Staff Paper

Project:	**Insurance**	**Meeting:**	AASB August 2016 (M153)
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Analysis of key issues arising from forthcoming IFRS 17 in context of AASB's *Process for Modifying IFRS for NFP*

1 Introduction

1.1 This paper:

(a) notes background on the context for applying the AASB's *Process for Modifying IFRS for NFP* based on feedback received from key public sector insurance stakeholders;

(b) highlights characteristics of public sector insurers and the public sector insurance environment that could be relevant in applying the *Process*;

(c) identifies several matters for the Board to consider in terms of whether the forthcoming IFRS 17 *Insurance Contracts* might need modification for application by public sector insurers; and

(d) seeks the Board's views on the matters identified.

1.2 This paper is structured as follows:

Section 2 Context for applying the AASB's *Process* in relation to the insurance contracts project;

Section 3 Steps in the *Process*;

Section 4 Public sector context;

Section 5 Analysis of the issues that might warrant modifications:

5.1 Insurance contracts or other binding arrangements?;

5.2 Risk Adjustments;*

5.3 Contractual service margins;*

5.4 Contract boundary;*

5.5 Onerous contracts;*

5.6 Combination of contract boundary and onerous contract issues;*

Appendix Compulsory Third Party Motor Vehicle Insurance by jurisdiction; and

* Board decisions are sought on staff comments in these Sections.

1.3 References in this paper to AASB 4 *Insurance Contracts*, AASB 1023 *General Insurance Contracts* and AASB 1038 *Life Insurance Contracts* can also be taken to

be references to NZ IFRS 4 *Insurance Contracts* and Appendices C and D to NZ IFRS 4.

1.4 At its June 2016 meeting, the Board considered a staff paper on issues of potential significance to the public sector. The Board noted there are currently no public sector or not-for-profit specific requirements in Australian-New Zealand GAAP for insurance contract accounting.

1.5 The Board asked for a more detailed paper for consideration at the August Board meeting on whether any differences from the forthcoming IFRS 17 might be justified for public sector insurers. The Board asked that the paper be prepared:

(a) in the context of the AASB's *Process for Modifying IFRS for NFP*; and

(b) with the benefit of more feedback from public sector insurance stakeholders.

Spectrum of 'insurance' coverage

1.6 Governments manage a wide variety of risks and create a variety of entities to deal with them – some involve contracts with potential claimants as 'policyholders' and some do not. For example:

(a) Medicare could be seen as a form of insurance, but is generally regarded as an integral part of the health system and is not accounted for using the insurance standards; and

(b) the various WorkSafe and WorkCover authorities in each state accept risks facing employers and, depending on the circumstances, are accounted for using the insurance standards.

1.7 The situation in the public sector is complicated because activities identified as being insurance activities are often interrelated with other broader government responsibilities and the distinction can be a function of how the activities are funded.[1]

1.8 The main focus of this paper is on the activities of government entities regarded as accepting insurance risks or insurance-like risks from other entities, which could be other parts of government or entities outside government.

2 Context for applying the AASB's *Process* in relation to the insurance contracts project

Why focus on public sector entities rather than not-for-profit entities?

2.1 As the title indicates, under the AASB's *Process for Modifying IFRS for NFP*, the Board usually examines whether any modifications need to be made to IFRS to adequately address the not-for-profit entity context. However, in the case of insurance contracts, staff consider the issues are around whether any modifications need to be made to IFRS to adequately address the public sector entity context, for the reasons noted below.

1 In health care, for example, there is scope for cost shifting between the Commonwealth and state/territory governments and between government and the private sector: Productivity Commission Research Paper Efficiency in Health published in April 2015

Mutual insurers

2.2 Not-for-profit private sector insurers in Australia and New Zealand are essentially mutual entities. Mutual private sector insurers have a large share of certain market segments in Australia and New Zealand – for example, medical professional indemnity insurance.[2]

2.3 The IASB's focus is generally on private sector commercial businesses. However, the IASB has considered mutual insurers, probably because some of the world's largest insurers are mutual.[3] In general, the IASB has taken the view that a mutual entity's members can act in two capacities:

(i) as policyholders; and

(ii) as owners/equityholders.[4]

Accordingly, contracts between mutual insurers and their policyholders are treated in the same way as other insurance contacts.

Public sector insurers

2.4 The following interrelated features might distinguish public sector insurers from mainstream private sector insurers:

(a) monopoly status;

(b) inability to withdraw from particular lines of business;

(c) operating in an area of market failure;

(d) the interrelationship between insured and non-insured activities;[5] and

(e) being an instrument of government policy.

2.5 These features might create a context that justifies a modification from the forthcoming IFRS 17 in order to help ensure the financial reporting by particular types of public sector insurers remains relevant and useful.

2.6 Some public sector insurance entities identify as for-profit entities and others as not-for-profit entities. In some cases, the distinction seems to be based on whether or not the premium pricing incorporates a margin to enable the entity pay a 'dividend' to consolidated revenue.

2.7 It is difficult to differentiate the activities of some of those entities that identify as for-profit from those that identify as not-for-profit. Accordingly, for the purposes of

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2 The AASB has Interpretation 1047 *Professional Indemnity Claims Liabilities in Medical Defence Organisations* that was developed to address business under which such organisations may have discretion to refuse assistance to a member reporting a claim. Agenda paper 4.4 discusses the Interpretation.

3 According to the International Cooperative and Mutual Insurance Federation, around a quarter of the global insurance market is held by mutual insurers: http://www.icmif.org/media-centre/key-facts/about-sector

4 For example, see: http://www.ifrs.org/Meetings/MeetingDocs/IASB/2015/October/AP02C-Insurance-Contracts.pdf, in particular, pages 8 to 10.

5 Given the particular policy focus of public sector entities on community wellbeing and the potential for cost shifting between public sector entities and functions. [For example, in health care, there is an interrelationship due to the scope for cost shifting between the Commonwealth and state/territory governments and between government and the private sector – Productivity Commission Research Paper *Efficiency in Health* published in April 2015.]

this staff paper, a single analysis is done for public sector entities (both for-profit versus not-for-profit) using the *Process*.

3 Steps in the *Process*

3.1 Paragraph 9 of the AASB's *Process for Modifying IFRS for NFP* notes:

> Two questions would generally be considered before modifying an IFRS for PBE/NFP:
>
> (a) Are there issues that might warrant modifying an IFRS for PBE/NFP?
>
> (b) Are the identified issues sufficiently significant to warrant a departure from an IFRS?

3.2 Paragraph 12 of the *Process* notes:

> The following factors would generally be reviewed when considering differences in user needs between the for-profit and NFP sectors:
>
> (a) nature of transactions, events and circumstances and their impact on PBE/NFP;
>
> (b) benefits to users of complying with the IFRS; and
>
> (c) costs of complying with the IFRS.

Section 4 of this paper identifies matters relevant to these factors.

3.3 Staff also note paragraph 6 of the *Process* comments that disagreement with the IASB's treatment is unlikely to provide good reason, in and of itself, for changing the requirement in an IFRS.

What are the issues for which there might need to be modifications?

3.4 At first glance, there may appear to be no need to consider applying the *Process* to the forthcoming IFRS 17 because it is not planned to change the definitions of 'insurance contract' and 'insurance risk' from those in the existing IFRS 4 and in AASB 4. However, staff consider the potential impact of several aspects of the forthcoming IFRS 17 need to be considered, including:

~ the contract boundary;

~ the grouping requirements for identifying onerous contracts; and

~ the focus on risk adjustments and contractual service margins (CSM).

Section 5 discusses these issues.

4. Public sector context

4.1 Nature of the contracts/transactions

4.1.1 The insurance contracts themselves 'sold' by public sector insurers often have the same or similar terms and conditions as those sold by for-profit private sector insurers. Examples include:

~ professional indemnity insurance provided by public sector entities for medical practitioners working in public hospitals and similar cover purchased by

individual medical practitioners relating to risks they face in private practice; and

- ~ compulsory third party insurance[6] (CTP) vehicle insurance contracts sold in each state and territory through a mix of public and private sector entities.

4.1.2 The main differences between public sector insurers and private sector insurers, which might affect the nature of the contracts/transactions are:

- ~ the monopoly position of a public sector insurer;
- ~ the extent of underwriting[7] that is (or can) be performed; and
- ~ the nature of the 'premiums' collected.

The example of CTP insurance

4.1.3 The above differences are interrelated. The Appendix to this paper shows a comparison of the various CTP schemes and is intended to help illustrate those differences.

4.1.4 Monopoly public sector entities sell CTP cover in Tasmania, Victoria, Western Australia and the Northern Territory. In New South Wales, Queensland, South Australia and the ACT, private sector insurers sell largely 'fault-based' CTP insurance,[8] with some offering 'at fault' cover as an option. Separate monopoly public sector schemes in NSW, South Australia and Western Australia[9] extend cover to cases such as 'catastrophic injury' to drivers at fault and/or to people who have been unable to identify a driver at fault.[10]

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6 Compulsory Third Party motor vehicle insurance – the three parties are: (1) the owner/driver of the vehicle 'at fault'; (2) the CTP insurer of the vehicle 'at fault'; and (3) the injured person.

7 Underwriting is the process of assessing risk to help ensure that the cost of the cover is proportionate to the risks faced by the (prospective) policyholder(s) concerned. Policyholders with the same or similar risk pay the same or similar premiums.

8 Fault-based schemes only cover victims (passengers, pedestrian, cyclists, etc.) of road accidents who are not at fault drivers and, in some cases, only when an at fault driver with CTP insurance can be identified. No fault schemes cover victims regardless of whether they are at fault, provided it can be established that the claim arises because of a motor vehicle accident.

9 From 1 July 2016

10 Some of these schemes are recently established and seem to have been created in response to a Productivity Commission Enquiry Report on Disability Care and Support published in 2011. That Report noted:

> The major flaw in the remaining fault-based arrangements is that people who cannot establish the legal liability of another party in a catastrophic accident get inadequate support. Even when an at-fault party can be identified, the processes for securing compensation for support through litigation are drawn out and costly in fault-based regimes. Nor is there evidence that the common law right to sue for compensation for care costs increases incentives for prudent behaviour by drivers, doctors and other parties. The Commission recommends no-fault insurance arrangements — operating at the state and territory level — for the long-term care and support of people experiencing catastrophic injuries from all types of accidents. Acting collaboratively, the state and territory no-fault schemes would ensure national coverage. [page 43]

The Productivity Commission is effectively arguing there is market failure and the public sector needs to step in. This might imply that the no-fault schemes operate in a social benefit context that distinguishes them from commercial insurance arrangements. The Productivity Commission Report also points out that the alternative to no-fault schemes is to place a burden on the public health care system more generally.

4.1.5 In general, this means the public sector entities in Tasmania, Victoria, Western Australia and the Northern Territory are providing a range of CTP insurance covers in single transactions that are being provided by a combination of public and private sector insurers in NSW, Queensland and South Australia in separate transactions.

4.1.6 In the case of Tasmania, Victoria, Western Australia and the Northern Territory, the level of cross-subsidisation is across all types of risks involving particular classes of vehicle (passenger, motorbike, etc.) because there is a single transaction type for each class of vehicle. In the case of NSW, Queensland and South Australia, the public sector entities are picking up CTP risks not otherwise covered by the private sector insurers and funding their activities through a levy on the contracts sold by private sector insurers.

4.1.7 The public sector entities that enter into arrangements only for no fault cover tend to apply AASB 137 *Provisions, Contingent Liabilities and Contingent Assets* in measuring their liabilities, rather than the insurance standards. There appear to be a mix of factors involved in choosing to apply AASB 137, including the nature of the cover and the entities' monopoly status, indicating they may consider themselves as not really bearing insurance risk because they can pass that risk back to their 'captive' customers.

The example of workers' compensation insurance

4.1.8 In most Australian jurisdictions, public sector entities conduct workers' compensation insurance, usually alongside private sector insurers and with some employers self-insuring.[11, 12] In respect of workers' compensation schemes generally, the publication *Comparison of workers' compensation arrangements in Australia and New Zealand* (2015) by Safe Work Australia notes:

> Premium rates are generally pooled across similar risk profile groups. This allows employers who share a common set of risks to spread the risk across their industry type. Across the schemes there are hundreds of specified premium rates for industry types. Employers that operate in more than one jurisdiction have to pay the relevant premium in each jurisdiction. Premiums are usually expressed as a percentage of employers' total wages bills. The rates depend on an employer's:
>
> - size
> - industry
> - individual claims experience, and
> - the way that 'wages' are defined for workers' compensation purposes, which can vary across the jurisdictions. [page 197]

4.1.9 Accordingly, there is a significant element of underwriting involved in public sector workers' compensation schemes, similar to commercial insurance contracts.

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11 Large employers with the capacity to fully fund expected claims can usually self-insure.

12 The legislation on insurance cover provided by public sector entities is evolving and worker's compensation insurance has recently been the subject of much change. In 2014-15 alone, NSW conducted a fundamental review of its worker's compensation insurance arrangements and most other jurisdictions are still implementing changes relating to earlier reviews.

Staff comments: The nature of the contracts/transactions undertaken in a public sector environment are highly similar to those undertaken in the for-profit private sector. However, the extent of underwriting can be more limited for public sector insurers. This and other factors (such as monopoly or near-monopoly status) are discussed further in the analysis in Section 5.

4.2 Stated purposes/mandates

4.2.1 The mandates of Australian public sector insurers vary as does the extent to which they conduct risk management/advice activities. However, most emphasise roles in community wellbeing ahead of their roles as bearers of insurance risk. For example:

> **Accident Compensation Corporation**
>
> The purpose of the Scheme is to deliver injury prevention initiatives and no-fault personal injury cover for everyone in New Zealand, including overseas visitors.
>
> ACC's 2015-2019 Statement of Intent sets out the outcomes on which we report at the end of each year. These are:
>
> - reduce the incidence and severity of injury in New Zealand
> - rehabilitate injured people in New Zealand more effectively
> - New Zealand has an affordable and sustainable scheme. [ACC Annual Report 2016, page 6]
>
> **Victorian Managed Insurance Authority**
>
> As a Victorian statutory authority reporting to the Minister for Finance, VMIA's core business is service delivery on our statutory charter in four key result areas:
>
> - Prevention – helping the state prepare for, prevent or reduce the impact of harm
> - Recovery – helping our clients restore services and recover quickly
> - Assurance – helping improve risk governance and management
> - Financial sustainability – operating effectively and efficiently. [VMIA Annual Report 2014-15, page 7]
>
> **NSW Lifetime Care & Support Authority**
>
> We support injured people to achieve an optimal quality of life by providing lifelong treatment, rehabilitation and care for people severely injured in a motor vehicle accident in NSW, regardless who was at fault.
>
> OUR MISSION We protect, insure, care
>
> - Protect from harm
> - Insure for when things go wrong
> - Care for people when they are injured [NSW LCSA Annual Report 2014-15, pages 6 & 14]

4.2.2 Private sector not-for-profit (mutual) insurers similarly identify roles in harm protection, presumably to help to reduce claims to support profits and their brands. In broad terms, public sector insurers' mandates are further along the social benefit spectrum than their private sector counterparts, but the whole sector shares a similar function in society, which is facilitating economic and social activity.[13]

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13 *The Social and Economic Value of Insurance*, A Geneva Association Paper, September 2012.

Staff comments: The nature of the mandates of public sector insurers does not seem, of itself, to be a critical factor that distinguishes them from their private sector counterparts. In financial terms, public sector insurers' mandates focus on financial sustainability rather than returns to owners – this factor is discussed below in the context of premium/levy pricing.

4.3 The basis for setting premiums/levies

4.3.1 Premiums in the for-profit private sector are driven primarily by competitive forces. State-based public sector insurers are also affected by competitive forces in a broader sense and comparisons are often made between the costs of particular lines of insurance across the states. However, the public sector context might lead to a different approach to setting premiums/levies.

4.3.2 The following table shows some of the organisational and contextual factors affecting premium/levy pricing for annual business in each sector. [14]

Factor	Public sector	Private for-profit sector
Expected claims	Typically need to be confident of meeting claims and other costs over many years (could be a decade) in monopoly markets –underwriting profit not necessary in each year.	Typically need to be confident of meeting claims and directly-related costs in each year from that year's premiums – to make an underwriting profit in each year.
Investment returns	Typically take a long-term view of expected investment returns.	Typically take a long-term view of expected investment returns.
Capital employed	Can be minimal and often supported by a capital guarantee. However, many benchmark to APRA capital adequacy requirements.	At least sufficient to meet APRA capital adequacy requirements[15]
Return on capital	Typically commercially based, but capital guarantees usually free May allow for dividends	Commercially based Allow for dividends
Ability to accumulate capital	Within bounds of political sensitivities, can obtain more capital through higher premiums through monopoly power	Due to competitive pressures, may not be able to obtain more capital through higher premiums
Market cycles	Generally only exposed at a reinsurance level	Exposed at both the direct and reinsurance levels

4.3.3 As indicated in the above table, the financial dimension to the operations of public sector insurers is more likely to be focused on financial sustainability, rather than returns to owners. However, the need for some public sector insurers to pay capital charges and yield dividends is little different in principle from the private sector.

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14 Assumes annual contracts

15 The Australian Prudential Regulation Authority requires general insurers to have sufficient capital to meet particular percentage risk factors under its Prudential Standards.

Staff comments: Most of the above factors mean that, at any given time, pre-claims liabilities (represented by deferred premiums) of public sector insurers are much closer to the best estimates of claims liabilities than for private sector insurers. This means risk adjustments and any CSM may be smaller relative to the for-profit private sector. However, apart from the relative magnitude of risk adjustments and CSM, the actual accounting for them seems applicable across sectors.

4.4 Benefits to users of complying with IFRS

4.4.1 Based on outreach with public sector insurance stakeholders, the main focus of the usefulness of financial statements (and financial information more generally) of public sector entities bearing insurance risk are benchmarking and financial sustainability, which are interrelated.

4.4.2 Benchmarking can involve comparing the relative costs insurance imposes on businesses and others in the different jurisdictions. For example, financial statement information facilitates preparation of metrics such as the percentage of payroll various employers pay for workers' compensation insurance in each jurisdiction.

4.4.3 It is difficult to say whether the application of identical insurance standards across the private and public sectors is essential to this benchmarking, but it could be inferred that common standards facilitate the benchmarking in view of the involvement of both private and public sector insurers in the same markets.

4.4.4 Financial sustainability for public sector insurers is essentially about breaking even over the long term and possible generating sufficient surplus to meet a capital charge and/or dividend payment. In concept, as indicated in Section 4.3 (on premium setting), the fact that private sector insurers might be aiming for a profit target and a risk adjustment that meets APRA requirements, makes little difference. Compared with public sector insurers, they are simply aiming for targets on a different part of the same spectrum.

4.4.5 Public sector insurers seem to use many of the same types of financial metrics (drawn from the financial statements) as private sector insurers. These include various ratios of premiums compared to claims, administrative costs to premiums or claims, funding ratios and, in some cases, return on equity.

Staff comments: There is nothing that stands out as being different about the financial statement information needs of users of public sector insurers compared with private sector insurers to imply the standards for each sector need to differ. Accordingly, the needs of public sector users do not seem to be critical a factor to be used to assess whether modifications to IFRS are made for public sector insurers.

5. Analysis of the issues that might warrant modifications

5.1 Insurance contracts or other binding arrangements?

Definitions

5.1.1 The definitions of 'insurance contract' and 'insurance risk' in existing IFRS 4 and AASB 4 are the same as those definitions for the forthcoming IFRS 17,[16] as follows:

> **insurance contract:** A contract under which one party (the issuer) accepts significant **insurance risk** from another party (the **policyholder**) by agreeing to compensate the policyholder if a specified uncertain future event (the **insured event**) adversely affects the **policyholder**.
>
> **insurance risk:** Risk, other than **financial risk**, transferred from the holder of a contract to the issuer.

5.1.2 The definition of 'financial risk' is also expected to remain the same:

> **financial risk:** The risk of a possible future change in one or more of a specified interest rate, financial instrument price, commodity price, foreign exchange rate, index of prices or rates, credit rating or credit index or other variable, provided in the case of a non-financial variable that the variable is not specific to a party to the contract.

5.1.3 From a financial reporting perspective, the differences between a transaction being treated as an insurance contract (or by analogy as an insurance contract) or as a non-insurance are significant. The main alternative would be AASB 137. The main differences between the insurance standards and AASB 137 would be:

AASB 137	***Insurance standards***
One liability for each contract or set of contracts	Two liabilities – one for future coverage – one for claims liabilities
No explicit requirement for a margin related to inherent risk of uncertainty of the liability amount	Explicit risk adjustment relating to uncertainty of the liability amount
Movements in provisions would be the only sources of income	Income would be from releases from the risk margin and the CSM and from changes in claims liabilities
General disclosures around the risks and uncertainties of the provisions	Targeted disclosures about insurance risks

Existence of contracts

5.1.4 The existence or otherwise of a contract has proved to be a critical issue when deciding whether an instrument falls within AASB 139 *Financial Instruments: Recognition and Measurement* or AASB 9 *Financial Instruments*. For example,

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16 The same definitions apply in AASB 1023 *General Insurance Contracts* and Appendix D *Financial Reporting of Insurance Activities* of NZ IFRS 4 *Insurance Contracts* AASB 1038 *Life Insurance Contracts* or Appendix C *Life Insurance Entities* of NZ IFRS 4. As previously noted, the reporting requirements for insurers are identical in Australia and New Zealand. Staff are not aware of any life insurance contracts within Australian and New Zealand government entities.

instruments that have a legislative basis rather than a contractual basis are generally regarded as not being within AASB 139 or AASB 9. In relation to statutory receivables, such as income tax receivables, the Board has previously:

> … confirmed its view that AASB 136 *Impairment of Assets* (rather than AASB 139 *Financial Instruments: Recognition and Measurement*) applies to the impairment of statutory receivables because of the non-contractual nature of such receivables. [April 2010 AASB minutes]

Accordingly, the Board saw a clear distinction between statutory and contractual arrangements.

5.1.5 The same issue arises in the context of the insurance standards, but there has been less attention paid to it because existing Australian-New Zealand GAAP was largely grandfathered when IFRS were adopted.

5.1.6 IFRS 4 and IAS 39/IFRS 9 do not include definitions of 'contract'. However, IFRS 5 *Revenue from Contracts with Customers* includes the following definition:

contract	An agreement between two or more parties that creates enforceable rights and obligations

5.1.7 Identifying whether there is a contact, rather than a statutory arrangement involved in an insurance transaction between a government entity and another party can be problematic. The issue is complicated by the fact that different entities (public and private sector) capture the same risks under different types of arrangements. For example, in relation to the coverage of drivers, CTP insurance in New South Wales and Victoria can be illustrated as being provided as follows:

Risk	***NSW entity***	***NSW funding***	***VIC entity***	***VIC funding***
Driver not at fault non-catastrophic injury	Private sector insurer chosen from panel by driver[17]	CTP premiums	Transport Accident Commission	CTP premiums
Driver catastrophic injury	Lifetime Care and Support Authority (LCSA)	Explicit levy on CTP premiums	Transport Accident Commission	CTP premiums

5.1.8 In the above example, two aspects of cover are bundled together in Victoria, but not in New South Wales. Staff note it could be argued, among other things, that:

(a) in form, catastrophic injury risk might be viewed as the subject of a contract in Victoria, but might not be in New South Wales;

(b) based on the IFRS 15 definition of 'contract' the catastrophic injury risk in NSW could be viewed as the subject of a contract because the driver has entered into an 'agreement' to pay the levy and receive the cover;

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17 The NSW State Insurance Regulatory Authority oversees the whole system

(c) the explicit levy in New South Wales is simply a way of funding the cover in a targeted way, rather than from taxes more generally, and is not part of an 'agreement' as such between the LCSA and drivers;

(d) when there is a monopoly, there is no point in debating whether something is a statutory levy or contractual premium – the same level of 'agreement' or 'statutory compulsion' applies to both; and

(e) both the New South Wales and Victorian arrangements in their entirety are not contracts because drivers are compelled by statute to enter into the arrangements.

5.1.9 As indicated earlier in this paper, some public sector entities that enter into insurance (or insurance-like) arrangements are applying AASB 137 in measuring their liabilities, rather than the insurance standards either directly or by analogy.[18] That could be because they don't view themselves as covering insurance risks or because they don't regard themselves as having contracts.

Staff comments: The AASB has not previously provided guidance (in addition to IFRS) on what constitutes a contract and staff suggest we don't do that now because it's a broad issue that also relates to financial instruments more generally and to revenue recognition.

The impacts of applying the insurance standards compared with AASB 137 are touched on in parts of the remainder of Section 5, but are not the main focus of the Section. The main focus is on whether modifications to the forthcoming IFRS 17 might be warranted in respect of public sector entities.

5.2 Risk adjustments

5.2.1 The forthcoming IFRS 17 includes two measurement models – the general model and the simplified model. For the sake of simplicity, and for all practical purposes, the following discussion assumes annual coverage contracts are accounted for using the simplified model and contracts for longer coverage periods are accounted for using the general model.[19]

5.2.2 The simplified model only relates to the 'pre-claims' liability, which is the liability relating to the period of coverage that remains in the future. The simplified model allows deferred premium to be used as the 'pre-claims' insurance liability (in the absence of there being evidence of onerous contracts). The deferred premium is presumed to incorporate a risk margin and CSM. The fact that the premium pricing may not include a risk adjustment and/or CSM in the case of a public sector insurer has no significance in terms of the practical application of the simplified model.

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18 In accordance with paragraph 11 of AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors*.

19 In broad terms, contracts with coverage periods of a year or less can be accounted for using the simplified model by default. Contracts with longer coverage periods could be accounted for using the simplified model, but it would need to be established that it results in materially the same outcomes as the general approach.

5.2.3 Once the coverage period commences and there are incurred claims (reported or unreported), under the forthcoming IFRS 17, the general model applies. This model explicitly requires a risk adjustment to be included in insurance liabilities.

5.2.4 The following diagram helps illustrate how the two models interrelate in respect of a single annual insurance contract with a premium of $100 incepting on 1 October 2016 and claims expected to remain outstanding for many years for an entity with a 30 June year end:

1 October 2016 **30 June 2016** **30 June 2017**

Simplified		
$25 premium liability[20]	**Simplified**	
$75 premium income	$25 premium income	
General	**General**	**General**
$liability for expected claims for risk borne to June 2016	$liability for expected claims for risk borne to 30 September 2017[21]	$liability for expected claims for risk borne to 30 September 2017
	$movement in claims liability to 30 June 2017 (includes: new claims, claims development & claim payments)	$movement in claims liability from 1 July 2017 (includes: new claims, claims development & claim payments)

5.2.5 Some public sector entities have only one anniversary date or only a few anniversary dates for all their insurance arrangements.[22] The extent of pre-claims liabilities will depend on the time lag between those anniversary dates and the entities' year ends.

5.2.6 The general model is a discounted cash flow model relating to all the expected future inflows and outflows under insurance contracts. For the general model, IASB ED/2013/7 *Insurance Contracts* proposed:[23]

> When determining the fulfilment cash flows, an entity shall apply a **risk adjustment** to the expected present value of cash flows used [paragraph 27]
>
> **risk adjustment**: The compensation that an entity requires for bearing the uncertainty about the amount and timing of the cash flows that arise as the entity fulfils the insurance contract. [ED/2013/7, Appendix A Defined terms]

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20 Assumes even coverage over the year

21 Expiry date for annual contract

22 **Accident Compensation Corporation:** "ACC recognises levy revenue that will be earned up to the end of the levy year for the three levy funded Accounts. The levy year runs from 1 April to 31 March for the Earners' Account and Work Account and from 1 July to 30 June for the Motor Vehicle Account. At 30 June 2015 ACC has therefore recognised levy revenue for the period 1 July 2015 to 31 March 2016 for both the Earners' and the Work Accounts." [ACC Annual Report 2014-15, page 104].
Victorian Managed Insurance Authority: "The majority of VMIA's insurance policies with its clients incept at 4.00pm on 30 June year and accordingly the majority of such gross premium written is unearned at 30 June each year." [VMIA Annual Report 2014-15, page 68]

23 The IASB has not made any decisions to change this proposal

5.2.7 In broad terms, the same requirement prevails under AASB 1023, which includes the following recognition and measurement requirement:

> An outstanding claims liability shall be recognised in respect of direct business and reinsurance business and shall be measured as the central estimate of the present value of the expected future payments for claims incurred with **an additional risk margin** to allow for the inherent uncertainty in the central estimate. [paragraph 5.1]

5.2.8 The requirements relating to risk margins in AASB 1023 and the forthcoming IFRS 17 give rise to the same issues for public sector insurers. If the public sector insurer does not price premiums for inherent uncertainty risk in each year, all other things being equal, an insurer could appear underfunded when it could be argued that it is not.

5.2.9 The circumstances and accounting responses of the various public sector entities differ. Some are fully funded for the risk margin through contributed capital from their owners or a 'buffer' from past premiums/levies[24] and apply AASB 1023. Some do not identify as insurers. For example:

> **NSW Lifetime Care and Support Authority**
>
> Levy contributions are adjusted over time in order to remain sufficient to fund the full cost of providing lifetime care and treatment to participants and meet other Scheme expenses. [LCSA Annual Report 2014-15, page 6]
>
> If the Lifetime Care and Support Scheme was an insurer (which it is not), then under Australian Accounting Standard AASB 1023 it would be required to add a risk margin to its liabilities. Based on the minimum level required by APRA of a 75% probability of Sufficiency/Adequacy this would result in the Authority's liabilities increasing by $410.7 million and reducing its accumulated surplus to $865.4 million. [LCSA Annual Report 2014-15, page 71]
>
> **Lifetime Support Authority of South Australia**
>
> Australian Accounting Standard 137 (AASB 137) applies to the Scheme in preparing an estimate of the outstanding claims liability in its annual financial statements. We have prepared our estimate of outstanding claims to be consistent with this Accounting Standard's requirements. [Extract from Actuarial Certificate, LSASA Annual Report 2014-15, page 57]
>
> **Queensland Building and Construction Commission**
>
> Valuation of outstanding claims liabilities: The actuaries incorporated a prudential margin loading of 16.6% in relation to projected future claims in order to achieve a 75% confidence level that the outstanding claims provision would be adequate. No additional contingency margin was incorporated. [QBCC Annual Report 2014-15, page 119]
>
> **Insurance Commission of Western Australia (as manager of RiskCover)[25]**
>
> In determining the outstanding claims liability the RiskCover Fund follows the requirements of AASB 137 'Provisions, Contingent Liabilities and Contingent Assets'. Like AASB 1023 this standard also requires the use of a risk-free discount

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24 New Zealand's ACC moved from a pay-as-you-go scheme to a funded scheme through its levies.

25 This information about RiskCover is a note disclosure by the ICWA, which manages RiskCover on behalf of the government. RiskCover is directly consolidated by the WA government and is not regarded as being controlled by the ICWA.

factor when determining the outstanding claims liability however it differs significantly in that it does not require the inclusion of a prudential margin.

In 2006, the State Government Expenditure Review Committee authorised the RiskCover Fund to maintain a separate Prudential Reserve equivalent in value to an APRA prudential margin sufficient to achieve a 75% likelihood of adequacy with respect to the provision for outstanding claims. [ICWA Annual Report 2014-15, page 119]

Accident Compensation Corporation

The accrued outstanding claims liability is the central estimate of the present value of expected future payments on claims occurring on or before the balance date, 30 June 2015, plus a risk margin to ensure the accrued liability is sufficient to meet all the costs of future claim payments 75% of the time. [ACC Annual Report 2014-15, page 75]

5.2.10 The reasons for incorporating a risk adjustment (depicting the maximum amount an insurer would rationally pay to be relieved of the risk) were articulated in the IASB's ED/2010/8 *Insurance Contracts*:[26]

(a) to convey useful information to users about the amount of risk associated with the insurer's insurance contracts because the management of risk is integral to the insurance business model;

(b) to reflect the insurer's view of the economic burden imposed on it by the presence of that risk; and

(c) to attain an element of consistency with requirements in IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*.

Staff are not aware of the IASB having changed its reasoning for risk adjustments since ED/2010/8.

Staff comments: Risk adjustments in the forthcoming IFRS 17 will reflect the insurer's view of the economic burden imposed on it by the presence of inherent risk in its claims liabilities. Accordingly, for public sector entities, the adjustment might be relatively smaller than for the private sector insurers because governments can provide the backing necessary for public sector entities to have a higher risk appetite than private sector entities.

The risk adjustments required under the forthcoming IFRS 17 might be different from the risk margins under the existing insurance standards. However, in principle, there is nothing new about having a risk adjustment that would particularly affect public sector entities compared with private sector entities or affect their accounting policy choices (insurance standards versus AASB 137).

Staff recommendation: Staff recommend no public sector modifications to the AASB standard incorporating the forthcoming IFRS 17 because the risk adjustment requirements pose no new challenges in a public sector context.

5.2 Does the Board agree with the staff recommendation?

26 Mainly in paragraphs BC109 and BC110

5.3 Contractual service margins (CSM)

Identification and measurement

5.3.1 In respect of the general model, IASB ED/2013/7 proposed that the cash flows used in measuring insurance liabilities incorporate a CSM:[27]

> **contractual service margin**: A component of the measurement of the insurance contract representing the unearned profit that the entity recognises as it provides services under the insurance contract. [ED/2013/7, Appendix A Defined terms]

5.3.2 The IASB's basis for there being a CSM has changed as the insurance contracts project has developed. The IASB's ED/2010/8 referred to a 'residual margin' and articulated the following possible reasons for its existence:[28]

(a) compensation for the cost and effort of originating the contracts and assembling them into the portfolio;

(b) compensation for providing ancillary services that are not unbundled (and so are not treated as arising from a separate service contract within the scope of standards on revenue recognition);

(c) compensation for product development;

(d) additional returns if the insurer has significant pricing power, or conversely discounts if the insurer is seeking to build or maintain market power; and

(e) the risk that the insurer might not satisfy its obligation to perform under the contract.

5.3.3 Staff consider that many of the reasons noted above would imply immediate recognition in income, and the margin probably owes its very existence to a disquiet about recognising profits at inception of a potentially long-term contract.

5.3.4 By the time of the IASB's ED/2013/7, the rationale became that an excess of the present value of expected income over expected costs (CSM) must relate to other services the insurer will provide policyholders in addition to bearing risk. Accordingly, the insurance liability should include that margin to reflect those performance obligations.

5.3.5 Notwithstanding the rationale for the CSM, it is still to be measured as a residual (assuming the contract is not onerous) after determining the best estimate of cash inflows and outflows under a contract and adding the risk adjustment. The determination of a CSM is illustrated in the following simple example.

Present value of premiums is expected to be:	\$100
Present value claims/claims handling is expected to be:	\$70
Risk adjustment is estimated at:	\$20
The CSM is the residual:	\$10

27 The IASB has not made any decisions to change this proposal. A CSM is not explicitly recognised under the simplified model.

28 Mainly in paragraph BC125 of ED/2010/8.

5.3.6 Since a CSM need only be separately identified under the general model, it effectively only applies when the contract coverage period is longer than a year. An example of this would be residential builders' insurance that is provided in most states by a public sector entity and usually has a coverage period in the seven to ten year range.

5.3.7 Since residential builders' insurance does not involve life insurance risks, it is currently accounted for by both private and public sector insurers in accordance with AASB 1023 using the equivalent of the simplified model. Unless it can be established that the simplified model will provide materially the same outcomes as the general model, the basis for reporting on builders' warranty insurance will fundamentally change under the forthcoming IFRS 17 and any CSM will need to be identified and accounted for.

Staff comments: In economic terms, it could be argued that the same drivers exist for there being CSMs in the private sector, being a reward for risking capital. Private for-profit insurers might also periodically be able to take advantage of good market conditions to generate higher CSM. Due to their mandates, public sector insurers would tend to not to engage in that behaviour.

If a public sector entity were to undertake the above calculation it may identify a residual, which for example, could be due to:

~ a capital charge built into its premiums/levies; and/or

~ a margin to allow a dividend to be paid to government.

In the absence of onerous contracts, the CSM is measured as a residual, and the reason for that residual's existence and its size make no difference to that accounting.

Staff recommendation: Staff recommend no public sector modifications to the AASB standard incorporating the forthcoming IFRS 17 because identifying and measuring a CSM poses no special challenges in a public sector context.

5.3.1 Does the Board agree with the staff recommendation?

CSM recognition

5.3.8 In respect of the general model, at its meeting on 21 May 2014 the IASB tentatively decided:

a. to confirm the principle in the 2013 ED that an entity should recognise the remaining contractual service margin in profit or loss over the coverage period in the systematic way that best reflects the remaining transfer of the services that are provided under an insurance contract; and

b. clarify that, for contracts with no participating features, the service represented by the contractual service margin is insurance coverage that:

   i. is provided on the basis of the passage of time; and

   ii. reflects the expected number of contracts in force.

5.3.9 As previously discussed by the AASB, staff do not agree with the IASB's tentative decision and regard it as a departure from the principle (reflected in sub-paragraph a.

above) in ED/2013/7. This is because it has the potential to smooth CSM recognition over the coverage period when the entity expends an uneven level of effort and capital over the coverage period. If the IASB regarded the CSM as merely a residual (as per ED/2010/8), the IASB's approach seems reasonable, but not under its current thinking.

5.3.10 As noted above, the *Process* comments that disagreement with the IASB's treatment is unlikely to provide good reason, in and of itself, for changing the requirement in an IFRS.

Staff comments: Although staff disagree with the IASB's approach to CSM recognition, there appears to be no public sector specific reason for a different treatment.

If anything, due to their mandates, public sector insurers are likely to be less affected by the new requirements because their CSM will tend to be smaller (on average) than for private sector for-profit insurers.

Staff recommendation: Staff recommend no public sector modifications to the AASB standard incorporating the forthcoming IFRS 17 because CSM recognition poses no special challenges in a public sector context.

5.3.2 Does the Board agree with the staff recommendation?

5.4 Contract boundary

5.4.1 The existing Australian and New Zealand requirements effectively assume the contract boundary is the period stated in an insurance contract, or a period based on the expectations of the entity about contract 'renewals' within a contractually-stated period.[29] In contrast, the forthcoming IFRS 17 includes a principle for determining contract boundaries.

5.4.2 The wording that the IASB will use in the forthcoming IFRS 17 is not yet available; however, it is likely that wording along the lines of the following from paragraph 23 of IASB ED/2013/7 will be used.

> Cash flows are within the boundary of an insurance contract when the entity can compel the policyholder to pay the premiums or has a substantive obligation to provide the policyholder with coverage or other services. A substantive obligation to provide coverage or other services ends when:
>
> (a) the entity has the right or 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 right or the practical ability to reassess the risk of the portfolio of insurance contracts that contains the contract and, as a

29 For example, for some life business, the period over which policyholders are expected to keep exercising their right to renew, or in the case of annuity contracts, the period over which annuitants are expected to live.

result, can set a price or level of benefits that fully reflects the risk of that portfolio; and

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

5.4.3 In essence, a contract ends when the insurer can fully reprice the relevant risks, either on a contract-by-contract basis or for a portfolio of contracts with the proviso that, for a portfolio, there is not cross-subsidisation of future risks from current premiums.

5.4.4 There is a presumption in the forthcoming IFRS 17 that contracts with a coverage period of a year or less can apply the simplified (deferred premium) model for measuring insurance liabilities.[30] This model aligns with the existing approach in AASB 1023 that public sector insurers currently apply.

5.4.5 Based on staff outreach with public sector insurance stakeholders, in practice, risks are generally fully repriced each year using expert advice. Accordingly, they would meet the condition in paragraph 23(b)(i) of ED/2013/7.

5.4.6 Government policy could potentially cause a public sector insurer to cross-subsidise between contracts in a portfolio over time, but the evidence suggests this is not prevalent practice. If that remains the case, public sector insurers would also meet the condition in paragraph 23(b)(ii) of ED/2013/7 and be able to automatically apply the simplified model to annual contracts .

Contracts covering multiple years

5.4.7 If there were cross-subsidisation between 'annual' contracts in a portfolio over time, and the contracts were deemed to relate to multiple periods, the general model would need to be applied under the forthcoming IFRS 17. The entity would need to undertake a discounted cash flow measurement relating to all the expected cash outflows (claims and costs) and inflows (premiums) over the multi-period contract. For example, if premiums are higher in year 1 for policy reasons than would be suggested by the relevant risks for that period and premiums in year 2 can consequently be made lower, the general model would measure insurance liabilities by including the expected premiums and claims for both years. All other things being equal, an 'excess' accounting profit in year 1 would be averted by assuming the contracts have two-year terms and applying the general model.

5.4.8 On the face of it, this might seem appropriate. However, an alternative view is that it would be more useful if the accounting information showed an 'excess' profit in year 1 to demonstrate the impact of the policy decision on that year.

30 This relates to the pre-claims liabilities for the period of risk yet to expire.

Staff comments: On its own, the contract boundary requirements in the forthcoming IFRS 17 are not expected to have much impact on public sector insurers because they fully reprice contracts each year using expert advice. [However, also see Section 5.6 on the potential combined impact of the contract boundary and onerous contract requirements.]

Staff recommendation: Staff recommend no public sector modifications to the AASB standard incorporating the forthcoming IFRS 17 because the IASB's contract boundary principle seems no less sound in a public sector context than a private sector context.

5.4 Does the Board agree with the staff recommendation?

5.5 Onerous contracts

5.5.1 The existing Australian and New Zealand requirements include a 'Liability Adequacy Test' (LAT) for general insurance contracts that is applied to each portfolio of contracts. For life insurance contracts, the current value measure of expected net cash outflows is determined for each portfolio each reporting date and losses recognised when the 'margin on services' (the deferred profit component, similar to the IASB's CSM) becomes negative. In the case of both general and life insurance, in practice, those portfolios are usually the contract groupings used to determine premiums.

5.5.2 The unit of account for the onerous contract assessment under the forthcoming IFRS 17 is likely to be more granular. At its meeting on 20 January 2016 the IASB tentatively decided:

> to require a loss for onerous contracts to be recognised only when the contractual service margin is negative for a group of contracts, and that the group should comprise contracts that at inception:
>
> (a) have cash flows that the entity expects will respond in similar ways to key drivers of risk in terms of amount and timing; and
>
> (b) had similar expected profitability (ie similar contractual service margin as a percentage of the premium).
>
> At the same meeting the Board also tentatively decided that there should be no exception to the level of aggregation for determining onerous contracts or the allocation of the contractual service margin when regulation affects the pricing of contracts. Accordingly, contracts with dissimilar profitability, even if as a consequence of regulation, may not be grouped for determining onerous contracts and for the allocation of the contractual service margin.[31]

5.5.3 There will be insurers in both the private and public sector that will be able to identify loss-making groups of policyholders within their portfolios. Accordingly, it seems likely there would be more up-front loss recognition under the forthcoming IFRS 17 than under the existing Australian and New Zealand requirements. For example, insurers offering CTP vehicle insurance may be able to identify high-risk

31 file://mel_1/AASB_Profiles/athomson/Downloads/Effect-of-redeliberations-on-the-ED%20(1).pdf

policyholders who, as a group, are loss-makers but by regulation are charged the same premiums as low-risk policyholders who, as a group, are profit-making.

5.5.4 In a stable market, the year-on-year impact on the income statement of the onerous contract requirements in the forthcoming IFRS 17 would be minimal. There are conflicting views on whether the information would be helpful to users of public sector insurers' financial statements:

(a) some think identifying onerous contracts within a portfolio that is expected to break-even or be profitable overall is a waste of time, particularly when the insurer is a monopoly; and

(b) others think it might be useful for financial information to highlight to policymakers that high-risk policyholders are being subsidised by lower risk policyholders (although the information presented in financial statements might not be sufficiently granular to detect this in any case).

5.5.5 In respect of onerous contracts, two factors potentially set public sector insurers apart from their private sector counterparts. Public sector insurers are more likely to be:

(a) subject to regulation that limits underwriting (pricing risks differently for different policyholders); and

(b) unable to withdraw from a particular insurance market.

5.5.6 Public sector insurers (in common with their private sector not-for-profit counterparts) are also more likely to have onerous sub-groups of contracts than for-profit private sector insurers because they tend to be focused on breaking even. That is, they will always tend to be much closer to the onerous contract tipping point because any margins (for example, for capital charges) are likely to be slimmer than the profit margins sought by for-profit private sector insurers.

5.5.7 Public sector decision makers are usually focused on long-term financial sustainability, consistent with their not-for-profit focus. Some might argue this long-term focus means that identifying onerous sub-groups of insurance arrangements is of less relevance in the public sector. However, there is no precedent for this thinking in respect of onerous contracts based on the decisions taken by the AASB to-date on other IFRS. There are no public sector-specific (or not-for-profit sector-specific) onerous contract modifications to AASB 137.[32, 33]

5.5.8 Staff are sceptical about whether the focus on sub-groups within portfolios (and bringing forward loss recognition) is a cost-beneficial approach because we consider most users of financial statements will be more interested in knowing whether a line of business (portfolio) as a whole is profitable. However, this view applies to all insurance arrangements across all sectors and the *Process* comments that

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32 The additional 'Aus' paragraphs in AASB 137 are not about onerous contracts – they note that a government public policy, budget policy, election promise or statement of intent does not of itself create a present obligation which is binding.

33 Although the NZASB's PBE IPSAS 19 *Provisions, Contingent Liabilities and Contingent Assets* definition of 'onerous contract' is different from the IAS 37 definition, it remains substantively the same. [For the record, the differences are references to 'for the exchange of assets or service' and to 'service potential'. The PBE IPSAS 19 definition is: "An onerous contract is a contract for the exchange of assets or services in which the unavoidable costs of meeting the obligations under the contract exceed the economic benefits or service potential expected to be received under it."]

disagreement with the IASB's treatment is unlikely to provide good reason, in and of itself, for changing the requirement in an IFRS.

Staff comments: The fact that public sector insurers may be more likely to be subject to regulation preventing them from differentially pricing risks and may be unable to withdraw from a particular insurance market are not, of themselves, reasons for departing from IFRS. The intention of the forthcoming IFRS 17 is to reveal onerous sub-groups of contracts wherever they exist and they are bound to exist in the public sector as they do in the private sector.

It could be argued that a monopoly provider can claw back losses from those sub-groups if a policy decision were taken to do so. However, that argument might logically lead to the conclusion (noted above in Section 4.1) that the arrangements are not insurance contracts or not insurance-like.

Staff recommendation: On balance, staff recommend no public sector modifications to the AASB standard incorporating the forthcoming IFRS 17 in respect of the onerous contract requirements in isolation. The intended outcomes seem the same regardless of whether the onerous contracts arise in the public or private sectors. However, also see Section 5.6 on the potential combined impact of the contract boundary and onerous contract requirements.

5.5 Does the Board agree with the staff recommendation?

5.6 Combination of contract boundary and onerous contract issues

5.6.1 The IASB acknowledges it has more work to do to explain the various units of account in the forthcoming IFRS 17. Accordingly, there may be clarifications that would affect the conclusions in this Section. Based on the most recent information available, there are different units of account for:

(a) determining risk margins (potentially across portfolios, depending on the extent to which entities take diversification into account in setting premiums);

(b) determining most of the financial statement presentation classifications and making disclosures (portfolios); and

(c) determining onerous (based on information available about each sub-group at inception, which may be within portfolios).

5.6.2 It is not yet clear how these different units of account will function and interrelate with other parts of the forthcoming IFRS 17. For example, it is not yet clear whether the unit of account for onerous contracts and the contract boundary requirements will affect which of the measurement models can be applied. [The contract boundary decision is also effectively a unit of account decision.] Understandably, IASB staff are not yet necessarily in a position to provide a definitive response on this matter and the field tests currently underway might help clarify this interrelationship.

5.6.3 One possible scenario is that, when onerous sub-groups of annual contracts can be identified, the fact that a public sector insurer might be unable to withdraw from providing them with 'under-priced' insurance would mean they are contracts providing long-term coverage. That could mean the relevant insurance liability

would need to be measured under the general model because they are unable to be repriced to adequately reflect the risks of that sub-group and the contract boundary is deemed to go beyond the current year. Accordingly, insurance liabilities for some parts of a portfolio might need to be measured using the general model while the entity could choose to measure other (profitable) parts of the same portfolio using the simplified model.

5.6.4 Potentially, the coverage periods might be judged to be indefinite. Much like the conundrum surrounding social benefits more broadly, it could be implied that a public sector insurer has an onerous contract into perpetuity for those loss-making sub-groups. For example, based on existing government policy, a public sector insurer could be regarded as being committed to providing loss-making CTP cover to successive generations of male drivers under the age of 25.

5.6.5 The same issue applies, for example, to private sector health insurers in relation to generations of older people, but those insurers may be in a position to withdraw from the market.[34]

Staff comments: Staff consider that the combination of the onerous contract requirements and the nature of public sector insurers might have the effect of forcing them to apply the general model, when private sector insurers that can exit markets would not.

Staff also consider that applying the general model for measuring insurance liabilities to some public sector insurance arrangements might lead to the same issues that remain unresolved in relation to social benefits more broadly. Those issues include identifying obligating events under social benefit programs.

Staff recommendation: Depending on the final wording of the forthcoming IFRS 17, the Board should be prepared to make public sector modifications to the AASB standard incorporating the forthcoming IFRS 17 in respect the interaction between contract boundary and onerous contract requirements. This is because public sector insurers are often in a special position of being monopoly providers that cannot choose to withdraw from their markets.

5.6 Does the Board agree with the staff recommendation?

34 Although not a matter for this paper, staff note the health insurer example is complicated by the 'community rating' system operating in Australia under which:

(a) everyone is entitled to buy the same product, at the same price (except for Lifetime Health Cover), and is guaranteed the right to renew their policy;

(b) a health insurer cannot refuse to insure you or refuse to sell you any policy you want to buy on the basis of your health or how likely you are to claim; and

(c) there is a Risk Equalisation Trust Fund designed to spread the claim burden of individual health insurers by pooling the claims experience of all insurers for members over 55 years and so-called 'high cost' claims. [Research Paper 1 *Competition in the Australian Health Insurance Market*, page 23, Private Health Insurance Administration Council, June 2015]

Appendix – Compulsory Third Party Motor Vehicle Insurance by jurisdiction

The comparison below is based on a review of information available on the websites of the entities concerned and limited outreach and may be incomplete and is only designed as being indicative for the purposes of the AASB's decision making

	Public sector reporting entity	**Other parties**[35]	**Premiums/Underwriting**	**Benefits**[36 37]	**Comments**
ACT	ACT Third-Party Insurance Regulator (CTPR)	Private sector insurers	CTPR assesses and can reject premium proposals – at least once a year Private sector insurers can underwrite by type of vehicle	Fault-based compensation for * medical costs, including rehabilitation * economic loss, including income support * serious injuries under common law Additional at-fault cover available	Public sector entity only has regulatory role
NSW	State Insurance Regulatory Authority (SIRA)	Private sector insurers	SIRA assesses and can reject insurers' premium proposals – at least once a year Insurers can underwrite for driver age, vehicle age, driving record, address, type of vehicle & claims history	Fault-based compensation for: * medical costs, including rehabilitation * economic loss, including income support * pain and suffering Additional at fault cover available	Public sector entity only has regulatory role
NSW	Lifetime Care and Support Authority (LTCSA)	None	Levy on all CTP policies	All covered for catastrophic injury	Public sector entity bearing insurance risk

35 Schemes involving private sector insurers are designed to set premiums at a level that balances cost containment and attracting insurers to the scheme. Premiums are usually set to provide a profit margin in excess of claims and related costs that represents an adequate return on capital invested and compensation for the risks taken.

36 Dollar limits for particular types of injuries apply in most jurisdictions.

37 Fault-based schemes can provide no compensation for the person at fault, but fault is often apportioned and the extent of fault can determine the extent of compensation available.

	Public sector reporting entity	**Other parties**[35]	**Premiums/Underwriting**	**Benefits**[36 37]	**Comments**
NT	Territory Insurance Office	TIO operations outsourced to a private sector insurer	CTP premium paid with registration determined annually TIO underwrites by type of vehicle	No fault compensation for: * medical costs, including rehabilitation * economic loss, including income support * serious injuries under common law Potentially reduced compensation for drivers committing an offence	Public sector entity bearing insurance risk
QLD	Motor Accident Insurance Commission (MAIC)	Private sector insurers	MAIC sets price range annually Private sector insurers can underwrite by type of vehicle	Fault-based compensation for: * medical costs, including rehabilitation * economic loss, including income support * pain and suffering Additional at fault cover available	Public sector entity only has regulatory role
QLD	National Injury Insurance Scheme (NIIS) Queensland	None	Levy on all CTP policies	No fault compensation for serious injury care	Public sector entity bearing insurance risk
SA	CTP Insurance Regulator (CTPIR)	Private sector insurers – scheme automatically allocates drivers to a particular insurer	Premiums fixed by CTPIR annually CTPIR underwrites for type of vehicle	Fault-based compensation for: * medical costs, including rehabilitation * economic loss, including income support * pain and suffering Private sector insurer can seek to recover claims from at fault drivers who have committed an offence	Public sector entity only has regulatory role
SA	Lifetime Support Authority (LSA)	None	Levy on registration	No fault compensation for serious injury care	Public sector entity bearing insurance risk

	Public sector reporting entity	**Other parties**[35]	**Premiums/Underwriting**	**Benefits**[36] [37]	**Comments**
TAS	Motor Accidents Insurance Board (MAIB)	None	CTP premium paid with registration determined annually MAIB underwrites for type of vehicle	No fault compensation for: * medical costs, including rehabilitation * economic loss, including income support * serious injuries under common law MAIB may seek to recover costs from drivers committing serious offences	Public sector entity bearing insurance risk
VIC	Transport Accident Commission (TAC)	None	CTP premium paid with registration determined annually TAC underwrites for type of vehicle	No fault compensation for: * medical costs, including rehabilitation * economic loss, including income support * serious injuries under common law Drivers committing an offence not eligible for economic loss compensation	Public sector entity bearing insurance risk
WA	Insurance Commission of Western Australia (ICWA)	None	CTP premium paid with registration determined annually ICWA underwrites for type of vehicle	Fault-based compensation for: * medical costs, including rehabilitation * economic loss, including income support No fault scheme compensates for catastrophic injury	Public sector entity bearing insurance risk
NZ	Accident Compensation Corporation (ACC)	None	Levy on vehicle registration and share of petrol excise determined annually Registration levy based on type of vehicle Share of petrol excise based on petrol usage	No fault compensation for: * medical costs, including rehabilitation * economic loss, including income support No access to Common Law	Public sector entity bearing insurance risk