Application of IFRS 17 in Korea

Reinsurance

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※ The views expressed in this presentation are those of the presenters. Official positions of the KASB on accounting matters are determined only after extensive due process and deliberation.

Contents

1. Overview

focused on reinsurance contracts held

1. Scope and Measurement Model

IFRS 17 applies to:

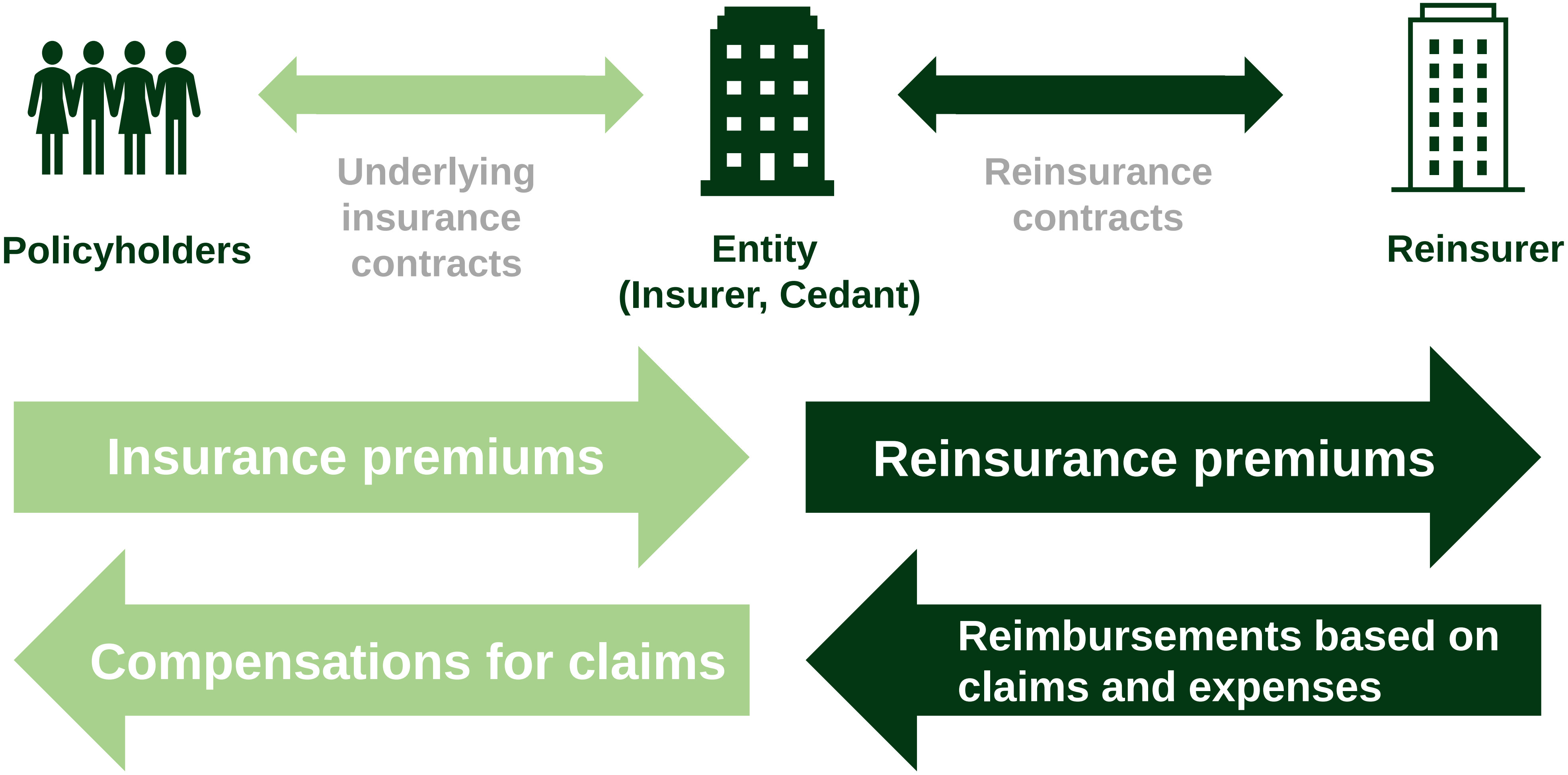
(a) insurance contracts issued (including **reinsurance contracts issued**);

(b) **reinsurance contracts held**; and

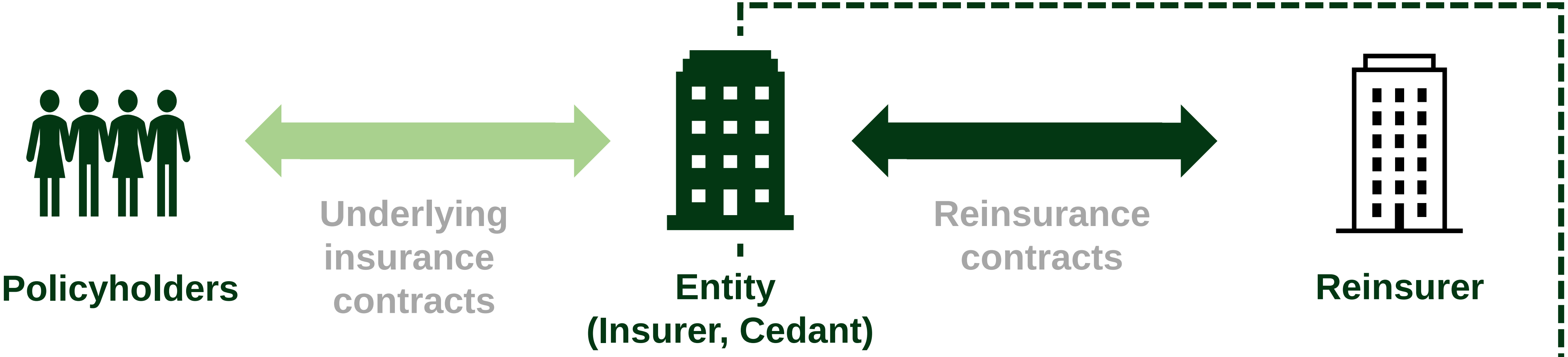
(c) investment contracts with discretionary participation features issued by an entity that also issues insurance contracts

Reinsurance Contracts held	**Apply the general measurement model with certain modifications**
Reinsurance Contracts issued	**Apply the general measurement model (BBA)**

2. Reinsurance Contracts : structure of transaction



3. Cedant's accounting



The cedant recognizes, measures and presents separately

Insurance Contracts (In general, a liability)	Reinsurance Contracts held (In general, an asset)

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4. Reinsurer's accounting

Reinsurance contracts

Entity (Insurer, Cedant)

Reinsurer

Cedant's accounting

Reinsurance Contracts held

Apply GM(BBA) with certain modifications

Reinsurer's accounting

Reinsurance Contracts issued

Apply GM(BBA)

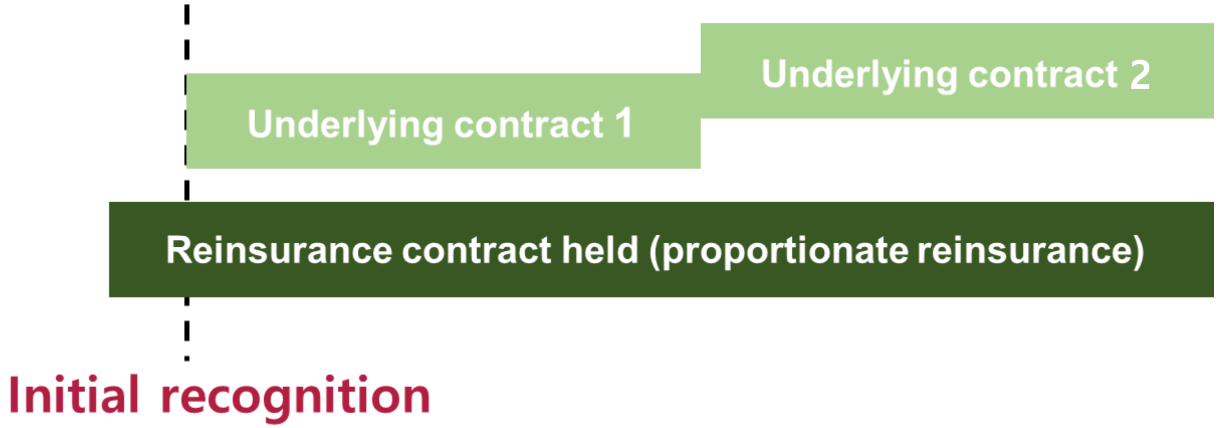
No detailed requirements for reinsurance contracts issued in IFRS 17

5. Recognition

Proportionate reinsurance - later of:

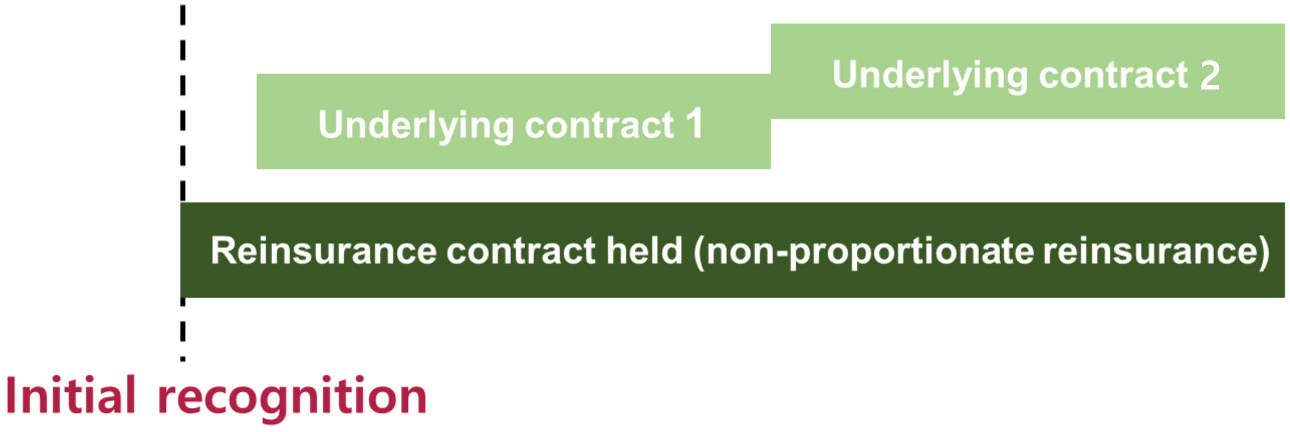
(a) beginning of coverage period of the group of reinsurance contracts; or

(b) the initial recognition of any underlying insurance contract.



5. Recognition

In other cases, at the beginning of the coverage period of the group of reinsurance contracts held



Insurance contracts issued

Earliest of:
(a) the beginning of the coverage period of the group of insurance contracts;
(b) the date the first payment from a policyholder in the group becomes due; or
(c) for a group of onerous contracts, when the group becomes onerous

6. Measurement – Principle

Measured as the sum of:

1. **Fulfilment cash flows (FCF)**
   - ① **PV** of probability-weighted expected future cash flows (reflecting financial risk)
   - ② Explicit risk adjustment for non-financial risk **(RA)**
2. **Contractual service margin (CSM)**
   - ③ Net **cost or gain** on purchasing reinsurance

① PV of CF | ② RA (FCF) + ③ Net cost/gain (CSM) = IFRS 17 asset or liability

Insurance contracts issued

CSM : Unearned profit, Expected loss → immediately in profit or loss

6. Measurement on initial recognition – ① PV of FCF

Expected cash flows

- Consistent assumptions with the underlying insurance contracts to estimate each CF of reinsurance contract held
- To forecast CF within reinsurance contract boundary (consistent with reinsurance contract issued)
- The boundary of CF might include cash flows related to underlying insurance contracts that are expected to be issued in the future
- Measure non-performance risk of reinsurer

How to measure?

Discount rate

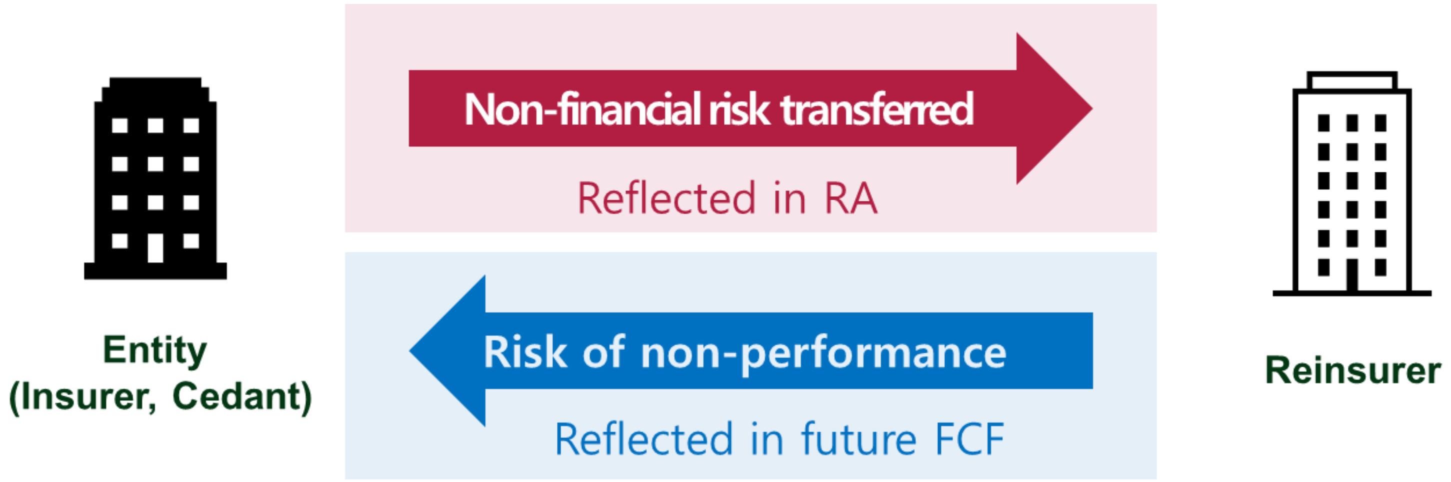
- Reflects the nature and timing of CF and the liquidity characteristics of the reinsurance contracts held

6. Measurement on initial recognition – ② RA

Risk adjustment for non-financial risk

- The amount of risk transferred to reinsurer by the entity (cedant)

Transfer of risk between an insurer and a reinsurer



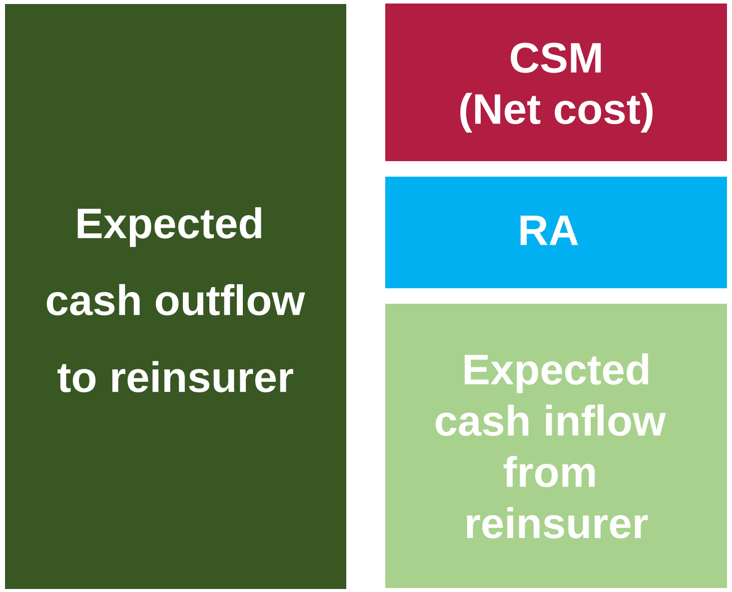
Insurance contracts issued

the compensation an entity requires for bearing the uncertainty about the amount and timing of the cash flows from non-financial risk

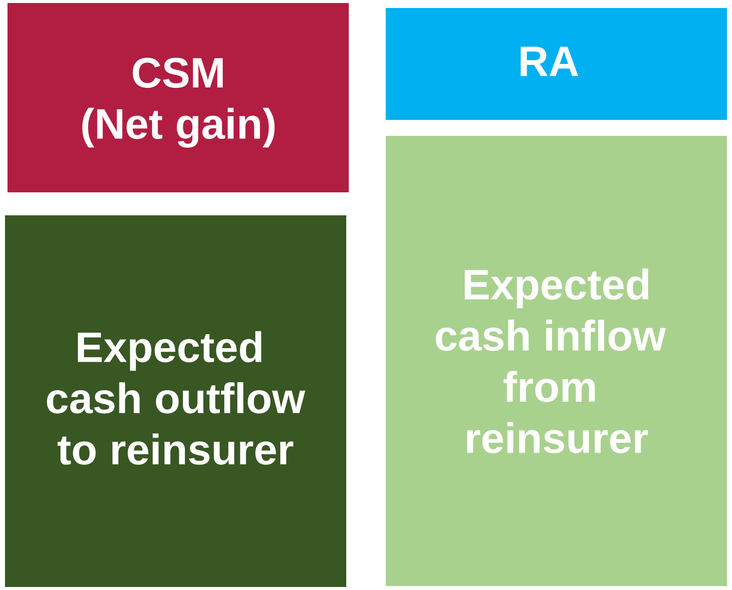
6. Measurement on initial recognition – ③ CSM

CSM on initial recognition

Net cost
on purchasing reinsurance



Net gain
on purchasing reinsurance



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6. Measurement on initial recognition – ③ CSM

Example : CSM on initial recognition

Underlying insurance contracts

PV of future cash-in	(1,000)
PV of future cash-out	900
PV of future CF	(100)
Risk adjustment	60
FCF	(40)
CSM	40
Insurance contract liability (asset)	**-**

Reinsurance contract
: covering 30% of claim
in return for fixed premium

Reinsurance contracts held

	Case 1 Premium paid : 260	Case 2 Premium paid : 300
PV of future cash-in (recoveries)	(270)	(270)
PV of future cash-out (premium paid)	260	300
PV of future CF	(10)	30
Risk adjustment	(18)	(18)
FCF	(28)	12
CSM	28	(12)
Reinsurance contract asset	**-**	**-**
Profit or loss on initial recognition	**-**	**-**

7. Level of aggregation

Portfolio & Group of contracts

- The portfolio or group may be a single contract
- If the portfolio has more than one contracts, divide portfolio into groups at initial recognition:
    1. net gain of purchasing reinsurance (i.e., net inflow)
    2. net cost of purchasing reinsurance (i.e., net outflow) with no significant possibility of becoming a net gain with no significant possibility of becoming a net gain
    3. other net cost of purchasing reinsurance (i.e., net outflow)
- Not allowed to group contracts purchased more than a year apart
- Groups are not reassessed

8. Subsequent Measurement

	Initial measurement	Subsequent measurement
① PV of CF	Current assumptions	Current assumptions
② RA	Current assumptions	Current assumptions
③ CSM	The amount that represents the net cost or net gain of purchasing reinsurance	Update by reflecting: • Time value of money • Adjustments to related to future service • Allocation for services

(CSM) Exceptions to the general measurement model

- Change in FCF related to future service in reinsurance contract held
  - ✓ if this change results from a change in FCF allocated to underlying insurance contracts that is recognized in profit or loss
- Reversals of a loss recovery-component

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9. Presentation

Reinsurance contracts held are presented separately from insurance contracts issued on the face of:

- statement of financial position
- statements of financial performance

Example : presentation of insurance service result

Net presentation

	2021
Insurance revenue	1,000,000
Insurance service expense	(600,000)
Net expense from reinsurance contracts	(100,000)
Insurance service result	300,000

Gross presentation

	2021
Insurance revenue	1,000,000
Insurance service expense	(600,000)
Amounts recovered from reinsurance	200,000
Reinsurance premiums	(300,000)
Insurance service result	300,000

10. Disclosures

Separate reconciliations shall be disclosed for insurance contracts issued and reinsurance contracts held.

- shall be adapted to reflect the features of reinsurance contracts held that differ from insurance contracts issued

Separate information shall be provided for insurance contracts issued and reinsurance contracts held

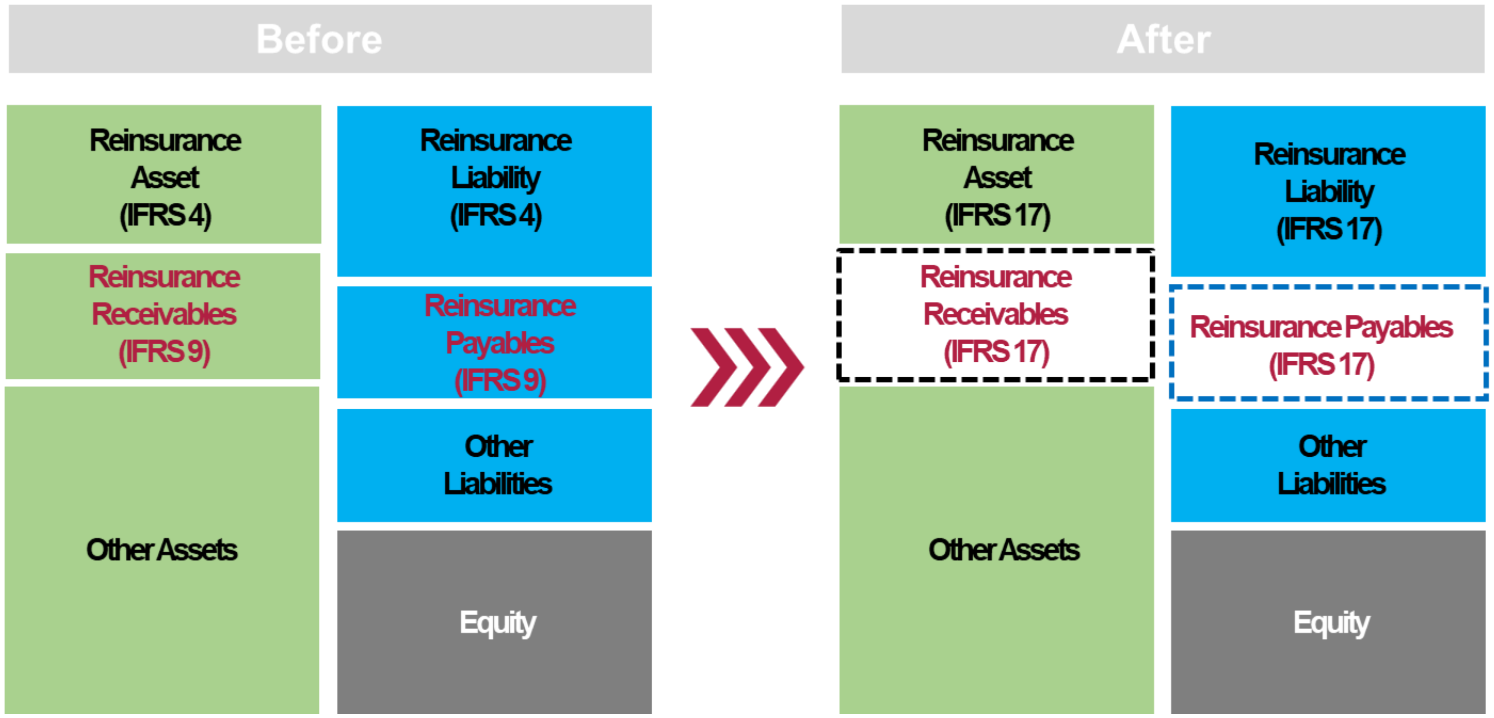
- explaining when an entity expects to recognise the contractual service margin remaining at the end of a reporting period in profit or loss.

Disclosure on the revenue is not required to reinsurance contracts held.

- applying IFRS 17, revenue does not arise from reinsurance contracts held

2. Effects of IFRS 17 on Reinsurer

1. Financial Effects : Statement of financial position



Effects on FS

- ✓ Decrease in total assets & total liabilities
- ✓ Increase in volatility of net asset due to FV measurement of insurance liability

In IFRS 17, CFs related to ‘reinsurance receivables and payables’ (※), are included in the measurement of expected CF of reinsurance asset (reinsurance contracts held) and reinsurance liability (reinsurance contracts issued) in IFRS 17

(※) Reinsurance receivables and payables were recognized as asset/liabilities in IFRS 4

2. Financial Effects : Statement of financial performance

IFRS 4	IFRS 17
I. Revenue	**I. Insurance service result**
1. Insurance operation revenue	1. Insurance revenue
(a) Premiums (insurance contracts issued)	(a) Claims incurred (expected)
(b) Reimbursements (insurance contracts held)	(b) Other expense incurred (expected)
(c) Commissions (insurance contracts held)	(c) RA release / CSM allocation
…	…
2. Investment operation revenue	2. Insurance expense
3. Special account revenue / Other revenue	(a) Claims incurred (actual)
…	(b) Other expense incurred (actual)
II. Expense	(c) Loss from onerous contract
1. Insurance operation expense	…
(a) Increase in insurance contract liabilities	**II. Investment revenue**
(b) Claims paid (insurance contracts issued)	1. Insurance finance income
(c) Premiums paid (insurance contracts held)	(a) Interest income from insurance assets
(d) Commissions (insurance contracts issued)	(b) Foreign exchange gain from insurance liabilities
(e) Operating expense	…
…	**III. Investment Expense**
2. Investment operation expense	1. Insurance finance expense
3. Special account expense / Other expense	(a) Interest expense from insurance liabilities
…	(b) Foreign exchange loss from insurance liabilities
	…
	…

IFRS 4	IFRS 17
IV. Operating income	**III. Operating income**
VI. Non-operating income	**IV. Non-operating income**
VII. Income tax expense	**VI. Income tax expense**
VII. Profit for the year	**VII. Profit for the year**
IX. Other comprehensive income	**VIII. Other comprehensive income**
	(a) Effect of a change in discount rate (insurance liabilities)
IIX. Total comprehensive income	**IX. Total comprehensive income**

2. Financial Effects : Statement of financial performance

Effects on FS

✓ **Decrease in insurance revenue and insurance expense due to recognition of investment component**

- (Before) Insurance revenue and expense were recognized on cash basis

✓ **Improvement in comparability by providing quantitative information on expected and actual insurance income or expense**

- (Before) No provision of the information regarding expectation

✓ **Clearer analysis of underwriting result by disaggregating foreign exchange gain/loss from insurance expense**

- (Before) Foreign exchange gain/loss was included in insurance operation expense

✓ **Improvement in timeliness of P&L by using current estimation**

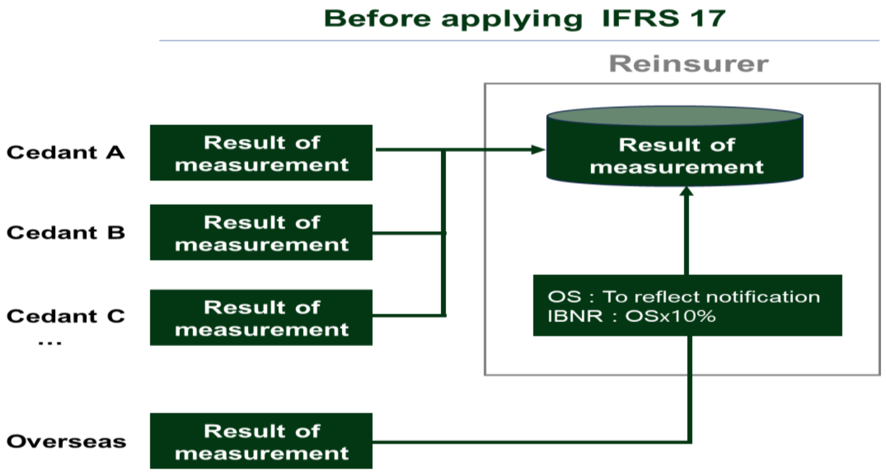
- (Before) Time-lag in obtaining reinsurance invoices from cedants → Delay in recognition & measurement

3. Key Accounting Policies of Reinsurer

1. Reinsurer's estimation of future CFs from insurance contracts issued

How to reasonably measure reinsurance contracts issued without information from cedants?

- IFRS17 sets out the principle of including all available reasonable and supportable information about estimates of future cash flows
- However, specific methodology for estimating future cash flows of reinsurance contracts issued is not provided, and it was not discussed even in the TRG
- Before applying IFRS 17, industry practice was for the reinsurer to receive only a settlement letter from the cedent, which is a summary of the reinsurance premiums to be received and reimbursements to be paid



1. Reinsurer's estimation of future CFs from insurance contracts issued

IFRS 17 paragraph 33, B37

33 … The estimates of future cash flows shall:

(a) incorporate, in an unbiased way, all reasonable and supportable information available without undue cost or effort about the amount, timing and uncertainty of those future cash flows. …

B37 The objective of estimating future cash flows is to determine the expected value, or probability-weighted mean, of the full range of possible outcomes, considering all reasonable and supportable information available at the reporting date without undue cost or effort. Reasonable and supportable information available at the reporting date without undue cost or effort includes information about past events and current conditions, and forecasts of future conditions.

1. Reinsurer's estimation of future CFs from insurance contracts issued

(Policy) A model averaging over some of the treaties for which information is available
→ determined after consultation with an auditor

Initial measurement

- To generate hypothetical holding contract information by sampling contracts per case from informed treaties
- Detailed procedure
  1. To create a pool to generate holding contract information from data of similar treaties and;
  2. Extract contracts per case with the features of treaty such as collateral class and contract year from the pool
  3. Determine the sampling level so that the distribution of contracts in the sample would be similar to the distribution of informed treaties

Subsequent measurement

- To update the data to the average of informed treaties as of the measurement date by re-sampling

Setting actuarial assumptions to estimate future cash flows

- By analogizing actuarial assumptions that were used to measure the treaties to which the sample belong

3. Portfolio

How to determine portfolio of insurance contracts?

- Generally, treaty covers various kinds of risks from underlying insurance contracts
- It's very difficult to set portfolio for some treaties which covers all underlying insurance contracts of an insurer (cedant).

IFRS 17 paragraph 14

14 An entity shall identify portfolios of insurance contracts. A portfolio comprises contracts subject to similar risks and managed together.. …

2. Portfolio

(Policy) To set portfolio in accordance with the criteria for underlying insurance contracts after considering **risks (similar risks)** and ways of **management (managed together)**

1. Similar risks

Alternatives considered

(View 1) Identify the 'representative' risk of a particular treaty and classify it according to the portfolio classification criteria for underlying insurance contracts

(View 2) All treaty reinsurance should be grouped into a portfolio called 'composite' risk

Conclusion

Apply (View 1) in principle, but apply (View 2) to treaties difficult to identify the representative risk

2. Managed together

Conclusion

Group into **'Proportional'** and '**Non-proportional'** based on how responsibility is shared considering that **'Proportional'** and '**Non-proportional'** contracts are managed separately due to their different way of sharing responsibility

03 Key Accounting Policies of Reinsurer

2. Portfolio

Underlying insurance contract

Life Insurance

Similar risk	Single Group
Death	Non-par
	Par
	Variable
Health	Non-par
	Par
	Variable
Pension/ Savings	Non-par
	Par
	Variable
	Asset-linked
Others	Non-par
	Par
	Variable

Long-term Non-life Insurance

Similar risk	Single Group
Casualty	Non-par
	Par
Disease	Non-par
	Par
Property	Non-par
	Par
Pension/ Savings	Non-par
	Par
	Asset-linked
Others	Non-par
	Par

General non-life Insurance

Collaterial
Fire
Comprehensive
Marine
Worker Compensation
Liability
Casualty
Technology
Guarantee
Car
Overseas
Others

Reinsurance contract

Life Insurance

Similar risk	Single Group
Death	Propotional
	Non-propotional
Health	Propotional
	Non-propotional
Pension/ Savings	Propotional
	Non-propotional
Others	Propotional
	Non-propotional
Composite	Propotional
	Non-propotional

Long-term Non-life Insurance

Similar risk	Single Group
Casualty	Propotional
	Non-propotional
Disease	Propotional
	Non-propotional
Property	Propotional
	Non-propotional
Pension/ Savings	Propotional
	Non-propotional
Others	Propotional
	Non-propotional

General non-life Insurance

Collaterial	Single Group
Fire	Propotional
	Non-propotional
Comprehensive	Propotional
	Non-propotional
Marine	Propotional
	Non-propotional
Worker Compensation	Propotional
	Non-propotional
Liability	Propotional
	Non-propotional
Casualty	Propotional
	Non-propotional
Technology	Propotional
	Non-propotional
Guarantee	Propotional
	Non-propotional
Car	Propotional
	Non-propotional
Overseas	Propotional
	Non-propotional
Others	Propotional
	Non-propotional
Composite	Propotional
	Non-propotional

2. Portfolio : Unit of account

(Policy) To set up a unit of account based on individual reinsurance contract (ex: a treaty)

- Setting up a group of contracts based on policies contained within a treaty may be inconsistent with IFRS 17
- However, the group of contracts (CoC) is subject to annual cohort requirement
- Therefore, in general, GoCs are determined based on underwriting year of underlying insurance contracts covered by the reinsurance contract

IFRS 17 paragraph 22

16 An entity shall divide a portfolio of insurance contracts issued into a minimum of:
(a) a group of contracts that are onerous at initial recognition, if any;
(b) a group of contracts that are onerous at initial recognition, if any; a group of contracts that at initial recognition have no significant possibility of becoming onerous subsequently, if any; and
(c) a group of the remaining contracts in the portfolio, if any.

22 … An entity shall not include contracts issued more than one year apart in the same group. To achieve this the entity shall, if necessary, further divide the groups

3. Boundary of a reinsurance contract

How to determine contract boundary of reinsurance contracts issued?

Contract boundary

Cash flows are within the boundary of an insurance contract if they arise from **substantive rights and obligations** that exist during the reporting period in which the entity **can compel the policyholder to pay the premiums** or in which the entity has a **substantive obligation to provide the policyholder with insurance contract services**

IFRS 17 paragraph 34

34 … A substantive obligation to provide insurance contract services ends when:

(a) the entity has the practical ability to reassess the risks of the particular policyholder and, as a result, can set a price or level of benefits that fully reflects those risks; or

(b) both of the following criteria are satisfied:

(i) the entity has the practical ability to reassess the risks of the portfolio of insurance contracts that contains the contract and, as a result, can set a price or level of benefits that fully reflects the risk of that portfolio; and

(ii) the pricing of the premiums up to the date when the risks are reassessed does not take into account the risks that relate to periods after the reassessment date.

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3. Boundary of a reinsurance contract

Comparison of contract boundary (required by IFRS 17)

		Insurer (cedant)		Reinsurer
		Underlying insurance contract	Reinsurance contract held	Reinsurance contract issued
Rights	Definition	Right to compel policyholder to pay premiums	Right to reinsurance services	Right to compel insurer(cedant) to pay premiums
	Termination	When policyholder has a right to terminate unilaterally	When reinsurer has the practical ability to reassess reinsurance premium or reinsurer has a right to terminate contract unilaterally	When insurer(cedant) has a right to terminate contract unilaterally
obligation	Definition	Obligation to provide insurance services	Obligation to pay reinsurance premium	Obligation to provide reinsurance services
	Termination	When insurer has the practical ability to reassess insurance premium or insurer has a right to terminate contract unilaterally	When insurer(cedant) has a right to terminate contract unilaterally	When reinsurer has the practical ability to reassess reinsurance premium or reinsurer has a right to terminate contract unilaterally
Contract boundary Match?		May not match	May not match / Match	Match

3. Boundary of a reinsurance contract

Cedant	Reinsurer	Type1	Type2	Type3	Type4
Right	Obligation	○	○	X	X
Obligation	Right	○	X	○	X
Contract boundary		Continue	Continue	Continue	End

[Type1] Both cedant' right to reinsurance service and obligation to pay premiums continue	
Type1	Notwithstanding Article XX of these Special Conditions, in the case of a reinsurance contract for which the period set out below has elapsed, the ceding company may, by mutual agreement with the reinsurer, cease to cede all or part of the retained contract from the date of payment of the reinsurance premium for the following year → **Possible to terminate an existing reinsurance contract by mutual consent**
Type2	Upon the expiry of the term of the treaty of 15 years or more, the cedant shall have the right to cease ceding for all or part of the in-force contract by giving the reinsurer 90 days' written notice prior to the renewal date set out in the special clause → **The cedant can terminate the in-force reinsurance contract by unilateral notice, but the reinsurer has no option**
Type3	For the 5y, 7y and 10y renewable products the reinsurer shall be able to increase reinsurance rates after 5, 7 and 10 treaty years, respectively, and then after each subsequent 5 year period. Revised reinsurance premium rates shall apply to policies as from their next renewal dates. Reinsurance premium rate increases shall be based on the claims ratio in the treaty year immediately preceding the repricing date as per the following schedule → **Reinsurer can calculate reinsurance premium rates at renewal based on the cedant's loss ratio(*) but the cedent has no option to terminate the in-force reinsurance contract**
Type4	The reinsurer remains liable for the ceded individual contracts up to 10 years from the date of formation of the underlying insurance contracts, at which point the ceded individual contracts revert to the cedant → **At a certain point, the existing reinsurance contracts are automatically recaptured to the cedant**

4. Boundary of a reinsurance contract : New contracts

Case	Clause of treaty	Estimated period of future new contracts after initial recognition
Always 3 months' notice	This Agreement shall be effective as of 10 February 2014. This Agreement may be terminated by either party upon three months' written notice.	3 months
3 months' notice as of 31 December	This treaty applies to underlying insurance contracts for which liability commences on or after 2 September 2013. It may be terminated as of 31 December of each year. However, it shall continue in force unless notice of termination is given in writing not less than three months prior to the date of termination. Reinsurance contracts already in force and continuing to be maintained shall continue in force until the expiry of the underlying insurance period, even after the termination of this treaty.	By the end of December
Notifiable after some point in the future	This Agreement shall be effective as of 22 October 2010. This Agreement may be amended by agreement of the parties on or after 1 January 2012, and either party may terminate this Agreement for new contracts as of 31 December of each year by giving at least three months' prior notice.	By specific point of time in the future

Needed to estimate and recognise the volume of future new contracts until such time as ceding new contracts can be discontinued

4. investment component

Whether an investment component exists in a reinsurance contract with profit commission?

Definition

'Investment component' is defined as the **(minimum)** amounts that an insurance contract requires the entity to repay to a policyholder in all circumstances, regardless of whether an insured event occurs

- Profit commissions, which are mandatory ex-post reimbursements by the reinsurer to the cedant, taking into account the loss ratio, meet the definition of an investment component
- However, in the case of reinsurance contracts where the cedant only cedes risk premiums, no investment component relating to surrender or maturity refunds exist in such reinsurance contracts, underlying insurance contracts

4. investment component

IFRS 17 Appendix A, paagraph BC34

Appendix A
investment component : The amounts that an insurance contract requires the entity to repay to a policyholder in all circumstances, regardless of whether an insured event occurs.

BC34 … However, the Board decided that defining an investment component in this way does not faithfully represent the fact that the amount accumulated in the account balance through deposits by the policyholder is paid to the policyholder in all circumstances, including in the event of the policyholder’s death. In the Board’s view, the insurance benefit is the additional amount that the entity would be required to pay if an insured event occurs.

4. investment component

(Policy) To identify the cash flows corresponding to the investment component under the terms of the contract to distinguish between the investment and insurance component

Example
: Reinsurance premium 1000, Profit commission rate 80%

`	Case 1 Loss ratio : 0%	Case 2 Loss ratio : 60%	Case 3 Loss ratio : 80%	Case 4 Loss ratio: 110%
Premium	1,000	1,000	1,000	1,000
Loss ratio commission (A)	**-**	**(600)**	**(800)**	**(1,100)**
Profit before settlement	1,000	400	200	(100)
Profit commission %	80%	80%	80%	80%
Profit commission (B)	(800)	(320)	(160)	-
Total commission (A+B)	**(800)**	**(920)**	**(960)**	**(1,100)**

Investment component : 800 = 1,000 (premium) x 80% (profit commission ratio)

Thank you very much for listening!
Any Questions?

THANK YOU