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# Response AASB17 Fatal-Flaw Review

November 2022

**Executive Summary**

This paper is in response to the Australian Accounting Standards Board's (AASB) request for comments on the Fatal-Flaw Review in respect of amendments to AASB 17 *Insurance Contracts* and AASB 1050 *Administered Items* for the public sector.

**Background**

The AASB introduced the Australian Accounting Standard 17 Insurance Contracts (AASB17) in May 2017 with an effective date of 1 January 2023. It is not currently applicable for the public sector.

The Australian Accounting Standards Board (AASB) issued a Fatal- Flaw Review for amendments to AASB 17 *Insurance Contracts* and AASB 1050 *Administered Items* 11 November 2022 (Appendix A). The intent of the proposed amendments appears to be the uniform application of AASB 17 on all insurance and 'insurance like' public sector schemes.

The principle of the AASB17 is to ensure that insurance and insurance like arrangements are accounted for as insurance contracts. The purpose of an insurance contract is the indemnification for a loss resulting from a specified event.

Compensation Schemes established and managed by icare are not designed for the indemnification of loss, they are social benefit structures designed to ensure that the people of New South Wales are supported as a result of disability or injury resulting from either exposure to Dust or injury from a motor vehicle.

These schemes are social benefit schemes akin to the NDIS and Medicare not insurance arrangements.

The fatal flaw version of the standard continues to put at risk social benefit schemes that are akin to Medicare and NDIS which are currently accounted for under AASB137. The consequence of the introduction of a risk adjustment for these arrangements would require funding to be increased to account for the higher level of assets that are required to be held. These requirements are indicatively: -

| Scheme | Impact |
|---|---|
| Lifetime Care and Support Fund | $1.7 billion at a PoA of 75% |
| Motor Accident Benefits Fund | $0.14 billion at a PoA of 75% |

The inclusion of the risk adjustment will have an adverse impact on the funding required by the schemes which will result in either Government funding redirected that could be used for the betterment of the NSW economy or an increase in the levies imposed on motorists or employers being held in deposit to meet the requirements of the new accounting standard.

This $1.84 billion could be used for essential services necessary for the ongoing running and development of the State, such as building more schools and hospitals. Locking this away to comply with an accounting standard could not reasonably be considered in the public interest or in the best interests of the Australian economy.

Our initial estimates suggest that CTP Insurers in NSW will have to increase the annual CTP levy by approximately $425 per car to fund the risk adjustments should Lifetime Care have to comply with the requirements of AASB 17. The above cost increase will put significant pressure on household budgets, particularly in an environment where inflation and interest rates are increasing relative to real wages. This will also significantly impact NSW community's ability to recover from the economic impacts of COVID.

## Scope

**The amendments provide the factors to consider for identifying arrangements that fall within the scope of AASB 17 in a public sector context.**

**Enforceability of the arrangement**

An insurance contract is defined as one party accepting significant insurance risk from another party by agreeing to compensation for a specified future event. Where an arrangement is not enforceable then there is no agreement to accept any risk.

Within the public sector there are arrangements that should not be defined as an insurance contract. The key principles that should be included in sections E11-E13 to demonstrate that there is no enforceable arrangement, and therefore no insurance contract, are the ability: -

- Unilaterally change pricing
- Unilaterally change eligibility
- Unilaterally change benefits

Change of Pricing

A public sector arrangement that can unilaterally set the pricing of the levies that it charges are indicative of a social benefit. Where the public sector entity calculates the "pricing" of levies based on cumulative funding requirements as opposed to pricing based on the prospective cover and "risk" being provided demonstrates that there is no insurance risk transferred.

Change of Eligibility

Eligibility criteria that can be changed in a public sector arrangement is indicative that there is no transfer of insurance risk and therefore no enforceable arrangement. Eligibility criteria is a critical principle as it demonstrates that there no agreement, or enforceability, for transferring the risk for a specified future event. For example, where eligibility criteria are extended or reduced through the issuing of the criteria it is indicative that the public sector entity has unilateral discretion on what is covered under the scheme. This is akin to the Medicare scheme arrangements where benefits are extended or reduced at the government's discretion.

Change of Benefits

Where a public sector arrangement can alter the benefits provided under the arrangement for historical and future events there is no enforceable agreement and no insurance contract. This can be demonstrated through the issuance of guidelines that are able to be revised and reissued by the public sector arrangement. This ability to deny/change benefits provides should be clear that there is no enforceable arrangement.

**Identifiable Coverage Period**

The identifiable coverage period paragraphs included in E14 to E19 results in unintended outcomes for arrangements that do not have coverage periods.

A levy that is changed via a private insurance contract does not establish a coverage period; it is merely a funding mechanism used for expedience. There is not a nexus between the policy issued privately and the levy charged by the public sector.

Similarly, the connection to the financial year is an arbitrary period for the schemes and does not establish a coverage period.

More appropriately, the standard should expand the indicators listed in E18 that where entry into the scheme is based on eligibility criteria. Schemes such as the Lifetime Care Scheme provide benefits based on criteria rather than the receipt of a levy. This principle is established for Medicare, as the Medicare levy does not create a coverage period for the year it was charged through the taxation system nor is it a requirement for benefits.

E18 should be extended to include arrangements where eligibility criteria are the critical factor, especially where the receipt of a levy is not a factor in acceptance.

**Similarity of Risks and benefits provided**

Similarity of risks and benefits is too broad. Where the market is only serviced by public sector arrangements, such as catastrophic injuries, then the extending to generic personal injury cover is not appropriate. It is clear these schemes are for social benefit as the risk is uninsurable. This aligns with social benefits such as Medicare.

## Other items

### Accounting Policy Choice

***The amendments that allow public sector arrangements to have an accounting policy choice to measure liabilities for remaining coverage applying the premium allocation approach***.

Icare supports the accounting policy choice.

## Onerous Contracts

***The amendments relating to the exemption from sub-grouping onerous versus non-onerous contracts at initial recognition.***

Icare supports the relief from sub-grouping for onerous and non-onerous contracts.

## Annual Cohorts

***The amendments relating to the exemption from sub-grouping contracts issued no more than a year apart.***

Icare supports the relief for the subgrouping of annual contracts.

Initial Recognition of onerous contracts

***The amendment to the initial recognition requirements so that they do not depend on when contracts become onerous.***

Icare supports the relief from initial recognition requirements when contracts become onerous.

Guidance on coverage periods

***Guidance on coverage periods in a public sector context, which has consequences for determining the cash flows used to measure insurance liabilities and the pattern of revenue recognition***.

Icare comments on coverage periods are included in the identifiable coverage period response above.

Effective Date

***The deferral of the effective date of AASB 17 to annual reporting periods beginning on or after 1 July 2025.***

Icare supports the effective date to annual reporting periods beginning on or after 1st July 2025.

AASB1050

***Amendments to permitting a choice of Standard for administered items.***

Icare supports the choice of standard for administered items.