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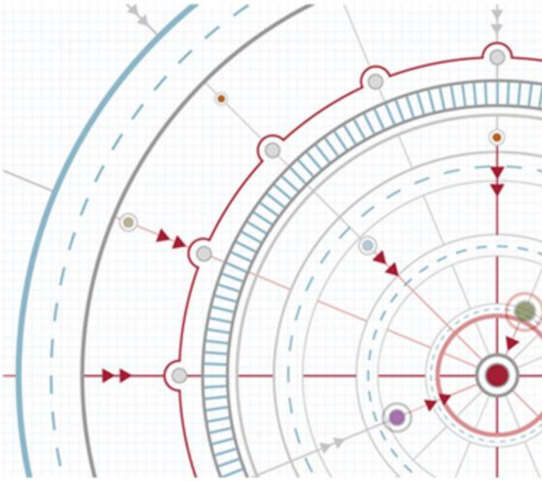

Premium Allocation Approach: example with comparison to existing accounting practice

IFRS 17 *Insurance Contracts*

The views expressed in this presentation are those of the presenter, not necessarily those of the International Accounting Standards Board (the Board) or IFRS Foundation.

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Introduction

This example illustrates the mechanics of the premium allocation approach (PAA) requirements in IFRS 17 *Insurance Contracts* for contracts with short coverage periods. It includes a comparison to the accounting commonly used applying existing practice for these contracts.

This example demonstrates that:

- the timing of premium receipts do not directly affect the revenue recognition pattern applying the PAA
- the PAA may result in similar measurement outcomes to existing practice

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Requirements in IFRS 17 *Insurance Contracts* and guidance in the Basis for Conclusions on IFRS 17 *Insurance Contracts*
Paragraphs 53–59 of IFRS 17 Insurance Contracts
Paragraphs BC288–BC295 of the Basis for Conclusions on IFRS 17 *Insurance Contracts*

Transition Resource Group for IFRS 17
This example was included as an Appendix to Agenda Paper 6 discussed at the 2 May 2018 Transition Resource Group for IFRS 17 (TRG) meeting.
- *Agenda Paper 6: Implementation challenges outreach report*
- *Summary of the Transition Resource Group for IFRS 17* Insurance Contracts *meeting held on 2 May 2018*
Available at: https://www.ifrs.org/news-and-events/calendar/2018/may/ifrs-17-transition-resource-group/

Webcast explaining the premium allocation approach requirements
- *Simplified accounting for contracts with short coverage periods: part 1*
- *Simplified accounting for contracts with short coverage periods: part 2*
Available at: go.ifrs.org/IFRS-17-implementation

3 scenarios in this example

Scenario 1 – Premium paid up front

Scenario 2 – Premium paid at the end of the coverage period

Scenario 3 – Premium paid on a monthly basis

Fact pattern for all 3 scenarios

An entity issues an insurance contract on **1 July 20X1**

The coverage period is **1 year** (1 July 20X1 – 30 June 20X2)

The premium charged is **CU1200**

Insurance acquisition cash flows of **CU180** are paid on **1 July 20X1**

<u>Assumptions</u>

- Insurance services are provided evenly over the coverage period
- No claims are incurred
- For IFRS 17 measurement, the insurance contract is accounted for as a group of insurance contracts

Scenario 1 – Premium paid upfront
Existing practice

Insurance line items on the statement of financial position and revenue reported

Reporting date	01.07.X1	30.09.X1	31.12.X1	31.03.X2	30.06.X2
Premium receivable	0	0	0	0	0
Unearned premium reserve (UPR)	(1200)	(900)	(600)	(300)	0
Deferred acquisition cost (DAC)	180	135	90	45	0
Sum of insurance line items on the statement of financial position (overall liability position)	**(1020)**	**(765)**	**(510)**	**(255)**	**0**
Revenue for each period (change in UPR)		**300**	**300**	**300**	**300**

Scenario 1 – Premium paid upfront
IFRS 17 PAA

6

Insurance contract asset / (liability) on the statement of financial position and revenue reported

Reporting date	01.07.X1	30.09.X1	31.12.X1	31.03.X2	30.06.X2
Opening balance	0	(1020)	(765)	(510)	(255)
55(a)(i) Premium received on initial recognition	(1200)				
55(a)(ii) Insurance acquisition cash flows	180				
55(b)(i) Premiums received in the period		0	0	0	0
55(b)(iii) Amortisation of insurance acquisition cash flows		(45)	(45)	(45)	(45)
55(b)(v) Insurance revenue applying B126[1]		**300**	**300**	**300**	**300**
Closing balance of insurance contract asset / (liability)	**(1020)**	**(765)**	**(510)**	**(255)**	**0**

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[1] Expected premium receipts allocated to coverage periods (CU1200 / 4 periods = CU300)

<u>Journal entries</u>

<u>At initial recognition – 01.07.X1</u>

Receipt of premiums:

Dr	Cash	1200	
Cr	Insurance contract liability		1200

Insurance acquisition cash flows:

Dr	Insurance contract liability	180	
Cr	Cash		180

<u>At each reporting date (30.09.X1, 31.12.X1, 31.03.X2 and 30.06.X2)</u>

Amortisation of insurance acquisition cash flows:

Dr	Insurance service expenses	45	
Cr	Insurance contract liability		45

Insurance revenue:

Dr	Insurance contract liability	300	
Cr	Insurance revenue		300

Scenario 2 – Premium paid at the end
Existing practice

Insurance line items on the statement of financial position and revenue reported

Reporting date	01.07.X1	30.09.X1	31.12.X1	31.03.X2	30.06.X2
Premium receivable	1200	1200	1200	1200	0
Unearned premium reserve (UPR)	(1200)	(900)	(600)	(300)	0
Deferred acquisition cost (DAC)	180	135	90	45	0
Sum of insurance line items on the statement of financial position (overall asset position)	**180**	**435**	**690**	**945**	**0**
Revenue for each period (change in UPR)		**300**	**300**	**300**	**300**

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Scenario 2 – Premium paid at the end
IFRS 17 PAA

8

Insurance contract asset / (liability) on the statement of financial position and revenue reported

Reporting date	01.07.X1	30.09.X1	31.12.X1	31.03.X2	30.06.X2
Opening balance	0	180	435	690	945
55(a)(i) Premium received on initial recognition	0				
55(a)(ii) Insurance acquisition cash flows	180				
55(b)(i) Premiums received in the period		0	0	0	(1200)
55(b)(iii) Amortisation of insurance acquisition cash flows		(45)	(45)	(45)	(45)
55(b)(v) Insurance revenue applying B126[1]		**300**	**300**	**300**	**300**
Closing balance of insurance contract asset / (liability)	**180**	**435**	**690**	**945**	**0**

[1] Expected premium receipts allocated to coverage periods (CU1200 / 4 periods = CU300)

Journal entries

At initial recognition – 01.07.X1

Insurance acquisition cash flows:

Dr	Insurance contract asset	180
Cr	Cash	180

At each reporting date (30.09.X1, 31.12.X1, 31.03.X2 and 30.06.X2)

Amortisation of insurance acquisition cash flows:

Dr	Insurance service expenses	45
Cr	Insurance contract asset	45

Insurance revenue :

Dr	Insurance contract asset	300
Cr	Insurance revenue	300

At the end of the coverage period (30.6.X2)

Receipt of premium:

Dr	Cash	1200
Cr	Insurance contract asset	1200

Scenario 3 – Premium paid monthly
Existing practice

Insurance line items on the statement of financial position and revenue reported

Reporting date	01.07.X1	30.09.X1	31.12.X1	31.03.X2	30.06.X2
Premium receivable	1200	900	600	300	0
Unearned premium reserve (UPR)	(1200)	(900)	(600)	(300)	0
Deferred acquisition cost (DAC)	180	135	90	45	0
Sum of insurance line items on the statement of financial position (overall asset position)	**180**	**135**	**90**	**45**	**0**
Revenue for each period (change in UPR)		**300**	**300**	**300**	**300**

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Scenario 3 – Premium paid monthly
IFRS 17 PAA

10

Insurance contract asset / (liability) on the statement of financial position and revenue reported

Reporting date	01.07.X1	30.09.X1	31.12.X1	31.03.X2	30.06.X2
Opening balance	0	180	135	90	45
55(a)(i) Premium received on initial recognition	0				
55(a)(ii) Insurance acquisition cash flows	180				
55(b)(i) Premiums received in the period		(300)	(300)	(300)	(300)
55(b)(iii) Amortisation of insurance acquisition cash flows		(45)	(45)	(45)	(45)
55(b)(v) Insurance revenue applying B126[1]		**300**	**300**	**300**	**300**
Closing balance of insurance contract asset / (liability)	**180**	**135**	**90**	**45**	**0**

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[1] Expected premium receipts allocated to coverage periods (CU1200 / 4 periods = CU300)

Journal entries

At initial recognition – 01.07.X1

Insurance acquisition cash flows:

Dr	Insurance contract asset	180
Cr	Cash	180

At each reporting date (30.09.X1, 31.12.X1, 31.03.X2 and 30.06.X2)

Receipt of premiums:

Dr	Cash	300
Cr	Insurance contract asset	300

Amortisation of insurance acquisition cash flows:

Dr	Insurance service expenses	45
Cr	Insurance contract asset	45

Insurance revenue:

Dr	Insurance contract asset	300
Cr	Insurance revenue	300

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