverage is expected to end earlier than originally expected (at the end of period 2 instead of period 3)
 - No other changes (eg quantity of benefit of CSM)



Assumption: interest is accreted on the CSM at 0% and there are no adjustments for CSM

Further information:

IFRS 17 paragraph B119

Basis for Conclusions on IFRS 17 paragraphs BC279, BC282 and BC283

Example – increase in coverage duration

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- Recognition at the end of period 3
 - Same scenario as base example (slide 13), expect that in period 3 it becomes known that expected coverage will continue longer than originally expected (for 4 periods)
 - No other changes (eg quantity of benefit of CSM)

	Period 1	Period 2	Period 3	Period 4
Coverage units	10	10	10	10
CSM in P/L	CU50	CU50	CU25	
CSM in B/S CU150	CU100	CU50	CU25	

- 10/20 (current/(current + remaining) coverage units)
 - Recognise 1/2 X CU50 CSM in the profit or loss



Assumption: interest is accreted on the CSM at 0% and there are no adjustments for CSM

Further information:

IFRS 17 paragraph B119

Basis for Conclusions on IFRS 17 paragraphs BC279, BC282 and BC283

Other topics

Coverage units

Considering time value of money when allocating the CSM

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- IFRS 17 does not specify whether to reflect the timing of the expected provision of coverage in determining the equal allocation of the CSM to the coverage units provided
 - Entity's judgement
- This does not affect the CSM determined at initial recognition of a group of contracts



Further information:

IFRS 17 paragraphs 44(e), 45(e) and B119

Basis for Conclusions on IFRS 17 paragraph BC282

Considering time value of money when allocating the CSM

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Without reflecting the timing of coverage

Nominal coverage units provided in current period
divided by

Nominal coverage units provided in the current period + remaining expected duration

Reflecting the timing of coverage*

Present value coverage units provided in current period
divided by

Present value of coverage units provided in current period + remaining expected duration

*See Appendix for a simplified example



Further information:

IFRS 17 paragraphs 44(e), 45(e) and B119

Basis for Conclusions on IFRS 17 paragraph BC282

Keep up to date



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Appendix A

Example - time value of money when allocating the CSM

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- Fact sheet:
 - Day 1 CSM of CU500
 - Discount rate of 10%
 - Expected coverage duration of 5 periods
 - Identical coverage units provided in each period
 - Assume no changes



Further information:

IFRS 17 paragraphs 44(e), 45(e) and B119

Basis for Conclusions on IFRS 17 paragraph BC282

Appendix A

Allocation without reflecting the timing of coverage

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CSM \ Period *	1	2	3	4	5
Opening Balance	CU500	CU440	CU363	CU266	CU146
Accretion—interest	CU50	CU44	CU36	CU27	CU15
Allocated to P&L	CU110	CU121	CU133	CU146	CU161
Closing balance	CU440	CU363	CU266	CU146	CU0
Nominal					
Coverage units	1	1	1	1	1
Coverage units provided	1	1	1	1	1
Coverage units provided and over remaining periods	5	4	3	2	1
Coverage units allocation	1/5	1/4	1/3	1/2	1/1

* Rounded for presentation



Further information:

IFRS 17 paragraphs 44(e), 45(e) and B119

Basis for Conclusions on IFRS 17 paragraph BC282

Appendix A

Allocation reflecting the timing of coverage

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CSM \ Period *	1	2	3	4	5
Opening Balance	CU500	CU418	CU328	CU229	CU120
Accretion—interest	CU50	CU42	CU33	CU23	CU12
Allocated to P&L	CU132	CU132	CU132	CU132	CU132
Closing balance	CU418	CU328	CU229	CU120	CU0
Nominal coverage units	1	1	1	1	1
PV coverage units provided	1	1	1	1	1
PV coverage units provided and over remaining periods	4.17	3.49	2.74	1.91	1
Coverage units allocation	1/4.17	1/3.49	1/2.74	1/1.91	1/1

*Rounded for presentation

For simplicity, coverage is assumed to be provided at the end of the period



Further information:

IFRS 17 paragraphs 44(e), 45(e) and B119

Basis for Conclusions on IFRS 17 paragraph BC282