



**ACT**  
Government

Chief Minister, Treasury and  
Economic Development

Ms Kris Peach  
The Chair  
Australian Accounting Standards Board  
PO Box 204  
Collins Street West  
Victoria 8007

*Kris*  
Dear Ms Peach

## **DISCUSSION PAPER AUSTRALIAN-SPECIFIC INSURANCE ISSUES – REGULATORY DISCLOSURES AND PUBLIC SECTOR ENTITIES**

The Heads of Treasuries Accounting and Reporting Advisory Committee (HoTARAC) welcomes the opportunity to provide comments to the Australian Accounting Standards Board (AASB) on its Discussion Paper (DP) *Australian-specific Insurance Issues – Regulatory Disclosures and Public Sector Entities*.

HoTARAC agrees with the AASB's proposed objective of greater consistency of financial reporting across public sector entities engaging in insurance activities. HoTARAC recommends the proposals be modified to exclude social benefit payments that are provided by governments to all citizens of its jurisdiction.

The attachment to this letter sets out HoTARAC's comments on the specific matters. If you have any queries regarding our comments, please contact Peter Brown from the Commonwealth Department of Finance on (02) 6215 2969 or by email to [peter.brown@finance.gov.au](mailto:peter.brown@finance.gov.au).

Yours sincerely,

David Nicol

CHAIR

Heads of Treasuries Accounting and Reporting Advisory Committee

7 March 2018

## General Matters

### 1.0 For Public Sector Entities

1. Do you agree with the objective of the proposed Implementation Guidance to achieve greater consistency of financial reporting across the public sector among entities engaging in insurance activities for the benefit of users of that information? Why or why not?

HoTARAC agrees as there is inconsistency in the application of accounting standards between private and public sectors. Economically similar liabilities should be accounted for consistently.

Two jurisdictions noted that where the proposed changes capture schemes currently not applying insurance accounting, this increase in liabilities is likely to result in increased levies to the public.

All entities that currently issue insurance contracts account for the schemes under AASB 1023 General Insurance Contracts. This is consistent with the private sector. All insurance schemes that do not issue insurance contracts account for their liabilities under AASB 137 Provisions, Contingent Liabilities and Contingent Assets.

2. Do you agree with the proposed Implementation Guidance for determining when public sector entities should be required to apply AASB 17 Insurance Contracts and will the Guidance achieve its objective of greater consistency of financial reporting? Why or why not?

HoTARAC agrees that the proposed implementation guidance is suitable for public sector arrangements that are insurance-like. However, HoTARAC is concerned that the proposed guidance does not clearly distinguish between these type of arrangements and social benefit payments that are made by governments and are available to all citizens of that jurisdiction. HoTARAC recommends the AASB await further work on the IPSASB's project on social benefits, currently in the exposure draft stage, before proceeding with defining arrangements that are insurance like. There is a risk that social benefits, available to all citizens, on occurrence of an event such as becoming unemployed or becoming disabled, may inadvertently fall within the scope of the proposals.

HoTARAC questions the Board's rationale for rejecting the work completed by the IPSASB in paragraph BC28(a). AASB 1049 *Whole of Government and General Government Sector Financial Reporting* harmonises accounting and Government Finance Statistics (GFS) at the whole of government level, so it would be consistent and desirable to use GFS definitions where these are available.

Even if the Board elects to disregard the work of IPSASB, HoTARAC recommends at least considering accounting for social benefits before proceeding with the application of insurance principles to the public sector, as both payments are made on the occurrence of an event, such as an accident, and clear guidance is needed to distinguish between the two.

Notwithstanding the AASB's conceptual concerns with the IPSASB's approach, HoTARAC notes that restricting the application of the insurance standard to situations where funding is provided by beneficiaries would avoid confusion with social benefit payments that are payable when recipients meet specified eligibility criteria. As outlined in the responses below, HoTARAC is not convinced the criteria used in the consultation paper in the absence of this simple test are adequate.

HoTARAC notes that social benefits are recognised on a 'due and payable' basis, when an applicant fulfils the eligibility criteria for that fortnight's payment. Application of the measurement principles of AASB 17 to these benefits would result in the recognition of lifetime liabilities with no corresponding asset for the government's right to tax future earnings.

The funding criterion in Example 3B and Example 4 are not consistent. Both examples are funded by the government, rather than levies. However, in 3B the funding criterion is met when the Government funds are contributions under legislation, while in 4 where funding is received from a government appropriation the criteria is not met. This should not create a difference in whether the criteria will be met, and the rationale given does not address this. In both examples, neither the insured nor the party creating the risk pays anything. If this is considered irrelevant, then the funding criterion itself would appear to be conceptually irrelevant.

3. Are there other forms of Implementation Guidance that would be more likely to achieve the objective of greater consistency of financial reporting for the benefit of users?

HoTARAC fails to understand the point of criteria E14(a) on funding, as it seems to cover all potential sources of funds. This would be more useful if it specifically excludes amounts paid out of consolidated revenue.

In applying criteria E14(b) it is important to distinguish between assessments made to determine insurance premiums, such as those undertaken by a private insurer, and those undertaken for policy and planning purposes. Government entities may undertake analysis to assess future taxation requirement to fund social benefits such as pensions, manage health care outcomes for beneficiaries of the National Disability Insurance Scheme or engage an actuary to assess the budget impacts of continuing with a particular benefit payment. None of these is evidence of an insurance-like arrangement.

Criterion E13(c) seems applicable to any government benefit payment, where the only qualifying criteria is meeting the eligibility requirements for the period.

It is also questionable whether any arrangement that involves government payments would not satisfy E13(a). HoTARAC also suggests the term 'commercial substance' is a misnomer, as the only criteria is a change in future cash flows.

HoTARAC supports E14(d), but this should be clearer that benefits funded from general taxation revenue are excluded.

4. Do you agree the amendments to AASB 17 should apply to both for-profit and not-for-profit public sector entities?

HoTARAC agrees, subject to resolution of the distinction between insurance and social benefits.

#### **Risk Adjustment for Non-financial Risk**

5. Do the proposals provide sufficient guidance to determine the risk adjustment factor for non-financial risk? If not, what additional guidance is needed?

HoTARAC recommends further guidance on the techniques used to determine the non-financial risk adjustment. Otherwise there is a risk of loss of transparency and comparability through inconsistent treatments. Examples of estimation techniques that can be used would be valuable as it will reduce the possibility of increased inconsistencies in reporting.

HoTARAC also recommends the risk adjustment factor should be determined by each scheme giving due consideration to the risks of each scheme.

6. Are there any situations where there might be a risk adjustment factor of zero (refer paragraph BC11)?

Three HoTARAC members identified situations where the risk adjustment factor could be zero. For example, where a scheme is so long tail that volatility is largely mitigated by the smoothing over time. Other members were not aware of these situations.

**Determining the Contract Boundary**

7. When determining the contract boundary, are there any other instances apart from those illustrated in the examples, where there is no premium or the contract boundary is longer than 12 months, but it would still be permitted to apply the simplified approach under AASB 17? If so, do you agree that all public sector entities should be given an exemption to apply the premium allocation approach (the simplified approach) under AASB 17?

HoTARAC is not aware of entities being permitted to apply the simplified approach outside those specified in AASB 17. Nonetheless, HoTARAC's preference is for all public sector entities to apply the simplified approach, irrespective of contract boundaries.

8. Do you agree with the following interpretation? If the funding can only be changed with a corresponding change in legislation, then the presumption exists that the simplified approach is not available for application. However, if the funding can be changed at will, then the presumption that the contract boundary is less than 12 months can be supported and the simplified method will be available for use.

HoTARAC agrees.

**Captive insurance arrangements**

9. Where subsidiaries apply AASB 17 to insurance and insurance-like contracts in the subsidiary's separate financial statements, but at the consolidated group level such contracts are regarded as self-insurance and consequently outside the scope of AASB 17, should such arrangements be scoped out of AASB 17 for the subsidiary's separate financial statements?

HoTARAC agrees they should be scoped out. In these circumstances the government is self-insuring and simply instituting internal cash transfers.

**Investment contracts with discretionary participation features**

10. Under AASB 17 para 3(c) an entity is required to apply AASB 17 to investment contracts with discretionary participation features, if the entity also issues insurance contracts.

(a) Do not-for-profit public sector entities regularly issue both insurance contracts as well as investment contracts with discretionary participation features?

(b) If so, would the accounting treatment of such investment contracts with discretionary participation features be significantly different under AASB 17 as compared to their current accounting treatment?

(c) If the existing accounting treatment is significantly different, would the proposed accounting treatment under AASB 17 impose undue cost or effort on the entity?

(d) If the answers to questions (a)-(c) were affirmative, do you propose that all investment contracts with discretionary participation features issued by a not-for-profit public sector entity should be entirely scoped out of AASB 17? If so, what requirements should apply?

HoTARAC has not identified circumstances where public sector entities issue both insurance contracts and investment contracts with discretionary features. HoTARAC notes that this is more a feature of private sector arrangements.

11. Are there other matters raised by the requirements of AASB 17 that you consider should be addressed in respect of public sector entities?

Governments often act as ‘insurers of last resort’, where private sector entities are unwilling to provide insurance. Examples include terrorism and some natural disasters. Accordingly, the government may accept insurance risk that are intrinsically difficult to measure reliably.

Legislative changes could retrospectively amend beneficial rights. Accordingly, criteria 13b should be made clearer.

Differences between insurance contracts (legally binding instruments) vs. social benefit schemes where the benefits are determined by legislature and therefore can be adjusted retrospectively should be considered.

12. Overall, are the proposals for public sector insurance accounting in the best interests of the Australian economy?

The majority of HoTARAC agrees to the extent the proposals are modified to exclude social benefit payments. The proposals have the potential to increase the focus on risk and risk management across public sector insurance funds.

One member’s view is where the benefits for levy funded public sector schemes are set by legislation, introducing the requirement for a risk margin means that either:

- additional government funds will be locked up in investment funds, raised through increased levies or increased Government contributions; or
- the benefits to participants would need to be reduced to maintain the funding ratio.

## **2.0 For-Profit Private Sector Entities**

13. AASB 1023 and AASB 1038 included some regulatory disclosure requirements that have not been carried forward into AASB 17. Do you agree with the AASB’s recommendation that these disclosure requirements should not be carried forward to either AASB 17 or AASB 1054 Australian Additional Disclosures?

HoTARAC agrees.

