

STAFF PAPER

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IASB® meeting

Project	Insurance Contracts		
Paper topic	Future cash flows in the measurement of reinsurance contracts held		
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Purpose and structure of the paper

1. This paper discusses future cash flows in the measurement of reinsurance contracts held. Other aspects of the accounting for reinsurance contracts held will be discussed in a future meeting of the International Accounting Standards Board (Board).
2. This paper provides:
 - (a) an overview of the requirements in IFRS 17 *Insurance Contracts*;
 - (b) a summary of the Board's rationale for setting those requirements, including an overview of the Board's previous discussions;
 - (c) an overview of the concerns and implementation challenges expressed since IFRS 17 was issued; and
 - (d) the staff analysis, recommendation and a question for Board members.
3. Appendix A to this paper provides an example of measuring a reinsurance contract held and the underlying insurance contracts issued.

Staff recommendation

4. The staff recommend that the Board should not amend the requirements in IFRS 17 for future cash flows in the measurement of reinsurance contracts held.

IFRS 17 requirements

5. Insurance contracts issued and reinsurance contracts held are measured applying the same measurement model. The measurement includes a probability-weighted average estimate of all future cash flows within the contract boundary and an explicit risk adjustment to reflect the uncertainty in the timing and amount of cash flows that arises from non-financial risk.
6. To reflect that reinsurance contracts held are not issued by the entity, paragraphs 60–70 of IFRS 17 modify the general requirements.¹ Paragraphs 7–9 of this paper summarise the requirements for determining the cash flows within the boundary of a contract.
7. An entity applies the contract boundary requirements in paragraph 34 of IFRS 17 to the insurance contracts it issues and the reinsurance contracts it holds. This means that:
 - (a) the cash flows within the boundary of an insurance contract issued arise from the entity’s substantive rights and substantive obligations as the issuer of that contract. These include the substantive right to receive amounts from the policyholder and the substantive obligation to provide services to the policyholder.
 - (b) the cash flows within the boundary of a reinsurance contract held arise from the entity’s substantive rights and substantive obligations as the holder of that contract. These include the substantive right to receive services from the reinsurer and the substantive obligation to pay amounts to the reinsurer.
8. A substantive right to receive services from the reinsurer ends when the reinsurer has the practical ability to reassess the risks transferred to the reinsurer and can set a price or level of benefits for the contract to fully reflect the reassessed risk or the reinsurer has a substantive right to terminate the coverage.²

¹ The staff have published an *IFRS 17 Pocket Guide on reinsurance contracts held* which is a helpful reference tool on how IFRS 17 applies to reinsurance contracts held.

² This topic was discussed at the February 2018 Transition Resource Group for IFRS 17 (TRG) meeting. A summary of the observations made in that meeting can be found in the *Summary of the Transition Resource Group for IFRS 17 Insurance Contracts meeting held on 6 February 2018*.

9. Accordingly:
- (a) if the entity *has* a substantive right to receive services from the reinsurer relating to underlying contracts that are expected to be issued in the future, cash flows within the boundary of the reinsurance contract held will include cash flows relating to those future underlying contracts.
 - (b) if the entity *does not have* a substantive right to receive services from the reinsurer relating to underlying contracts that are expected to be issued in the future, the cash flows relating to those future underlying contracts will belong to a future reinsurance contract held (assuming the entity does not have a substantive obligation to pay amounts to the reinsurer).³

Board's rationale

10. A fundamental aspect of measuring an insurance contract is determining which future cash flows should be included in the measurement, ie determining which cash flows are within the contract boundary. In most accounting models, the boundary of a contract is determined by the explicit contract terms. However, during the development of IFRS 17, the Board noted that a common feature of insurance contracts is that it can be difficult to determine where the boundaries of the contract lie because they often bind the entity issuing the contract more closely than the other party. For example, in many contracts the contract requires the entity to continue to accept premiums but permits the policyholder to stop paying premiums. The Board concluded that the contract boundary should be determined on the basis of the substantive rights and substantive obligations created by the contract for the entity.
11. The Board concluded that expected future cash flows for reinsurance contracts held and insurance contracts issued should be measured using a similar approach. This means that the reinsurance contract held is measured the same way as insurance

³ Generally, an entity can choose to stop paying premiums to the reinsurer, thus terminating coverage. However, in some reinsurance arrangements the entity is compelled to continue paying premiums. An example of such a reinsurance arrangement was discussed at the May 2018 TRG meeting. A summary of the observations made in that meeting can be found in the *Summary of the Transition Resource Group for IFRS 17 Insurance Contracts meeting held on 2 May 2018*.

contracts issued, including reinsurance contracts issued. It also means that consistent assumptions are used to measure the reinsurance contract held and the underlying insurance contracts (for example, the assumptions about expected lapses).⁴

12. Hence, if the entity has a substantive right to receive services from the reinsurer in respect of underlying insurance contracts it issues that are covered by the reinsurance contract, the cash flows within the boundary of the reinsurance contract held include all the cash flows expected to arise from those underlying insurance contracts expected to be covered by the reinsurance contract. This includes a substantive right relating to underlying contracts expected to be issued in the future.

Concerns and implementation challenges expressed since IFRS 17 was issued

13. Stakeholders have expressed three concerns with applying the contract boundary requirements to reinsurance contracts held. Those concerns are described in paragraphs 14–16 of this paper.
14. Firstly, stakeholders think the requirements are operationally complex. Applying existing practice for measuring reinsurance contracts held, entities do not typically estimate future cash flows relating to insurance contracts not yet issued. Instead, reinsurance contracts held are typically measured using a ‘mirroring approach’, essentially matching reinsurance contract revenue, costs, assets and liabilities to the underlying insurance contracts. Stakeholders are concerned that measuring future cash flows for the reinsurance contract that relate to future underlying contracts is operationally complex and will result in that measurement being uncertain and unreliable, given that cash flows relating to future underlying contracts are uncertain.
15. Secondly, stakeholders think that the requirements will create a mismatch between the insurance contract liability and the reinsurance contract asset because the reinsurance

⁴ The Board concluded on this fundamental principle in an early stage of the insurance contracts project (see [Discussion Paper Preliminary Views on Insurance Contracts](#) May 2007). This principle has been reflected in the Board’s outreach and decisions throughout the project. Generally, feedback throughout the project was supportive of this fundamental principle. However, the Board noted at an early stage that some stakeholders interpret ‘consistent’ differently to the Board. Those stakeholders thought that to measure a reinsurance contract held consistently with insurance contracts issued should mean to apply ‘mirror’ accounting, similarly to existing accounting practice.

contract asset will be ‘grossed up’ with the cash flows for future underlying contracts that have not yet been issued.

16. Thirdly, stakeholders think that the requirements might result in the contractual service margin for the reinsurance contracts held being recognised in an inconsistent way to the recognition of the contractual service margin for the underlying insurance contracts.
17. Some stakeholders have proposed amendments to IFRS 17 that they think would address their concerns. The two amendments proposed are:
 - (a) amend the recognition requirements for reinsurance contracts held in paragraph 62(a) of IFRS 17 to require a group of reinsurance contracts held that provides proportionate coverage to be recognised at the later of:
 - (i) the beginning of the coverage period of the group of reinsurance contracts held; or
 - (ii) at the initial recognition of *the* underlying contracts (instead of at the initial recognition of *any* underlying contract, as stated in IFRS 17).
 - (b) modify the contract boundary requirements in paragraph 34 of IFRS 17 for reinsurance contracts held so that cash flows relating to underlying insurance contracts are included in the measurement of the reinsurance contract held only at the time that those underlying insurance contracts are recognised.

Staff analysis and recommendation

18. The staff do not think that an amendment to IFRS 17 is justified because of stakeholder concerns about the uncertainty of future cash flows, described in paragraph 14 of this paper. The staff observe that cash flows of uncertain timing and amounts are included in the measurement of all insurance contracts. This is not unique

to reinsurance contracts held. For example, for all insurance contracts the entity is required to estimate the probability and amounts of claims that will be incurred.

19. The staff do not think that an amendment to IFRS 17 is justified because of stakeholder concerns about a ‘grossed up’ reinsurance contract, described in paragraph 15 of this paper. The staff observe that future underlying insurance contracts are reflected in the cash inflows, cash outflows, risk adjustment for non-financial risk and contractual service margin included in the measurement of the reinsurance contract held. Those amounts sum to nil up until the point that one of the following events occurs:
 - (a) the entity pays or receives amounts relating to the reinsurance on those future underlying contracts (for example, the entity pays reinsurance premiums); or
 - (b) those underlying contracts are issued and the entity starts receiving reinsurance services relating to those contracts.

20. When one of those events occurs, the amounts included in the measurement of the reinsurance contract held relating to those contracts will no longer sum to nil. For example, when the entity pays reinsurance premiums which relate to underlying insurance contracts, the entity reduces the cash asset by paying the premium and in turn increases the reinsurance asset to reflect the service it will receive as a result of paying those premiums. That reinsurance asset is then reduced as the contract is fulfilled.

21. The staff do not think that an amendment to IFRS 17 is justified because of stakeholder concerns about the pattern of recognition of the contractual service margin, described in paragraph 16 of this paper. The staff observe that the contractual service margin recognised in a reporting period is determined considering the services received in the current period and expected to be received in future periods under the reinsurance contract held. This is consistent with the requirements for insurance contracts issued. The staff observe that in circumstances that the service the entity receives from the reinsurer is proportionate to the service that the entity provides to the policyholder, the identification and allocation of coverage units for reinsurance

contracts held will result in a pattern of contractual service margin recognition which reflects that symmetry.

22. The staff have published an educational example to demonstrate that the requirements in IFRS 17 reflect an entity's rights and obligations under a reinsurance contract held, and do not result in the apparent mismatches that stakeholders are concerned about, as described in this paper. That educational example is included in Appendix A to this paper.
23. In summary, the staff think that modifying the contract boundary requirements in IFRS 17 for reinsurance contracts held is not justified. In particular, the staff think that modifying the IFRS 17 contract boundary requirements for reinsurance contracts held as proposed by stakeholders in paragraph 17(b) of this paper would result in a significant loss of useful information relative to that which would otherwise be provided by IFRS 17 for users of financial statements, for the following reasons:
 - (a) the measurement of reinsurance contracts held would not fully reflect the entity's substantive right to receive services from the reinsurer. This would reduce the relevance and faithful representation of information in the financial statements.
 - (b) the proposed amendment would go against the fundamental principle in IFRS 17 that all future cash flows within the contract boundary are reflected in the measurement of an insurance contract.
 - (c) the proposed amendment would add complexity to the contract boundary requirements.
24. The staff observe that the amendment proposed in paragraph 17(a), alone, would not address stakeholders' concerns in the way they expect because the requirement in paragraph 62(a) of IFRS 17 relates to the initial recognition of a group of reinsurance contracts held, and not the measurement. For that amendment to achieve what stakeholders expect, IFRS 17 would also need to be amended to require that a reinsurance contract held that covers multiple underlying insurance contracts be separated and treated as a number of separate reinsurance contracts (ie a reinsurance

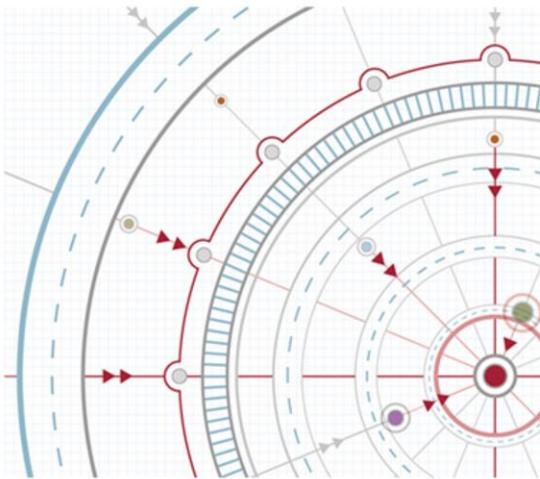
contract for each underlying insurance contract), and entities would need to group each of those contracts separately.

25. The staff also observe that the purpose of the amendment proposed in paragraph 17(a) is to achieve ‘mirror’ accounting between the reinsurance contract held and the underlying insurance contracts issued. This approach was considered and rejected by the Board during the development of IFRS 17 because such an approach is contradictory to the fundamental principle that a reinsurance contract held should be accounted for in the same manner as insurance contracts issued, including reinsurance contracts issued.
26. For those reasons, this paper does not consider further the amendment proposed in paragraph 17(a) of this paper.
27. The staff therefore recommend that the Board should not amend the requirements in IFRS 17 relating to future cash flows in the measurement of reinsurance contracts held.

Question for Board members

Do you agree that the Board should not amend the requirements in IFRS 17 relating to future cash flows in the measurement of reinsurance contracts held?

IFRS® Foundation



Reinsurance contracts held: an example of proportionate reinsurance coverage

IFRS 17 Insurance Contracts

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This example illustrates the requirements in IFRS 17 *Insurance Contracts*:

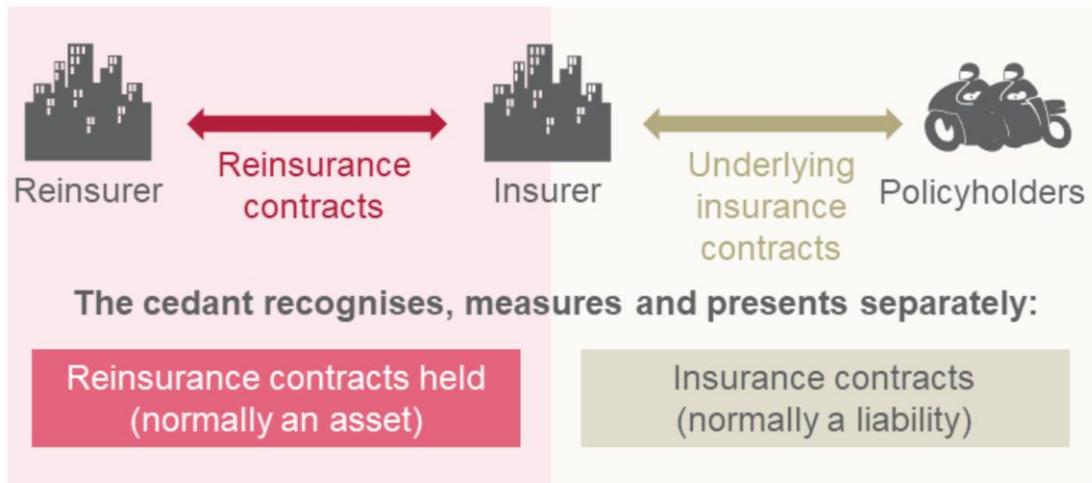
- a) applied to a group of underlying insurance contracts; and
- b) applied to a group of reinsurance contracts held that provides proportionate coverage for that group of underlying insurance contracts

This example demonstrates that:

- the measurement of a group of reinsurance contracts held is consistent with the measurement of any underlying insurance contracts
- the timing of cash flows do not directly affect the recognition of reinsurance income or expenses

Reminder: IFRS 17 requirements

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Further information

Paragraphs 60-70 of IFRS 17 *Insurance Contracts*

Paragraphs BC296-BC315 of the Basis for Conclusions on IFRS 17 *Insurance Contracts*

Webcast *Reinsurance contracts held* available at: go.ifrs.org/IFRS-17-implementation

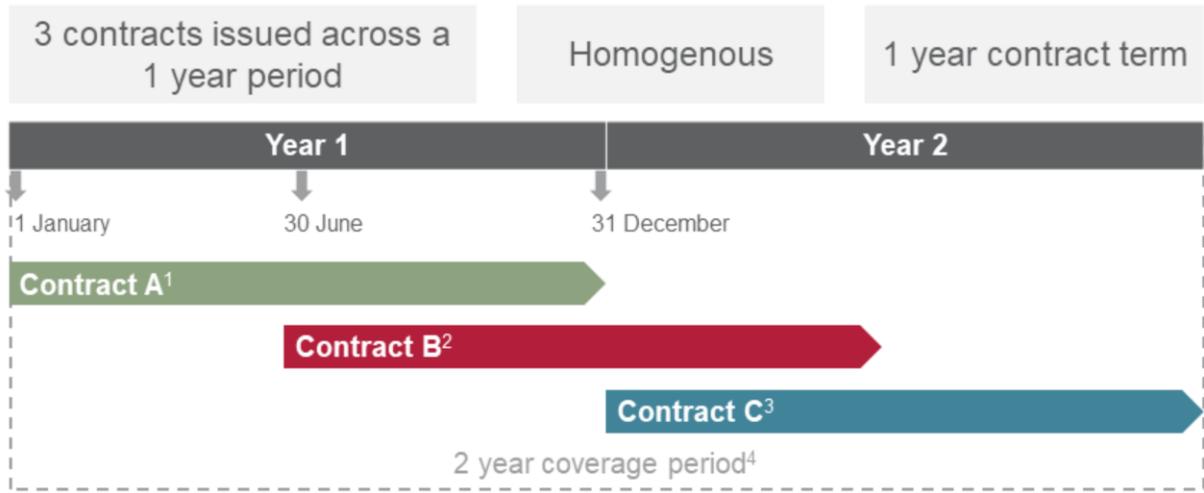
- IFRS 17 general model (not PAA)
- Risk adjustment for non-financial risk is nil
- Discount rate 0%
- Services are provided by the insurer evenly over the contract term for each contract
- All events occur as expected at initial recognition

Further information

The objective of this example is to demonstrate the mechanics of the IFRS 17 requirements for reinsurance contracts held. For simplicity, a number of assumptions have been made. This example is not intended to reflect a real fact pattern.

Group of underlying insurance contracts

A group of insurance contracts issued



Further information

¹ Contract A is issued on 1 January in year 1

² Contract B is issued on 30 June in year 1

³ Contract C is issued on 31 December in year 1

⁴ Initial recognition of the group of insurance contracts: 1 January in year 1 is the beginning of the coverage period of the group of insurance contracts (paragraph 25(a) of IFRS 17). The coverage period for the group of insurance contracts is from 1 January in year 1 to 30 December in year 2. For simplicity, in this example the coverage period is referred as 2 years.

Cash flows

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	Year 1			Year 2		Total
	1 Jan	30 June	31 Dec	30 June	31 Dec	
Premiums ¹	300	300	300	-	-	900
Claims ²	-	(100)	(200)	(200)	(100)	(600)
Net cash inflow						300



Further information

All events occur as expected at initial recognition.

¹ Premiums of 300 are expected on day 1 for each of the 3 underlying insurance contracts.

² Claims of 600 are expected for the group of insurance contracts. Claims are incurred equally by each of the 3 underlying insurance contracts. For each underlying insurance contract, claims occur evenly over the 1 year contract term as services are provided and are paid immediately after incurred. The claims cash flows at each reporting date can be analysed as:

- Year 1 30 June – Contract A 100
- Year 1 31 December – Contract A 100 + Contract B 100
- Year 2 30 June – Contract B 100 + Contract C 100
- Year 2 31 December – Contract C 100

Statement of financial position

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	Year 1			Year 2	
	1 Jan ¹	30 June ²	31 Dec ³	30 June ⁴	31 Dec ⁵
Fulfilment cash flows	(200)	(300)	(300)	(100)	-
Contractual service margin	(100)	(150)	(150)	(50)	-
Insurance contract asset / (liability)	(300)	(450)	(450)	(150)	-



Further information

¹ At 1 January in year 1 the group is recognised and consists of the cash flows for Contract A only.

- FCF: premiums of 300 for Contract A are received on 1 January. The fulfilment cash flows at this date reflect expected claims of 200.
- CSM: the CSM of 100 at initial recognition is the amount that results in no income or expenses arising from the initial recognition of the fulfilment cash flows of 200 and the premiums received on that date of 300.

² At 30 June in year 1 the cash flows for Contract B are added to the group.

- FCF: premiums of 300 for Contract B are received on 30 June. The fulfilment cash flows reflect expected claims of 300 (opening balance of 200 plus 200 expected claims for Contract B minus 100 claims paid in the period).
- CSM: the balance of the CSM is 150 (opening balance of 100 plus 100 for Contract B minus 50 recognised as revenue in the period (see profit or loss slide 9)).

³ At 31 December in year 1 the cash flows for Contract C are added to the group.

- FCF: premiums of 300 for Contract C are received on 31 December. The fulfilment cash flows reflect expected claims of 300 (opening balance of 300 plus 200 expected claims for Contract C minus 200 claims paid in the period).
- CSM: the balance of the CSM is 150 (opening balance of 150 plus 100 for Contract C minus 100 recognised as revenue in the period).

⁴ At 30 June in year 2 no new cash flows are added to the group.

- FCF: the fulfilment cash flows reflect expected claims of 100 (opening balance of 300 minus 200 claims paid in the period).
- CSM: the balance of the CSM is 50 (opening balance of 150 minus 100 recognised as revenue in the period).

⁵ At 31 December in year 2 the group is derecognised.

- FCF: the fulfilment cash flows reflect expected claims of 0 (opening balance of 100 minus 100 claims paid in the period).
- CSM: the balance of the CSM is 0 (opening balance of 50 minus 50 recognised as revenue in the period).

Statement of profit or loss

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	Year 1		Year 2	
	1Jan-30Jun	1Jul-31Dec	1Jan-30Jun	1Jul-31Dec
Expected claims incurred ¹	100	200	200	100
Contractual service margin	50 ²	100	100	50
Insurance revenue	150	300	300	150
Actual claims incurred ¹	(100)	(200)	(200)	(100)
Insurance service expenses	(100)	(200)	(200)	(100)
Insurance service result	50	100	100	50



Further information

¹ In this example, for each underlying insurance contract, claims are incurred evenly over the 1 year contract term as services are provided and are paid immediately when incurred. All events occur as expected. See cash flows slide 7.

² At 30 June in year 1, the CSM before recognising any amount in profit or loss is 200. The CSM recognised for the period of six months ending 30 June in year 1 is 50. 50 reflects the amount allocated to coverage provided in the period (contract 1 was in force for six months) while the remaining 150 reflects coverage expected to be provided in the future (contract 1 is expected to be in-force for six months and contract 2 expected to be in force for a year). The CSM recognised in the remaining periods is determined in the same way.



Reinsurance contract held: timing of cash flows match timing of cash flows for the underlying insurance contracts

Proportionate reinsurance contract held



Further information

¹ The reinsurance contract held is recognised on 1 January in year 1. In this example the reinsurance contract held, as a single contract, is identified as a group of insurance contracts. In this example, the group is referred to as the reinsurance contract held.

² Initial recognition of reinsurance contract held: 1 January in year 1 is the beginning of the coverage period for the reinsurance contract held and is also the initial recognition of the first underlying insurance contract added to the group (paragraph 62(a) of IFRS 17). The coverage period for the reinsurance contract held is equal to the coverage period for the group of underlying insurance contracts, from 1 January in year 1 to 30 December in year 2. For simplicity, in this example the coverage period is referred to as 2 years.

Cash flows

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	Year 1			Year 2		Total
	1 Jan	30 June	31 Dec	30 June	31 Dec	
Premiums ¹	(300)	(300)	(300)	-	-	(900)
Claims ²	-	100	200	200	100	600
Net cash outflow						(300)



Further information

¹ Premiums expected to be paid to the reinsurer are equal to the premiums received from the policyholder on the underlying insurance contracts. Premiums are expected to be paid to the reinsurer on the same day that premiums are received from the policyholder.

² Claims expected to be received from the reinsurer are equal to the claims expected to be paid to the policyholder on the underlying insurance contracts. Claims are expected to be received from the reinsurer on the same day that claims are paid to the policyholder.

See slide 7 for the cash flows arising from the group of underlying insurance contracts.

Statement of financial position

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	Year 1			Year 2	
	1 Jan ³	30 June ⁴	31 Dec ⁵	30 June ⁶	31 Dec ⁷
Fulfilment cash flows ¹	0	200	300	100	-
Contractual service margin ²	300	250	150	50	-
Reinsurance contract asset / (liability)	300	450	450	150	-



Further information

¹The fulfilment cash flows of the reinsurance contract held reflect all future cash flows expected to arise within the boundary of the reinsurance contract held. In this example, those cash flows relate to all underlying insurance contracts expected to be covered by the reinsurance contract including underlying insurance contracts that have not been issued yet.

²The CSM for the reinsurance contract held represents the net cost of purchasing reinsurance.

³At 1 January in year 1 the reinsurance contract held is recognised.

- FCF: the fulfilment cash flows are 0 (opening balance of 0 plus 900 expected premiums minus 600 expected claims minus 300 premiums paid relating to Contract A).
- CSM: the CSM of 300 at initial recognition is the amount that results in no income or expenses arising from the initial recognition of the fulfilment cash flows of 0 and the premiums paid on that date of 300.

⁴At 30 June in year 1:

- FCF: the fulfilment cash flows are 200 (opening balance of 0 minus 100 claims received plus 300 premiums paid relating to Contract B).
- CSM: the balance of the CSM is 250 (opening balance of 300 minus 50 recognised as reinsurance contract expenses in the period (see profit or loss slide 14)).

⁵At 31 December in year 1:

- FCF: the fulfilment cash flows are 300 (opening balance of 200 minus 200 claims received plus 300 premiums paid relating to Contract C).
- CSM: the balance of the CSM is 150 (opening balance of 250 minus 100 recognised as reinsurance contract expenses in the period).

⁶At 30 June in year 2:

- FCF: the fulfilment cash flows are 100 (opening balance of 300 minus 200 claims received)
- CSM: the balance of the CSM is 50 (opening balance of 150 minus 100 recognised as reinsurance contract expenses in the period).

⁷At 31 December in year 2 the reinsurance contract held is derecognised.

- FCF: the fulfilment cash flows are 0 (opening balance of 100 minus 100 claims received).
- CSM: the balance of the CSM is 0 (opening balance of 50 minus 50 recognised as reinsurance contract expenses in the period).

Statement of profit or loss

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	Year 1		Year 2	
	1Jan-30Jun	1Jul-31Dec	1Jan-30Jun	1Jul-31Dec
Reinsurance premiums ¹ :				
Expected claims recovered ²	(100)	(200)	(200)	(100)
Contractual service margin ³	(50)	(100)	(100)	(50)
Amounts recovered from reinsurance ²	100	200	200	100
Net expense from reinsurance contracts	(50)	(100)	(100)	(50)

Further information

¹ The breakdown of the reinsurance premiums amount is given in the slide to explain the results in this example. Applying IFRS 17, revenue does not arise from reinsurance contracts held. Accordingly, the requirements for revenue, including the related disclosures, do not apply.

² In this example, claims received from the reinsurer are equal to the claims paid to the policyholder on the underlying insurance contracts. Claims are received from the reinsurer on the same day that those claims are paid to the policyholder. All events occur as expected. See expected cash flows - slide 12.

³ To determine the amount of the contractual service margin to be recognised in profit or loss in the period for the reinsurance contract held, in this example, the insurer considers the relevant facts and circumstances related to the underlying insurance contracts and determines that the amount and timing of services received under the reinsurance contract held are consistent to the amount and timing of services provided under the underlying insurance contracts (see slide 9).

Statement of financial position:

the whole picture

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	Year 1			Year 2	
	1 Jan	30 June	31 Dec	30 June	31 Dec
Fulfilment cash flows	(200)	(300)	(300)	(100)	-
Contractual service margin	(100)	(150)	(150)	(50)	-
Insurance contract asset / (liability)	(300)	(450)	(450)	(150)	-
Fulfilment cash flows	0	200	300	100	-
Contractual service margin	300	250	150	50	-
Reinsurance contract asset / (liability)	300	450	450	150	-



Further information

FCF: in this example, the cash flows for the reinsurance contract held are equal to the cash flows for the group of underlying insurance contracts and they occur at the exact same time.

CSM: in this example, the insurer provides service equally over the contract term for each underlying insurance contract. In this example, the insurer determines that the amount and timing of services received under the reinsurance contract held are equal to the amount and timing of services provided under the underlying insurance contracts.

As a result of the above, the balance of the reinsurance contract asset is equal to the balance of the insurance contract liability.

Statement of profit or loss

the whole picture

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	Year 1		Year 2	
	1Jan-30Jun	1Jul-31Dec	1Jan-30Jun	1Jul-31Dec
Insurance revenue	150	300	300	150
Insurance service expenses	(100)	(200)	(200)	(100)
Net expense from reinsurance contracts	(50)	(100)	(100)	(50)
Insurance service result	-	-	-	-



Further information

This is a simplified example of 100% proportionate reinsurance coverage. In this example, the services provided by the insurer under the underlying insurance contracts in each period are consistent with the services received from the reinsurer under the reinsurance contract held in each period. Also, the consideration to which the insurer expects to be entitled to in exchange for the services provided under the underlying insurance contracts is equal to the consideration the insurer expects to pay to the reinsurer in exchange for the services received under the reinsurance contract held.

As a result, there is a nil impact on the statement of profit or loss.

Reinsurance contract held:
cash flows are settled net at
the end of the coverage
period

Cash flows

18

Same fact pattern, expect that all reinsurance contract cash flows are settled net at the end of the coverage period

	Year 1			Year 2		Total
	1 Jan	30 June	31 Dec	30 June	31 Dec	
Premiums	-	-	-	-	(900)	(900)
Claims	-	-	-	-	600	600
Net cash outflow						(300)



Further information

A net amount of 300 is expected to be paid to the reinsurer at the end of the coverage period (900 premiums minus 600 claims).

Statement of financial position

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	Year 1			Year 2	
	1 Jan	30 June	31 Dec	30 June	31 Dec
Fulfilment cash flows ¹	(300)	(300)	(300)	(300)	-
Contractual service margin ²	300	250	150	50	-
Reinsurance contract asset / (liability) ³	-	(50)	(150)	(250)	-



Further information

¹ The fulfilment cash flows at each reporting date is 300 until the end of the coverage period. This reflects that the insurer expects to make one payment of 300 to the reinsurer at the end of the coverage period.

² The contractual service margin is measured and recognised in the same way as in the previous example (see slides 13–14) because the services provided under the reinsurance contract held are the same. The only difference in this example is the timing of the cash flows.

³ In this example, the balance is a reinsurance contract liability because the expected future cash flows are a net outflow.

Statement of profit or loss

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	Year 1		Year 2	
	1Jan-30Jun	1Jul-31Dec	1Jan-30Jun	1Jul-31Dec
Reinsurance premiums:				
Expected claims recovered	(100)	(200)	(200)	(100)
Contractual service margin	(50)	(100)	(100)	(50)
Amounts recovered from reinsurance	100	200	200	100
Net reinsurance contract expenses	(50)	(100)	(100)	(50)

Further information

The statement of profit or loss in this example is the same as the statement of profit or loss in the previous example (see slides 13–14) because the services provided under the reinsurance contract held are the same. The only difference in this example is the timing of the cash flows. The timing of cash flows may impact insurance finance income or expenses however, for simplicity in this example, the discount rate is 0%.

Statement of financial position:

the whole picture

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	Year 1			Year 2	
	1 Jan	30 June	31 Dec	30 June	31 Dec
Fulfilment cash flows	(200)	(300)	(300)	(100)	-
Contractual service margin	(100)	(150)	(150)	(50)	-
Insurance contract asset / (liability)	(300)	(450)	(450)	(150)	-
Fulfilment cash flows	(300)	(300)	(300)	(300)	-
Contractual service margin	300	250	150	50	-
Reinsurance contract asset / (liability)	-	(50)	(150)	(250)	-



Further information

FCF: in this example, the cash flows for the reinsurance contract held are equal to the cash flows for the group of underlying insurance contracts, however the cash flows occur at different times.

CSM: as with the previous example, the insurer provides service equally over the contract term for each underlying insurance contract. Also in this example, the insurer determines that the amount and timing of services received under the reinsurance contract held are equal to the amount and timing of services provided under the underlying insurance contracts.

As a result of the above, the balance of the reinsurance contract liability is not equal to the balance of the insurance contract liability. This reflects the fact that, at each reporting period, the expected future cash flows under the reinsurance contract held are different to the expected future cash flows under the group of underlying insurance contracts.

Statement of profit or loss

the whole picture

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	Year 1		Year 2	
	1Jan-30Jun	1Jul-31Dec	1Jan-30Jun	1Jul-31Dec
Insurance revenue	150	300	300	150
Insurance service expenses	(100)	(200)	(200)	(100)
Net expense from reinsurance contracts	(50)	(100)	(100)	(50)
Insurance service result	-	-	-	-



Further information

See slide 16.

- In practice it is likely that there will be differences between the cash flows arising from:
 - a) the rights and obligations of the underlying insurance contracts; and
 - b) the rights and obligations of the reinsurance contract held.
- These differences may exist, for example, because:
 - a) the timing of cash flows can vary, which can also impact insurance finance income or expenses; or
 - b) the reinsurer prices the reinsurance contract differently to the pricing of the underlying contracts.

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