Recognising the contractual service margin in profit or loss

Basic overview
### IFRS 17 webcasts

#### This webinar
- March 2018: Recognising the contractual service margin in profit or loss

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

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**Further information:**
go.ifrs.org/IFRS-17-implementation and IFRS 17 webcasts YouTube playlist:
https://www.youtube.com/playlist?list=PLrLeeuMbuaUeLNX7Qoqlq7Oh3csegFwYn
Today’s topics

Basic overview

• The objective of the allocation of the contractual service margin
• Allocating the contractual service margin
• Other topics
  – Considering the time value of money when allocating the contractual service margin (CSM)
The objective of the allocation of the contractual service margin
Reminder: IFRS 17 core requirements

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

1. PV of future cash flows
2. Risk adjustment
3. Unearned profit

= IFRS 17 asset or liability

Further information:
IFRS 17 paragraph 32
IFRS 17 Appendix A definitions:
- Contractual service margin
- Risk adjustment for non-financial risk
- Fulfilment cash flows
- Financial risk

Basis for Conclusions on IFRS 17 paragraphs BC16-BC21
Webcast Core requirements: measurement essentials of IFRS 17
at go.ifrs.org/IFRS-17-implementation and IFRS 17 youtube playlist:
https://www.youtube.com/playlist?list=PLrLeeuMbuaUeLNX7qoqlq7Oh3csegFwYn
### Further information:

- IFRS 17 paragraphs 83-85 and B120-B124
- Basis for Conclusions on IFRS 17 paragraphs BC35-BC37, BC222-BC223 and BC279(a)
- Webcast "Core requirements: measurement essentials of IFRS 17"
  - at go.ifrs.org/IFRS-17-implementation and IFRS 17 youtube playlist: [https://www.youtube.com/playlist?list=PLrLeeuMbuaUeLNX7Qoqlq7Oh3csegFwYn](https://www.youtube.com/playlist?list=PLrLeeuMbuaUeLNX7Qoqlq7Oh3csegFwYn)
Further information:
IFRS 17 paragraphs 14-24
Basis for Conclusions on IFRS 17 paragraphs BC115-BC139
Webcast IFRS 17 Level of Aggregation (Part 1) at go.ifrs.org/IFRS-17-implementation and IFRS 17 YouTube playlist
https://www.youtube.com/playlist?list=PLrLeeuMbuaUeLNX7Qoqlq7Oh3csegFwYn
Further information:
IFRS 17 paragraphs 43, 44(e), 45(e) and B119
Basis for Conclusions on IFRS 17 paragraphs BC118, BC120 and BC279 – BC283
Further information:
IFRS 17 paragraphs 43-44 and B96-B100
Basis for Conclusions on IFRS 17 paragraphs BC22-BC24 and BC220-BC224
Webcast Core requirements: measurement essentials of IFRS 17
at go.ifrs.org/IFRS-17-implementation and IFRS 17 youtube playlist:
https://www.youtube.com/playlist?list=PLrLeeuMbuaUeLNX7Qoqlq7Oh3cssegFwYn
Recognising CSM in profit or loss

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

Further information:
IFRS 17 paragraphs 44(e), 45(e) and B119
Basis for Conclusions of IFRS 17 paragraphs BC220, BC221 and BC279-BC283
Identify the number of coverage units

- The total number of coverage units of a group is the quantity of coverage provided by contracts in the group over the expected coverage period

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

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

Further information:
IFRS 17 paragraph B119
Basis for Conclusions on IFRS 17 paragraphs BC279, BC282 and BC283
Discussed at the February 2018 meeting of the Transition Resource Group on IFRS 17 Insurance Contracts - Agenda Paper 5 http://www.ifrs.org/groups/transition-resource-group-for-insurance-contracts/#meetings
Assessment of coverage units

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

Further information:
IFRS 17 paragraph B119
Basis for Conclusions on IFRS 17 paragraph BC279
Webcast IFRS 17 Core requirements: Recognition and derecognition at go.ifrs.org/IFRS-17-implementation and IFRS 17 youtube playlist: https://www.youtube.com/playlist?list=PLrLeeuMbuaUeLNX7Qoqlq7Oh 3csegFwYn
Discussed at the February 2018 meeting of the Transition Resource Group on IFRS 17 Insurance Contracts - Agenda Paper 5 http://www.ifrs.org/groups/transition-resource-group-for-insurance-contracts/#meetings
Further information:
IFRS 17 paragraph B119
Basis for Conclusions on IFRS 17 paragraphs BC279, BC282 and BC283
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IFRS 17 paragraph B119
Basis for Conclusions on IFRS 17 paragraphs BC279, BC282 and BC283
Example – increase in coverage duration

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

<table>
<thead>
<tr>
<th>Coverage units</th>
<th>Period 1</th>
<th>Period 2</th>
<th>Period 3</th>
<th>Period 4</th>
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<tr>
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<table>
<thead>
<tr>
<th>CSM in P/L</th>
<th>CU50</th>
<th>CU50</th>
<th>CU25</th>
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</table>

<table>
<thead>
<tr>
<th>CSM in B/S CU150</th>
<th>CU100</th>
<th>CU50</th>
<th>CU25</th>
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</table>

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

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

Further information:
IFRS 17 paragraph B119
Basis for Conclusions on IFRS 17 paragraphs BC279, BC282 and BC283
Other topics
Coverage units
Considering time value of money when allocating the CSM

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

Further information:
IFRS 17 paragraphs 44(e), 45(e) and B119
Basis for Conclusions on IFRS 17 paragraph BC282
**Further information:**
IFRS 17 paragraphs 44(e), 45(e) and B119
Basis for Conclusions on IFRS 17 paragraph BC282
Appendix A
Example - time value of money when allocating the CSM

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

Further information:
IFRS 17 paragraphs 44(e), 45(e) and B119
Basis for Conclusions on IFRS 17 paragraph BC282
### Further information:
- IFRS 17 paragraphs 44(e), 45(e) and B119
- Basis for Conclusions on IFRS 17 paragraph BC282
### Appendix A
Allocation reflecting the timing of coverage

<table>
<thead>
<tr>
<th>CSM \ Period *</th>
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<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
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<tbody>
<tr>
<td>Opening Balance</td>
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<td>CU328</td>
<td>CU229</td>
<td>CU120</td>
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<td>Accretion—interest</td>
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<td>CU42</td>
<td>CU33</td>
<td>CU23</td>
<td>CU12</td>
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<tr>
<td>Allocated to P&amp;L</td>
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<td>CU132</td>
<td>CU132</td>
<td>CU132</td>
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<tr>
<td>Closing balance</td>
<td>CU418</td>
<td>CU328</td>
<td>CU229</td>
<td>CU120</td>
<td>CU0</td>
</tr>
</tbody>
</table>

Nominal coverage units: 1 1 1 1 1 1
PV coverage units provided: 1 1 1 1 1 1
PV coverage units provided and over remaining periods: 4.17 3.49 2.74 1.91 1 1
Coverage units allocation: 1/4.17 1/3.49 1/2.74 1/1.91 1/1

*Rounded for presentation
For simplicity, coverage is assumed to be provided at the end of the period

**Further information:**
IFRS 17 paragraphs 44(e), 45(e) and B119
Basis for Conclusions on IFRS 17 paragraph BC282