



**INSTITUTE OF
CERTIFIED PUBLIC ACCOUNTANTS
OF UGANDA**

IFRS 17 IMPLEMENTATION GUIDANCE

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A large number of dark grey umbrellas are arranged in a grid, receding into the distance. In the center of the foreground, a single bright yellow umbrella stands out. The text "IFRS 17" is printed in white on the yellow umbrella.

IFRS 17

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PURPOSE

This Guidance has been designed to assist accountants in business and industry to comply with the requirements of IFRS 17 *Insurance Contracts*. The Guidance also intends to give practicing accountants an appreciation of the requirements of IFRS 17 and how their clients apply the standard. This Guidance gives an analysis of the requirements around the scope, aggregation, and recognition of insurance contracts, as well as their measurement, modification & derecognition, presentation, and disclosure requirements.

Every effort has been taken to give a general appreciation and pointer to the expected direction when applying the requirements of IFRS 17. A number of illustrations have been incorporated to enable a better appreciation of the concepts within the standard.

DISCLAIMER

This Guidance is persuasive rather than prescriptive. It is not intended to be comprehensive or to deal with all situations that might be encountered, i.e. it is supplementary to but not a substitute for the International Financial Reporting Standards (IFRS) and any other directives that may be developed over time by ICPAU, which should be regarded as the primary source of guidance for accountants. Accountants are encouraged to apply professional judgment in complying with the requirements of IFRS 17.

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ICPAU will not be liable for any reliance placed on the information in this material. Users of this publication are advised to seek independent professional guidance whenever faced with complex matters in applying IFRS 17.

IFRS 17



1.0 INTRODUCTION

1.1 Background

In March 2004 the International Accounting Standards Board (Board) issued IFRS 4 Insurance Contracts, an interim standard which was meant to be in place until the Board completed its project on insurance contracts. IFRS 4 permitted entities to use a wide variety of accounting practices for insurance contracts, reflecting national accounting requirements and variations of those requirements, subject to limited improvements and specified disclosures. Many of such policies resulted in lack of useful financial information and hindered proper understanding of the performance of an entity.

For example, these policies allowed insurance entities to use assumptions that existed when an insurance contract was issued and these weren't subsequently updated even when it later became clear to the entities that some of these assumptions had become outdated. This allowed for recognition of profits at different points which made it difficult to understand how profit was earned from an insurance contract. IFRS 4 allowed for reporting of revenue on cash basis and including deposits collected which was inconsistent with other accounting standards such as IFRS 15.

In May 2017, after over 20 years in development, the Board completed its project on insurance contracts with the issuance of IFRS 17 Insurance Contracts with an effective date of 1 January 2021. The effective date was later extended to 1 January 2023. IFRS 17 is designed to curb the challenges that IFRS 4 brought about. The notable differences between IFRS 4 and IFRS 17 are illustrated in Table 1 below.

IFRS 4—little transparent or useful information	IFRS 17—more transparent and useful information
Information about the value of insurance obligations	
Some companies measure insurance contracts using out-of-date information.	Companies will measure insurance contracts at current value
Some companies do not consider the time value of money when measuring liabilities for claims.	Companies will reflect the time value of money in estimated payments to settle incurred claims.
Some companies measure insurance contracts based on the value of their investment portfolios.	Companies will measure their insurance contracts based only on the obligations created by these contracts.
Information about profitability	
Some companies do not provide consistent information about the sources of profit recognised from insurance contracts.	Companies will provide consistent information about components of current and future profits from insurance contracts.
Many companies provide alternative performance measures—non-GAAP measures—to supplement IFRS 4 information, such as embedded value information.	Companies and users of financial statements will use fewer non-GAAP measures; supplementary information will enable more meaningful comparisons.

Table 1: Summary of differences between IFRS 4 & IFRS 17 (Source: IFRS 17 Fact Sheet available <https://cdn.ifrs.org/-/media/project/insurance-contracts/ifrs-standard/ifrs-17-factsheet.pdf>)

1.2 About IFRS 17

Like all IFRS Standards, IFRS 17 focuses on transactions rather than entities—in this case, specifically on insurance contracts and not insurance entities.

IFRS 17 establishes principles for the recognition, measurement, presentation and disclosure of insurance contracts issued, reinsurance contracts held and investment contracts with discretionary participation features that an entity issues. IFRS 17 combines current measurement of the future cash flows with the recognition of profit over the period that services are provided under the contract; presents insurance service results (including presentation of insurance revenue) separately from insurance finance income or expenses; and requires an entity to make an accounting policy choice of whether to recognise all insurance finance income or expenses in profit or loss or to recognise some of that income or expenses in other comprehensive income.

Under IFRS 17, an insurer measures insurance contracts basing on updated information. The Standard aligns revenue recognition principles of insurance contracts with those that apply to other types of contracts; making it easier to compare financial information of insurance companies with that of other industries and sectors. IFRS 17 requires entities to provide consistent information about the drivers of current and future profits. Using the current value approach to measure insurance contracts, an insurer recognises profit as the insurer delivers/provides a service and is released from risk rather than when it receives the premium. Applying IFRS 17 introduces consistent accounting for all insurance contracts that requires entities to provide updated information about obligations, risks and performance of insurance contracts leading to increased transparency in financial information reported by insurance companies. Detailed note disclosures explain how items like new business issued, experience in the year, cash receipts and payments, and changes in assumptions affected the performance and the carrying amount of insurance contracts both insurers and other industries.

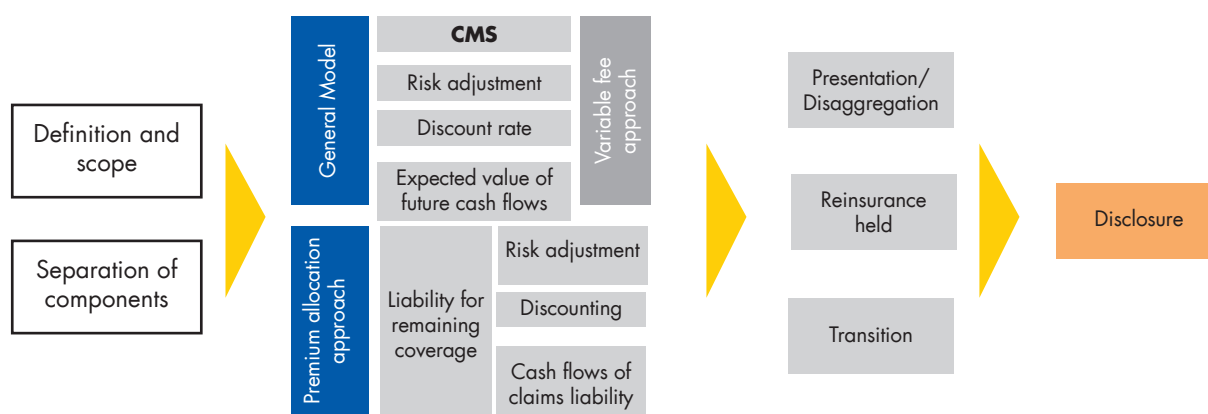


Figure 1 Key principles in IFRS 17

IFRS 17 requires an entity to follow the steps below:

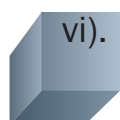
- i). Identify as insurance contracts those contracts under which the entity accepts significant insurance risk from another party (the policyholder) by agreeing to compensate the policyholder if a specified uncertain future event (the insured event) adversely affects the policyholder.
- ii). Separate specified embedded derivatives, distinct investment components and distinct performance obligations from the insurance contracts.
- iii). Divide the contracts into groups that the entity will recognise and measure.
- iv). Recognise and measure groups of insurance contracts at:
 - A risk-adjusted present value of the future cash flows (the fulfilment cash flows) that incorporates all of the available information about the fulfilment cash flows in

a way that is consistent with observable market information; plus (if this value is a liability) or minus (if this value is an asset)

- An amount representing the unearned profit in the group of contracts (the contractual service margin);



▶ Recognise the profit from a group of insurance contracts over the period the entity provides insurance contract services, and as the entity is released from risk. If a group of contracts is or becomes loss-making (onerous), an entity recognises the loss immediately.



▶ Present separately insurance revenue (that excludes the receipt of any investment component), insurance service expenses (that excludes the repayment of any investment components) and insurance finance income or expenses.



▶ Disclose information to enable users of financial statements to assess the effect that contracts within the scope of IFRS 17 have on the financial position, financial performance and cash flows of an entity.

2.0 SCOPE OF IFRS 17

IFRS 17 applies to insurance contracts and reinsurance contracts issued by the entity; reinsurance contracts held by the entity; and Investment contracts with discretionary participation features issued by the entity, provided that the entity also issues insurance contracts,¹ in otherwards provided the entity is an insurer.

2.1 Insurance Contract Definition

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 policyholder².

2.2 Significant Insurance Risk

For an insurance contract to exist, there must be transfer of significant insurance risk from one party to another.

Insurance risk refers to risk, other than financial risk, that is transferred from the holder of a contract to the issuer. Essentially, insurance risk excludes risk which relates to 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 contract³.

Insurance risk is significant if it meets the assessment criteria set out in IFRS 17: B18–B23. In a nutshell, significant insurance risk is that which creates a scenario of commercial substance and a possibility that the issuer is likely to suffer loss caused by the occurrence of an insured event. Additionally, insurance risk may be assessed as significant if the possible payout is likely to be sufficiently great.

Insurance risk includes risk of death, injury, illness/disability, loss of property due to theft/damage, damage of property due to weather conditions, loss while travelling, change in a non-financial variable in a contract.

1 IFRS 17:3
2 IFRS 17: Appendix A
3 IFRS 17: Appendix A

2.1.2 Uncertain Future Event.

To meet the definition of an insurance contract, at least one of the following shall be uncertain at inception of the contract⁴:

- (a) the probability of an insured event occurring;
- (b) when the insured event will occur; or
- (c) how much the insurer will need to pay if the insured event occurs.

Example 1:

As part of its customer assistance programs, ABC Limited repairs specified machine after a malfunction. Would such repairs meet the definition of an insurance contract?

Solution 1:

Yes. The repairs meet the definition of an insurance contract because:

- (i) It is *uncertain* whether or when the repairs will be needed;
- (ii) The customer would be adversely affected by the machine malfunction if it occurred; and
- (iii) ABC Limited would perform the relevant repairs when the malfunction occurs.

2.2 Types of Insurance

Insurance is of two types:

2.2.1 Life insurance

This is insurance that pays out a sum of money either upon the death of the insured or after a set period of time. For example, mortality insurance.

2.2.2 Non-life insurance

This refers to general insurance policies that provide payments depending on the loss from a particular financial event. Examples include travel, property, health, accident, aviation, motor vehicle, among others.

2.3 IFRS 17 Scope Exceptions

Some contracts may meet the definition of an insurance contract but are **not** within the scope of IFRS 17. The following are examples of such contracts:

2.3.1 Warranties

A warranty is a guarantee from a seller that a defective product will be repaired or replaced within a specific time. A warranty that is provided by a manufacturer, dealer or retailer in connection with the sale of its own goods and services is not within the scope of IFRS 17⁵.

4 IFRS 17: B3
5 IFRS 17:7(a)

Examples	Answer	Applicable Standards
(a) An entity is in the business of manufacturing washing machines and selling these along with related warranties through its retail stores. Are such warranties within the scope of IFRS 17?	No.	IFRS 15 IAS 37
(b) A microfinance institution sells a warranty on a vehicle purchased for resale. Is the warranty within the scope of IFRS 17?	Yes.	

2.3.2 Contractual rights or obligations

An entity shall not apply IFRS 17 to contractual rights or contractual obligations that are contingent on the future use of, or the right to use of, a non-financial item.

2.3.3 Other Scope Exceptions

An entity shall not apply IFRS 17 to the following⁶:

S/N	DETAILS	APPLICABLE STANDARD(S)
1.	Assets and liabilities from employee benefit plans and retirement benefit obligations.	IAS 19 IFRS 2 IAS 26
2.	Contingent contractual rights/obligations related to non-financial items.	IFRS 15 IAS 38 IFRS 16
3.	Residual value guarantees*.	IFRS 15 IFRS 16
4.	Contingent consideration payable or receivable in a business combination.	IFRS 3
5.	Insurance contracts in which the entity is the policyholder, unless those contracts are reinsurance contracts** held	IAS 37 IAS 16
6.	Credit card contracts (or similar contracts) that provide insurance coverage and IFRS 9 does not require the insurance component to be separated out.	IFRS 9

* A residual value guarantee refers to a guarantee made to a lessor by a party unrelated to the lessor that the value (or part of the value) of an underlying asset at the end of a lease will be at least a specified amount [IFRS 16: Appendix A].

** Reinsurance contracts are insurance contracts issued by Entity A (the reinsurer) to compensate Entity B for claims arising from one or more insurance contracts (underlying contracts) issued by Entity B [IFRS 17: Appendix A].

2.4 Scope Exclusions

IFRS 17 allows entities the option to account for the following contracts under IFRS 17 or another applicable IFRS:

2.4.1 Financial Guarantee Contracts⁷

This is a contract that requires the issuer to make specified payments to reimburse the holder for a loss the holder incurs in the event that a specified debtor fails to make payment when it falls due.

⁶ IFRS 17:7
⁷ IFRS 17:7(e)

An entity may choose to apply IFRS 17 or IFRS 9, IFRS 7 & IAS 32 to account for financial guarantee contracts. However, if the entity previously asserted explicitly that it regards such contracts as insurance contracts and used accounting applicable to insurance contracts, then IFRS 17 would apply. Such choice may be made on a contract-by-contract basis.

2.4.2 Fixed Fee Service Contracts⁸

This is a contract where the contractor pays a fixed price for the agreed upon work regardless of the ultimate cost to complete the project.

Some insurance contracts may be Fixed Fee Service Contracts. An entity may choose to apply IFRS 15 instead of IFRS 17 to such contracts that it issues if, and only if, the conditions specified in [IFRS 17:8] are met. The entity may make that choice contract by contract, but the choice for each contract is irrevocable.

3.0 SEPARATING COMPONENTS FROM AN INSURANCE CONTRACT

Some types of insurance contracts only provide insurance coverage such as most short-term non-life insurance contracts.

However, some insurance contracts may contain two or more components that would be in the scope of other IFRS standards if they were separate contracts. In this case, IFRS 7 requires an entity to separate the components of the insurance contract in the following order:

Component	Applicable IFRS
(i) Embedded derivatives [IFRS 7:11] An entity applies IFRS 9 to determine whether there is an embedded derivative and how to account for it.	IFRS 9
(ii) Distinct* investment components [IFRS 7:11] Investment components represent amounts that an insurance contract requires the entity to repay to a policyholder even if an insured event does not occur, such as transactions where an entity receives a specified sum from a client and then undertakes to repay that sum with a return such as interest. An investment component shall be separated from the host insurance contract and accounted for in accordance with IFRS 9 if it is <u>distinct</u> , unless it is an Investment contract with discretionary participation features**.	IFRS 9
(iii) Distinct goods and services [IFRS 7:12] For example: pension administration, risk management, asset management and custodial services.	IFRS 15
(iv) Remaining components Includes non-distinct investment components and insurance components.	IFRS 17

* An investment component is distinct if it and the insurance component are not highly interrelated. IFRS 17: B31-B32 provides additional guidance on the term “distinct”.

** IFRS 17 applies to Investment contracts with discretionary participation features (DPF) issued by an entity, provided that the entity also issues insurance contracts [IFRS 17:3]. There is a specific measurement model for these types of contracts known as the variable fee approach.

NOTE:

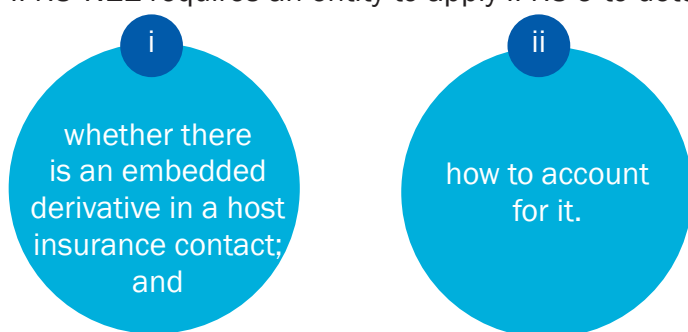
Entities are urged to review and align their current separation policies with the new requirements introduced by IFRS 17: 10-13.

3.1 Embedded derivatives

An embedded derivative is a component of a hybrid contract that includes a non-derivative host. Essentially, the cashflows of the combined instrument vary in a way similar to a stand-alone derivative.

An embedded derivative causes some or all of the cashflows that otherwise would be required by the contract to be modified. This is determined according to a specified interest rate, financial instrument price, commodity price, foreign exchange rate, price or rate index, credit rating or index, or other variable, provided that, in the case of a non-financial variable, the variable is not specific to a party to the contract⁹.

IFRS 7:11 requires an entity to apply IFRS 9 to determine:



An embedded derivative is separated from the host contract if, and only if, all of the criteria below are met¹⁰:

- a. the economic characteristics and risks of the embedded derivative are not closely related¹¹ to the economic characteristics and risks of the host;
- b. a separate instrument with the same terms as the embedded derivative would meet the definition of a derivative within the scope of IFRS 9; and
- c. the hybrid contract is not measured at fair value with changes in fair value recognised in profit or loss (i.e., a derivative that is embedded in a financial liability at fair value through profit or loss is not separated).

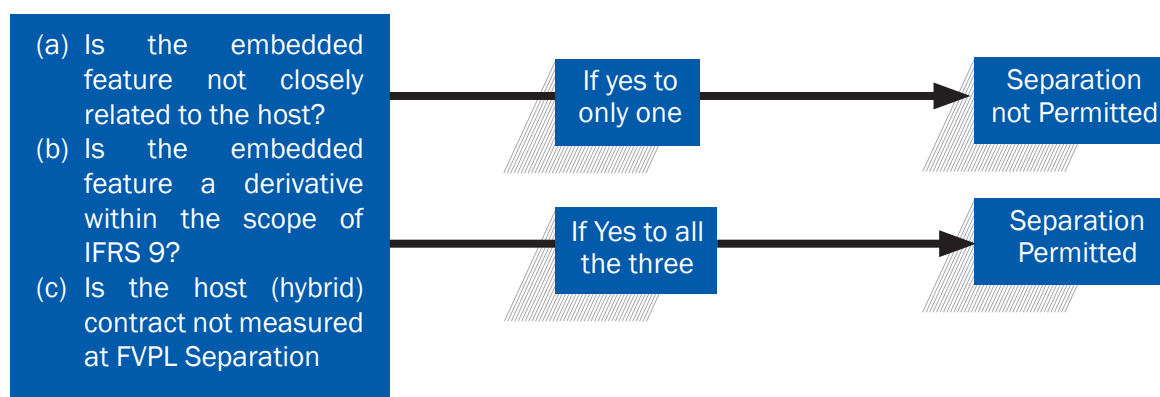


Figure 2 Applying IFRS 17 the separation criteria to embedded derivatives

According to IFRS 9, a derivative that is embedded in an insurance contract relates closely to the host insurance contract if the embedded derivative and host insurance contract are so interdependent that an entity cannot measure the embedded derivative separately (without considering the host contract).¹²

9 IFRS 9.4.3.1

10 IFRS 9.4.3.3

11 Although the term "closely related" is not directly defined in IFRS 9, there are examples that illustrate what is meant and why under Paragraph IFRS 9.B4.3.5 and IFRS 9.B4.3.8

12 IFRS 9.B4.3.8(h)

Examples of embedded derivatives in insurance contracts include interest rate options and options linked to an equity index.

3.2 Investment components

Whereas IFRS 4 made reference to the notion of a deposit component, IFRS 17 introduces a new concept called an investment component instead. An investment component is the amount in an insurance contract that requires the entity to repay to a policyholder even if an insured event does not occur.

An example of an investment component is an insurance contract where premiums are paid into an account balance and that balance (or a portion thereof) is guaranteed to be repaid to the policyholder on maturity or surrender of the contract, i.e., even if an insured event such as death does not occur.

IFRS 17 requires an entity to separate distinct investment components from the host insurance contract.¹³ An investment component is distinct if both of the following conditions are met:¹⁴

- The investment component and the insurance component are not highly interrelated; and
- 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.

An investment component and an insurance component are highly interrelated if:¹⁵

- The entity is unable to measure one component without considering the other. For example, if the value of one component varies according to the value of the other, an entity should apply IFRS 17 to account for the combined investment and insurance components.
- The policyholder is unable to benefit from one component unless the other is also present. For example, if the lapse or maturity of one component in a contract causes the lapse or maturity of the other, the entity should apply IFRS 17 to account for the combined investment and insurance components.

¹³ IFRS 4.10-12, 20D and B28

¹⁴ IFRS 17.11

¹⁵ IFRS 17.B32

Example 2 – Insurance contract with an account balance and a minimum death benefit

An entity issues a life insurance contract with an account balance. The entity receives a premium when the contract is issued. The account balance is increased annually by voluntary amounts paid by the policyholder, increased or decreased by amounts calculated using the returns from specified assets and decreased by fees charged by the entity.

The contract promises to pay the following:

- (a) a death benefit, equal to the excess of the guaranteed amount over the account balance, if the insured person dies during the coverage period; or
- (b) the account balance, if the contract is cancelled (i.e., there are no surrender charges).

The existence of similar investment products indicates that the components may be distinct. However, the death benefits either lapse or mature at the same time as the account balance, so the components are highly interrelated and are not distinct.

Consequently, the account balance would not be separated because:

- The entity could not measure the death benefit without considering the amount of the account balance.
- The policyholder is unable to benefit from one component unless the other is also present.

Therefore, the entity accounts for the investment components under IFRS 17.

Non-distinct investment components (e.g., some surrender values, account balances, no claims bonuses or profit commissions) are not separated from the measurement of the liabilities for insurance contracts, but are excluded from insurance revenue and insurance service expenses in the statement of profit or loss. The IASB decided that including receipts and repayments of such investment components in revenue and incurred claims would not faithfully represent the similarities between financial instruments within the scope of IFRS 9 and investment components embedded in insurance contracts within the scope of IFRS 17.¹⁶

3.3 Goods and non-insurance services

After applying IFRS 9 to embedded derivatives and separating a distinct investment component from a host insurance contract as seen in figure 2 and explained above, an entity is required to separate any promise to transfer distinct goods or services to a policyholder from the host insurance contract.

Activities an entity needs to perform to fulfil the contract, for example, administrative tasks to set up a contract or claims processing, that do not transfer a service to the policyholder as they are performed, should not be separated.¹⁷

A promised good or non-insurance service to the policyholder is not distinct if¹⁸:

- The cashflows and risks associated with the goods or services are highly interrelated with the cash flows and risks associated with the insurance components in the contract, and
- The entity provides a significant service in integrating the goods or non-insurance services with the insurance components.

16 IFRS 17.BC33
17 IFRS 17.B33
18 IFRS 17.B35

Example 3 – Consideration in case of non-distinct goods or non-insurance services

As a follow up of Example 2 above, assume that the entity has a claims processing department to process the claims received and an asset management department to manage investments. An investment product that has equivalent terms to the account balance, but without the insurance coverage, is sold by another financial institution. Are the claims processing and asset management service distinct?

Solution 3

No. Claims processing and asset management activities are activities the entity must undertake to fulfil the contract. Therefore, they are not distinct because the policyholder cannot benefit either on their own or together with other resources readily available. Thus, the entity should not separate the claims processing or asset management service components from the insurance contract.

Goods or non-insurance services promised to a policyholder are distinct if the policyholder can benefit from them either on its own or with other readily available resources¹⁹. An entity applies the principles in IFRS 15 Revenue from Contracts with Customers on how to separate a contract with a customer that is partially within the scope of IFRS 15 and partially within the scope of other IFRS standards.

3.4 Voluntary separation of components of an insurance contract

As a general provision, IFRS 4 permits voluntary separation of non-insurance components in an insurance contract where separation (referred to as “unbundling”) is not required.²⁰ Some entities used this option to voluntarily separate non-insurance components from their host insurance contracts and account for them under other IFRSs.

The IASB considered whether to permit an entity to separate a non-insurance component when not required to do so by IFRS 17, for example, some investment components with interrelated cash flows, such as policy loans. However, the IASB concluded that it would not be possible to separate a component in a non-arbitrary way that is not distinct from the insurance contract nor would such a result be desirable.²¹

In such cases, entities shall assess whether separation of the non-insurance components is required under IFRS 17. Any such components not requiring mandatory separation will have to be accounted for together with the host insurance contract under IFRS 17.

19 IFRS 17.B34
20 IFRS 4.10(b)
21 IFRS 17. BC114

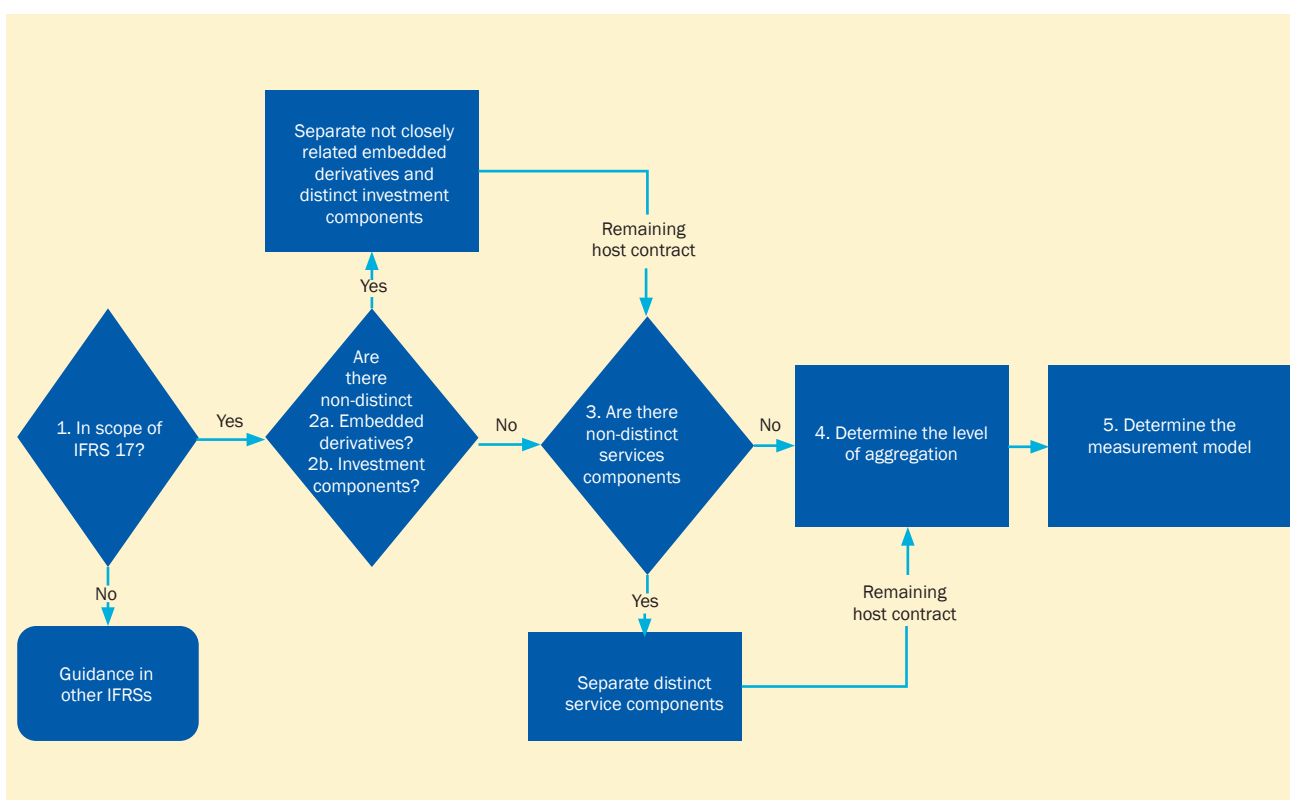


Figure 3 Illustration on Separating Components of an Insurance Contract

4.0 COMBINING INSURANCE CONTRACTS

To prevent entities from entering into contracts that individually transfer significant insurance risk if looked at separately but collectively do not, IFRS 17 allows entities to treat a set or series of insurance contracts as a whole in the event that such contracts:

- (i) have the same or a related counterparty; and
- (ii) may achieve, or be designed to achieve, an overall commercial effect.

Essentially, accounting for such contracts separately would not give the true reflection of the substance of the agreement²². Effectively, the standard allows that such contracts are accounted for as a single arrangement if:

- (i) the counter parties to the contracts meet the definition of related party in IAS 24 Related Party Transactions; and
- (ii) the contracts are designed to achieve an overall commercial effect.

NOTE: Combining insurance contracts involves significant judgment and careful consideration of all relevant facts and circumstances available without undue cost.

Among others, an entity may consider the followings considerations in the assessment of whether a set or series of insurance contracts achieve, or are designed to achieve, an overall commercial effect:

- (i) Whether contracts are priced as a single risk.
- (ii) Whether the lapse of one contract changes the rights and obligations of another contracts.

- (iii) Whether measuring the contract separately result in one or more contracts being onerous while if measured as a whole they would be profitable.
- (iv) Whether both direct and indirect policies cover the same underlying insurance risk.
- (v) Whether the contracts are impacted similarly by underlying insured events.
- (vi) Whether the rights and obligations are different when looked at together compared to when looked at individually (for example, the rights and obligations of one contract negate the rights and obligations of another contract entered into at the same time with the same counterparty, the combined effect is that no rights or obligations exist).
- (vii) Whether the entity is able to measure one contract without considering the other. An entity may consider the interdependency between the different risks covered in each contract and whether the contracts lapse together. When cashflows are interdependent, separating them can be arbitrary.²³

The principle of combining insurance contracts seems to resonate with the guidance under the Conceptual Framework, which is to the effect that: “A group or series of contracts may achieve or be designed to achieve an overall commercial effect. To report the substance of such contracts, it may be necessary to treat rights and obligations arising from that group or series as a single unit of account. For example, if the rights or obligations in one contract merely nullify all the rights or obligations in another contract entered into at the same time with the same counterparty, the combined effect is that the two contracts create no rights or obligations. Conversely, if a single contract creates two or more sets of rights and obligations that could have been created through two or more separate contracts, an entity may need to account for each set as if it arose from separate contracts in order to faithfully represent the rights and obligations²⁴”

NOTE: While no single factor is determinative in applying the above assessment, when the lapse or maturity of one contract causes the lapse or maturity of another contract, there is a strong indication that the contracts were designed to achieve an overall commercial effect. However, the fact that a set or series of insurance contracts with the same counterparty are entered into at the same time may not, in itself, be sufficient to conclude that they achieve, or are designed to achieve, an overall commercial effect. Determining whether it is necessary to treat a set or series of insurance contracts as a single contract involves significant judgement and careful consideration of all relevant facts and circumstances.

Moreover, the counter parties to the contract should meet the *related party* definition in IAS 24 *Related Party Transactions*.

²³ IFRS 17:9

²⁴ Paragraph 4.62 of the Conceptual Framework

5.0 LEVEL OF AGGREGATION OF INSURANCE CONTRACTS

The level of aggregation of insurance contracts determines the unit of account to be used when applying IFRS 17. Aggregation of insurance contracts shall among other things, affect the allocation of contractual service margin (CSM) to insurance revenue and the level at which onerous contracts are identified. Accordingly, these requirements affect how the performance of the insurer will be reported in its financial statements. Therefore, the level of aggregation affects how the profitability of the business is reported.

IFRS 17 requires insurance contracts to be arranged into groups based on three stages or levels as shown below:

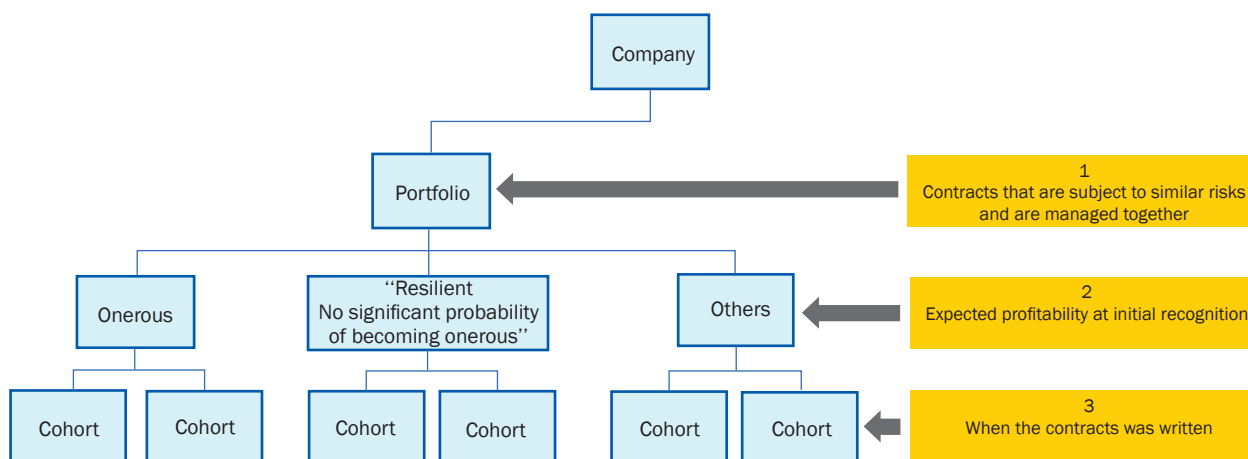


Figure 4: Stages of Aggregation

5.1 Portfolio level

Aggregation of Insurance Contracts starts with identification of portfolios of insurance contracts. A portfolio of insurance contracts comprises contracts that are subject to *similar risks* and can be *managed together* as a single pool²⁵.

Similar risks: Contracts may have similar risks if the entity expects their cash flows will respond similarly in amount and timing to changes in key assumptions. Examples of contracts with similar risks may include contracts that have similar perils such as non-life insurance contracts; contracts issued in the same geographical area; or contracts that have profit-sharing arrangements. Accordingly, contracts in different product lines (such as regular term life insurance) are not expected to have similar risks and hence are expected to be grouped in different portfolios.

Managed together: Insurance contracts may be considered as managed together if they have a consistent approach to pricing; consistent product design and development; or consistent claims handling procedures. Thus, Contracts in different business lines are expected to be managed in different ways.

This aggregation of insurance contracts is done when contracts are issued and is not subsequently revised²⁶.

NOTE: Deciding which contracts have similar risks is a matter of judgment. A number of insurance products provide a primary level of insurance cover with optional additions (or extensions) at the discretion of the policyholder.

25 IFRS 17:14-23

26 IFRS 17:24

IFRS 17 is silent as to whether an insurance contract can be separated into different insurance components and, if so, the basis for such a separation. Some entities may combine, for example, House owners cover with Householders, all risks, occupier’s liability among others as a single domestic package contract and also issue these products separately.

The standard seems to imply that, in these circumstances, the entity would have five portfolios (House owners cover, Householders, all risks, occupier’s liability and a domestic package cover) because the contracts contain five different types of risk. However, IFRS 17 refers to groups of insurance contracts and is silent as to whether an insurance contract may be separated into different “sub-insurance components” voluntarily.

The lowest unit of account in IFRS 17 has been considered to be the insurance contract and that **there is not** an accounting policy choice to further subdivide a single contract and allocate the pieces to different portfolios. However, under certain circumstances, where a single contract combined a number of individual contracts into one document, then separation may be required to reflect economic substance taking into consideration the following factors;

- interaction between the different claim payments of the components.
- whether premiums relating to different investment components were invested in different underlying assets.
- whether components are distinct, e.g., they do not lapse together, any combined discount is small, etc.²⁷

5.2 Expected Profitability at initial recognition

IFRS 17:16 requires the entity to divide a portfolio into a minimum of:

- A group of contracts that are onerous (loss making) at initial recognition, if any;
- A group of contracts that at initial recognition have no significant possibility of becoming onerous subsequently (resilient contracts), if any; and
- A group of the remaining contracts in the portfolio, if any.

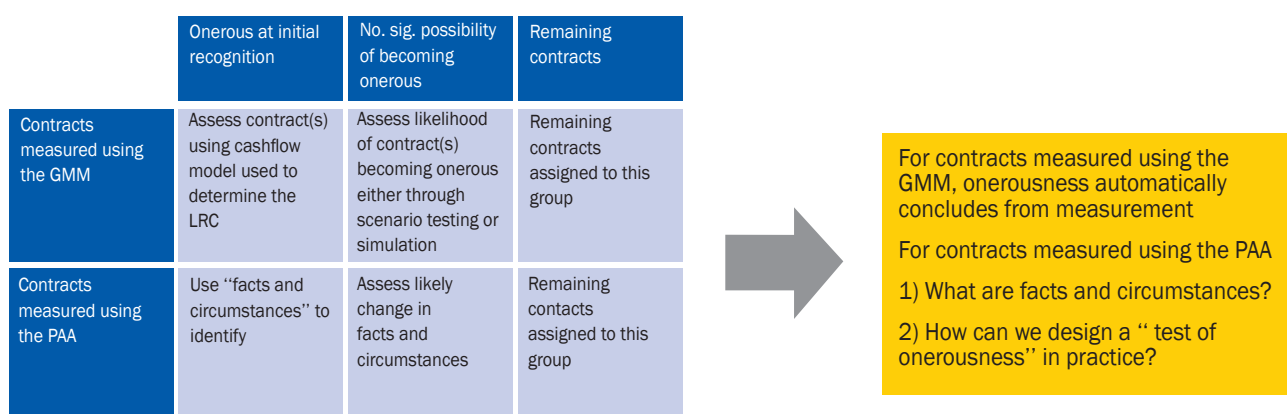


Figure 5: Aggregation by Expected Profitability at initial recognition

The approach to grouping depends on the type of measurement model applicable to the group. For contracts that will be accounted for using the Premium Allocation Approach (PAA), IFRS 17 allows entities to assume that those contracts are profitable unless facts

27 Insurance contracts: Responding to the external editorial review, IASB staff paper 2C, February 2017, Issue A8

and circumstances indicate otherwise²⁸. For contracts accounted for using the General Measurement Model (GMM), the entity needs to perform sophisticated quantitative modeling to determine if the contract is onerous at initial recognition.

5.2.1 Onerous contracts

Insurance Contracts shall be considered onerous at initial recognition if the fulfillment cash flow arising from the contract is a net outflow²⁹. In this case, the insurer recognizes an immediate loss in the financial statements and a Contractual Service Margin (CSM) of zero is established.

The assessment to determine if a contract that is not onerous has no significant possibility of becoming onerous can be based on the sensitivity of the profit to the assumptions used (which calls for some judgment) and on internal reporting information. The objective, however, is to ensure that contracts are separated into groups that are initially onerous, and contracts that could join the onerous group at a future date, so that there is reasonably prompt recognition of losses on onerous contracts within each issue year cohort.

5.2.2 Resilient contracts

The group of contracts that have a significant possibility of becoming onerous subsequent to initial recognition could be described as contracts with a low profitability at inception or as contracts where the profitability is highly variable. In contrast, the group of contracts that have no significant possibility of becoming onerous subsequently could be described as profitable contracts at inception or as contracts where profitability is relatively stable.

For contracts that are not onerous at inception, an entity will need to distinguish, at initial recognition, between profitable contracts with no significant possibility of becoming onerous subsequently and other contracts expected to be profitable.

Assessing whether a contract, or set of contracts, has no significant risk of subsequently becoming onerous should:

- (i) Be based on the likelihood of changes in assumptions which, if they occurred, would result in the contracts becoming onerous.
- (ii) Use information about estimates provided by the entity's internal reporting.

Example

Assume that an insurer issues 2 sets of insurance contracts, set A and set B. Set B policyholders are considered to be riskier than set A. The insurer has decided to set an equal premium for both sets of contracts. Assume that set B contracts are onerous while set A contracts are profitable.

Following the requirements in IFRS 17:16, the contracts in set A and set B cannot be grouped together.

28 IFRS 17:18
29 IFRS 17: 47

What if the Contracts that are onerous only because of law and regulation?

An insurer who is restricted by regulation to set a premium which is higher for onerous contracts and that makes those contracts to be onerous as a result of the regulation, may group onerous and resilient contracts together³⁰. For example, if two or more contracts have different characteristics but can not be priced differently because of regulation, an entity may apply the practical expedient above.

Example

Assume that an insurer issues 2 sets of insurance contracts, set A and set B. Set B policyholders are considered to be riskier than set A. The insurer is restricted by regulation to set equal premium for both sets of contracts.

Following the requirements in IFRS 17:20, the contracts in set A and set B shall be grouped together.

5.3 When the contract was written

An entity is prohibited from grouping contracts issued more than one year apart, except under circumstances at transition to IFRS 17³¹. IFRS 17 requires a portfolio of contracts to be divided into annual 'cohorts' or time buckets.

Insurers issue insurance contracts at a particular pricing level which often remains stable for a certain period. Changes in economic circumstances or other factors may result in an insurer changing its pricing over time and hence the expected profitability of new contracts may vary. As a result, a group may not include contracts issued more than one year apart.

The restriction aims to prevent entities from, in effect, having perpetually open portfolios as this would lead to the loss of information about the development of profitability over time, causing the CSM to persist beyond the duration of contracts in the group, and, consequently, resulting in profits not being recognised in the correct periods.

Since IFRS 17 does not require any particular approach and entities are not required to use a 12-month period when grouping insurance contracts, a cohort can be based on an issuing period that is less than one year. However, it is also possible for an entity to divide the groups using an annual period that coincides with an entity's financial reporting period.

For example: contracts issued between 1 January 20XX and 31 December 20XX would form a group for an entity with an annual reporting period ending 31 December 20XX.

³⁰ IFRS 17:20

³¹ IFRS 17.22, IFRS 17: B137

		Portfolio A	Portfolio B	...
		Portfolio A	Portfolio B	...
2021		Portfolio A	Portfolio B	...
	2022	No significant possibility of becoming onerous	No significant possibility of becoming onerous	No significant possibility of becoming onerous
		Other profitable	Other profitable	Other profitable
	2023	Onerous at inception	Onerous at inception	Onerous at inception

Figure 6: Illustration of aggregation based on when the contract was written

NOTE: Entities may further sub-divide the groups/portfolios above into, for example, more groups that are not onerous at initial recognition; and more than one group of contracts that are onerous at initial recognition³². This may be necessary to ensure that contracts that are issued more than one year apart are not grouped together.

6.0 RECOGNITION

6.1 Initial Recognition

6.1.1 Pre-Recognition Period

This is the period from the *inception date* (when the company accepts risk arising from the insurance contract) till just before the contract is recognised. During this stage, three points need to be considered namely:

(i) Whether the issued contracts are within the scope of IFRS 17;

If the company establishes that contracts are eligible for IFRS 17, it will then decide if it wishes to apply the Premium Allocation Approach (PAA) at the inception date. The standard also lays out requirements for contracts with/without direct participation features.

(ii) Whether there are any insurance acquisition cash flows;

Insurance acquisition cash flows are cash flows arising from the costs of selling, underwriting and starting a group of insurance contracts that are directly attributable to the portfolio of insurance contracts to which the group belongs.

Insurance acquisition cash flows that are sometimes paid/received by the entity before the related groups of contracts are recognised, are recognised as an asset or liability and are presented in the carrying amount of the related groups of insurance contracts issued. However, a practical expedient exists for contracts that qualify for the Premium Allocation Approach.

(iii) Whether there are any onerous contracts.

Normally, insurance contracts are recognised and measured after the inception date. However, a company may recognise insurance contracts on the contracts' inception date or during the period between the inception date and the normal recognition date when those contracts are deemed to be onerous³³. In such an event, the company would measure the contracts and immediately recognise them as onerous.

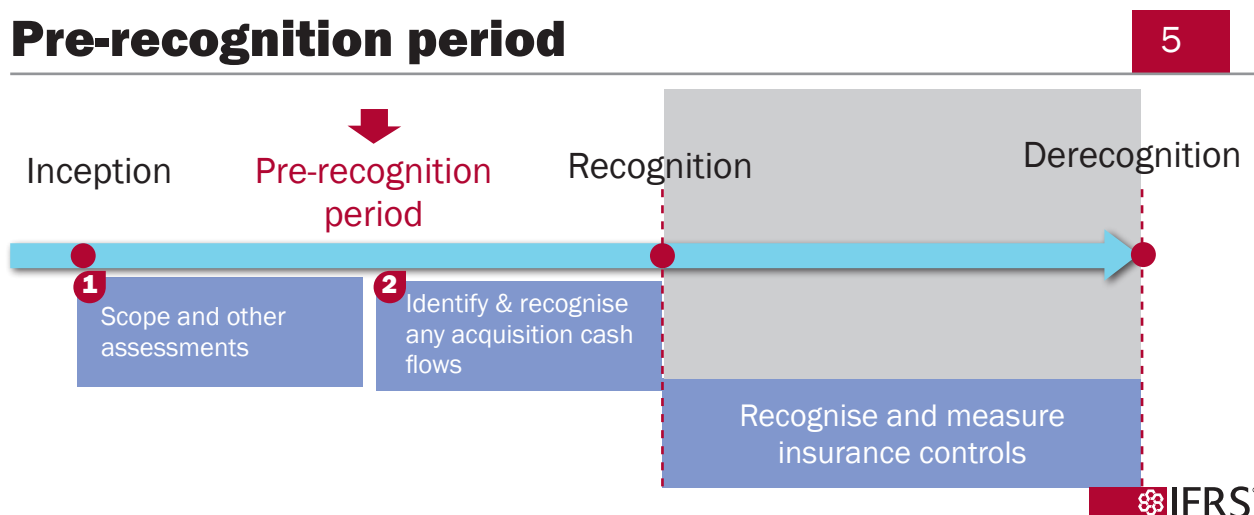


Figure 7: Illustration of IFRS 17 pre-recognition activities [Source: IFRS 17 Insurance Contracts core requirements: Recognition a Derecognition November 2017, IFRS Foundation]

6.1.2 Recognition Date

Recognition may be either normal or early. Normal recognition is done for profitable contracts and occurs at the earlier of³⁴:

- (i) the beginning of the coverage period (the period during which the entity provides coverage for insured events) of the group of contracts; and
- (ii) the date when the first payment from a policyholder in the group becomes due. If there is no contractual due date, the first payment from the policyholder is deemed to be due when it is received³⁵.

However:

- a) For onerous contracts, the entity would recognise the loss immediately³⁶.
- b) An insurer may recognise any insurance acquisition cashflows as expenses under the PAA³⁷.

33 Applying paragraphs 16 and 25.

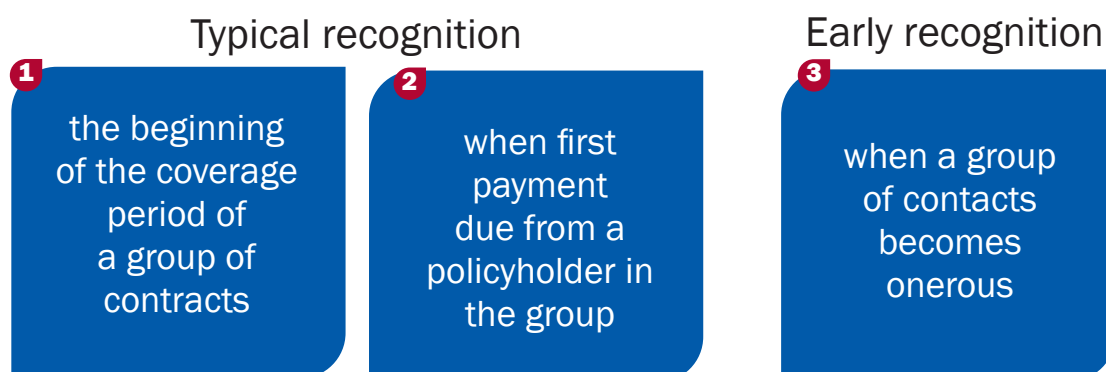
34 IFRS 17:25

35 IFRS 17:26

36 IFRS 17:25

37 IFRS 17:59 (a)

The **earliest date** of any of the following:*



*These requirements are modified for reinsurance contracts held and investment contracts with discretionary participation features



Figure 8: Illustration of IFRS 17 Recognition activities [Source: IFRS 17 Insurance Contracts core requirements: Recognition a Derecognition November 2017, IFRS Foundation]

Illustration 1: Coverage period earlier

XXM Limited issues a group of insurance contracts to policyholders beginning on 30 June 20X0. The coverage period of the group begins on 1 July 20X0. The due date for the first premium from a policyholder in the group is 30 July 20X0. The Management of XXM Limited has determined that the group of **insurance contracts is not onerous**.

Timing of Initial Recognition of Insurance contracts

Basing on the criteria in IFRS 17:25, initial recognition date would be the earlier of the start of the coverage period of the group and the date that the first premium is due. In this case, the coverage period comes earlier therefore, the initial recognition date would be 1 July 20X0.

Illustration 2: Premium Payments earlier

An entity issues insurance contracts that form a group to policyholders beginning on 20 June 20X1. The coverage period of the group begins on 1 July 20X1 and the first premium from a policyholder in the group is due on 27 June 20X1. The group of insurance contracts is not onerous.

Timing of Initial Recognition of Insurance contracts

The group of insurance contracts is recognised on 27 June 2021 (i.e., the date that the first premium is due), which is before the beginning of the coverage period. However, if the entity has a reporting date of 30 June 2021, only those contracts within the group issued as of the reporting date would be recognised in the financial statements for the period ending 30 June 2021.

Illustration 3: Onerous Contracts

XXM Limited issues a group of insurance contracts to policyholders beginning on 27 June 20X0. On the same day, Management of XXM Limited determines that the group of insurance contracts is onerous. The coverage period of the group begins on 1 July 20X0 and the first premium from a policyholder in the group is due on 31 July 20X0.

Timing of Initial Recognition of Insurance contracts

This group of insurance contracts would be recognised on the date when it was determined to be onerous which is, 27 June 20X0. However, if XXM Limited has a reporting date of 30 June 20X0, only those contracts within the group issued as at the reporting date would be recognised in the financial statements for the period ending 30 June 20X0.

NOTE: The inception date of a contract is when an entity has a contractual obligation to accept risk (also known as the issue date of a contract). The inception date is typically before the beginning of coverage and due date for the initial premium. However, IFRS 17 only requires recognition of issued insurance contracts before the beginning of the coverage date and due date for the initial premium if facts and circumstances indicate that the contracts in the group are onerous.

6.1.3 Group contracts and initial recognition

An insurance contract may, at initial recognition, join an existing group of insurance contracts if all the contracts have similar expected profitability at the time of initial recognition and are issued within a year of each other (i.e., as discussed under the section on cohorts in level of aggregation (see 5.3 above).

When contracts are added to a group in a subsequent reporting period, this may result in a change in determining discount rates at the date of initial recognition of the group as discount rates may be determined using weighted average rates over the period that contracts in the group are issued. When this occurs, an entity should apply the revised (weighted average) discount rates from the start of the reporting period in which the new contracts are added to the group. There is no retrospective catch-up adjustment.

NOTE:

The date on which an entity recognises a group of insurance contracts is particularly important as it is key when;

- **Determining the CSM.** On initial recognition, the entity measures the fulfilment cash flows arising from a group of insurance contracts and determines the CSM, which is subsequently recognised in profit or loss over the coverage period.
- **Determining the discount rate on initial recognition.** This rate is used throughout the general measurement model. For contracts without direct participation features measured applying the general measurement model, this discount rate is used to:
 - accrete the interest on the CSM;
 - measure the changes in fulfilment cash flows that adjust the CSM; and
 - depending on the circumstances, present the insurance finance income or expense recognised in profit or loss.

6.1.4 Insurance acquisition cash flows

An entity:

- recognises an asset for any insurance acquisition cash flows relating to a group of existing or future insurance contracts that it pays (or for which a liability has been recognised under another standard) before the related group is recognised. This may

be when the insurance coverage is realized or when the performance obligation is made by the insurer;

- derecognises that asset (or a portion of it) when the group of insurance contracts is recognised; and
- assesses the recoverability of the asset if facts and circumstances indicate that the asset may be impaired and recognises an impairment loss at each reporting date if it is impaired (IFRS 17.28B–28D)

NOTE:

For many insurance contracts, the main cash flows paid before initial recognition of a group of contracts are the insurance acquisition cash flows. Recognising insurance acquisition cash flows paid as assets until the related group of insurance contracts has been recognised ensures that these cash flows are not recognised immediately as an expense. This accounting treatment may appear similar to recognising the related insurance contracts from the date on which those insurance acquisition cash flows occur. However, in many cases the initial recognition requirements for the group will not have been met at that time. Therefore, there will be no need to determine the CSM until those requirements are met (IFRS 17. BC145).

7.0 MEASUREMENT OF INSURANCE CONTRACTS

As discussed in 5.0 above, insurance contracts shall be aggregated into groups to which IFRS 17 recognition and measurement requirements will apply. Groups of Insurance contracts may be measured using one of the following approaches:

- (i) General Measurement Approach
- (ii) Premium Allocation Approach
- (iii) Variable Fee Approach

7.1 The General Model

The general model is the default measurement model because it provides a comprehensive and coherent framework that can be used for any insurance contract, including a reinsurance contract. The model is also known as the “Building Block Approach” because it is made up of four “blocks” that are shown below:

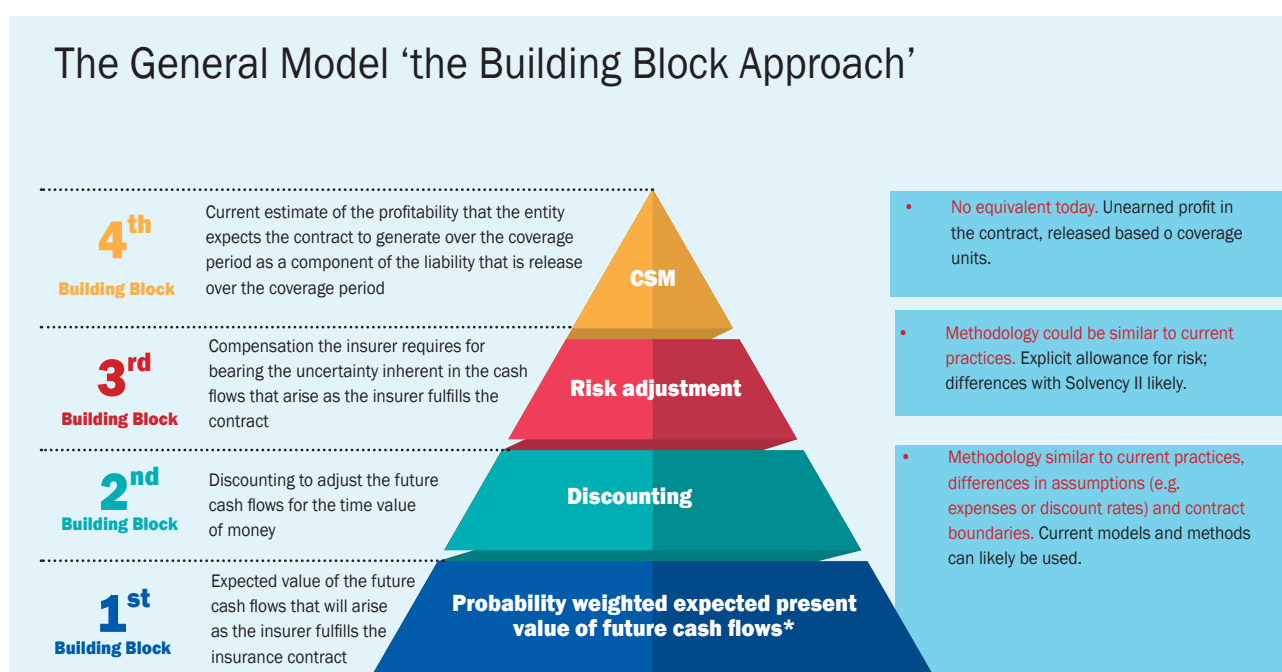


Figure 9: The Building Blocks of the General Measurement Model

- (i) 1st Building Block: Present value of future cash flows

This the expected value of the future cash flows that will arise as the insurer fulfils the insurance contract obligations. The cash flows should be probability weighted. Cashflows include claims payments plus other additional cash flows. In generating estimates of future cash flows, an insurer considers a range of scenarios that would reflect the possible outcomes from the contracts. For each scenario, the insurer determines the timing and amount of the cash flows expected to arise under each outcome. The insurer then allocates a probability of that outcome actually happening.

- (ii) 2nd Building Block: Discounting

This involves discounting of the future cash outflows to account for the time value of money. The cash flows from the 1st building block are discounted and weighted based on those allocated probabilities so as to arrive at the Net Present Value (NPV). The NPV is then used to determine the insurance contract liability or asset. The discount rates should be consistent with observable current market prices. Discounting may take the

top-down or bottom-up approach. The two approaches yield different results but these needn't be reconciled.

Discount rate - Top down vs. bottom up

Top down discount rate	
Actual or expected reference portfolio rate	7.0%
Duration mismatches	-0.3%
Market risk premium for expected credit losses	-0.1%
Market risk premium for unexpected credit losses	-0.6%
Insurance contract discount rate	5.7%
Difference between the two methods not required to be reconciled	
Bottom up discount rate	
Insurance contract discount rate	5.5%
Liquidity premium	1.5%
Risk free rate of return	4.0%

Figure 10: Approaches to Discounting

(iii) 3rd Building Block: Risk Adjustment

The risk adjustment reflects the compensation that an insurer would require for bearing the uncertainty inherent within the timing and amounts of the cash flows arising from non-financial risk as expected throughout the life of the contract.

Example: An insurer has two groups of accounts with different outcomes as shown below:

Group A Contracts		Group B Contracts	
Probability	Payout	Probability	Payout
50%	1,000,000	50%	510,000
50%	0	50%	490,000
Probability weighted average = (50%*1,000,000) + (50%*0) = 500,000		Probability weighted average = (50%*510,000) + (50%*490,000) = 500,000	

Note that Group A contracts are riskier because of the big variability in potential payouts. On the other hand, the potential payouts involved with Group B contracts are less in variance making this group less risky.

IFRS 17 requires the entity to disclose the level of confidence to which the risk adjustment has been computed. Risk assumptions should be reviewed at every reporting date. All current period adjustments go to the P/L while future period adjustments go to the CSM.

(iv) 4th Building Block: Contractual Service Margin (CSM)

CSM refers to the current estimate of the profitability that the entity expects the contract to generate over the coverage period as a component of the liability that is released over the coverage period. At the start date of the contract, there will be unearned profit due to the fact that services have not been provided. As the insurer provides services to the

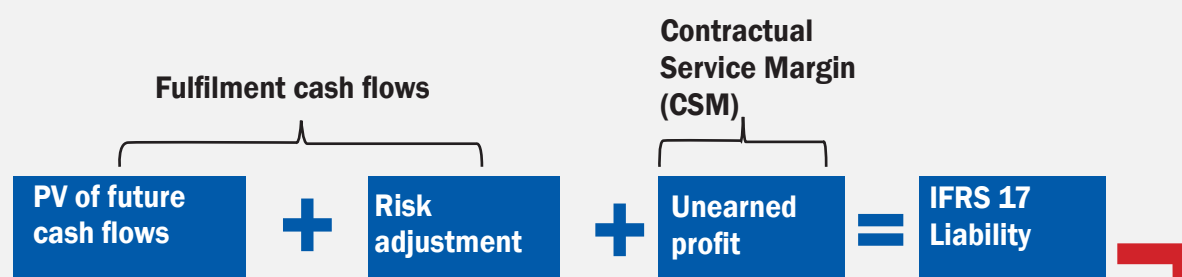
policyholder, the profit will become earned and will be recognised in the Profit or Loss Account. At the end of the coverage period, the CSM would have been fully recognised to the P/L.

7.1.1 Measurement on initial recognition (Initial Measurement)

The liability (or asset) recognized for a group of insurance contracts is measured, on initial recognition and subsequently, as the sum of the fulfilment cash flows and the Contractual Service Margin (CSM). The insurer sums up the ‘building blocks’ as follows:

- (i) Fulfilment cash flows, comprising:
- 1st building block: An unbiased and probability-weighted estimate of future cash flows - that will arise as the entity fulfils the contracts
 - 2nd building block: A discount adjustment to present value to reflect the time value of money and financial risks (related to the expected cash flows (to the extent that they are not already included in the estimates of expected cash flows)
 - 3rd building block: A risk adjustment for non-financial risk - to reflect the compensation that the entity requires for bearing the uncertainty about the amount and timing of cash flows that arise from non-financial risk; plus
- (ii) A CSM representing unearned profit an entity will recognise as it provides service under the insurance contracts in the group.

The General Model ‘the Building Block Approach’



Balance sheet	202.3	2022
Financial assets	226,297	196,700
Re/Insurance contract assets	20,572	17,882
Other assets	36,002	31,293
Total Assets	282,871	245,875
Insurance contract liabilities	205,724	178,818
Other liabilities	51,431	44,705
Equity liabilities	25,716	22,352
Total liabilities and equities	282,871	245,875

Figure 11: Insurance Liability or Asset

However, an entity may choose not to use the GMM. In such a case, the entity will have to justify that choice. For many contracts, this will be the only option.

Example of the general model when the insurance contract is profitable

An insurer issues 100 motor insurance contracts (included in one group) with a coverage period of 3 years. The insurer receives premiums on Shs 900 in advance. It is estimated that the present value of the future claim payments (i.e., the cash outflows) is Shs. 545 (using a discount rate of 5%). The estimated risk adjustment for non-financial risk on initial recognition is Shs. 120. It is assumed that all the 100 contracts are not profitable.

At initial recognition;

DR Bank A/c	900
CR Insurance contract liabilities A/c	900

NOTE:

The Insurance contract liabilities amount is made up of the following:

- The PV of future cash outflows of Shs 545
- Risk adjustment of Shs 120
- The contractual service margin (which is the balancing figure) of Shs 235

Example of the general model when the insurance contract is onerous

The loss is taken straight to the P/L on day one. We have no CSM under onerous contracts.

An insurer issues 100 motor insurance contracts (included in one group) with a coverage period of 3 years. The insurer receives premiums on Shs 900 in advance. It is estimated that the present value of the future claim payments (i.e., the cash outflows) is Shs. 800 (using a discount rate of 5%). The estimated risk adjustment for non-financial risk on initial recognition is Shs. 120. It is assumed that all the 100 contracts are profitable.

At initial recognition;

DR Bank A/c	900
DR Onerous loss in the P or L A/c	20
CR Insurance contract liabilities A/c	920

NOTE:



The Insurance contract liabilities amount is made up of the following:

- The PV of future cash outflows of Shs 800
- Risk adjustment of Shs 120

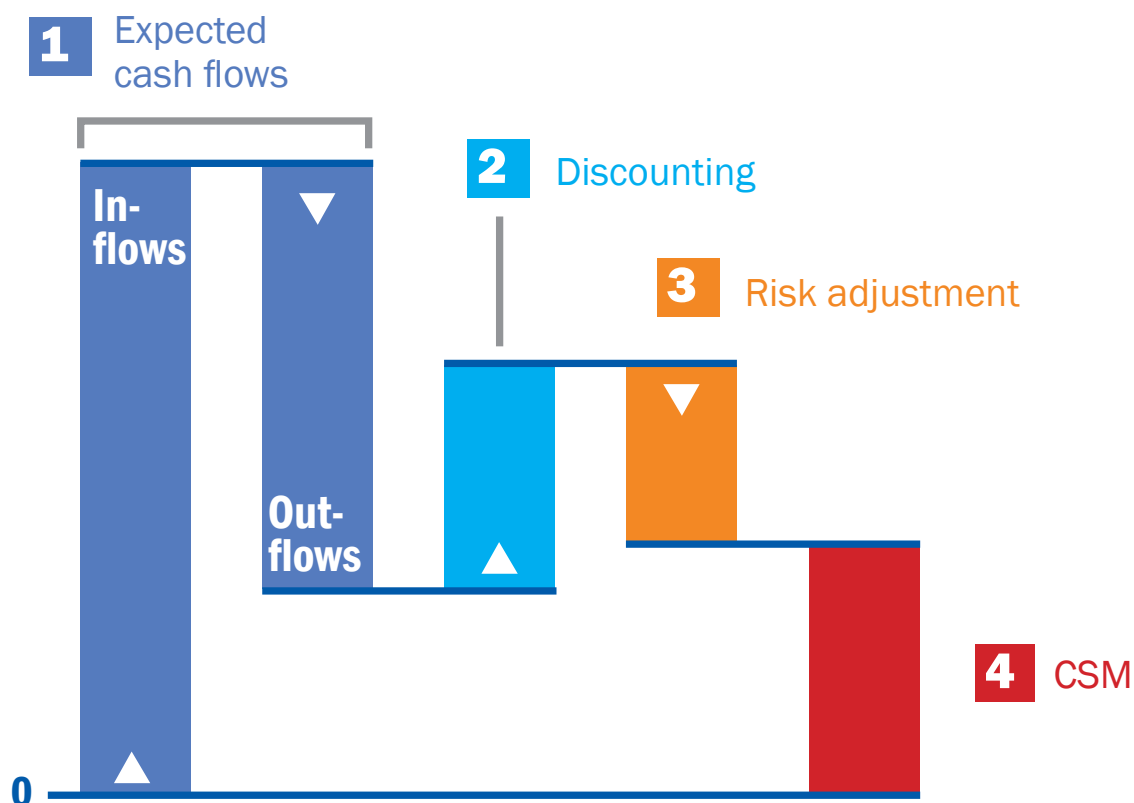
The following cashflows may be considered

The General Model

Cash Flows

Included*	Excluded
<ul style="list-style-type: none"> Premiums and related payments  Claims and benefits, including paid in kind Discretionary payments and payments that vary with returns on underlying items Payments from embedded derivatives, including options and guarantees Insurance acquisition cash flows Claim handling costs Administration and maintenance costs Transaction-based taxes and levies Recoveries such as salvage and subrogation Fixed and variable overheads Other costs 	<ul style="list-style-type: none"> Some not directly attributed acquisition costs, such as product development and training costs Assets investments return Cash flows from reinsurance contracts held Income taxes Cash flows related to components separated from insurance contracts 

* Only if directly related to the fulfilment of the contract



NOTE:

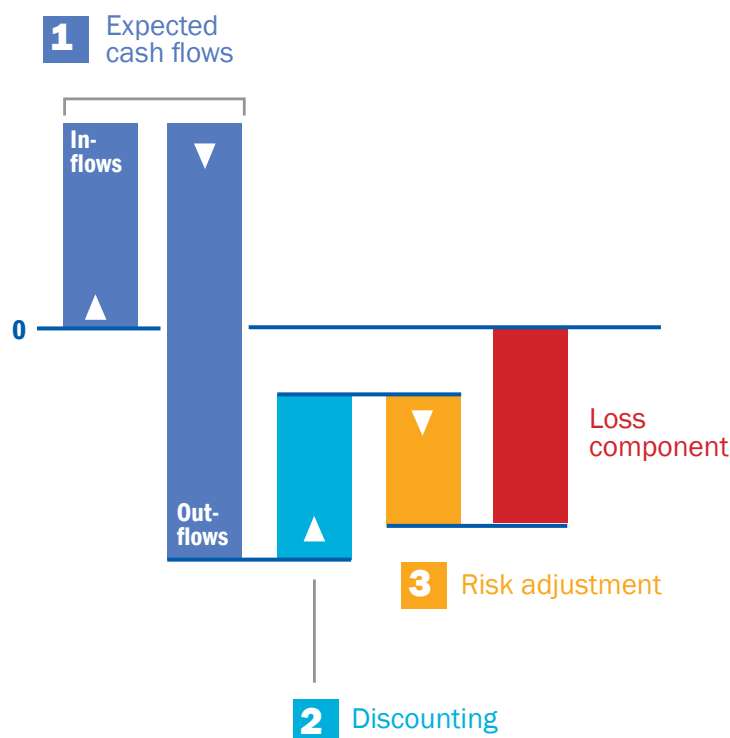
Depending on the facts and circumstances, the size and direction of the components could vary.

On initial recognition, for profitable groups of contracts, the total net cash inflow is-

- the fulfilment cash flows;
- the derecognition of any asset recognised for insurance acquisition cash flows related to the group of contracts;
- the derecognition of any asset or liability previously recognised under other standards for cash flows related to the group of contracts; and
- any cash flows arising from the contracts in the group at that date (IFRS 17.32, 38).

The CSM is the equal and opposite amount to that net inflow. The CSM has an equal and opposite value on initial recognition to the fulfilment cash flows, plus any cash flows arising from the group at or before that date. This is because the entire value of the contracts relates to services to be provided in the future and, therefore, profit to be earned in the future. It ensures that no income or expense arises from the group of contracts on initial recognition.

However, where the total mentioned above is a net cash outflow, then the group of contracts is onerous. A loss is recognised immediately in the statement of financial performance for the entire net cash outflow. This results in the carrying amount of the insurance liability for the group being equal to the fulfilment cash flows and the CSM of the group being zero. A loss component is created for this net cash outflow, which determines the amounts that are subsequently presented in profit or loss as reversals of losses on onerous groups. These amounts are not included in determining insurance revenue (IFRS 17.47–49).



NOTE:

Depending on the facts and circumstances, the size and direction of the components could vary.

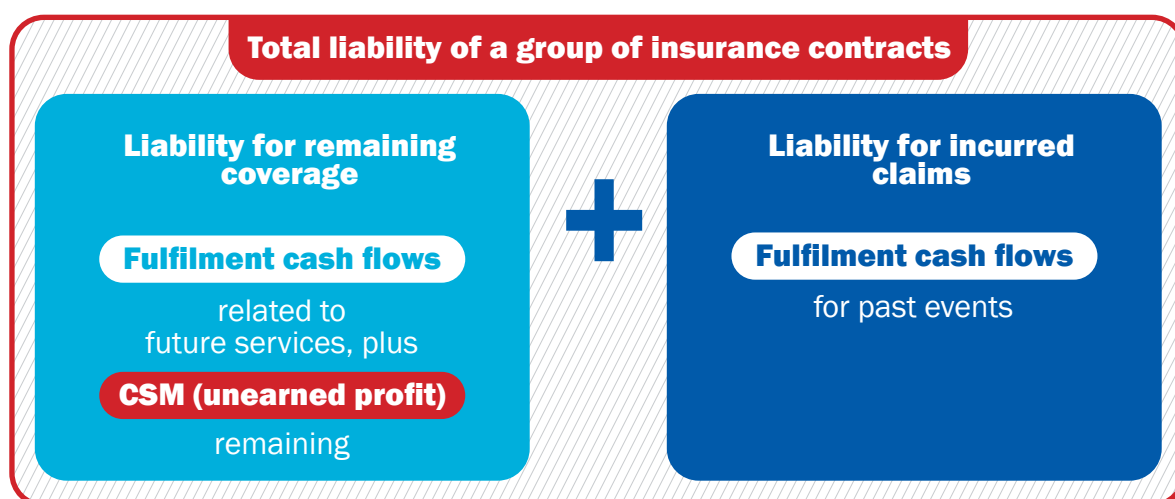
Depending on the facts and circumstances, the size and direction of the components could vary.

7.1.2 Subsequent Measurement - The general measurement model

After initial recognition of a group of insurance contracts, the carrying amount of the group at each reporting date is the sum of (IFRS 17.40, A, BC25):

- (a) The liability for remaining coverage, comprising:
 - The fulfilment cash flows related to future service allocated to the group at that date - (which in essence establishes the entity’s obligation to pay for future insured events and insurance contract services plus any investment components or other amounts not transferred to liability for incurred claims)
 - The CSM of the group at that date; **And**
- (b) The liability for incurred claims comprising the fulfilment cash flows related to past service allocated to the group at that date – (which in essence establish the entity’s obligation to pay for insured events that have occurred and insurance contract services already provided plus any investment components or other amounts transferred from the liability for remaining coverage. This includes loss events that have occurred but not been reported (Incurred but not Recorded) and other incurred expenses.

Therefore, the components of the liability of a profitable group of insurance contracts are as follows.



The fulfilment cash flows are remeasured at each reporting date to reflect estimates based on current assumptions, applying the same requirements that apply to initial measurement. Changes in estimates of the fulfilment cash flows are reflected in either profit or loss or OCI – or, in some cases, they adjust the CSM – depending on their nature (IFRS 17.43–44, BC22–BC24)

For contracts without direct participation features, interest is accredited on the carrying amount of the CSM during the reporting period using the discount rate applied on initial recognition to reflect the time value of money. The balance is allocated to profit or loss each reporting period to reflect the provision of insurance contract services in the period.

The CSM at each reporting date represents the profit in the group of contracts that has not yet been recognised in profit or loss because it relates to future service.

Snapshot on subsequent measurement

ICL component	Initial measurement	Subsequent measurement
PV of future cash flows	Current assumptions	Current assumptions
Risk adjustment	Current assumptions	Current assumptions
Unearned profit/ Contractual service margin	<ul style="list-style-type: none"> Represents unearned profit in contract. The amount that results in no gain recognised in profit or loss 	Update by reflecting: <ul style="list-style-type: none"> Time value of money Adjustments related to future service Allocation of the amount earned for service provide

Example on the general approach: Premiums = 900, Discounted PV = 545, Risk adjustment = 120, CSM = 235, n = 3years, discount rate = 5%

- (i) Premiums received: On day one, we DR. Cash and CR Insurance Contract Liability with the amount of premiums received which is 900.

Since the PV was discounted, we unwind the discount. So, we recognise a finance cost on that balance which increases the insurance contract liability.

$$\text{Finance cost} = 5\% * 545 = 27$$

DR	Finance cost (expense)	27
CR	PV of future cash flows (liability)	27

- (ii) The entity revises its estimates of future cashflows for Year 2 and now expects to pay less than initially estimated. The PV of the reduction is 80.

Note that this means the CSM increased by 80. Since it is in PV terms, we needn't discount it.

DR	PV of future cash flows (liability)	80
CR	CSM (liability)	80

- (iii) Claims payment: At the end of year 1, actual claims incurred was 200*. However, the entity only paid out 120 in year 1.

DR	PV of future cash flows (liability)	120
CR	Bank/Cash	120

* The difference between 200 and 120 is ignored as it is already included in the PV of future cashflows. Therefore, we only record the 120 that was paid out.

- (iv) Risk adjustment: at the end of year 1, the entity revises the risk adjustment for non-financial risk related to estimates of future cashflows downward by 10.

Note that opening risk adjustment = 120. To recognise year 1 risk adjustment, we release 120 evenly over the 3 years coverage period

$$= 120/3 = 40 \text{ p. a}$$

DR	Risk adjustment year 1	40
CR	P/L	40

To recognise the downward risk adjustment of 10:

DR	Risk adjustment	10
CR	CSM	10

Note: IFRS 17 allows entities as an accounting policy choice, not to account for finance costs for the risk adjustment.

- (v) Contractual service margin (CSM) Computation

Note that opening CSM = 235.

Recognising the finance cost to opening CSM = $5\% * 235 = 12$

DR	Finance cost	12
CR	CSM	12

To recognise year 1 CSM, we release 235 evenly over the 3 years coverage period

$$= (235+12+90)/3 = 112$$

DR	CSM	112
CR	P/L	112

- (vi) Insurance Service Expense Computation

= claims incurred + net revenue

$$= 200 + 152$$

$$= 352$$

Year 1	Present value of future cash flows (A)	Risk adjustment for non-financial risk (B)	Contractual service margin (C)	Insurance contract liability (D=A+B+C)	
Opening balance	(545)	(120)	(235)	(900)	900 = premiums received at start of contract
Insurance finance expenses (finance cost)	(27)		(12)	(39)	39 Goes to P/L as finance costs
Changes related to future service	80	10	(90)		
Changes related to current service		40	112	152	152 Goes to P/L as Insurance Service Results
Cash out flows	120			120	120 Goes to bank account i.e., claim payments
Year 1 Closing balance/ year 2 opening balance	(372)	(70)	(225)	(667)	667 Appears on the face of the balance sheet as year 1 closing insurance contract liability

7.2 Modifications to the General Measurement Model

The general measurement model applies to all groups of insurance contracts in the scope of IFRS 17. However, modifications apply to the following groups of contracts:

- Reinsurance contracts held.
- Investment contracts with discretionary participation features.
- Contracts with direct participation features – the variable fee approach.

Overview of the measurement approaches

	(1) General Approach (GA)	(2) Premium Allocation Approach (PAA)	(3) Variable Fee Approach (VFA)
Why is it needed?	Default model for all insurance contracts.	To simplify for short term contracts with little variability.	To deal with participating business where payments to policyholders are linked to underlying items like assets
Types of contract	<ul style="list-style-type: none"> • Long-term insurance, protection business. • Annuities. • Reinsurance written • Long-term general insurance contracts 	<ul style="list-style-type: none"> • General insurance, short term. • Short-term life and certain group contracts. • Reinsurance written 	<ul style="list-style-type: none"> • Unit-linked contracts. • Certain profit sharing contracts
Mandatory?	Mandatory	Optional	Mandatory

7.2.1 Premium Allocation Approach

An entity is permitted to simplify the measurement of eligible groups of insurance contracts by applying an approach referred to as '*Premium Allocation Approach*'. The *Premium Allocation Approach* (PAA) does not require an entity to measure the CSM explicitly or update the liability for remaining coverage for changes in discount rates and other financial variables.

The PAA is an optional measurement approach. It provides simplifications for measurement of the liability of remaining coverage. The liability for incurred claims is based on probability weighted discounted cashflows as defined under the General Approach. However, CSM is not required under the PAA.

Premium Allocation Approach - The simplified approach

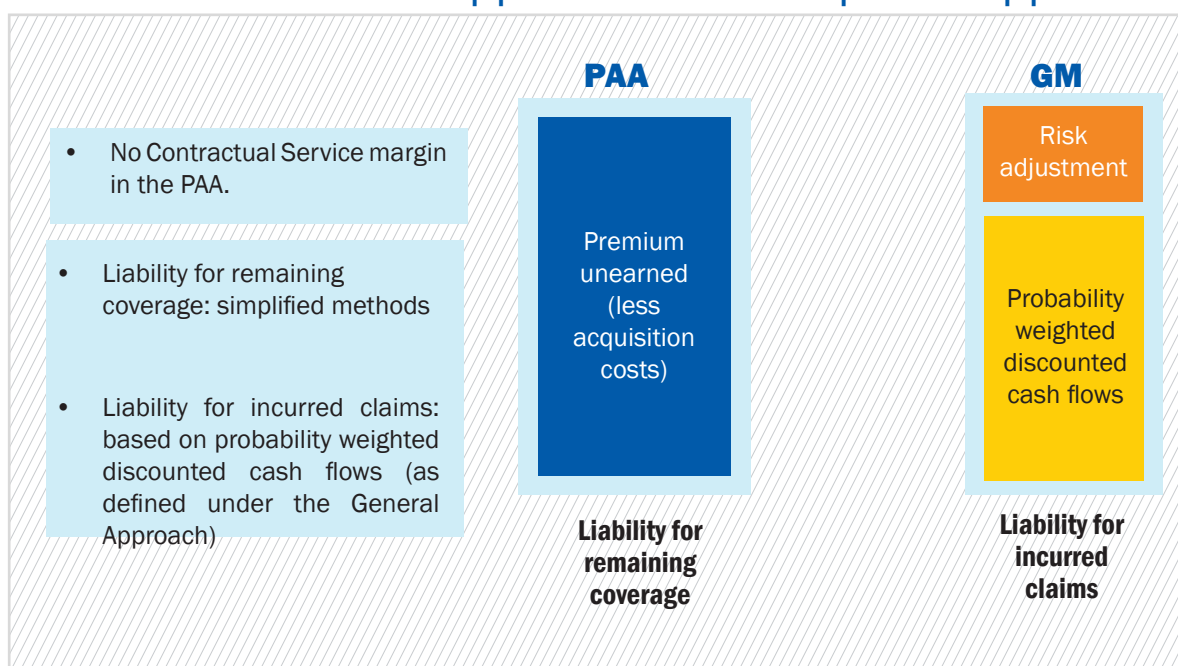


Figure 12: The Premium Allocation Approach (PAA)

Example on PAA

An insurer issues a short term whole turnover contract on 30 July 2023, for a coverage period of 12 months. The contract is covering against risk on non-payment by debtors. The insurer's reporting date is 31 December 2023. The insurer has received premiums of Shs. 1,230 in advance. Assuming that the insurer had nil acquisition costs.

Insurance Contract Revenue (ICR)=Amount of premium allocated to the period

ICR as of 31 December 2023 = 1,230 * (5/12) = Shs 513

At initial recognition:

Liability = premiums – acquisition costs

= 1230 – 0

= 1230

Dr Premiums 1230

Cr insurance Contract Liability 1230

NOTE: Under the PAA, the Insurance Contract Liability needn't be split into CSM, risk adjustment and PV of cashflows as is the case for the general model.

At subsequent recognition, 1230 shall be amortised to the P/L over the coverage period based on passage of time.

Insurance contract revenue (ICR) = Amount of premium allocated to the period

ICR as at 31/12/2023 = 1230 * (7/12)

= 717

Therefore, the liability of the remaining coverage period is Shs. 717

NOTE: Acquisition costs go to the P/L as expenses under insurance service expenses. Premiums are amortised over the same period using a similar method. These are reflected in the ICR.

PAA Eligibility Assessment

The PAA applies to short term contracts of a period of one year or less. For long term contracts, the entity shall demonstrate that applying the PAA won't lead to results that are materially different from those obtained applying the General Model. Additionally, if cashflows are expected to be significantly variable, the PAA may not be used.

Premium Allocation Approach - Eligibility

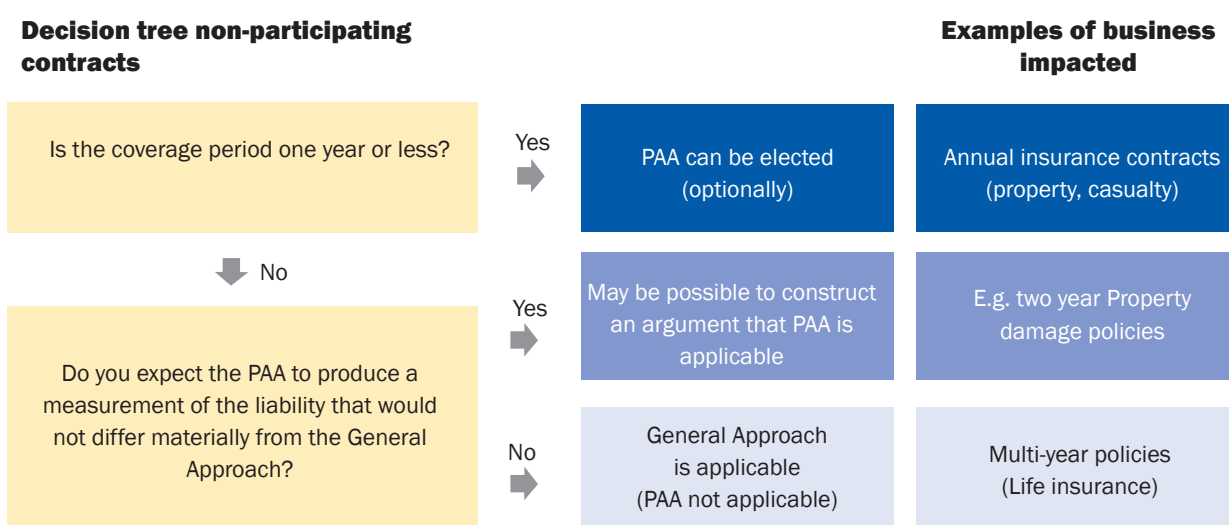


Figure 13: The PAA eligibility Assessment Criteria

NOTE:

As an entity conducts eligibility assessment, it will need to group contracts together following the aggregation principles discussed earlier. The assessment is done at inception of each group and not re-assessed subsequently.

8.0 PRESENTATION

8.1 Presentation in the statement of financial position³⁸

Illustrative statement of financial position for a life insurer ³⁹	Note	2023 SHS'000	2022 SHS'000 (restated)	AS AT 1 JANUARY 2022 SHS'000 (restated) ⁴⁰	IFRS References
Assets					IAS 1:51(d),(e)
Cash and cash equivalents		xxx	xxx	xxx	IAS 1:54(i)
Equity and debt instruments at fair value through profit or loss		xxx	xxx	xxx	IAS 1:54(d), IFRS 7:8(a)
Debt instruments at fair value through other comprehensive income		xxx	xxx	xxx	IFRS 7:8(h)
Debt instruments at amortised cost		xxx	xxx	xxx	
Insurance contract assets		xxx	xxx	xxx	IFRS 17:78(a)
Reinsurance contract assets		xxx	xxx	xxx	IFRS 17:78(c)
Property, Plant and Equipment		xxx	xxx	xxx	IAS 1:54(a)
Intangible assets		xxx	xxx	xxx	IAS 1:54(c)
Deferred tax assets		xxx	xxx	xxx	IAS 1:54(o)
Other assets		xxx	xxx	xxx	IAS 1:55
Total assets		xxx		xxx	
Liabilities					
Current tax liabilities		xxx	xxx	xxx	IAS 1:54(n)
Insurance contract liabilities		xxx	xxx	xxx	IFRS 17:78(b)
Reinsurance contract liabilities		xxx	xxx	xxx	IFRS 17:78(d)
Borrowings		xxx	xxx	xxx	IAS 1:54(m), 55
Deferred tax liabilities		xxx	xxx	xxx	IAS 1:56, IAS 1:54(0)
Other payables		xxx	xxx	xxx	IAS 1:55
Total liabilities		xxx		xxx	
Equity					
Issued Share Capital		xxx	xxx	xxx	IAS 1:54(r), IAS 1:78(e)
Share premium		xxx	xxx	xxx	IAS 1:78(e)
Retained earnings		xxx	xxx	xxx	IAS 1:54(r), IAS 1:78(e)
Fair value reserve		xxx	xxx	xxx	IAS 1:54(r), IAS 1:78(e)
Insurance/reinsurance finance reserve		(xxx)	(xxx)	(xxx)	IAS 1:54(r), IAS 1:78(e)
Total equity		xxx	xxx	xxx	
Total liabilities and equity		(xxx)		(xxx)	

³⁸ IFRS 17:78-79

³⁹ Good Life Insurance (International) Limited – IFRS 17 General Model (EY, 2021) https://www.ey.com/en_gl/ifrs-technical-resources/good-life-insurance-international-limited

⁴⁰ IAS 1.10(a), IAS 1.51 (b)(c)

8.2 Recognition and presentation in the statement of financial performance⁴¹

Illustrative statement of profit or loss for a life insurer ⁴²	Note	2023 SHS'000	2022 SHS'000 (restated)	IFRS References
Insurance revenue		xxx	xxx	IAS 1:46, IAS 1:45
Insurance service expenses		(xxx)	(xxx)	IAS 1:82(a)(ii), IFRS 17:83
Insurance service result before reinsurance contracts held		xxx	xxx	IAS 1:82(ab), IFRS 17:84
Allocation of reinsurance premiums paid		(xxx)	(xxx)	IFRS 17:86
Amounts recoverable from reinsurers from incurred claims		xxx	xxx	IFRS 17:86
Net expenses from reinsurance contracts held		(xxx)	(xxx)	IAS 1:82(ac), IFRS 17:82
Insurance service result		xxx	xxx	IFRS 17:80(a), IAS 1:85
Interest revenue calculated using the effective interest method		xxx	xxx	IAS 1:82(a)(i)
Other interest and similar income		xxx	xxx	
Net fair value gains/(losses) on financial assets at fair value through profit or loss		xxx	xxx	IFRS 7:20(a)(i)
Net fair value gains/(losses) on derecognition of financial assets measured at fair value through other comprehensive income		x	-	IAS 1:82(aa)
Impairment loss on financial assets		(x)	(x)	IAS 1:82(ba)
Net foreign exchange (expense) / income		(x)	x	
Total investment income		xxx	xxx	
Insurance finance expenses for insurance contracts issued		(xxx)	(xxx)	IAS 1:82(bb), IFRS 17:87
Reinsurance finance income for reinsurance contracts held		xx	xx	IAS 1:82(bc), IFRS 17:82
Net insurance financial result		(xxx)	(xxx)	
Other income and expenses		(xxx)	(xxx)	
Profit before tax		xxx	xxx	
Income tax expenses		(xxx)	(xxx)	IAS 1:82(d), IAS 12:77
Profit for the year		xxx	xxx	IAS 1:81A

9.0 DISCLOSURE

An entity shall disclose qualitative and quantitative information about:

- the amounts recognised in its financial statements for contracts within the scope of IFRS 17 (see paragraphs 97–116);
- the significant judgements, and changes in those judgements, made when applying IFRS 17 (see paragraphs 117–120); and
- the nature and extent of the risks from contracts within the scope of IFRS 17 (see paragraphs 121–132).

41 IFRS 17: 80, B120–B136

42 Good Life Insurance (International) Limited – IFRS 17 General Model (EY, 2021) https://www.ey.com/en_gl/ifrs-technical-resources/good-life-insurance-international-limited

9.1 Transitional Disclosures

An entity is expected to disclose the following information under significant accounting policies in the Notes to the Financial Statements:

9.1.1 The type of insurance contracts issued and how these are accounted for applying IFRS 17

For Example: The Company issues the following types of contracts that are accounted for in accordance with IFRS 17:

- a) Motor and home insurance policies:

These comprise comprehensive and third-party liability car insurance policies as well as home insurance policies for contents and buildings with coverage of one year or less. The Company accounts for these contracts applying the Premium Allocation Approach (PAA).

9.1.2 The significant accounting policies used

Insurers are expected to include the following information:

- a) Combining a set or series of contracts
- b) Separating components from insurance and reinsurance contracts
- c) Level of aggregation
- d) Initial and subsequent recognition
- e) Measurement of insurance contracts issued

9.1.3 Key sources of estimation uncertainty

For an insurer, these may include:

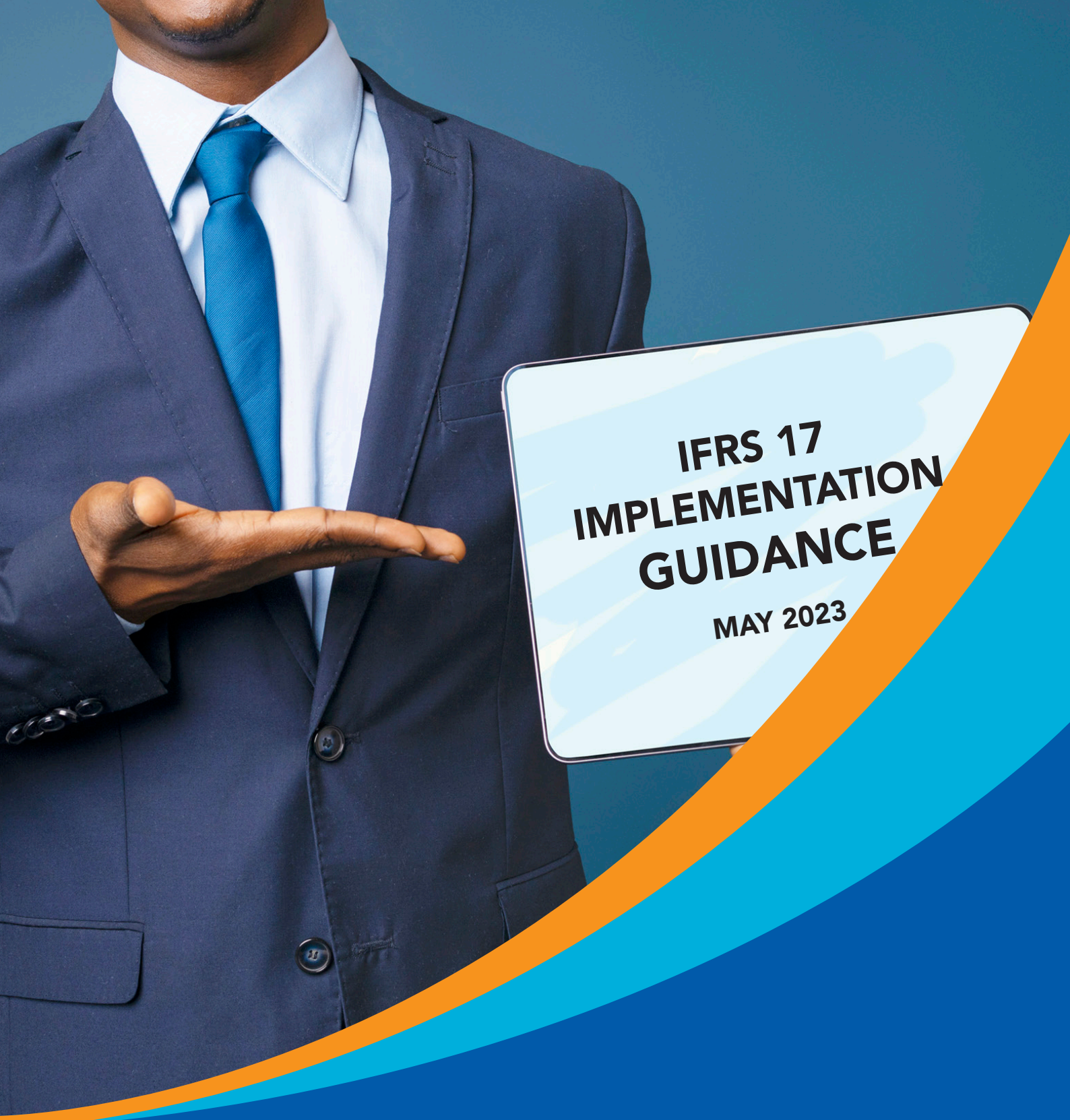
- a) Future cashflows
- b) Discount rates
- c) Allocation rate for insurance finance income or expenses
- d) Risk adjustment for non-financial risk

9.1.4 Critical judgements in applying the group's accounting policies

The following are the expected critical judgements:

- a) Assessment of significance of insurance risk
- b) Combination of insurance contracts
- c) Separation of insurance and non-insurance components from insurance contracts
- d) Identification of portfolios
- e) Applying the level of aggregation
- f) Assessment of directly attributable cashflows

- g) Assessment of eligibility for the Premium Allocation Approach
- h) Assessment of significance of modification




IFRS 17 IMPLEMENTATION GUIDANCE

MAY 2023

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