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STAFF PAPER

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Project	Transition Resource Group for IFRS 17 *Insurance Contracts*		
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This agenda paper is reposted for corrections to the examples included in paragraphs 39-44, B3(b) and B5(d). Those corrections do not change the accounting analysis provided in this paper.

Introduction

1. We have received a number of submissions about amounts exchanged between the issuer of a reinsurance contract (the reinsurer) and the holder of a reinsurance contract (the cedant). The submissions question how the following should be accounted for in the financial statements of the reinsurer:

   (a) common types of commissions due to the cedant; and

   (b) reinstatement premiums charged to the cedant following the occurrence of an insured event.

2. The objective of the paper is to provide background and an accounting analysis to support discussion at the Transition Resource Group for IFRS 17 *Insurance Contracts* (TRG).

Structure of the paper

3. This paper includes the following:
    (a) background information (paragraphs 5–14).
    (b) implementation question (paragraphs 15–17).
    (c) review of accounting requirements:
        (i) commissions that are not contingent on claims (paragraphs 18–35);
        (ii) commissions that are contingent on claims (paragraphs 35–46); and
        (iii) reinstatement premiums (paragraphs 47–58).
4. This paper includes two appendices:
    (a) Appendix A—Flowchart; and
    (b) Appendix B—Examples of commissions and other contract features contingent on claims.

Background information

5. Paragraph 42(a) of IFRS 17 requires an entity to recognise insurance service expenses for claims incurred in the period.
6. Paragraph 83 of IFRS 17 states:

> An entity shall present in profit or loss insurance revenue arising from the groups of insurance contracts issued. Insurance revenue shall depict the provision of coverage and other services arising from the group of insurance contracts at an amount that reflects the consideration to which the entity expects to be entitled in exchange for those services. Paragraphs B120–B127 specify how an entity measures insurance revenue.

7. Paragraph 86 of IFRS 17 sets out the requirements for presenting income or expense from a group of reinsurance contracts held. It states:

> An entity may present the income or expenses from a group of reinsurance contracts held (see paragraphs 60–70), other than insurance finance income or expenses, as a single amount; or the entity may present separately the amounts recovered from the reinsurer and an allocation of the premiums paid that together give a net amount equal to that single amount. If an entity presents separately the amounts recovered from the reinsurer and an allocation of the premiums paid it shall:
>
> (a) treat reinsurance cash flows that are contingent on claims on the underlying contracts as part of the claims that are expected to be reimbursed under the reinsurance contract held
>
> (b) treat amounts from the reinsurer that it expects to receive that are not contingent on claims of the underlying contracts (for example, some types of ceding commissions) as a reduction in the premiums to be paid to the reinsurer; and
>
> (c) not present the allocation of premiums paid as a reduction in revenue.

8. Paragraph B123 of IFRS 17 requires that insurance revenue for a period relating to the provision of services is determined based on the changes in the liability for remaining coverage excluding changes that do not relate to services expected to be covered by the consideration received by the entity. Changes that do not relate to services expected to be covered by the consideration received by the entity include changes that do not relate to services provided in the period, such as changes resulting from the receipt of cash for premiums and changes that relate to investment components in the period. Insurance revenue for a period relating to insurance acquisition cash flows is determined as set out in paragraph B125 of IFRS 17.

9. Paragraph B126 of IFRS 17 states that when an entity applies the premium allocation approach, insurance revenue for the period is the amount of expected premium receipts (excluding any investment component and adjusted to reflect

the time value of money and the effect of financial risk, if applicable) allocated to the period.

10. Appendix A of IFRS 17 defines insurance acquisition cash flows as:

> 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. Such cash flows include cash flows that are not directly attributable to individual contracts or groups of insurance contracts within the portfolio.

11. Appendix A of IFRS 17 defines an investment component as:

> The amount that an insurance contract requires the entity to repay to a policyholder even if an insured event does not occur.

12. Paragraph BC34 of the Basis for Conclusions on IFRS 17 explains that the International Accounting Standards Board (Board) decided that an investment component should be defined as the amount that is paid to the policyholder in all circumstances, regardless of whether the insured event occurs. In the Board's view, the insurance benefit is the additional amount that the entity would be required to pay if an insured event occurs.

13. Paragraph BC299 of the Basis for Conclusions on IFRS 17 explains:

> The amount an entity pays for reinsurance coverage consists of premiums the entity pays minus any amounts paid by the reinsurer to the entity to compensate the entity for expenses it incurs, such as underwriting or acquisition expenses (often referred to as 'ceding commissions'). […]

14. Paragraph BC346 of the Basis for Conclusions on IFRS 17 provides explanation about the economic effect of the commissions describes in paragraph 86 of IFRS 17:

> […] IFRS 17 allows an entity to present income or expenses from reinsurance contracts held either as a single net amount or as separate amounts recovered from the reinsurer and an allocation of the premiums paid. If it presents separate amounts, IFRS 17 requires the entity to treat:

(a) cash flows contingent on the claims or benefits in the underlying contracts, including ceding commissions, as part of the claims that are expected to be reimbursed under the reinsurance contract held, unless those cash flows need to be accounted for as investment components. In the Board's view, the economic effect of changes in those cash flows is equivalent to the effect of reimbursing a different amount of claims than expected.

(b) ceding commissions that are not contingent on claims of the underlying contracts as a reduction of the premiums to be paid to the reinsurer. The economic effect of such ceding commissions is equivalent to the effect of charging a lower premium with no ceding commissions.

Implementation question

15. The submissions describe common types of commissions due from a reinsurer to a cedant and question how these should be accounted for in the financial statements of the reinsurer. The submissions describe both:

    (a) commissions that are not contingent on claims; and

    (b) commissions that are contingent on claims.

16. The submissions ask:

    (a) for each type of commission, whether it is considered part of the premium or part of claims.

    (b) whether all or some of the amounts related to these commissions meet the definition of:

        (i) insurance acquisition cash flows; or

        (ii) an investment component.

17. The submissions also describe reinstatement premiums charged to a cedant of a reinsurance contract following the occurrence of an insured event. The submissions question how these reinstatement premiums should be accounted for

in the financial statements of the reinsurer. One of the submissions distinguishes between mandatory and voluntary reinstatement premiums.

Review of accounting requirements

Commissions that are not contingent on claims

18. The commission is described in the submissions as an amount due from the reinsurer to the cedant with the following characteristics:[1]

    (a) the amount of the commission due to the cedant is often settled net with the premium charged to the cedant (or otherwise paid upfront); and

    (b) the amount of the commission due to the cedant is not dependent on claims or is otherwise fixed.

19. One of the submissions provides the following example:

Cash flow	Description	Amount
Reinsurance premium	60% of premium on underlying insurance contracts	6,000
Ceding commission	30% of reinsurance premium (6,000 x 30%)	1,800
Net amount	Amount received from the cedant (reinsurance premium minus ceding commission)	4,200

20. Exchanges between a reinsurer and a cedant need to be identified as either part of claims or part of premiums for the reinsurer that issues the contract to either recognise these amounts within claims incurred as insurance service expenses

[1] The submissions note that the existing practice for these types of commissions is to present the commission separately as an acquisition expense, ie it is not netted against the premium.

applying paragraph 42(a) of IFRS 17 or recognise these amounts as insurance revenue applying paragraph B123 or B126 of IFRS 17.

21. IFRS 17 does not provide specific requirements for determining whether exchanges between the entity and the policyholder are part of the premium or part of claims, except with respect to the presentation of income or expenses from reinsurance contracts held in paragraph 86 of IFRS 17.

22. The staff observe that the requirements for the presentation of income or expenses from reinsurance contracts held are based on the economic effect of exchanges between the reinsurer and the cedant, and therefore the staff consider that an assessment of the economic effect of such exchanges would be appropriate to apply to reinsurance contracts issued as well.

23. The staff observe that the economic effect of ceding commissions that are not contingent on claims, such as in the example in paragraph 19 of this paper, is equivalent to the effect of charging a lower premium with no ceding commission. Therefore, the ceding commission is part of the premium and, applying paragraph B123 or B126 of IFRS 17, insurance revenue for the reinsurer in this example should be 4,200 for the contract.

24. For the example in paragraph 19 of this paper, assume that the group of insurance contracts comprises a single reinsurance contract and that the group is recognised on the day that the premium (net of commission) is settled. The expected claims are 3,500. For simplicity, the risk adjustment for non-financial risk is nil and the discount rate is 0%. The entity determines the following:

    (a) the liability for remaining coverage at initial recognition is 4,200 consisting of fulfilment cash flows of 3,500 and a contractual service margin of 700 (4,200 - 3,500). Applying paragraph B123 of IFRS 17, the change in the liability for remaining coverage during the coverage period is 4,200, reflecting the insurance revenue. If, alternatively the commission was expected to be paid after the day of initial recognition, the same revenue of 4,200 would be recognise because the total change in the liability for remaining coverage would be 6,000 and applying paragraph B123(a) of IFRS 17 the change that relates to the commission of 1,800 would be considered related to premium and therefore would be eliminated from the total change to arrive at the insurance revenue.

(b) alternatively, insurance revenue of 4,200 can be analysed applying paragraph B124 of IFRS 17 as consisting of the expected insurance service expenses of 3,500 and the contractual service margin recognised in profit or loss of 700.

(c) applying paragraph B126 of IFRS 17, the amount of expected premium receipts allocated over the coverage period as revenue is 4,200.

25. The submission also considers whether the ceding commission in the example in paragraph 19 of this paper meets the definition of insurance acquisition cash flows.

26. Another submission notes that in some reinsurance contracts such ceding commissions are fixed, not adjusted subsequently and not repaid in any circumstances. This submission considers whether these ceding commissions meet the definition of insurance acquisition cash flows, noting that the commission would be paid even if no premium is ceded eventually, and therefore may not be considered as an adjustment to the premium for the contract.

27. Insurance acquisition cash flows are defined as cash flows arising from costs—the costs of selling, underwriting and starting a group of insurance contracts. The staff observe that unless the cedant provides a distinct service to the reinsurer that results in a cost to the reinsurer for selling, underwriting and starting a group of reinsurance contracts that it issues, the ceding commission reflects a reduction in the transaction price, and not insurance acquisition cash flows of the reinsurer. The ceding commission may reflect compensation that the reinsurer provides the cedant for acquisition costs that the cedant incurs for underlying insurance contracts, but this does not make the commission an acquisition costs of the reinsurer. While the activities taken by the cedant to sell, underwrite and start a group of underlying insurance contracts may benefit the reinsurer, the cedant

undertakes these activities in its own right in order to sell insurance contracts to its policyholders, rather than to provide a distinct service to the reinsurer. If the cedant were to undertake activities and incur costs in order to provide a distinct service to the reinsurer, those costs may not meet the definition of insurance acquisition cash flows from the cedant's perspective.

28. The staff observe that unlike insurance acquisition costs that are usually paid, for example, to a third-party intermediary, ceding commissions are paid by the reinsurer to the cedant who is the customer buying the contract.

29. The staff observe that for circumstances in which ceding commissions are fixed, not adjusted subsequently, not repaid in any circumstances and the reinsurer expects that no premium would be ceded or that the expected premium is insufficient to recover the costs of fulfilling the contracts (including the commission), the reinsurance contract issued would be considered an onerous contract.

30. One of the submissions also considers whether the ceding commission in this example is an investment component. An investment component is an amount that an insurance contract requires the entity to repay to a policyholder even if an insured event does not occur and is excluded from the insurance service expenses and insurance revenue. The staff observe that ceding commissions may meet the definition of investment component if they are *repaid* to the cedant in *all circumstances*.

31. However, for the fact pattern provided, the staff view is that the ceding commission is not an investment component even if it is an amount due to the cedant in all circumstances. This is because it is settled net of premium charged to the cedant. In this example, no payment to the reinsurer or from the reinsurer after the premium is received includes amounts that the reinsurer is required to *repay* to the cedant in all circumstances. If, alternatively, the ceding commission was paid to the cedant at a later date than the premium is received, the ceding commission may meet the definition of an investment component. This is because in this case it would reflect a financial component within the insurance contract recognised,

similar to a deposit. The outcome, in terms of excluding the commission from the contract revenue would be the same, however in this case, additional disclosures related to investment components may be required applying paragraph 103(c) of IFRS 17.

32. One of the submissions questions whether ceding commissions that are fixed, not adjusted subsequently and not repaid in any circumstances can be considered a compensation for a distinct service that the cedant is providing to the reinsurer. The submission notes that the cedant may have promised the reinsurer to manage sales and underwriting, claims handling and other administrative matters related to the contract, and that judgement should be applied to consider whether a distinct service is provided to the reinsurer and an intangible asset may be recognised with respect to the commission.

33. Although the staff agree that entities should consider all relevant facts and circumstances and apply judgement to determine whether a separate service is being provided to the reinsurer within the reinsurance contract, the staff do not think a service is being provided in the specific fact pattern provided. While managing sales, underwriting and handling claims of the contract may benefit the reinsurer, it is not a service provided by the cedant to the reinsurer, rather it is an activity the cedant undertakes in its own right to fulfil the insurance contracts it has issued.

34. In summary, the staff observe that amounts exchanged between the issuer of an insurance contract and the policyholder that are not contingent on claims:

    (a) are part of the premium and would therefore be recognised as part of the insurance revenue; and

    (b) if paid after the premium is received, may meet the definition of an investment component, provided the amounts are repaid to the policyholder in all circumstances.

Commissions that are contingent on claims

35. Commissions that are contingent on claims are commissions that are adjusted according to the claims that are incurred. One of the submissions refers to contracts with such commissions and other contracts with similar features as retrospectively rated contracts, noting that those features are common in reinsurance contracts and commercial line insurance contracts. That submission notes that these types of commissions can be used when the reinsurer and the cedant cannot agree on a fixed price for the risk or when the cedant wants to participate in the benefits of controlling its claims.

36. The submissions provide a number of examples. The discussion in this paper uses a sliding scale commission as an example to facilitate the analysis. Additional examples are provided in Appendix B to this paper.

37. The submission describes the sliding scale commission as an amount due from the reinsurer to the cedant.[2] The terms of the sliding scale commission are as follows:

    (a) the commission amount is dependent on the loss experience of the contract, while a minimum amount is due to the cedant regardless of the loss experience of the contract;

    (b) a provisional commission amount is settled net with the premium charged to the cedant; and

    (c) the final commission amount is determined, and any adjustments to the provisional amount are settled several years after the coverage period, when all claims are fully paid.

[2] The submission notes that the existing practice for these types of commissions is to present the commission separately as expense, ie it is not netted against the premium.

38. The submission provides the following example:

Cash flow	Description	Amount
Reinsurance premium	60% of premium on underlying insurance contracts	6,000
Provisional commission	30% of reinsurance premium assuming a 65% loss ratio[3] (6,000 x 30%)	1,800
Net amount initially received	Amount received from the cedant (reinsurance premium minus provisional ceding commission)	4,200

The commission due to the cedant is between 20% and 40% of the reinsurance premium, contingent on the loss ratio of the contract. Adjustments to the provisional commission amount based on the ultimate loss ratio of the contract are determined and settled several years after the coverage period as follows:

Loss ratio	Commission as % of reinsurance premium	Amount
Above 75%	Minimum commission of 20%	1,200
55%–75%	Commission in the range of 20%–40%	Sliding scale
Below 55%	Maximum commission of 40%	2,400

39. Considering the economic effect of the ceding commission, the staff have analysed the cash flows from the ceding commission as not contingent on claims—in this example the amount that is due to the cedant regardless of the loss experience of the contract is 2,400. If there are no claims, cash flows of 2,400 are due to the cedant.[4] If there are claims, the cedant receives 2,400 plus a portion of

[3] Loss ratio is a measurement reflecting the loss experience of a contract.

[4] If claims are 0 the commission is 2,400 because the loss ratio is below 55%.

the amount claimed.[5] It does not matter whether the amounts are described as commissions or as claims, or as a combination depending on insurance outcomes.

40. Consistent with the analysis in paragraphs 22–23 of this paper, for this example the staff view the economic effect of the ceding commission as equivalent to the effect of charging a lower premium.

41. In other words, for this example, the economic effect of the commission is equivalent to the effect of charging a premium of 3,600 rather than 6,000. The analysis provided in paragraphs 22–23 of this paper for commissions that are not contingent on claims is therefore relevant.

42. Therefore, applying paragraph B123 of IFRS 17 or paragraph B126 of IFRS 17, insurance revenue for the reinsurer in this example should be 3,600 for the contract.

43. The submission considers whether the ceding commission in this example is, or includes, an investment component. Consistent with the analysis in paragraphs 30–31 of this paper, the staff observe that in this example the provisional ceding commission is not an investment component. In the fact pattern provided, the provisional ceding commission is settled net of premium charged to the cedant. The excess of 2,400 over the provisional commission of 1,800 will meet the definition of an investment component if it is an amount that will be repaid at a future date to the cedant in all circumstances (for example, also on cancellation of the contract).

44. Treating the additional amount that the reinsurer is required to repay to the cedant as an investment component reflects that the contract with the cedant includes a financial component, similar to a deposit.

45. The staff observe that the ceding commission, or any part of it, is not an insurance acquisition cash flow as discussed in paragraphs 27–28 of this paper, nor does it

[5] For example, if there are claims of 5,000 the commission is 1,200 because the loss ratio is above 75%.

reflect a distinct service provided by the cedant to the reinsurer as discussed in paragraph 33 of this paper.

46. In summary, the staff observe that amounts exchanged between the issuer of an insurance contract and a policyholder that are contingent on claims (ie the amounts excluding any minimum amounts that are, in effect, non-contingent) are part of claims and would therefore be recognised as part of insurance service expenses.

Reinstatement premiums

47. The reinstatement premium is described in the submissions as an amount charged to the cedant following an insured event occurring in order to continue coverage. One of the submissions distinguishes between mandatory and voluntary reinstatement premiums. The analysis in this paper is provided separately for each type of reinstatement premium.

Mandatory reinstatement premiums

48. One of the submissions provides a fact pattern of a mandatory reinstatement premium. The reinstatement premium is predetermined. This means that no additional underwriting or repricing can be done. It is assumed that the reinstatement premium is compulsory and it is assumed that the contract cannot be terminated before the end of its contractual term. The submission also provides the following information about the reinstatement premium:

   (a) the reinstatement premium amount is contingent on the claim amount;

   (b) if no insured event occurs, no reinstatement premium is charged to the cedant (ie there is no minimum reinstatement premium amount that is paid in all circumstances); and

   (c) the reinstatement premium is settled net with the claims paid to the cedant (reduces claims).

49. The submission provides the following example:[6]

Cash flow	Description	Amount
Reinsurance premium	Amount charged for coverage (see limit per claim and aggregate limit below)	250
Claim limit	Maximum amount that can be claimed per claim event	1,000
Aggregate claims limit	Maximum amount that can be claimed under the contract	2,000

The reinstatement premium is charged when a claim is incurred. The amount is based on a percentage of the premium charged and the amount of claims made. The following are examples of possible scenarios under the contract:

Scenario	Reinstatement premium	Amount
No claims	The cedant will not be charged an additional reinstatement premium	0
Claim of 100	The reinstatement premium is determined as 250 reinsurance premium x 10% of claim limit used (100/1,000)	25
Claims of 1,500 (from two events)	Maximum reinstatement premium of 250 (using all of the claim limit of 1,000 would require 100% of additional premium to be paid).	250

[6] The submission notes that the existing practice for this example is that the reinstatement premium is treated as a separate cash flow and presented separately to the premium for the contract. It is not netted against claims incurred.

50. The staff considered the economic effect of the reinstatement premium in this example to determine whether it reflects an additional premium or a reduction in the amount paid for claims.

51. The staff observe that the economic effect of the reinstatement premium is equivalent to the effect of reimbursing a different amount of claims to the cedant. In other words, for this example, the economic effect of a reinstatement premium is equivalent to the effect of charging a premium of 250 and paying 75% of the claims up to 1,000 and 100% of additional claims up to 2,000.

52. Therefore, applying paragraph B123 of IFRS 17 or paragraph B126 of IFRS 17, insurance revenue for the reinsurer in this example should be 250 for the contract. Any reinstatement premium would be recognised as part of insurance service expenses when incurred.

53. One of the submissions considers whether mandatory reinstatement premiums represent a premium of a new reinsurance contract. The staff observe that cash flows related to claims are within the contract boundary of the reinsurance contract issued, as well as the reinstatement premiums that accompany them. Therefore, mandatory reinstatement premiums cannot be considered cash flows related to a future contract.

Voluntary reinstatement premiums

54. A voluntary reinstatement premium is an amount charged to the cedant, on predetermined terms, following an insured event occurring. However, in contrast to the mandatory reinstatement premium, the cedant can decide not to pay the reinstatement premium and in this case the contract terminates. This means that voluntary reinstatement premiums are not contingent on claims as the cedant may decide to avoid paying those premiums and terminate the coverage instead.

55. The reinsurer is required to accept reinstatement premiums and to provide the related coverage.

56. One of the submissions considers whether voluntary reinstatement premiums represent a premium of a new reinsurance contract.

57. The staff observe that the economic effect of a voluntary reinstatement premium is equivalent to the effect of charging a higher premium to extend the contract coverage to an additional period/higher level of exposure.

58. The staff observe that applying paragraph 34 of IFRS 17, the reinstatement premium and related cash flows are within the boundary of the initial reinsurance contract. In the fact pattern provided, the reinsurer has no right to exit the contract and has no right to reprice the contract (the reinstatement premium is at predetermined rates). Therefore the expected cash flows related to the reinstatement premium are within the boundary of the initial reinsurance contract and voluntary reinstatement premiums cannot be considered cash flows related to a future contract.[7]

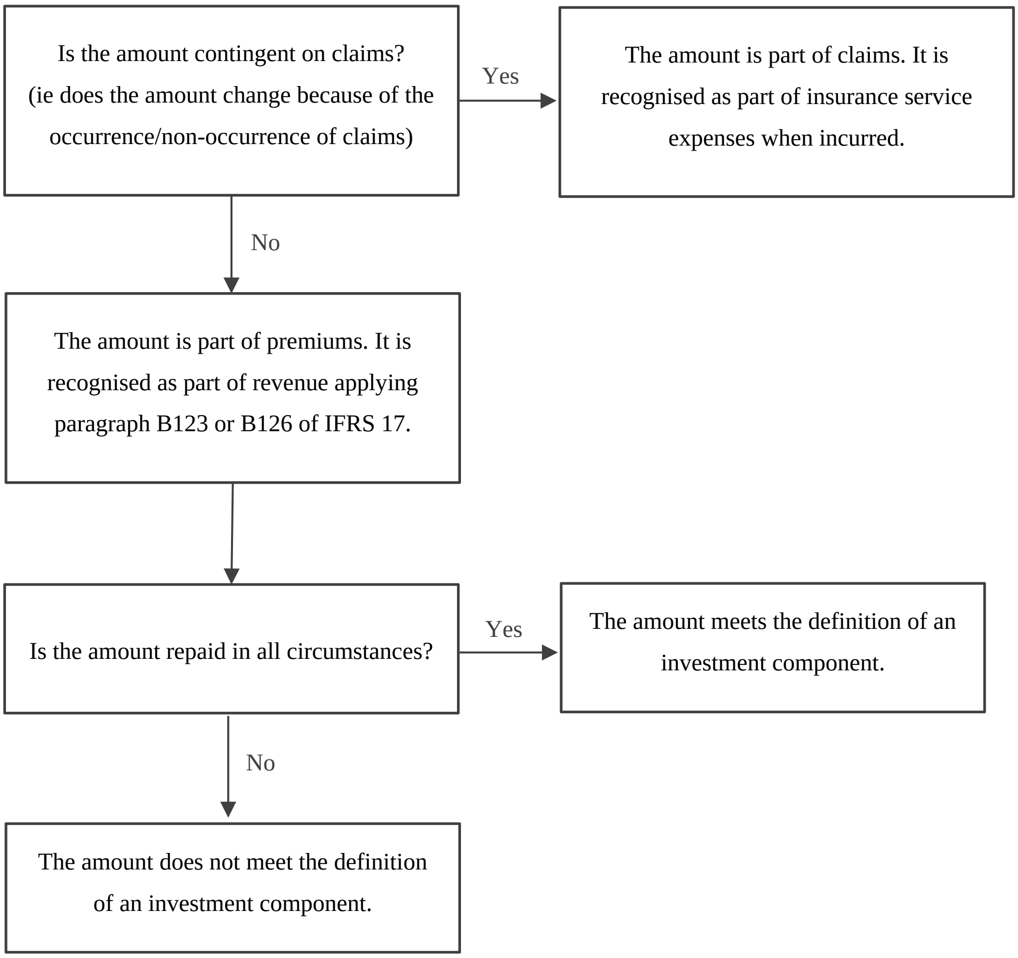
TRG Discussion

Question to TRG members
What are your views on the implementation question presented above?

[7] Agenda paper 3 *Cash flows within the contract boundary* from May 2018 TRG meeting and Agenda paper 5 *Cash flows that are outside the contract boundary at initial recognition* of the September 2018 TRG meeting discuss the topic of the boundary of an insurance contract in more detail.

Appendix A—Flowchart

A1. The following flowchart may assist the assessment of how to account for exchanges between a reinsurer and a cedant.[8]



[8] It is assumed that amounts due to the cedant are not compensation paid to it for a distinct service it provides to the reinsurer.

Appendix B—Examples of commissions and other contract features contingent on claims

Profit commission

B1. In the example, the profit commission is determined as 25% of the profit under the contract. The profit under the contract is the difference between the premiums and losses assumed by the reinsurer. The commission cannot be negative. The fact pattern is as follows:

Description	Amount
Reinsurance premium	1,000
Profit commission (profit = reinsurance premium minus claims incurred by the reinsurer under the contract)	25%

B2. The profit commission is contingent on the amount of losses assumed by the reinsurer under the contract, for example:

Claims	Calculation of commission	Profit commission	Total payment to cedant
0	(1,000 – 0) x 25%	250	250
100	(1,000 – 100) x 25%	225	325
500	(1,000 – 500) x 25%	125	625
1,500	1,000 – 1,500 = 500 loss	0	1,500

B3. Staff analysis applying IFRS 17:

(a) in all circumstances, the reinsurer will pay to the cedant a minimum amount of 250. All other payments to the cedant are contingent on claims.

(b) the staff observe that the economic effect of the profit commission is equivalent to the effect of charging a lower premium to the same extent. In other words, for this example, the economic effect of the profit commission is equivalent to the effect of charging a premium of 750 and paying 75% of the claims up to 1,000 and 100% of claims above 1,000.

(c) therefore, applying paragraph B123 of IFRS 17 or paragraph B126 of IFRS 17, insurance revenue for the reinsurer in this example should be 750 (1,000 - 250) for the contract. In the third scenario shown in which the claims are 500, the claims incurred applying IFRS 17 should be 375 (500 x 75%) for the contract and there would not be an additional/separate expense of 125 for the profit commission paid as this amount is part of the premium.

(d) assuming the cedant paid the premium of 1,000 at the inception of the contract, an amount of 250 may meet the definition of investment component.

Adjustments to premiums in a retrospectively rated insurance contract

B4. One of the submissions provides two examples of retrospectively rated contracts:

(a) contract 1—a premium of 200 is paid at the beginning of the coverage period, however an additional premium of 80% of claims is charged to the policyholder, up to a maximum additional premium of 800.

(b) contract 2—a premium of 1,000 is paid at the beginning of the coverage period, however the insurer will refund the policyholder 80% of any profit on the contract.

B5. Staff analysis applying IFRS 17:

(a) contract 1—a premium of 200 paid at the beginning of the coverage period is the contract premium applying IFRS 17 as this amount is not contingent on claims. An additional premium up to a maximum of 800 is contingent on claims as it is charged to the policyholder only if claims incur under the contract. The additional premium therefore is part of the claims and shall be recognised as part of insurance service expenses.

(b) contract 2—the premium of 1,000 paid at the beginning of the coverage period is the contract premium applying IFRS 17, however an amount of 800 may meet the definition of an investment component. An amount of 800 is not contingent on claims because it would be refunded to the policyholder if no claims occur (assuming 80% of the profit equals 80% of the premium in this simplified example) and it would be refunded to the policyholder if the maximum amount of claims occur (if the amount of claim is, for example, 1,500 – 800 of which is a premium refund). If an amount of 800 would be repaid to the policyholder in all circumstances it would meet the definition of investment component and therefore the insurance revenue for the contract would be 200.

(c) the staff observe that both contracts seem economically similar and therefore the contract revenue for both is the same. However, if contract 2 contains an investment component, it has a financial component that contract 1 does not have, and this would impact the financial income or expenses of contract 2.

(d) the staff observe that if under contract 2, the amount of 800 is not repaid to the policyholder in all circumstances (for example, if the contract is cancelled) this amount would not meet the definition of investment component.