Meeting information

AASB 17 *Insurance Contracts* Transition Resource Group (TRG)
7 December 2022
2pm – 4pm

Objective:

- Update from APRA on reporting and prudential standards, and APRA Connect
- Update on public sector insurance project
- Update on Tax and AASB 17 (ICA/FSC)
- Industry papers discussion:
    - ARPC cyclone reinsurance contract held - AASB 17 contract boundary
    - Tax accounting for AASB 17 transition adjustments
    - Taxes and levies – foreign resident reinsurer withholding tax
- IFRS Interpretation Committee outreach - premiums receivable from an intermediary

Topic	Agenda paper
Welcome and introduction	
Welcome and introduction by TRG Chair ("The Chair" hereafter).	
Update from APRA on reporting and prudential standards, and APRA Connect	
• APRA released a package that consists of prudential standards and reporting standards in Q3 2022 [actual date 27 September 2022]. • APRA has consulted on one narrow issue on accounting equity, which could arise if insurance liabilities under AASB 17 *Insurance Contracts* (AASB 17) are higher and therefore give accounting equity that is lower than the capital base, which under an extreme scenario could pose the risk of insolvency. The responses indicate that it is a very narrow issue that does not affect many insurers, however, it was noted by one member that the new requirements for accounting equity would impact all insurers. • The same member expressed concern about the consultation period being very short. APRA representative responded that the issue had been flagged in the two previous Quantitative Impact Studies (QIS) and a lot of work was done around calibration. • The Chair said that this issue should be discussed by the Actuaries Institute AASB 17 Taskforce APRA working group if the scope of this issue becomes broader than anticipated. • In response to a question regarding when reporting forms are expected to be made available APRA representative said they are still being developed; however, definitions and the nature of collections are provided in the finalised reporting standards and as such, entities are expected to be able to do some preliminary work on preparing collections. The	

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forms under development are closely aligned with reporting standards as well as QIS collections. In addition to the APRA Connect guidance already available for user familiarisation on APRA website, APRA plans to provide Excel based artefacts that provide more information including the final format of the tables, definitions and all the dimensions, concepts and labels that will be included in the collection. Further information is planned to be released by the end of Q1 2023 with information on artefacts likely to be made available earlier. Should the release be close to the reporting period, the release might be done in two stages in the external testing environment which users will have access to. The artefacts will cover both Level 1 and Level 2 entities. APRA is not considering a deferral of the effective date of 1 July 2023. • A member suggested that it would be useful to know which forms are expected to have material changes in the final version so that insurers can prepare for those changes in advance. • APRA representatives noted that the changes for both accounting and capital forms are not expected to be material. Next steps • APRA plans to provide a session on APRA Connect at a future TRG meeting.	
Updates from public sector insurance project	**ATT1**

• The AASB and the NZASB will finalise the modified AASB 17 for the public sector at their respective December 2022 board meetings.
• The Boards received three formal submissions as well as other informal feedback during the Fatal Flaw Review (FFR) draft Standard exposure period.
• Main differences between AASB ED 319/NZASB ED 2022-3 and the FFR draft Standard include:
    ○ the FFR draft Standard provides public sector entities with an accounting policy choice for the premium allocation approach.
    ○ the FFR draft Standard contains an additional transitional provision that would mean public sector entities apply AASB 17 to arrangements in run-off if they currently apply AASB 1023 *General Insurance Contracts*, and apply AASB 137 *Provisions, Contingent Liabilities and Contingent Assets* if they currently apply AASB 137.
 	
Next steps
 	
• The two Boards will consider whether to change the effective date to 1 July 2026 in their upcoming Board meetings. [Note the effective date of 1 July 2026 was approved at the December board meeting]	

Update on Tax and AASB 17 (ICA/FSC)	
• A representative from the Insurance Council of Australia (ICA) provided background and highlighted issues for general insurers: ○ Current tax laws are constructed in a way that imports accounting concepts of AASB 1023 *General Insurance Contracts* into tax law. When AASB 17 comes into effect, some of the existing AASB 1023 concepts will no longer exist.	

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- Absent any action by the ATO and Treasury, this leaves taxpayers with two options: (1) maintaining a second set of accounts based on the AASB 1023 basis; (2) adapting elements of AASB 17 into existing tax laws. If option 2 is chosen, there will be an inherent risk, and taxpayers might need to recognise uncertain tax positions in accordance with IFRIC 23 *Uncertainty over Income Tax Treatments*.
    - The ICA has engaged with the ATO and Treasury. The assistant treasurer has requested a second briefing paper from Treasury to help guide their decisions in relation to this.
    - The ICA hopes that Treasury will provide some form of statement or communication by the end of 2022 to help provide the industry with some direction so the tax impact of AASB 17 can be quantified.

- Representative from the Financial Services Council (FSC) provided background and an update from a life insurance perspective:
    - There is more alignment between the life tax code and the prudential standards compared to the general tax code. For example, when products go into loss recognition, there is an adjustment for tax purposes such that losses are deferred over the life of the policy.
    - Under AASB 17, for some products there is an option for life insurance companies to either continue recognising or derecognising some of the different acquisition costs.
    - Under current tax law, if life insurance companies recognise part of that deferred acquisition cost on entry into AASB 17 they will receive an upfront tax deduction.
    - Given life insurance losses over the last four to five years, life insurers may be entitled to a tax deduction but may not be able to absorb and utilise that for at least the next five years or more. Irrespective of their ability to absorb the acquisition costs deduction, technically these deductions will become available absent an announcement to the contrary from Treasury.
    - The FSC has made various representations to the Treasury, engaged with the industry, and documented the issues. The Treasury has issued a briefing note to the minister.
    - There has been discussion between the industry, ATO, and Treasury on potentially introducing tax transitional rules to spread the deduction on entry over five years or more.
    - The FSC is hoping to have an announcement from Treasury by the end of 2022.
- One member noted that for the last three years, we only received second-hand updates through the ICA and the FSC.
- The Chair asked, since the Treasury has issued a briefing note to the minister, whether there has been any indication that there will be an announcement. The representative from the FSC responded that they had tried numerous channels to understand what was in the briefing note. The only indication they received is that the Treasury is supportive of industry representations from a life insurance perspective.
- The Chair confirmed with the representative from the FSC that insurers' current year tax returns will not be affected, but their disclosures as at the end of December might be affected.
- One member asked a question about double taxation. The representative from the ICA responded that proposals discussed included a transitional measure to ensure that there will not be any double tax outcomes.

Next Steps

- Await announcement from Treasury.

Topic	Agenda paper
Industry papers discussion: ARPC cyclone contract- AASB 17 contract	**ATT2**

<u>Background</u>

- From 1 July 2022 the Australian Reinsurance Pool Corporation (ARPC) established a reinsurance pool for cyclones and related flood damage.
- Similar to the terrorism pool, the cyclone pool is designed to lower insurance premiums for households and small businesses with high cyclone and related flood damage by reducing the cost of reinsurance.
- Large insurers must join the pool before 31 December 2023, and insurers can progressively transfer eligible cyclone policies up to this date.
- Insurers pay reinsurance premiums into the pool which will cover all eligible cyclone and related flood damage above an excess.
- An event will be declared by the Bureau of Meteorology and will cover claims for the period from when the cyclone begins until 48 hrs after the cyclone ends.
- Unlike the terrorism pool, which insurers may join, insurers are required to join the cyclone reinsurance pool when they issue insurance contracts covering cyclone risks.
- When setting premiums that reinsurers are to pay under cyclone reinsurance contracts, the Corporation is to seek:
  (a) to ensure that, over the longer term, premiums paid under such contracts are sufficient to cover or offset:
    - the amounts paid in meeting the Corporation's liabilities under such contracts; and
    - all other amounts applied by the Corporation in so far as those amounts may reasonably be regarded as connected with the cyclone reinsurance scheme; and

  (b) in so far as those premiums are for reinsuring liability under pool insurance contracts that involve medium to high levels of exposure to eligible cyclone losses—to keep the premiums as low as possible while maintaining incentives to reduce and mitigate the risk of eligible cyclone losses; and
  (c) in so far as those premiums are for reinsuring liability under pool insurance contracts that involve lower levels of exposure to eligible cyclone losses—to keep those premiums at levels comparable to what would be charged by other reinsurers.

- AASB 17 contract boundary requirements were considered:
  - Paragraph 34
    - The contract boundary is the longer of;
      - Cedant's obligation to pay premium mirrored by reinsurer's right to compel the reinsured to pay premiums; and
      - Cedant's right to receive insurance service mirrored by reinsurer's obligation to provide insurance service.

  - Paragraph B64 - "*An entity has that practical ability in the absence of constraints that prevent the entity from setting the same price it would for a new contract with the same characteristics as the existing contract issued on that date*".

  - Paragraph BC309A - "*Estimates of future cash flows included in the measurement of a group of reinsurance contracts held include future cash flows that relate to insurance*

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contracts an entity expects to be covered by the reinsurance contracts held in the group. Such cash flows include cash flows related to insurance contracts the entity expects to issue in the future if the entity has a substantive right to receive reinsurance coverage for those insurance contracts."

- Alternative views on the contract boundary of ARPC reinsurance contracts held:

  - View 1 - Perpetual

    • So long as the entity issues underlying insurance contracts it is obliged by law to reinsurer into the pool, insurers cannot cancel the contract.
    • cash flows associated with an ARPC reinsurance contract held would be all the expected cash flows from substantive rights and obligations under the contract with the ARPC based on the expectations at the reporting date.

  - View 2 - Based on an entity's expectations of issuing eligible (underlying) insurance contracts covering eligible cyclone risks.

    • Similar to the first view an entity is obliged by law to reinsurer into the pool, they cannot cancel the contract so long as writing eligible underlying insurance contracts.
    • An entity may assess as part of its annual planning process whether it will continue to write eligible contracts, and therefore the contract boundary will be based on the entity's underlying expectations of how long it will continue to write the underlying contracts.

  - View 3 - Determined by reference to the entity's in-force (underlying) insurance contracts plus 6-month notice period, i.e. applying Clause 1(e) of ARPC reinsurance contract.
    • This is on the basis (per IFRS 17 TRG May 2018 AP3) the ARPC can set the same price for an existing contract and a new contract with the same characteristics.
    • The ARPC has the right (under the contract) to reprice on a 6-month basis, where the price charged for existing policies is the same as for new.
    • The policyholder then can either accept the price or exit the market through exiting the underlying, i.e. within the insurer's control.

<u>TRG discussion</u>

- Much of the discussion was on seeking clarification of Views 2 and 3, particularly around the mandatory nature of the ARPC reinsurance for entities issuing cyclone policies which could extend the period over which the cedant is compelled to pay reinsurance premium.
- In relation to View 2, Chair asked for clarification of the relevance of AASB 17 BC309 as that paragraph appears to focus on identifying the cash flows of future underlying contracts expected to be issued once the contract boundary has already been determined.
- There was discussion around the impact of the contract boundary of the in-force underlying contracts, noting the risks attaching nature of the ARPC contract. Some members held the view that it would be appropriate to determine the contract boundary of the reinsurance contract held based on the contract boundary of the in-force underlying contracts while others noted this to be inconsistent with their understanding of how AASB 17.34 operates.

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• For View 3, some members noted that it may be difficult for the cedant to argue that they can avoid being compelled to pay the reinsurance premium by merely having the ability to stop writing cyclone cover and that the intention to discontinue covering cyclone risk would need to be demonstrated, i.e. via business plan or strategy. • One member held the view that AASB 17.B64 would deem the practical ability to reprice to exist given the offering of 'current price' every six months as required by the ARPC reinsurance contract and this constraint applies to both existing and new contracts. • TRG members did not land on any of the three Views presented. Next steps • Revisit this topic at the next AALC (February 2022) meeting and TRG (March 2023) meeting, respectively.	
Industry papers discussion: AASB 17 tax accounting	**ATT3**

Background
 	
• To the extent an entity has reasonable and supportable information to apply a retrospective approach on transitioning to AASB 17, the requirements of AASB 17 must be applied retrospectively.
• Retrospective application will lead to various insurance liabilities and assets needing to be restated for reporting periods beginning on or after 1 January 2022, being the start date of the comparison year for the first set of AASB 17 financial statements for reporting periods beginning on or after 1 January 2023.
• The restatement will have a corresponding transitional impact on retained earnings.
• It is expected that deferred tax assets or liabilities will be recognised from the change to AASB 17. These tax effects may translate into current tax assets and liabilities in subsequent periods depending on the interaction with local tax laws. This paper addresses where in the financial statements the subsequent changes to these tax effects are recognised.
• Two possible approaches are identified.
  o Approach 1: Current and deferred tax relating to transition adjustments are subsequently recognised in equity, consistent with AASB 112.62A(a).
  o Approach 2: Current and deferred tax relating to transition adjustments are subsequently recognised as income or an expense and in profit or loss for the period, or outside profit or loss, either in other comprehensive income or directly in equity, as they would have been had the entity always applied AASB 17.
 	
TRG discussion
 	
• Two members expressed support for Approach 2 on the basis that the principle of accounting as if AASB 17 had always applied overrides the application of AASB 112.62A(a). There was no declared support for Approach 1.
• TRG members discussed the applicability of a full retrospective approach.
• The presenter stated that, in contrast with changes in other accounting standards, AASB 17 has a current tax impact.	

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Industry papers discussion: Foreign resident reinsurer withholding tax	**ATT4**

- TRG members discussed whether amounts paid by an insurer to the ATO in respect of reinsurance contracts held with a foreign resident reinsurer when the ceding Australian insurer makes an election under section 148 of the Income Tax Assessment Act 1936 fall within one or other of the following categories:
  - an amount collected by the insurer on behalf of a 3rd party, which is not treated as an expense or revenue of the insurer;
  - a cost of issuing insurance contracts, whereby any amount collected to defray the cost of the impost is treated as revenue and the amount paid to the government is treated as an expense of the insurer.
- TRG members noted that the issue has been discussed at two previous TRG meetings as part of a broader discussion on taxes and levies and there had been a lack of consensus about the categorisation of these particular payments. The two alternative views were discussed.
- View 1 is that the insurer is simply acting as a collector of income tax (or a substitute for income tax) for the government because the amount collected relates to particular transactions and is the amount 'paid' to government (albeit together with other taxes).
- View 2 is that, in effect, of the total reinsurance premium payable by the ceding insurer, 97% is paid to the reinsurer and 3% to the ATO. There is no additional cost to the ceding insurer, merely a direction to allocate reinsurance premiums in a particular manner. Hence, 100% of the premium ceded comprises an expense of the ceding insurer, with 3% of the total reinsurance premium paid to the ATO and the remaining 97% to the reinsurer.
- TRG members also noted that informal outreach conducted among Australian insurers in September and October 2022 indicated that most insurers currently apply View 2 in the context of AASB 4 *Insurance Contracts*, AASB 1023 and AASB 1038 *Life Insurance Contracts*.
- Those TRG members who expressed an opinion, supported using View 2 under AASB 17 for one or more of the following reasons:
  - Insurers may have a group of reinsurance contracts held that comprise contracts with both Australian and foreign resident reinsurers. It would seem counterintuitive to have an amount regarded as a 3rd-party collection for the contracts with foreign reinsurers and not for the Australian reinsurers when the insurance risk is the same. All reinsurers are subject to tax on their profits and the payment to the ATO by the insurer is simply an alternative (short-cut) approach to calculating and settling a foreign reinsurer's income tax liability.
  - The amounts paid to the ATO in respect of foreign resident reinsurers can be likened to amounts paid to the ATO on behalf of policyholders in respect of income replacement payments under disability insurance contracts, which the TRG had previously identified as falling within View 2.
  - The treatment of the payment to the ATO by the insurer could possibly be determined by analogy with amounts related to income tax that are specifically chargeable to the policyholder, which is regarded as part of insurance revenue based on AASB 17.B121(a)(ai). That is, they are amounts paid on behalf of the reinsurer and are therefore part of the insurer's expenses.

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Although the amounts are determinable in respect of the premiums ceded on a contract-by-contract basis, there may be multiple contracts with the same or different foreign reinsurers, and the amounts are remitted to the ATO with other taxes annually (and those other taxes are expenses/revenues of the insurer).	

- TRG members noted that a similar (but different) arrangement operates in New Zealand when an insured party pays a premium (including a reinsurance premium) to an overseas insurer, and that insurer (reinsurer) does not have a branch in New Zealand, the insured party is considered to be the insurer's agent. The insured party is required to file an annual income tax return as agent for the foreign insurer – unless the foreign insurer or person acting on their behalf has already filed a return. Ten percent of the premium is treated as taxable income, which is then taxed at the corporate tax rate (28%). The responsibility for filing the income tax return, and paying the income tax, lies with the party paying the premium.
- TRG members observed that different considerations might apply to the New Zealand circumstances than apply to the Australian circumstances.

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Other focus groups

- The updates from the Private Health Insurance (PHI) focus group and the Lenders Mortgage Insurance (LMI) focus group are available in the meeting papers.

IFRS Interpretations Committee outreach - premiums receivable from an intermediary

- The AASB TRG met on 14 November 2022 for impacted members to provide their feedback. The Chair sent out our responses to the IFRS interpretation committee a copy of which is included in the meeting papers. This is noted as an area of continuing uncertainty for implementation projects.

AASB/TRG – survey of AASB 17 disclosure policy choices and judgments

- The AASB TRG has sent out a survey to around 50 insurers to find out what key decisions are being made around AASB 17 disclosure policy choices and judgments.
- The deadline for this survey is 9 December 2022.
- The results will be reported in the March 2023 TRG meeting.

2023 TRG meetings (tentative):

- 22nd of March 2023
- 14th June 2023
- 18th October 2023

End Meeting

Attendance

Members	Anne Driver (Chair) Elaine Hultzer Cassandra Cope Brendan Counsell David Daniels Jennifer Dwyer Jane Clifford Scott Hadfield Richard Sheridan Louise Miller David Rush Frank Saliba Rob Sharma Rhian Saunsbury (for Rachel Poo) Warwick Spargo Leong Tan Ciara Wasley Brett Pickett Eric Cheng
Apologies	Regina Fikkers Toby Langley Anthony Coleman Leann Yuen
Other presenters	Angus Thomson Kos Dimitriou Michael Garrod Anna Donoghoe Andrew Toone Brett Pickett
Secretary	David Ji
AASB Staff	Eric Lee Patricia Au Jia Wei