



Meeting information

AASB 17 *Insurance Contracts* Transition Resource Group (TRG) December 2021
2pm – 4pm

Objective:

- Update from APRA on AASB 17, including APRA Connect
- Update on the AASB's project on the application of AASB 17 *Insurance Contracts* (AASB 17) for public sector entities
- Update from Insurance Council of Australia
- Industry papers discussion:
 - Risk adjustments
 - Treatment of government imposts
- Update from the PHI focus group
- Update from the Medical Indemnity Industry Forum
- Update from Actuaries Institute Taskforce

Note: These minutes provide a summary of discussion only and any views or interpretations do not constitute professional advice. The AASB expressly disclaims all liability for any loss or damages arising from reliance upon any information in this document.

Topic	Agenda paper
Welcome and introduction	
Welcome and introduction by TRG Chair.	
Update from APRA on AASB 17, including APRA Connect	
<ul style="list-style-type: none">• APRA's second Quantitative Impact Study (QIS) package set to be released this month.• The QIS package was noted as now also including sections related to PHI and Friendly Societies, respectively.• To better facilitate the completion of QIS, some flexibility has been allowed for participants to select the financial year ends to be tested.• The Chair asked about the Q&A process for queries:<ul style="list-style-type: none">○ APRA representative responded that the FAQ could be useful and for fundamental issues participants can reach out to APRA via contact details provided in the QIS.○ APRA office will reopen in the first week of January after the Christmas break.• QIS due date: 31 March 2022	

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Updates from public sector insurance project	ATT1
<ul style="list-style-type: none"> • The AASB considered a working draft Exposure Draft (ED) of the public sector specific proposals which the New Zealand Board will consider at its December 2021 Board Meeting. • The ED is expected to be published by the first quarter of next year and the project is expected to be finalised by September 2022. • A key issue is determining whether public sector schemes are within the scope of AASB 17 and to this end a range of indicators have been proposed. • An email with a survey instrument has been sent out to selected participants, with a view to obtaining feedback on the assessment based on the indicators which will be discussed at the February AASB Board Meeting. • Working draft of the ED is available on AASB website. • One member asked whether there is risk for public sector specific requirements to have unintended consequences for the application of AASB 17 in the private sector. <ul style="list-style-type: none"> ○ Representative responded that the way the specific public sector guidance is provided and explained will be made very clear in the usual fashion (with unique paragraph numbering) – accordingly, any differences from AASB 17 will be made clear. • One member asked if any other topics are expected to be discussed at the February AASB Board meeting. <ul style="list-style-type: none"> ○ The main focus will be on the indicators and Board will be reviewing for any fatal flaws. 	
Insurance Council of Australia	ATT2
<p>Tax issues related to AASB 17 implementation</p> <ul style="list-style-type: none"> • Given the limited time available until the effective date of AASB 17, a Special Purpose Insurance Council of Australia Working Group was formed to tackle potential tax issues arising from AASB 17 implementation, which may lead to guidance from the ATO or an amendment to the tax legislation. • The Working Group has been liaising with the Treasury and ATO and is trying to determine whether there are issues in need of resolution and if so, how they are to be resolved. • Key constraints are requisite tax data, time and insurers being at differing stages of AASB 17 implementation. Four key principles for the Working Group to guide the resolution process are: <ul style="list-style-type: none"> • Clear early regulatory guidance – As commencement date is as early as 1 January 2023 for 31 December year ends, legislative timetables will need to be considered if a legislative change is required prior to 1 January 2023 given there will be an election cycle in March or May. • Maximum alignment – As much as possible, tax should follow accounting treatment. • No permanent differences to maximise alignment - Any adjustments booked straight to equity should either be caught under the existing regime or there should 	

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<p>be transitional adjustments to identify them. Significant differences for items such as outstanding claims may be considered by the Treasury to decide whether the difference would be adjusted as one-off or over time.</p> <ul style="list-style-type: none"> • Simplicity of application to minimise administrative burden (one set of books) - Ensure tax compliance is not overly burdensome on the industry. Alignment between tax and accounts would also assist the ATO to attain assurance over what is being returned as taxable income by the industry. • Technical issues that are being considered: <ul style="list-style-type: none"> • Transitional Adjustments: For measurement adjustments for outstanding claims and adjustments for items booked to equity, transitional adjustments may be needed. • Application of the General Model (GM) – Contractual Service Margin (CSM): Existing regime for general insurers is akin to the Premium Allocation Approach. CSM allocation is not contemplated under the existing Division 321 (of income tax legislation) and therefore updating Division 321 to take into account the GM is being considered. • Losses on Onerous Contracts: Currently under Division 321 Liability Adequacy Test leads to a timing adjustment. The Treasury and ATO have been asked to consider whether the existing timing difference arising on the recognition of a liability adequacy provision should be maintained, and whether we can align tax and accounting in respect of onerous losses, particularly where this will not impact the taxable income returned over the life of the contract. • Deferred Acquisition Costs (DAC): Ability to write off DAC on Day 1. Currently under Division 321 there is an alignment between tax and accounting on the spreading of DAC done in an equal and opposite way. Where DAC is expensed as incurred in the accounts under PAA, there will be differences between tax and accounts if legislation is not updated. Treasury have been requested to consider legislative changes (noting PAA is also applied for contracts longer than 1 year, i.e., timing differences straddle year ends). Given that this issue would require separate tracking of DAC for tax purposes with minimal benefit from a tax revenue perspective, preference is for tax treatment to continue to align with accounts. • Liability For Incurred Claims (LIC): Although LIC is broadly similar to outstanding claims liability (OCL), and therefore the ATO could issue guidance to refer to OCL for guidance on LIC, it will be recommended that Division 321 be updated for LIC. 	
<p>Additional notes</p> <ul style="list-style-type: none"> • It was noted that the Working Group will reach out to include PHI perspectives in future discussions. • One member asked what the alignment between tax and accounting would mean for life insurers given their tax follows prudential standards and in response, it was noted that any differences between prudential and accounting standards with respect to tax will be considered to maximise alignment between tax and accounting. 	

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<p>Next steps</p> <ul style="list-style-type: none"> • The ATO agreed with an approach to organise a series of workshops with relevant experts including Treasury with a view to tackling the issues noted above, i.e., to determine how to identify and source the data required to quantify the scale of the issue. 	
Risk adjustment – LRC versus LIC	ATT3
<p>Questions raised/discussed:</p> <p>Question 1: Should the confidence level % used to determine the risk adjustment for the LRC be consistent with the entity’s premium setting approach?</p> <p>View 1: The confidence level % used for measurement of LRC and onerous contracts (and loss component if applicable) under AASB 17 needs to be consistent with the premium setting approach (including any profit margin).</p> <p>View 2: The entity does not need to consider the basis of premium setting when determining the confidence level % for the LRC or in the measurement of the loss component for onerous contracts. Decisions made around the actual premium charged are driven by market forces and strategic business decisions and would not necessarily achieve the theoretical “technical price” plus profit margin calculated.</p> <ul style="list-style-type: none"> • Members had mixed views on this matter, however, more members leaned towards view 1 noting that the amounts of RA could be based on a confidence level different from that on which actual pricing is based but there needed to be some way of explaining differences and understanding of differences. <ul style="list-style-type: none"> ○ One member supporting view 2 commented that the setting of the risk adjustment for liabilities should be totally independent of any risk adjustment set for the pricing. ○ Another member, also agreed with View 2 noting that, with level premium products, one may have set those premiums quite a long time before and the view of risk may be changing over time. It should give an indication from an accounting perspective, which is quite separate from other considerations such as market forces that drive premium rates. ○ One member agreed with View 1 and commented that it needs to be consistent, but not necessarily identical, as per previous TRG deliberations. ○ One member from a GI background supported View 1. ○ One member commented that they would be taking technical pricing into consideration but that it would only be one of the factors to consider in determining the risk adjustment. The member added that their view did not fit into either of the two views presented. <p>Question 2: Should the confidence level % be the same for the LIC and the LRC?</p>	

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<p>View 1: Even though the risk adjustment need not relate to a single decision made by the entity that is a party to the contract, the confidence level % cannot vary between the LIC and LRC within a group of contracts.</p> <p>View 2: Depending on the entity “facts and circumstances”, the risk adjustments for the LRC and LIC for a group of contracts could have different confidence levels because the entity’s view of compensation required to bear risk for a particular group of contracts can evolve over time.</p> <ul style="list-style-type: none"> • General consensus supported the view that the confidence level % does not need to be the same between LIC and LRC, for various reasons, including: <ul style="list-style-type: none"> ○ the nature of risk evolves over time, e.g., policies in run-off with little to no offsetting premiums ○ there may also be differences depending on the approach to being applied e.g., risk adjustments determined using a cost of capital approach may result in different confidence levels for LRC versus LIC. <p>Question 3: Will the risk adjustment for the LRC or LIC need to be consistent with the Regulator’s Capital Requirements?</p> <p>View 1: The risk margin set for capital calculations is specific to the regulator’s requirements and does not have to be the same as the AASB 17 risk adjustment unless it is also a reflection of “the compensation” an entity requires. For example, an entity may consider the relevant level of capital required to support insurance contracts when assessing the compensation required for bearing uncertainty in cash flows in order to protect capital. Some products that are more capital intensive than others, such as lenders mortgage, and may carry a higher risk adjustment at inception, which is released throughout the period of cover, to ensure that variation on cash flows does not erode capital. The level of capital required could therefore drive a desire for a higher confidence level% in setting the LIC for some products.</p> <p>View 2 Any other views?</p> <ul style="list-style-type: none"> • Broad consensus was reached for View 1. <ul style="list-style-type: none"> ○ One member asked if the industry view is significantly different to the regulator's view for the AASB reporting, whether that would call into question the regulator's capital requirements. The Chair responded that this would be hard to justify given the regulators across different parts of the globe have very different views on their capital. • Members also noted that it is possible to have a lower risk margin than that required by the regulator, i.e., APRA’s minimum requirement of 75% could be different to an entity’s requirements depending on the context e.g. an entity in a consolidated group could benefit from more diversification. <p>Question 4: Are there any additional factors to consider when applying the PAA (rather than the general measurement model) for LRC?</p> <p>View 1 The knowledge that the premium set for a group of contracts would only achieve the equivalent of a 55% confidence level, of itself, is a relevant fact and circumstance indicating the group of contracts might be onerous when the entity is generally applying 80% confidence level in determining the LIC.</p>	

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<p>View 2 Other facts and circumstances indicating the group of contracts might be onerous, beyond those identified in view 1, would also need to be present to justify testing to determine whether the group of contracts is onerous. For example, instead of the expected 90% COR%, early claims indicate the COR% will be 100%. It is relevant to note that an insurer applying the PAA and pricing contracts on a target COR% or a cost of capital basis may not be aware that its contracts would be regarded as onerous if the same confidence level were applied to determine risk adjustments for the LRC and LIC.</p> <ul style="list-style-type: none"> • Consensus was the knowledge that premium is set using a confidence level % lower than % for the LIC risk adjustment would be one relevant fact and circumstance, but would need to be considered together with other relevant facts/circumstances. <p>The Chair acknowledged the contribution of the paper to insurance industry and asked members to share examples of application in practice. The Chair also highlighted the need to keep abreast of developments taking place across the globe to ensure the views in Australia are not vastly different from those emerging elsewhere.</p>	
Treatment of government imposts	ATT4
<p>An industry representative gave an overview of the paper that deals with three types of government imposts. The Chair opened the floor for comments on the tentative conclusions listed in the paper.</p> <p>NSW Emergency Service Levy:</p> <ul style="list-style-type: none"> • One member noted the non-pass through nature of ESL which would differentiate it from GST. • There was a general agreement that ESL collected by insurers will be treated as insurance revenue and ESL paid as expenses under AASB 17. • It was noted that there were similar levies in different states that could have different outcomes under AASB 17. <p>GST:</p> <ul style="list-style-type: none"> • One member asked whether the GST collected as part of premium that is payable to the ATO is recognised as part of LRC or LIC. • The same member asked about ways to deal with a large timing difference between collection and passing it on to the ATO as, if discounting is applied, CSM amortisation could bring part of the tax into the profit or loss which should not be the case. • More detailed discussion for the accounting for GST is expected to take place at a future TRG meeting. <p>Next steps</p> <p>The Chair proposed seeking more clarity on this issue through the Insurance Council of Australia given the potential for diversity in views across general insurers regarding levies and GST.</p> <p>Australian Reinsurance Pool Corporation (ARPC):</p> <ul style="list-style-type: none"> • ARPC is a pooling arrangement run by the government to provide terrorism cover for properties for participating insurers. 	

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<ul style="list-style-type: none"> Given the mechanics of how the scheme operates, the view was that it should be treated as XOL reinsurance held under AASB 17. 	
PHI Update	ATT 5 and ATT 6
<ul style="list-style-type: none"> The papers for PHI were postponed for discussion until the next TRG meeting. 	
Medical Indemnity Update	ATT 7 and ATT 8
<ul style="list-style-type: none"> Similar to the PHI focus group, the function is to support with AASB 17 implementation issues of medical providers. The paper on the treatment of medical indemnity from government schemes will be considered at the next TRG meeting. Medical Indemnity focus group has been meeting monthly from the 21st of October, but it will now be on an as needs basis. The next meeting is expected to be held in February. 	
Institute of Actuaries Task Force Update	
<ul style="list-style-type: none"> Meeting has been postponed, to be held post APRA QIS. Focus is going to be on providing practical advice on responding to the APRA QIS and any feedback to APRA. Insight session is being planned to provide actuaries with guidance for the APRA QIS. 	
AASB update	
<ul style="list-style-type: none"> The AASB has released a domestic Agenda Consultation document to seek feedback on what projects should be initiated in the next 5-year term. Open for comment till 18 February 2022. Early next year TRG members will receive emails from staff to confirm whether members are interested to continue their membership on the TRG. 	
End Meeting	

Attendance

Members

- Anne Driver (Chair)
- Stuart Alexander
- Anthony Coleman
- Cassandra Cope
- Jennifer Dwyer
- Brendan Counsell
- Jane Clifford [Jane on behalf of Fehraz Fallil]
- Scott Hadfield
- Louise Miller
- David Rush
- Warwick Spargo
- Paul Stacey
- Leong Tan
- Ciara Wasley
- Rob Sharma
- Rhian Saunbury
- Frank Saliba
- Toby Langley
- Aiden Nguyen
- Frank Saliba
- Karl Marshall [on behalf of Rachel Poo]

Apologies

- Jac Birt
- Regina Fikkers
- Karen Foo
- Brett Pickett
- Leann Yuen
- Rachel Poo
- David Daniels
- Emily Evitts
- Charles Hett
- Chris Maher
- Jeroen Van Koert

Other presenters

- Angus Thomson
- Tomas Moodie
- Anna Donoghoe
- Alane Fineman
- Zhedi Wu

Secretary

- David Ji

AASB Staff

- Eric Lee
- Patricia Au
- Helena Simkova