IFRS

STAFF PAPER

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Project	Transition Resource Group for IFRS 17 *Insurance Contracts*		
Paper topic	Recovery of insurance acquisition cash flows		
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Introduction

1. We have received a submission about whether insurance acquisition cash flows and the related revenue are recognised in the statement(s) of financial performance applying paragraph B125 of IFRS 17 if those cash flows cannot be recovered from the cash flows of the portfolio of contracts.

2. We have also received a submission about the accounting for changes in insurance acquisition cash flows applying paragraphs B123 and B125 of IFRS 17.

3. 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

4. This paper includes the following:

    (a) background information;

    (b) implementation question; and

    (c) review of accounting requirements.

5. There are three appendices to this paper:

    (a) Appendix A—Paragraphs explaining the requirements for insurance acquisition cash flows in the Basis for Conclusions on IFRS 17;

    (b) Appendix B—Examples of applying the requirements in paragraphs B123 and B125 of IFRS 17 when insurance acquisition cash flows are not included in expected future cash flows; and

    (c) Appendix C—Examples of applying the requirements in paragraphs B123 and B125 of IFRS 17 when insurance acquisition cash flows are included in expected future cash flows.

Background information

6. On measuring the contractual service margin at initial recognition, paragraph 38 of IFRS 17 states:

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

(b) the derecognition at the date of initial recognition of any asset or liability recognised for insurance acquisition cash flows applying paragraph 27; and

(c) any cash flows arising from the contracts in the group at that date.

7. On identifying insurance contracts that are onerous at initial recognition paragraph 47 of IFRS 17 states:

> An insurance contract is onerous at the date of initial recognition if the fulfilment cash flows allocated to the contract, any previously recognised acquisition cash flows and any cash flows arising from the contract at the date of initial recognition in total are a net outflow. […]

8. 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.

9. On recognising insurance revenue, paragraphs B120–B125 of IFRS 17 state:

> B120 The total insurance revenue for a group of insurance contracts is the consideration for the contracts, ie the amount of premiums paid to the entity:
>
> (a) adjusted for a financing effect; and
>
> (b) excluding any investment components.
>
> B121 Paragraph 83 requires the amount of insurance revenue recognised in a period to depict the transfer of promised services at an amount that reflects the consideration to which the entity expects to be entitled in exchange for those services. The total consideration for a group of contracts covers the following amounts:
>
> (a) amounts related to the provision of services, comprising:

(i) insurance service expenses, excluding any amounts allocated to the loss component of the liability for remaining coverage;

(ii) the risk adjustment for non-financial risk, excluding any amounts allocated to the loss component of the liability for remaining coverage; and

(iii) the contractual service margin.

(b) amounts related to insurance acquisition cash flows.

B122 Insurance revenue for a period relating to the amounts described in paragraph B121(a) is determined as set out in paragraphs B123–B124. Insurance revenue for a period relating to amounts described in paragraph B121(b) is determined as set out in paragraph B125.

B123 Applying IFRS 15, when an entity provides services, it derecognises the performance obligation for those services and recognises revenue. Consistently, applying IFRS 17, when an entity provides services in a period, it reduces the liability for remaining coverage for the services provided and recognises insurance revenue. The reduction in the liability for remaining coverage that gives rise to insurance revenue excludes changes in the liability that do not relate to services expected to be covered by the consideration received by the entity. Those changes are:

(a) changes that do not relate to services provided in the period, for example:

[…]

(v) insurance acquisition cash flows (see paragraph B125); […]

B124 […]

B125 An entity shall determine insurance revenue related to insurance acquisition cash flows by allocating the portion of the premiums that relate to recovering those cash flows to each reporting period in a systematic way on the basis of the passage of time. An entity shall recognise the same amount as insurance service expenses.

Implementation question

10. One of the submissions asks whether insurance acquisition cash flows and the related revenue are recognised in the statement(s) of financial performance applying paragraph B125 of IFRS 17 if those cash flows cannot be recovered from the cash flows of the portfolio of contracts.

11. The submission expresses two views. The first is that if insurance acquisition cash flows are not recoverable, the portion of the premiums that relate to recovering those cash flows is nil applying paragraph B125 of IFRS 17. The second is that amounts related to insurance acquisition cash flows are presented as insurance revenue and insurance service expenses applying paragraph B125 of IFRS 17 regardless of whether or not the group of insurance contracts is onerous.

12. The second submission is about the accounting for changes in insurance acquisition cash flows applying paragraphs B123 and B125 of IFRS 17.

Review of accounting requirements

13. Insurance acquisition cash flows are reflected in the contractual service margin or loss component for a group of insurance contracts on initial recognition. IFRS 17 achieves this by requiring that:

    (a) insurance acquisition cash flows that occur on or before initial recognition are included in the measurement of the contractual service margin or loss component at initial recognition applying paragraphs 38(b)–(c) and 47 of IFRS 17; and

    (b) insurance acquisition cash flows that are expected to occur after initial recognition are included in the fulfilment cash flows at initial recognition applying paragraphs 38(a) and 47 of IFRS 17.

14. This means that insurance acquisition cash flows are treated in the same way as other cash flows incurred in fulfilling insurance contracts. The way that the measurement model in IFRS 17 works means that an entity is not required to separately identify whether it will recover insurance acquisition cash flows at each reporting date. For example, if premiums are lower than the sum of insurance acquisition cash flows and other cash flows incurred in fulfilling the contracts, the entity is not required to determine how much of the premium relates to recovering the insurance acquisition cash flows and how much of the premium relates to recovering the other cash flows incurred in fulfilling the contracts. Paragraph BC180 of the Basis for Conclusions on IFRS 17 explains that this is because the measurement model captures any lack of recoverability automatically by remeasuring the fulfilment cash flows.

15. Insurance revenue is determined by applying both paragraphs B123 and B125 of IFRS 17. Because an entity is not required to separately identify whether it will recover insurance acquisition cash flows, any reduction in the contractual service margin or any loss component recognised because premiums are lower than expected cash outflows (consisting of both insurance acquisition cash flows and other cash flows incurred in fulfilling the contracts) affects insurance revenue recognised applying paragraph B123 of IFRS 17. The staff observe that paragraph B125 of IFRS 17 assumes that the portion of premiums relating to the recovery of insurance acquisition cash flows is equal to the current estimate of total expected insurance acquisition cash flows at each reporting period. Appendix B and Appendix C to this paper include seven examples to illustrate how paragraphs B123 and B125 of IFRS 17 work together.

16. In some cases, the premiums may be or may become less than the insurance acquisition cash flows. In those cases, it is clear that some or all of the insurance acquisition cash flows are not recoverable. Because an entity is not required to separately identify how much of the premium relates to recovering insurance acquisition cash flows, when looking at the amount of insurance revenue determined applying paragraph B125 of IFRS 17 in isolation, the insurance

revenue would appear to be an amount that is higher than the premiums. The staff observe that paragraphs B123 and B125 of IFRS 17 work together to achieve an insurance revenue that reflects the total premium (adjusted for a financing effect and excluding any investment component) as required by paragraph B120 of IFRS 17. Therefore, the insurance revenue determined applying paragraphs B123 and B125 of IFRS 17 should be considered together and not in isolation. Example 4 in Appendix B to this paper demonstrates how paragraphs B123 and B125 of IFRS 17 work together when premium becomes lower than insurance acquisition cash flows.

17. The staff observe that insurance acquisition cash flows may change over time, ie they may be settled or expected to be settled in an amount different than originally expected. Changes in the insurance acquisition cash flows should not impact the overall revenue recognised from a group of insurance contracts as they do not affect the total premiums (adjusted for a financing effect and excluding any investment components). However, the actual amount of insurance acquisition cash flows should be recognised as expenses. The staff observe that paragraph B125 of IFRS 17 assumes that the portion of premiums relating to the recovery of insurance acquisition cash flows is equal to the current estimate of total expected insurance acquisition cash flows at each reporting period.

18. Paragraph B96(b) of IFRS 17 requires changes in the expected future cash flows in the liability for remaining coverage to adjust the contractual service margin of a group of contracts. Therefore, changes in the expected future cash flows related to insurance acquisition cash flows would adjust the contractual service margin. In addition, the amount recognised applying paragraph B125 of IFRS 17 reflects the updated amount. Example 7 in Appendix C to this paper demonstrates how paragraphs B123 and B125 of IFRS 17 work together with a change in the expected future cash flow in the liability for remaining coverage.

19. Experience adjustments for insurance acquisition cash flows are defined as the difference between the estimate at the beginning of the period of the amounts expected in the period and the actual cash flows in the period.

20. Paragraph B96(a) of IFRS 17 requires that experience adjustments arising from premiums that relate to future service and related insurance acquisition cash flows adjust the contractual service margin. These experience adjustments would be accounted for similarly to changes in the expected future cash flows related to insurance acquisition cash flows, discussed in paragraph 18 of this paper.

21. Paragraph B97(c) of IFRS 17 requires that experience adjustments, except those described in paragraph B96(a) of IFRS 17, shall not adjust the contractual service margin because they do not relate to future service. Experience adjustments for insurance acquisition cash flows related to current or past service are therefore included in insurance revenue and insurance service expenses determined applying paragraph B125 of IFRS 17. Example 6 in Appendix C to this paper demonstrates how paragraphs B123 and B125 of IFRS 17 work together with an experience adjustment that relates to current or past service.

22. In summary:

(a) any reduction in the contractual service margin or any loss component recognised because premiums are lower than expected cash outflows (consisting of both insurance acquisition cash flows and other cash flows incurred in fulfilling the contracts) affects insurance revenue applying paragraph B123 of IFRS 17 (see paragraph 15 of this paper);

(b) changes in expectations for insurance acquisition cash flows adjust the contractual service margin, which is recognised as insurance revenue applying paragraph B123 of IFRS 17 and are also reflected in insurance revenue and insurance service expenses applying paragraph B125 of IFRS 17 (see paragraph 18 of this paper); and

(c) experience adjustments relating to insurance acquisition cash flows affect insurance revenue applying B123 of IFRS 17 and insurance revenue and insurance service expenses applying paragraph B125 of IFRS 17 (see paragraph 21 of this paper).

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Additional points

23. One of the submissions refers to paragraph B65(h) of IFRS 17 which states that policy administration and maintenance costs include recurring commissions that are expected to be paid to intermediaries if a particular policyholder continues to pay premiums within the boundary of the insurance contract. The staff observe that paragraph B65(h) of IFRS 17 relates to commissions that do not meet the definition of insurance acquisition cash flows.

TRG Discussion

Question to TRG members

What are your views on the implementation question presented above?

Appendix A—Paragraphs explaining the requirements for insurance acquisition cash flows in the Basis for Conclusions on IFRS 17

A1. Paragraphs BC175–BC180 of the Basis for Conclusions on IFRS 17 explain the measurement approach for insurance acquisition cash flows:

> BC175 Entities often incur significant costs to sell, underwrite and start new insurance contracts. These costs are commonly referred to as ‘insurance acquisition cash flows’. Insurance contracts are generally priced to recover those costs through premiums or through surrender charges, or both.
>
> BC176 The measurement approach required in IFRS 17 represents a change from many previous accounting models that measure insurance contract liabilities initially at the amount of the premiums received, with deferral of insurance acquisition cash flows. Such models treat insurance acquisition cash flows as a representation of the cost of a recognisable asset, which, depending on the model, might be described as a contract asset or a customer relationship intangible asset. The Board concluded that such an asset either does not exist, if the entity recovers insurance acquisition cash flows from premiums already received, or relates to future cash flows that are included in the measurement of the contract. The Board noted that an entity typically charges the policyholder a price the entity regards as sufficient to compensate it for undertaking the obligation to pay for insured losses and for the cost of originating the contracts. Thus, a faithful representation of the remaining obligation to pay for insured losses should not include the part of the premium intended to compensate for the cost of originating the contracts.
>
> BC177 Consequently, the Board concluded that an entity should recognise insurance acquisition cash flows as an expense, and should recognise an amount of revenue equal to the portion of the premium that relates to recovering its insurance acquisition cash flows. IFRS 17 achieves this by requiring that the cash flows for a group of insurance contracts include the insurance acquisition cash outflows or inflows associated with the group of contracts (including amounts received or to

be received by the entity to acquire new insurance contracts). This approach reduces the contractual service margin on initial recognition of the group of insurance contracts and has the advantage that the insurance acquisition cash flows are treated the same as other cash flows incurred in fulfilling contracts.

BC178 In many cases, insurance acquisition cash flows occur at the beginning of the coverage period of a group of insurance contracts, before any coverage or other service has been provided. Because insurance revenue is recognised in the same pattern as changes in the liability for remaining coverage, this would mean that some of the insurance revenue would be recognised when the insurance acquisition cash flows are paid, often at the beginning of the coverage period.

BC179 The Board was concerned that recognising insurance revenue at the beginning of the coverage period would be inconsistent with the principles in IFRS 15 because, at the beginning of the coverage period, the entity has not satisfied any of the obligations to the policyholder under the contract. In contrast, IFRS 15 requires an entity to recognise as revenue the consideration received from the customer as it satisfies its performance obligations under the contract. Accordingly, the Board decided to include an exception in IFRS 17 for the treatment of insurance acquisition cash flows so that the premium related to insurance acquisition cash flows is not recognised as revenue when the insurance acquisition cash flows occur, but is separately identified and recognised over the coverage period. IFRS 17 also requires the insurance acquisition cash flows to be recognised as an expense over the same period.

BC180 The requirement to recognise insurance acquisition cash flows as an expense over the coverage period differs from recognising an asset or an explicit or implicit reduction in the carrying amount of the group of insurance contracts. At all times, the liability for the group is measured as the sum of the fulfilment cash flows, including any expected future insurance acquisition cash flows, and the contractual service margin. Because the contractual service margin cannot be less than zero, the

> entity need not test separately whether it will recover the insurance acquisition cash flows that have occurred but have not yet been recognised as an expense. The measurement model captures any lack of recoverability automatically by remeasuring the fulfilment cash flows.

A2. On insurance acquisition cash flows included in the measurement of insurance contracts, paragraph BC184 of the Basis for Conclusions on IFRS 17 explains:

> The Board also noted that the measurement approach in IFRS 17 automatically recognises as an immediate expense any insurance acquisition cash flows that cannot be recovered from the cash flows of the portfolio of contracts, because such cash flows reduce the contractual service margin below zero and must therefore be recognised as an expense. Hence, no amount can be recognised in the statement of financial position for insurance acquisition cash flows that are not recoverable.

Appendix B—Examples of applying the requirements in paragraphs B123 and B125 of IFRS 17 when insurance acquisition cash flows are not included in expected future cash flows

B1. This appendix includes four examples demonstrating the treatment of insurance acquisition cash flows that are not included in expected future cash flows. In these four examples all insurance acquisition cash flows are paid on the date of initial recognition and are not adjusted subsequently. The examples are of groups of contracts that are:

(a) Example 1—onerous at initial recognition;

(b) Example 2—profitable at initial recognition and onerous subsequently;

(c) Example 3—profitable at initial recognition and subsequently total premiums are less than the sum of expected cash flows and insurance acquisition cash flows paid; and

(d) Example 4—profitable at initial recognition and subsequently total premiums are less than insurance acquisition cash flows paid.

B2. For simplicity, the following assumptions apply in all examples:

(a) discount rates are 0%;

(b) the risk adjustment for non-financial risk (RA) is zero; and

(c) unless explicitly stated otherwise, services are provided evenly over the coverage period and claims are incurred evenly over the coverage period.

Example 1—onerous at initial recognition

B3. On 1 January 2021 an entity issues a set of 100 insurance contracts with a coverage period of one year. At initial recognition, the entity receives premiums of 1,000 and pays insurance acquisition cash flows of 100. The entity expects future cash outflows of 1,000. Applying paragraph 47 of IFRS 17 the entity determines that the set of insurance contracts is onerous and treats them as an onerous group of insurance contracts applying paragraph 16 of IFRS 17. The contractual service margin (CSM) is zero.

B4. Determining the loss component applying paragraph 47 of IFRS 17:

(a)	Expected future cash flows (CF)	1,000
(b)	Derecognition of any assets or liabilities recognised for insurance acquisition cash flows	0
(c)	Cash flows arising at that date:	
	Insurance acquisition cash flows paid	100
	Premium receipt	(1,000)
	Loss recognised in profit or loss immediately	**(100)**[1]

B5. At 31 December 2021, all events have occurred as expected and all claims have been paid. The change in the insurance contract liability following initial recognition can be analysed as follows:

	CF	**RA**	**CSM**	**Total**
1 January 2021	1,000	0	0	1,000
Cash outflows	(1,000)	0	0	(1,000)
31 December 2021	**0**	**0**	**0**	**0**

B6. The change in the insurance contract liability following initial recognition can also be analysed split between the liability for remaining coverage (LRC) and the liability for incurred claims (LIC) as follows:

[1] Applying IFRS 17 the entity is not required to identify how much of the loss component relates to insurance acquisition cash flows and how much relates to other future expected cash flows.

	LRC		LIC	Total
	Excluding loss component	Loss component		
1 January 2021	900	100	0	1,000
Insurance revenue	(1,000)[2]	0	0	(1,000)
Insurance service expenses:				
Incurred claims	0	0	1,000	1,000
Reversal of losses	0	(100)	0	(100)
Amortisation of insurance acquisition cash flows	100	0	0	100
Cash outflows	0	0	(1,000)	(1,000)
31 December 2021	**0**	**0**	**0**	**0**

B7. Extract of the statement of profit or loss for the year ended 31 December 2021:

Insurance revenue (900 + 100)	1,000
Insurance service expenses (100 + 1,000 – 100 + 100)	(1,100)
Insurance service result	**(100)**

[2] Insurance revenue of 900 applying paragraph B123 of IFRS 17 (the total reduction in the liability for remaining coverage excluding the loss component is 900 which reflects insurance services provided in the period) and 100 applying paragraph B125 of IFRS 17.

Example 2—profitable at initial recognition and onerous subsequently

B8. On 1 January 2021 an entity issues a set of 100 insurance contracts with a coverage period of one year. At initial recognition, the entity receives premiums of 1,000 and pays insurance acquisition cash flows of 100. The entity expects future cash outflows of 800. The entity treats the set of contracts as a group of insurance contracts.

B9. Applying paragraph 38 of IFRS 17 the entity measures the contractual service margin at initial recognition:

(a)	Expected future cash flows	800
(b)	Derecognition of any assets or liabilities recognised for insurance acquisition cash flows	0
(c)	Cash flows arising at that date:	
	Insurance acquisition cash flows paid	100
	Premium receipt	(1,000)
Contractual service margin		**100**

B10. The entity prepares interim reporting for the six months ended 30 June 2021. At 30 June 2021, 600 of claims have been incurred and paid compared to an expected amount of 400 (800/2). The entity changes its expectation for the second half of the year to 600 compared to an expected amount of 400.

B11. The change in the insurance contract liability following initial recognition for the period of six months ended 30 June 2021 can be analysed as follows:

	CF	RA	CSM	Total
1 January 2021	800	0	100	900
Changes related to future service	200	0	(100)	100
Changes related to current service	200	0	0	200
Cash outflows	(600)	0	0	(600)
30 June 2021	**600**	**0**	**0**	**600**

B12. The change in the insurance contract liability following initial recognition can also be analysed split between the LRC and the LIC as follows:

	LRC		LIC	Total
	Excluding loss component	Loss component		
1 January 2021	900	0	0	900
Insurance revenue	(450)[3]	0	0	(450)
Insurance service expenses:				
Incurred claims	0	0	600	600
Recognition of losses	0	100	0	100

[3] Insurance revenue of 400 applying paragraph B123 of IFRS 17 (the total reduction in the liability for remaining coverage excluding the loss component is 400 which reflects insurance services provided in the period) and insurance revenue of 50 applying paragraph B125 of IFRS 17.

Amortisation of insurance acquisition cash flows	50	0	0	50
Cash outflows	0	0	(600)	(600)
30 June 2021	**500**	**100**	**0**	**600**

B13. At 31 December 2021 all events have occurred as expected at 30 June 2021 and all claims have been paid. The change in the insurance contract liability following initial recognition for the period of six months ending 31 December 2021 can be analysed as follows:

	CF	**RA**	**CSM**	**Total**
30 June 2021	600	0	0	600
Cash outflows	(600)	0	0	(600)
31 December 2021	**0**	**0**	**0**	**0**

B14. The change in the insurance contract liability following initial recognition can also be analysed split between the LRC and the LIC as follows:

	LRC		**LIC**	**Total**
	Excluding loss component	**Loss component**		
30 June 2021	500	100	0	600

Insurance revenue	(550)[4]	0	0	(550)
Insurance service expenses				
Incurred claims	0	0	600	600
Reversal of losses	0	(100)	0	(100)
Amortisation of insurance acquisition cash flows	50	0	0	50
Cash outflows	0	0	(600)	(600)
31 December 2021	**0**	**0**	**0**	**0**

B15. Extract of the statement of profit or loss for the year ended 31 December 2021:

Insurance revenue (400 + 50 + 500 + 50)	1,000
Insurance service expenses (600 + 100 + 50 + 600 – 100 + 50)	(1,300)
Insurance service result	**(300)**

Example 3—profitable at initial recognition and subsequently total premiums are less than the sum of expected cash flows and insurance acquisition cash flows paid

B16. On 1 January 2021 an entity issues a set of 100 insurance contracts with a coverage period of one year. At initial recognition, the entity receives premiums of 1,000 which are contingent on the volume of the insurance coverage. The entity expects that the premium will be 1,000 (ie the entity expects there that will be no refund or extra payment of premium). The entity pays insurance acquisition cash

[4] Insurance revenue of 500 applying paragraph B123 of IFRS 17 (the total reduction in the liability for remaining coverage excluding the loss component is 500 which reflects insurance services provided in the period) and insurance revenue of 50 applying paragraph B125 of IFRS 17.

flows of 100 which are non-refundable. The entity expects future cash outflows of 800. The entity treats the set of contracts as a group of insurance contracts.

B17. Applying paragraph 38 of IFRS 17 the entity measures the contractual service margin at initial recognition:

(a)	Expected future cash flows	800
(b)	Derecognition of any assets or liabilities recognised for insurance acquisition cash flows	0
(c)	Cash flows arising at that date:	
	Insurance acquisition cash flows paid	100
	Premium receipt	(1,000)
Contractual service margin		**100**

B18. At 31 December 2021, it is determined that the entity provided only 25% of the insurance coverage it had expected to provide and claims incurred are only 200. The entity pays 950 to the policyholders consisting of a 750 premium refund and 200 claims incurred.

B19. The change in the insurance contract liability following initial recognition can be analysed as follows:

	CF	**RA**	**CSM**	**Total**
1 January 2021	800	0	100	900
Changes related to current service	150	0	(100)	50
Cash outflows	(950)	0	0	(950)
31 December 2021	**0**	**0**	**0**	**0**

B20. The change in the insurance contract liability following initial recognition can also be analysed split between the LRC and the LIC as follows:

	LRC	**LIC**	**Total**
1 January 2021	900	0	900
Insurance revenue	(250)[5]	0	(250)
Insurance service expenses:			
Incurred claims	0	200	200
Amortisation of insurance acquisition cash flows	100	0	100
Cash outflows	(750)	(200)	(950)
31 December 2021	**0**	**0**	**0**

B21. Extract of the statement of profit or loss for the year ended 31 December 2021:

Insurance revenue (150 + 100)	250

[5] Insurance revenue of 150 applying paragraph B123 of IFRS 17 and insurance revenue of 100 applying paragraph B125 of IFRS 17. The total reduction in the liability for remaining coverage is 900. Applying paragraph B123(a)(i) of IFRS 17, the reduction in the liability for remaining coverage that gives rise to insurance revenue excludes changes that result from cash inflows of premiums received. Therefore, the entity must exclude from the change of 900 the decrease of 750 from the refund of premiums. This means that the reduction in the liability for remaining coverage that gives rise to insurance revenue applying paragraph B123 of IFRS 17 is 150 (900 – 750 = 150).

Insurance service expenses (200 + 100)	(300)
Insurance service result	**(50)**

Example 4—profitable at initial recognition and subsequently total premiums are less than insurance acquisition cash flows paid

B22. On 1 January 2021 an entity issues a set of 100 insurance contracts with a coverage period of one year. At initial recognition, the entity receives premiums of 1,000 which are contingent on the volume of the insurance coverage. The entity expects that the premium will be 1,000 (ie the entity expects there that will be no refund or extra payment of premium). The entity pays insurance acquisition cash flows of 200 which are non-refundable. The entity expects future cash outflows of 700. The entity treats the set of contracts as a group of insurance contracts.

B23. Applying paragraph 38 of IFRS 17 the entity measures the contractual service margin at initial recognition:

(a)	Expected future cash flows	700
(b)	Derecognition of any assets or liabilities recognised for insurance acquisition cash flows	0
(c)	Cash flows arising at that date:	
	Insurance acquisition cash flows paid	200
	Premium receipt	(1,000)
Contractual service margin		**100**

B24. At 31 December 2021, it is determined that the entity provided only 10% of the insurance coverage it had expected to provide and incurred claims are only 70.

The entity pays 970 to the policyholders consisting of a 900 premium refund and 70 claims incurred.

B25. The change in the insurance contract liability following initial recognition can be analysed as follows:

	CF	**RA**	**CSM**	**Total**
1 January 2021	700	0	100	800
Changes related to current service	270	0	(100)	170
Cash outflows	(970)	0	0	(970)
31 December 2021	**0**	**0**	**0**	**0**

B26. The change in the insurance contract liability following initial recognition can also be analysed split between the LRC and the LIC as follows:

	LRC	**LIC**	**Total**
1 January 2021	800	0	800
Insurance revenue	(100)[6]	0	(100)
Insurance service expenses:			
Incurred claims	0	70	70

[6] Insurance revenue of (100) applying paragraph B123 of IFRS 17 and insurance revenue of 200 applying paragraph B125 of IFRS 17. The total reduction in the liability for remaining coverage is 800. Applying paragraph B123(a)(i) of IFRS 17, the reduction in the liability for remaining coverage that gives rise to insurance revenue excludes changes that result from cash inflows of premiums received. Therefore, the entity must exclude from the change of 800 the decrease of 900 from the refund of premiums. This means that the reduction in the liability for remaining coverage that gives rise to insurance revenue applying paragraph B123 of IFRS 17 is (100) (800 – 900 = -100).

Amortisation of insurance acquisition cash flows	200	0	200
Cash outflows	(900)	(70)	(970)
31 December 2021	**0**	**0**	**0**

B27. Extract of the statement of profit or loss for the year ended 31 December 2021:

Insurance revenue (-100 + 200)	100
Insurance service expenses (70 + 200)	(270)
Insurance service result	**(170)**

Appendix C—Examples of applying the requirements in paragraphs B123 and B125 of IFRS 17 when insurance acquisition cash flows are included in expected future cash flows

C1. This appendix includes three examples demonstrating the treatment of insurance acquisition cash flows that are contingent (ie variable) and therefore may change over time. The examples are:

(a) Example 5—onerous at initial recognition;

(b) Example 6—profitable with an experience adjustment relating to insurance acquisition cash flows; and

(c) Example 7—profitable with a change in expected future cash flows relating to insurance acquisition cash flows.

C2. For simplicity, the following assumptions apply in all examples:

(a) discount rates are 0%;

(b) the risk adjustment for non-financial risk (RA) is zero; and

(c) unless explicitly stated otherwise, services are provided evenly over the coverage period and claims are incurred evenly over the coverage period.

Example 5—Onerous at initial recognition

C3. On 1 January 2021 an entity issues a set of 100 insurance contracts with a coverage period of one year. At initial recognition, the entity receives premiums of 1,000. The entity expects future cash outflows of 1,100 including 100 insurance acquisition cash flows. Applying paragraph 47 of IFRS 17 the entity determines that the set of insurance contracts is onerous and treats them as an onerous group of insurance contracts applying paragraph 16 of IFRS 17. The contractual service margin is zero.

C4. Determining the loss component applying paragraph 47 of IFRS 17:

(a)	Expected future cash flows	1,100

(b)	Derecognition of any assets or liabilities recognised for insurance acquisition cash flows	0
(c)	Cash flows arising at that date:	
	Premium receipt	(1,000)
Loss recognised in profit or loss immediately		**(100)**

C5. At 31 December 2021, all events have occurred as expected and all claims have been paid. The change in the insurance contract liability following initial recognition can be analysed as follows:

	CF	**RA**	**CSM**	**Total**
1 January 2021	1,100	0	0	1,100
Cash outflows	(1,100)	0	0	(1,100)
31 December 2021	**0**	**0**	**0**	**0**

C6. The change in the insurance contract liability following initial recognition can also be analysed split between the LRC and the LIC as follows:

	LRC		**LIC**	**Total**
	Excluding loss component	**Loss component**		
1 January 2021	1,000	100	0	1,100
Insurance revenue	(1,000)[7]	0	0	(1,000)

[7] Insurance revenue of 900 applying paragraph B123 of IFRS 17 and insurance revenue of 100 applying paragraph B125 of IFRS 17. Applying paragraph B123(a)(v) of IFRS 17, the reduction in the liability for

Insurance service expenses:				
Incurred claims	0	0	1,000	1,000
Reversal of losses	0	(100)	0	(100)
Amortisation of insurance acquisition cash flows	100	0	0	100
Cash outflows	(100)	0	(1,000)	(1,100)
31 December 2021	**0**	**0**	**0**	**0**

C7. Extract of the statement of profit or loss for the year ended 31 December 2021:

Insurance revenue (900 + 100)	1,000
Insurance service expenses (100 + 1,000 – 100 + 100)	(1,100)
Insurance service result	**(100)**

Example 6—profitable with an experience adjustment relating to insurance acquisition cash flows

C8. On 1 January 2021 an entity issues a set of 100 insurance contracts with a coverage period of one year. At initial recognition, the entity receives premiums of 1,000. The entity expects future cash outflows of 800 consisting of 700 for expected claims and 100 relating to insurance acquisition cash flows to be paid at

remaining coverage excluding the loss component that gives rise to insurance revenue excludes changes that result from the payment of insurance acquisition cash flows. Therefore, the entity must exclude from the change of 1,000 the decrease of 100 because of the payment of insurance acquisition cash flows. This means that the reduction in the liability for remaining coverage that gives rise to insurance revenue applying paragraph B123 of IFRS 17 is 900 (1,000 – 100 = 900).

the end of the coverage period. The entity treats the set of contracts as a group of insurance contracts.

C9. Applying paragraph 38 of IFRS 17 the entity measures the contractual service margin at initial recognition:

(a)	Expected future cash flows	800
(b)	Derecognition of any assets or liabilities recognised for insurance acquisition cash flows	0
(c)	Cash flows arising at that date:	
	Insurance acquisition cash flows paid	0
	Premium receipt	(1,000)
Contractual service margin		**200**

C10. At 31 December 2021, all events have occurred as expected and all claims have been paid. However, insurance acquisition cash flows actually paid are 120 compared to the expectation of 100. The change in the insurance contract liability following initial recognition can be analysed as follows:

	CF	**RA**	**CSM**	**Total**
1 January 2021	800	0	200	1,000
Changes related to current service	20	0	(200)	(180)
Cash outflows	(820)	0	0	(820)
31 December 2021	**0**	**0**	**0**	**0**

C11. The change in the insurance contract liability following initial recognition can also be analysed split between the LRC and the LIC as follows:

	LRC	LIC	Total
1 January 2021	1,000	0	1,000
Insurance revenue	(1,000)[8]	0	(1,000)
Insurance service expenses:			
Incurred claims	0	700	700
Amortisation of insurance acquisition cash flows	120	0	120
Cash outflows	(120)	(700)	(820)
31 December 2021	**0**	**0**	**0**

C12. Extract of the statement of profit or loss for the year ended 31 December 2021:

Insurance revenue (880 + 120)	1,000
Insurance service expenses (700 + 120)	(820)
Insurance service result	**180**

[8] Insurance revenue of 880 applying paragraph B123 of IFRS 17 and insurance revenue of 120 applying paragraph B125 of IFRS 17. The total reduction in the liability for remaining coverage is 1,000. Applying paragraph B123(a)(v) of IFRS 17, the reduction in the liability for remaining coverage that gives rise to insurance revenue excludes changes that result from the payment of insurance acquisition cash flows. Therefore, the entity must exclude from the change of 1,000 the decrease of 120 from the payment of insurance acquisition cash flows. This means that the reduction in the liability that gives rise to insurance revenue applying paragraph B123 of IFRS 17 is 880 (1,000 – 120 = 880).

Example 7—profitable with change in expected future cash flows relating to insurance acquisition cash flows

C13. On 1 January 2021 an entity issues a set of 100 insurance contracts with a coverage period of one year. At initial recognition, the entity receives premiums of 1,000. The entity expects future cash outflows of 800 consisting of 700 for expected claims (paid as incurred) and 100 relating to insurance acquisition cash flows (to be paid at the end of the coverage period). The entity treats the set of contracts as a group of insurance contracts.

C14. Applying paragraph 38 of IFRS 17 the entity measures the contractual service margin at initial recognition:

(a)	Expected future cash flows	800
(b)	Derecognition of any assets or liabilities recognised for insurance acquisition cash flows	0
(c)	Cash flows arising at that date:	
	Insurance acquisition cash flows paid	0
	Premium receipt	(1,000)
Contractual service margin		**200**

C15. The entity prepares interim reporting for the six months ended 30 June 2021. At 30 June 2021, all claim events have occurred as expected and been paid and the entity makes no changes to its estimates of future cash flows relating to claims. However, the entity now expects to pay 120 for insurance acquisition cash flows at the end of the year compared to the original expectation of 100.

C16. The change in the insurance contract liability following initial recognition for the period of six months ending 30 June 2021 can be analysed as follows:

	CF	RA	CSM	Total
1 January 2021	800	0	200	1,000
Changes related to future service	20	0	(20)	0
Changes related to current service	0	0	(90)	(90)
Cash outflows	(350)	0	0	(350)
30 June 2021	**470**	**0**	**90**	**560**

C17. The change in the insurance contract liability following initial recognition can also be analysed split between the LRC and the LIC as follows:

	LRC	LIC	Total
1 January 2021	1,000	0	1,000
Insurance revenue	(500)[9]	0	(500)
Insurance service expenses:			
Incurred claims	0	350	350
Amortisation of insurance acquisition cash flows	60	0	60
Cash outflows	0	(350)	(350)
30 June 2021	**560**	**0**	**560**

[9] Insurance revenue of 440 applying paragraph B123 of IFRS 17 (the total reduction in the liability for remaining coverage is 440 which reflects insurance services provided in the period) and insurance revenue of 60 applying paragraph B125 of IFRS 17 (allocated in a systematic way on the basis of the passage of time).

C18. At 31 December 2021, all events have occurred as expected at 30 June 2021, all claims have been paid and insurance acquisition cash flows of 120 have been paid. The change in the insurance contract liability following initial recognition can be analysed as follows:

	CF	RA	CSM	Total
30 June 2021	470	0	90	560
Changes related to current service	0	0	(90)	(90)
Cash outflows	(470)	0	0	(470)
31 December 2021	**0**	**0**	**0**	**0**

C19. The change in the insurance contract liability following initial recognition can also be analysed split between the LRC and the LIC as follows:

	LRC	LIC	Total
30 June 2021	560	0	560
Insurance revenue	(500)[10]	0	(500)
Insurance service expenses:			
Incurred claims	0	350	350

[10] Insurance revenue of 440 applying paragraph B123 of IFRS 17 and insurance revenue of 60 applying paragraph B125 of IFRS 17 (allocated in a systematic way on the basis of the passage of time). The total reduction in the liability for remaining coverage is 560. Applying paragraph B123(a)(v) of IFRS 17, the reduction in the LRC that gives rise to insurance revenue excludes changes that result from the payment of insurance acquisition cash flows. Therefore, the entity must exclude from the change of 560 the decrease of 120 from the payment of insurance acquisition cash flows. This means that the reduction in the liability for remaining coverage that gives rise to insurance revenue applying paragraph B123 of IFRS 17 is 440 (560 – 120 = 440).

Amortisation of insurance acquisition cash flows	60	0	60
Cash outflows	(120)	(350)	(470)
31 December 2021	**0**	**0**	**0**

C20. Extract of the statement of profit or loss for the year ended 31 December 2021:

Insurance revenue (440 + 60 + 440 + 60)	1,000
Insurance service expenses (350 + 60 + 350 + 60)	(820)
Insurance service result	**180**