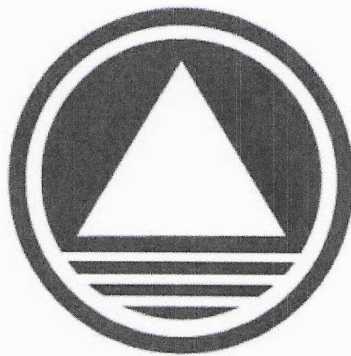




Thai General Insurance Association

IFRS 17 Insurance Contracts  
Practical Guidance

Topic 3: Level of Aggregation

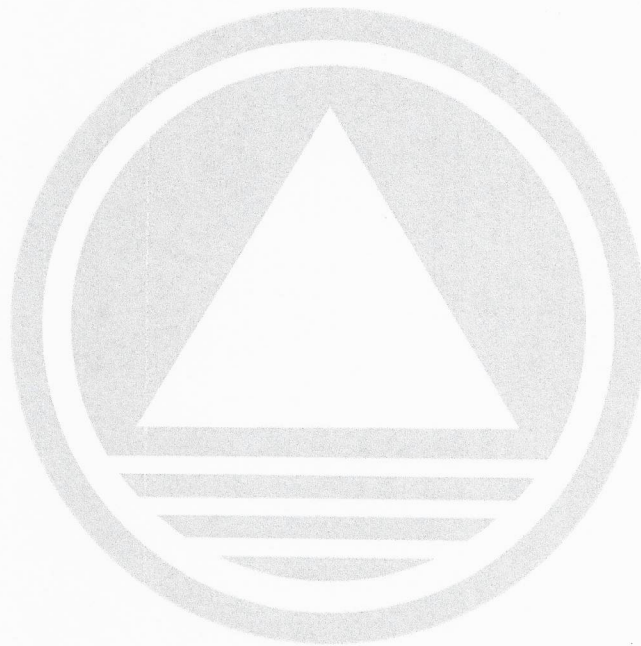
30 September 2021

## Disclaimer

This is a Practical Guidance in the application of IFRS 17 Insurance Contracts and is by no means a financial reporting standards.

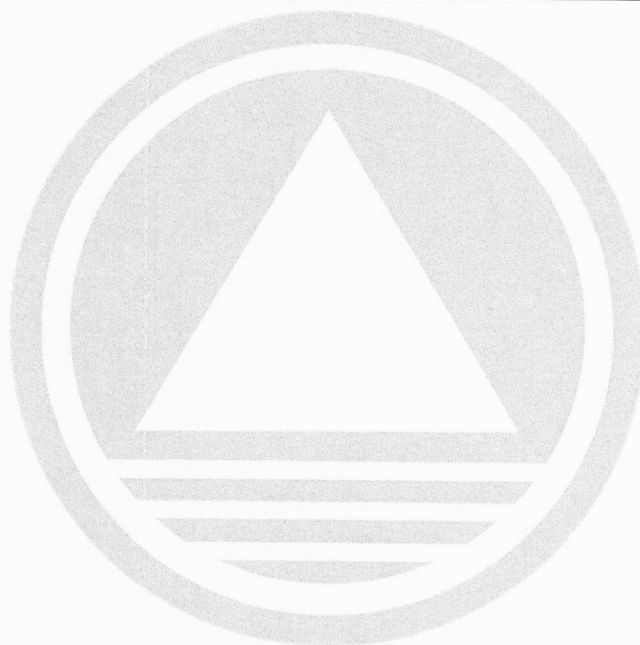
The IFRS is principles-based, therefore this guide aims to provide illustrative examples on how to apply the standards by IASB.

In the event of any conflict or inconsistency between the IFRS and the Practical Guidance, the IFRS shall prevail, and the accounting treatment should comply with the IFRS. Similarly, should the interpretation of the IFRS results in a contradicted conclusion from the example given in the Practical Guidance, the accounting treatment should observe IFRS.



## Contents

|     |                                                |    |
|-----|------------------------------------------------|----|
| 1.0 | Executive Summary                              | 4  |
| 2.0 | References                                     | 5  |
| 3.0 | Practical Guidance                             | 8  |
|     | 3.1 Portfolios                                 | 8  |
|     | 3.2 Cohorts                                    | 9  |
|     | 3.3 Profitability Groups                       | 10 |
|     | 3.4 Consideration for Interim Reporting        | 14 |
| 4.0 | Illustrations                                  | 15 |
|     | 4.1 Portfolios                                 | 15 |
|     | 4.2 Groups                                     | 16 |
| 5.0 | Frequently Asked Questions                     | 17 |
|     | 5.1 Level of Aggregation – Onerous Group       | 17 |
|     | 5.2 Level of Aggregation for Aggregation Cover | 18 |



## 1.0 Executive Summary

This report is part of a series of study papers guiding non-life insurers' implementation of the new Thai Financial Reporting Standard 17 for Insurance Contracts ("TFRS 17"), which has a mandatory effective date of 1 January 2024 or later (1 year after IASB effective date for IFRS 17).

The standard requires an entity to define unit of account for measurement and presentation. It is generally understood that the unit of account for measurement is group of insurance contracts and group of reinsurance contracts. Unit of account for presentation is portfolio of insurance contracts issued (or acquired).

As defined in the Standard, a portfolio of insurance contracts is subject to similar risks and managed together. Each portfolio forms a partition of the total insurance business of the reporting entity. There is no clear definition of "similar risk or managed together" given in the Standard. However, according to the Basis of Conclusion, "similar" does not mean identical and some variation in risks is reasonable.

A single reinsurance contract held by the Company may cover multiple groups of insurance contracts. However, within the context of reinsurance contracts, the definition of portfolio of being "managed together" should be driven more by the reinsurance contract itself and not the underlying insurance contracts.

The Standard requires a portfolio of insurance contracts to be divided into a minimum of three categories, based on the onerosity of the group of contracts. However, paragraph 17 of the Standard allows measuring the profitability of contracts on an aggregate level if there is reasonable and supportable information to conclude that the affected set of contracts will all be in the same group. Such information should be based on readily available internal reporting information that provides a consistent and reliable measure indicative of the profitability of a group of insurance contracts.

Applying paragraph 61 of the Standard, grouping of reinsurance contracts depends on whether the company expects to incur a net gain for purchasing the reinsurance contract. Therefore, applying the grouping requirements in paragraph 16 to reinsurance contracts, a portfolio of reinsurance contracts is divided into:

- a. A group of contracts on which there is a net gain at initial recognition, if any;
- b. A group of contracts on which at initial recognition there is no significant possibility of a net gain arising subsequently, if any; and
- c. A group of remaining contracts in the portfolio, if any.

The grouping of reinsurance contract held in turn depends on the onerosity of the underlying insurance contracts at initial recognition. Therefore, a straight-forward application of the grouping requirement is to divide a portfolio of reinsurance contracts by set of the underlying insurance contracts that they cover will not directly meet the definition of reinsurance contract held.

For direct and facultative inwards insurance contracts, the requirement in paragraph 22 for annual cohort refers to either the date of issuance or the date of policy inception, when read together with paragraph 24 and 28.

The results of the assessment for the topic are discussed in sections below.



## 2.0 References

### International Financial Reporting Standard 17

The following are references to the IFRS 17 referred to in this Practical Guidance:

| Name of the IFRS17 Topics | Reference in IFRS 17 (Paragraph) |
|---------------------------|----------------------------------|
| Portfolios                | 14                               |
| Cohorts                   | 22, 23, 24, 28                   |
| Groups                    | 16, 17, 18, 19, 20, 21, 24,      |
| Onerous Groups            | 47, 48, 50, 51, 52               |

#### Level of aggregation of insurance contracts

14 An entity shall identify portfolios of insurance contracts. A portfolio comprises contracts subject to similar risks and managed together. Contracts within a product line would be expected to have similar risks and hence would be expected to be in the same portfolio if they are managed together. Contracts in different product lines (for example single premium fixed annuities compared with regular term life assurance) would not be expected to have similar risks and hence would be expected to be in different portfolios.

16 An entity shall divide a portfolio of insurance contracts issued into a minimum of:

- a group of contracts that are onerous at initial recognition, if any;
- a group of contracts that at initial recognition have no significant possibility of becoming onerous subsequently, if any; and
- a group of the remaining contracts in the portfolio, if any.

17 If an entity has reasonable and supportable information to conclude that a set of contracts will all be in the same group applying paragraph 16, it may measure the set of contracts to determine if the contracts are onerous (see paragraph 47) and assess the set of contracts to determine if the contracts have no significant possibility of becoming onerous subsequently (see paragraph 19). If the entity does not have reasonable and supportable information to conclude that a set of contracts will all be in the same group, it shall determine the group to which contracts belong by considering individual contracts.

18 For contracts issued to which an entity applies the premium allocation approach (see paragraphs 53–59), the entity shall assume no contracts in the portfolio are onerous at initial recognition, unless facts and circumstances indicate otherwise. An entity shall assess whether contracts that are not onerous at initial recognition have no significant possibility of becoming onerous subsequently by assessing the likelihood of changes in applicable facts and circumstances.

19 For contracts issued to which an entity does not apply the premium allocation approach (see paragraphs 53–54), an entity shall assess whether contracts that are not onerous at initial recognition have no significant possibility of becoming onerous:

20 If, applying paragraphs 14–19, contracts within a portfolio would fall into different groups only because law or regulation specifically constrains the entity's practical ability to set a different price or level of benefits for policyholders with different characteristics, the entity may include those contracts in the same group. The entity shall not apply this paragraph by analogy to other items.

21 An entity is permitted to subdivide the groups described in paragraph 16. For example, an entity may choose to divide the portfolios into:

- (a) more groups that are not onerous at initial recognition—if the entity’s internal reporting provides information that distinguishes:
  - (i) different levels of profitability; or
  - (ii) different possibilities of contracts becoming onerous after initial recognition; and
- (b) more than one group of contracts that are onerous at initial recognition—if the entity’s internal reporting provides information at a more detailed level about the extent to which the contracts are onerous.

**22 An entity shall not include contracts issued more than one year apart in the same group. To achieve this the entity shall, if necessary, further divide the groups described in paragraphs 16–21.**

23 A group of insurance contracts shall comprise a single contract if that is the result of applying paragraphs 14–22.

24 An entity shall apply the recognition and measurement requirements of IFRS 17 to the groups of contracts determined by applying paragraphs 14–23. An entity shall establish the groups at initial recognition and add contracts to the groups applying paragraph 28. The entity shall not reassess the composition of the groups subsequently. To measure a group of contracts, an entity may estimate the fulfilment cash flows at a higher level of aggregation than the group or portfolio, provided the entity is able to include the appropriate fulfilment cash flows in the measurement of the group, applying paragraphs 32(a), 40(a)(i) and 40(b), by allocating such estimates to groups of contracts.

28 In recognising a group of insurance contracts in a reporting period, an entity shall include only contracts that individually meet one of the criteria set out in paragraph 25 and shall make estimates for the discount rates at the date of initial recognition (see paragraph B73) and the coverage units provided in the reporting period (see paragraph B119). An entity may include more contracts in the group after the end of a reporting period, subject to paragraphs 14–22. An entity shall add a contract to the group in the reporting period in which that contract meets one of the criteria set out in paragraph 25. This may result in a change to the determination of the discount rates at the date of initial recognition applying paragraph B73. An entity shall apply the revised rates from the start of the reporting period in which the new contracts are added to the group.

#### **Onerous contracts**

47 An insurance contract is onerous at the date of initial recognition if the fulfilment cash flows allocated to the contract, any previously recognized insurance acquisition cash flows and any cash flows arising from the contract at the date of initial recognition in total are a net outflow. Applying paragraph 16(a), an entity shall group such contracts separately from contracts that are not onerous. To the extent that paragraph 17 applies, an entity may identify the group of onerous contracts by measuring a set of contracts rather than individual contracts. An entity shall recognise a loss in profit or loss for the net outflow for the group of onerous contracts, resulting in the carrying amount of the liability for the group being equal to the fulfilment cash flows and the contractual service margin of the group being zero.



48 A group of insurance contracts becomes onerous (or more onerous) on subsequent measurement if the following amounts exceed the carrying amount of the contractual service margin:

- (a) unfavourable changes relating to future service in the fulfilment cash flows allocated to the group arising from changes in estimates of future cash flows and the risk adjustment for non-financial risk; and
- (b) for a group of insurance contracts with direct participation features, the decrease in the amount of the entity's share of the fair value of the underlying items.

Applying paragraphs 44(c)(i), 45(b)(ii) and 45(c)(ii), an entity shall recognise a loss in profit or loss to the extent of that excess.

50 After an entity has recognised a loss on an onerous group of insurance contracts, it shall allocate:

- (a) the subsequent changes in fulfilment cash flows of the liability for remaining coverage specified in paragraph 51 on a systematic basis between:
  - (i) the loss component of the liability for remaining coverage; and
  - (ii) the liability for remaining coverage, excluding the loss component.
- (b) solely to the loss component until that component is reduced to zero:
  - (i) any subsequent decrease relating to future service in fulfilment cash flows allocated to the group arising from changes in estimates of future cash flows and the risk adjustment for nonfinancial risk; and
  - (ii) any subsequent increases in the amount of the entity's share of the fair value of the underlying items.

Applying paragraphs 44(c)(ii), 45(b)(iii) and 45(c)(iii), an entity shall adjust the contractual service margin only for the excess of the decrease over the amount allocated to the loss component.

51 The subsequent changes in the fulfilment cash flows of the liability for remaining coverage to be allocated applying paragraph 50(a) are:

- (a) estimates of the present value of future cash flows for claims and expenses released from the liability for remaining coverage because of incurred insurance service expenses;
- (b) changes in the risk adjustment for non-financial risk recognised in profit or loss because of the release from risk; and
- (c) insurance finance income or expenses.

52 The systematic allocation required by paragraph 50(a) shall result in the total amounts allocated to the loss component in accordance with paragraphs 48–50 being equal to zero by the end of the coverage period of a group of contracts.

### 3.0 Practical Guidance

#### 3.1 Portfolios

During the process of identifying insurance contracts, unbundling of package products and combination of singular products has the intention to group similar risk together at a sufficient granular level. "Similar" risks does not mean "identical". Some variation in risk is reasonable, as long as the contracts are sufficiently similar. Since insurance is diverse and all portfolios are different, no prescriptive guidance can be provided on the correct level of materiality for the definition of "similar" and the decision process will be entity specific.

In the case of a contract with "multiple risks", the entity should determine the predominant risk for classification of the risk type, which would require management judgement. Thus, the contract is then assigned to a portfolio according to the predominant risk. In the case of singular products (if no unbundling is necessary), the aggregation should be based on the predominant risk of the contract.

A practical approach to determining the portfolios for an entity might rely on the internal management reporting systems. For example, an entity's internal management systems may consolidate results into product lines. These product lines could provide a suitable aggregation of similar risks; furthermore, an entity may have its systems aligned with its internal management structure and may disclose to the market on that basis. This might constitute a suitable aggregation basis for what is considered as 'managed together'.

Other factors to consider against the test of managed together could, amongst others, include:

- distribution channel(s) or countries that the contracts are sold through;
- the level at which regulation takes place, for example Auto. Compulsory;
- the operating model or management structure of the entity, including how management incentives are structured;
- treaty underwriter accounts assigned.

Main class as prescribed by OIC in the RBC statistical reporting may or may not be appropriate to define portfolios due to a different focus in IFRS 17 and depending on complexity of business, where the primary focus of IFRS17 is about reporting appropriate profit and loss in any reporting period (IFRS17.BC119) according to the risk characteristic. RBC primary focus is consistency in supervisory action. We suggest company to apply their judgement according to the complexity of the business. The following are examples where the portfolio could be more granular than current RBC statutory reporting:

- If a company sell a product which has significant exposure to foreign currency risk or other financial risks, under IFRS17.
- If a company sells a product that cover risk for more than 5 years period and it is significant in totality.
- If a company sells a product that covers risk in foreign location and it is significant in totality.
- If a company sells a new product that is newer sold in Thailand before and it is significant in totality.

We define proportional reinsurance as reinsurance contracts where both the company and the reinsurer shares the premiums and claims on a given risk in specific proportion, potentially with a minimum retention and/or maximum limit, as defined under the contract. This definition includes both treaties and facultative covers, as long as the reinsurance provides proportional coverage. For treaties, the coverage is usually arranged on a risk-attaching basis.

We define non-proportional reinsurance as reinsurance contracts whereby the reinsurance premium paid is not proportionate to the claims ceded to the reinsurer. For example, the reinsurance premium on whole account excess of loss is calculated based on a fixed percentage of the company's annual gross net premium income (GNPI), while the claims ceded depends on the layers of limit as specified in the reinsurance contract. Such reinsurance is usually arranged on a loss occurrence basis, i.e. it covers the losses that occur/made within the term rather than the risks incepted within the term.



Examples of contract within proportional and non-proportional reinsurance portfolios:

Proportional Coverage

- Facultative Outwards (Including Facultative Obligatory)
- Surplus Treaty Outwards
- Quota Share Treaty Outwards

Non-Proportional Coverage

- Whole Account XOL
- Combined Liability XOL
- All other XOLs

### 3.2 Cohorts

According to IFRS17.28, in recognising a group of insurance contracts in a reporting period, an entity shall include only contracts that individually meet one of the criteria set out in IFRS17.25. The approach is intuitive in the sense that this requirement is practical for implementation.

The requirement could be translated in the following methods:

- Underwriting year (using policy effective date)
- Policy year (using premium due date or issuance date)

For general insurance policies, the underwriting year is the preference and we would therefore recommend for implementation. In this regard, the pipeline premium will be estimated for the purpose of measurement under IFRS17.

The paragraph 28 also applies to reinsurance contract held, hence the initial recognition date of reinsurance contract is chosen for cohorting for reinsurance contract held.

Practically, the set of reinsurance contracts held is matched to the underlying group of insurance contracts for proportional coverage. Below is an illustration of how cohort 2028 reinsurance contract should be aggregated for the purpose of measurement and reporting under IFRS17.

| Underlying group of insurance contracts | Reinsurance contract   | Set of reinsurance contracts held                                                                                                            | Reinsurance portfolio   |
|-----------------------------------------|------------------------|----------------------------------------------------------------------------------------------------------------------------------------------|-------------------------|
| 2028 N Auto. Voluntary                  | 2028 Treaty QS – SR    | 2028 Treaty QS – SR – 2028 N Auto. Voluntary                                                                                                 | Proportional treaty     |
| 2028 O Auto. Voluntary                  | 2028 Treaty QS – HR    | 2028 Treaty QS – SR – 2028 O Auto. Voluntary<br>2028 Treaty QS – HR – 2028 N Auto. Voluntary<br>2028 Treaty QS – HR – 2028 O Auto. Voluntary |                         |
| 2028 O Auto. Compulsory                 | 2028 Treaty QS – SR    | 2028 Treaty QS – SR – 2028 N Auto. Compulsory<br>2028 Treaty QS – SR – 2028 O Auto. Compulsory                                               |                         |
| 2028 O Medical                          | 2028 Treaty QS – HR    | 2028 Treaty QS – HR – 2028 O Medical                                                                                                         |                         |
| All Property                            | 2028 Treaty XoL – SR   | 2028 Treaty XoL – SR                                                                                                                         | Non-proportional treaty |
| All Liability                           | 2028 Treaty XoL – SCOR | 2028 Treaty XoL – SCOR                                                                                                                       |                         |

For non-proportional coverage, the cohort will be chosen independently from the underlying group of insurance contracts, which is based on the reinsurance coverage effective date.

Proportional reinsurance arrangement is interpreted the same as reinsurance contract providing proportionate coverage and vice versa.

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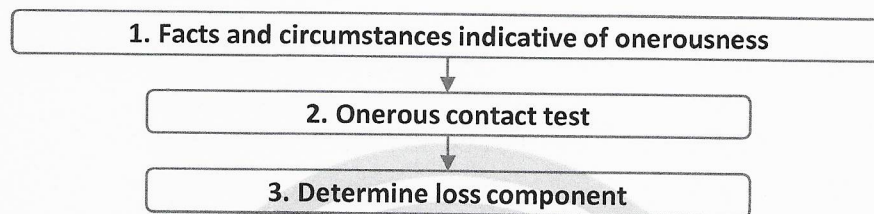
### 3.3 Profitability Groups

#### 3.3.1 Products identified for measurement under the Premium Allocation Approach (“PAA”)

##### Grouping onerous contracts

A contract is onerous according to IFRS17.47 if the discounted cash outflows (including the risk adjustment) exceed the discounted cash inflows, within the contract boundary.

As a determination of the fulfilment cash-flows as described above is generally not required under the PAA, these information are not readily available. In addition, contracts accounted for under the PAA are typically of short duration. So, the impact of recognizing losses from onerous contracts immediately as a result of the onerous contract test is less significant than for long-duration contracts. Thus, IFRS 17 has specified a simplified approach as follows:



##### Facts and circumstances

For contracts accounted for under the PAA, an entity shall assume no contracts in the portfolio are onerous at initial recognition, unless “facts and circumstances” indicate otherwise. If onerous contracts are identified, a quantitative onerous contract test (OCT) is required.

Determination of facts and circumstances is a qualitative assessment. An entity needs to assess facts and circumstances for existing portfolios and identify changes to facts and circumstances in subsequent years during the coverage period in order to identify whether there are indications for onerous contracts in the portfolio. This applies similarly for new business portfolios.

A key rationale of the IASB behind the introduction of the simplified PAA was to avoid operational complexity and introduction of new systems and processes for short duration contracts and non-complex multi-year contracts. Consistent with this rationale, the implementation of the OCT should not require significant new processes or data flows. Thus, the assessment of facts and circumstances shall be mainly based on the segmentation and information available as follows:

- Information and processes in scope of the regular IFRS audit (e.g., accounting and reserving data and processes).
- Internally reconciled data by lines of business (LoBs)/underwriters accounts/cedants.

For assessing facts and circumstances, onerous contracts are to be understood according to IFRS 17, i.e., based on the calculation of fulfilment cash flows. Thus, a reasonable approximation to fulfilment cash flows is required. It should be noted that undiscounted combined ratios may not be a good approximation. A better approximation is a ratio that is broadly consistent with IFRS 17. Hence, the relevant criteria for a ratio suitable for onerous contract testing (“OCT ratio”) are:

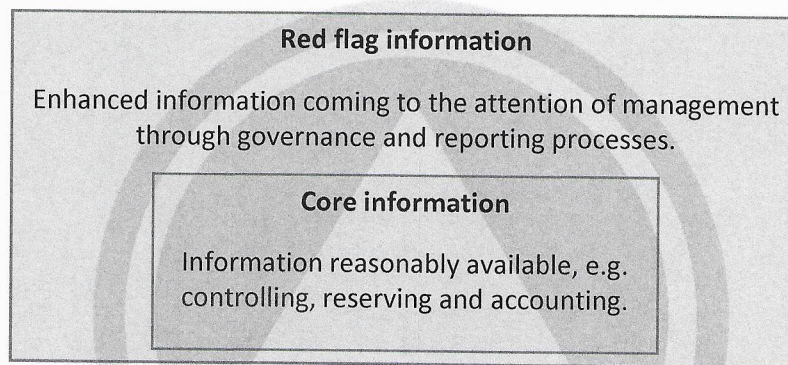
- Ratios (commission, claim, expenses) on a gross of reinsurance basis
- Discounted ratios above including an explicit risk adjustment loading
- Overheads being recognized in the same way they are recognized in cash flows, i.e. allocation of fixed and variable overheads directly attributable to fulfilling portfolio of insurance contracts
- No reflection of investment income, only discounting



Subsequently, the assessment is enhanced by additional red flag information, if relevant. This may require management judgement, while also avoiding undue costs and efforts. Red flag information may include:

- Information supporting regulatory reporting / arising from periodical regulatory inspection
- Information routinely used for business steering
- Specific events triggering facts and circumstances, for instance:
  - (Retroactive) regulatory changes
  - Major shifts in economic or market environment (e.g., new normal post pandemic)
  - Major cost allocation changes (e.g., double digit growth rate year on year)
  - Changes in acquisition costs (e.g., new distribution channel)
  - Discernible M&A effect on a cohort (e.g., economy of scale attained)
  - Booking corrections or re-allocations (e.g., accounting error)

The figure below summarizes the approach for determining facts and circumstances:



### **Onerous contract test ("OCT")**

If facts and circumstances are indicative for onerous contracts in a portfolio, an onerous contract test has to be performed. OCT is a quantitative assessment of fulfilment cash flows in comparison to the qualitative facts and circumstances. If OCT proves a group of contract to be onerous, the loss component of reserves must be set up.

### **Grouping contracts that have no significant possibility of becoming onerous subsequently**

When assessing the likelihood of changes in applicable facts and circumstances, the entity will need to refer to the same information and processes as above.

Only changes in facts and circumstances (e.g., assumption changes) affecting the unexpired portion of the coverage should be considered. For example, consider a contract which is not onerous at initial recognition. However, high losses may occur as time passes during the coverage period (e.g. due to natural hazard). The contract would not be considered as significant possibility of becoming onerous subsequently as a result of the potential high losses, because they relate to the expired portion of the coverage. Nevertheless, volatility in the expected probability of a future high loss event could have an impact on this assessment.



### 3.3.2 Products identified for measurement under the General Measurement Model (“GMM”)

Under the GMM, the entity has to calculate fulfilment cash flows as part of the liability for remaining coverage. Based on those cash flows, the CSM component is determined, which implies an automatic onerous contract test (where onerous being that the CSM is negative).

#### Grouping by cohort

The requirement for cohort of all groups is same as the approach described in section 3.2.

#### Grouping onerous contracts

IFRS17.17 allows measuring the profitability of contracts on an aggregated level if there is reasonable and supportable information to conclude that the affected set of contracts (e.g., policies of the same sub-class code) will all be in the same group.

In order to ensure consistent reporting over time, it is necessary to determine a stable criteria indicative of profitability for a given portfolio of insurance contracts. Based on the segmentation given by these criteria, the profitability buckets are defined and the CSM is determined.

For each portfolio:

- Profitability buckets sub-divide a given portfolio.
- Profitability buckets differentiate levels of profitability and in particular, identify onerous contracts and potentially onerous contracts.

On each level of profitable buckets, the CSM has to be calculated in initial recognition.

- Profitability buckets should remain mostly unchanged over time because onerous contracts should not be added to profitable contracts.
- Initial recognition assumption, once reset according to accounting policy choice, shall reset the composition of the profitability groups automatically.

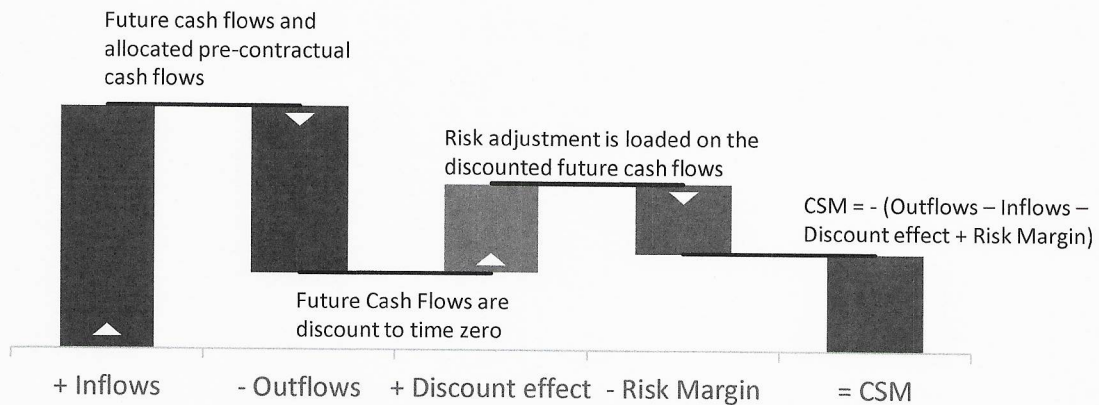
To derive the appropriate profitability buckets, the following steps are required:

| Recognition of Profitability Buckets  |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                         |
|---------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>1. Identify parameters</b>         | <p>Identification of main parameters (actuarial assumptions) indicative of profitability for each portfolio to determine profitability buckets, the assumption setting should take into account information reasonably available for each portfolio (not limited to) e.g.:</p> <ul style="list-style-type: none"> <li>• Information from regular planning and controlling</li> <li>• Information from product profitability assessment</li> <li>• Information available in regular governance process and /or available to senior management</li> </ul> <p>Potential approaches to derive these criteria may include:</p> <ul style="list-style-type: none"> <li>• Identify what have been the main clusters and triggers (materiality) which drove profitability in the past.</li> <li>• Which parameters drove movement analyses in the portfolio?</li> </ul> <p>Criteria which are not reflected in pricing due to legal constraints do not need to be assessed.</p> |
| <b>2. Slice portfolio</b>             | Based on the parameters identified in step one, the portfolio has to be segmented in profitability buckets.                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                             |
| <b>3. Calculate CSM</b>               | On each profitability bucket the CSM has to be determined. This means that the valuation (or a reasonable allocation) of fulfilment cash flows needs to be available on this level.                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                     |
| <b>4. Allocate to contract groups</b> | <p>Upon discretion of the entity at every closing:</p> <ul style="list-style-type: none"> <li>• The profitability buckets are aggregated into a group of onerous contracts and a group of non-onerous contracts (based on the result of the CSM calculation at that level); or</li> <li>• There are as many contract groups as there are profitability buckets.</li> </ul>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                              |

ลิขสิทธิ์ของสมาคมประกันวินาศภัยไทย ห้ามนำไปใช้ในการแสวงหากำไรทางการค้า



On initial recognition of any group of insurance contracts under the GMM, the CSM is the equal and opposite amount of the net inflow that arises from the following:



The derecognition of any asset or liability recognized for insurance acquisition cash flows is allocated to the future cash flows on initial recognition date (see "Attributable Insurance Expenses" technical paper for more information on pre-contractual; cash flows arising from the contracts in the group)

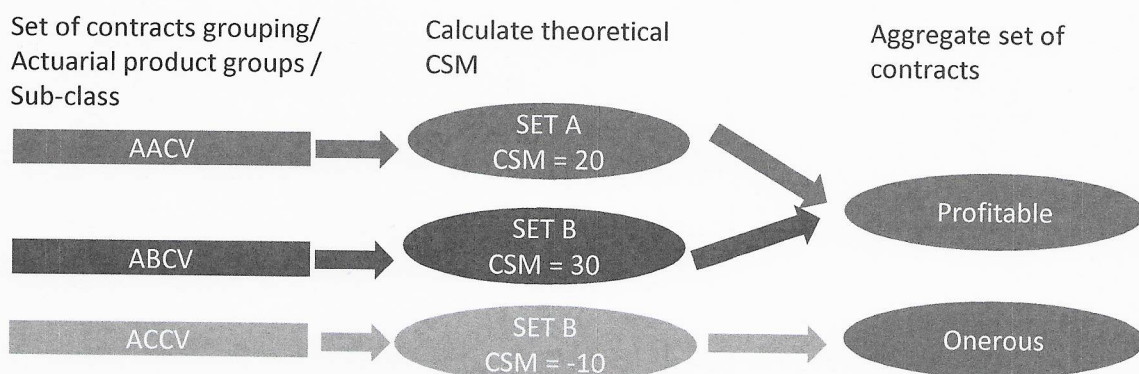
However, onerous contract test happens just before initial recognition, the theoretical CSM should be calculated for each insurance contract (otherwise set of insurance contracts) measured under GMM. This would require good computer memory power and storage capacity for proper tagging of profitability level of each new contract issued by the company.

In the same onerous contract test, if the sum of the previous elements result in a net outflow, then this amount will be considered as the loss component of the liability for remaining coverage, therefore the particular policy or set of insurance contracts is deemed onerous.

Cross subsidy between profitable and onerous contract is strictly not permissible under the GMM.

#### Examples of profitability buckets

Criteria could be distribution channels, segregated business with its own cost structure, etc. The choice of the buckets depends strongly on the local type of business and requires management judgement.



### 3.4 Consideration for Interim Reporting

#### Re-assessment of profitability buckets

The determination of groups of contracts is conducted at initial recognition and not adjusted for subsequent measurement until de-recognition. It is an accounting policy choice if initial recognition is accepted after the interim reporting.

For new cohorts entering the portfolio, the validity of the profitability buckets needs to be assessed regularly.

Profitability buckets are generally defined to provide a segmentation of portfolios that is stable over time. However, if reliable, sustainable and unquestionable insights emerge which are indicative of a systematic change of profitability drivers, a re-assessment of criteria for profitability buckets may be appropriate:

- *Reliable*: insights must result from a reliable source, e.g. information audited and reconciled in the usual governance process.
- *Sustainable*: insights must indicate a long-lasting, refined segmentation.
- *Unquestionable*: insights must point in the clear direction that a refinement of modelling buckets is necessary.

#### Annual Cohorts

As a matter of accounting choice, we can consider PTD or YTD accounting approach. The following is accounting estimates in YTD interim reporting:

- Locked-in interest rates: The difference between the annual cohort locked-in interest rates and the respective interim reporting locked-in interest rates is accounted for in P&L in the respective period (i.e., YTD basis).
- Unit of account: Labelling of the group of contracts is determined based on whether the first contract in the group is onerous or not. This labelling is retained, independently of whether contracts in the group are becoming profitable in subsequent reporting periods
- Current vs. prior period claims in P&C business: Consistent with current treatment, we assume a YTD view in determining whether claims are current or prior period.

#### GMM

- CSM release: the CSM release is determined on a YTD basis while all unlocking amounts are determined on an interim reporting period basis. This may result in the CSM release of the last interim reporting period as technical difference between the correct YTD CSM release and previous releases to become negative.
- The CSM release and RA release would allow for the risk supposedly recognized in the last interim report be updated on YTD basis.

#### PAA

- The insurance revenue recognized is determined on a YTD basis. This may allow pipeline results measured in the last interim reporting period be updated on YTD basis. This is relevant for accounting policy choice of selecting underwriting year as the method of cohorting instead of policy issuance year.



## 4.0 Illustrations

### 4.1 Portfolios

#### Examples for consideration by direct insurer:

A direct insurer could identify the following portfolios issued for IFRS 17 purpose:

| Example 1                                                          | Example 2                                                                                                                                                                                                        |
|--------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| In case RBC is appropriated, the following portfolios can be used. | Same as example 1, but further split between long term risks and short term risks. This is because some company may deem the long term risks to be significant to their business e.g. Fire, Engineering, Health. |
| 1. Auto. Compulsory (Automobile)                                   |                                                                                                                                                                                                                  |
| 2. Auto. Compulsory (motorcycle)                                   |                                                                                                                                                                                                                  |
| 3. Auto. Voluntary                                                 |                                                                                                                                                                                                                  |
| 4. Fire                                                            |                                                                                                                                                                                                                  |
| 5. Marine Cargo                                                    |                                                                                                                                                                                                                  |
| 6. Marine Hull                                                     | Significance is a judgement call by the management.                                                                                                                                                              |
| 7. Industrial All Risk                                             |                                                                                                                                                                                                                  |
| 8. Property                                                        |                                                                                                                                                                                                                  |
| 9. Public Liability                                                |                                                                                                                                                                                                                  |
| 10. Engineering                                                    |                                                                                                                                                                                                                  |
| 11. Aviation                                                       |                                                                                                                                                                                                                  |
| 12. Travel                                                         |                                                                                                                                                                                                                  |
| 13. PA & Health                                                    |                                                                                                                                                                                                                  |
| 14. Financial                                                      |                                                                                                                                                                                                                  |
| 15. Others                                                         |                                                                                                                                                                                                                  |

If the direct insurer assumes risks of any portfolio not issued by the company, the portfolio should be separately identified because the risks are obviously managed separately.

#### Example for consideration by reinsurer:

In contrast, a reinsurer could identify the following portfolios of reinsurance contracts issued for IFRS 17 purpose:

1. Facultative
2. Proportional treaty
3. Non-proportional treaty
4. Lloyd's participation

For facultative excess of loss, it could be deemed as facultative portfolio if it is scarce in the portfolio.

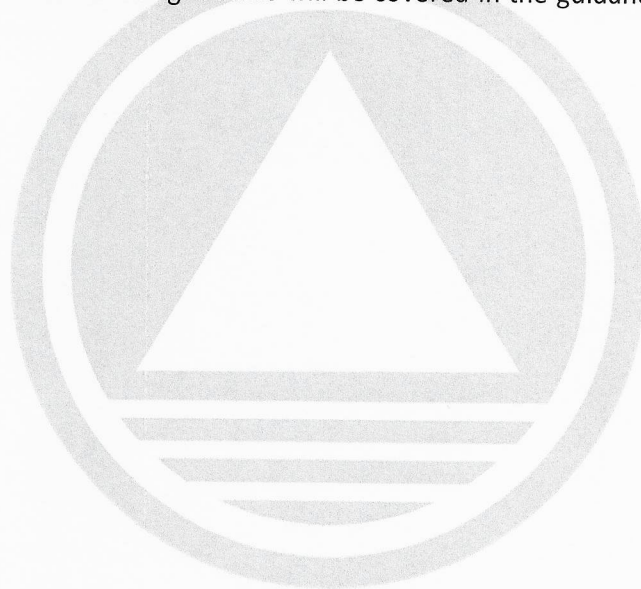
## 4.2 Groups

### Example for direct insurer:

The IFRS 17 grouping will differ among companies based on the respective companies' measurement model choices and profitability buckets.

For reinsurance contracts held that provide proportionate coverage, the lowest level of aggregation (group of reinsurance contracts) will be at the treaty/contract level. Entity is permitted (encourage but not compulsory) to further split for each underlying group of insurance contracts applying IFRS17.21, applicable to the proportional reinsurance contracts.

Essentially, the net gain or net cost will be unlocked separately for each set of reinsurance contracts. Operationally, it is more practical to model the set of reinsurance contract held that provides proportionate coverage cash flow separately for each insurance contract by treaty. This would allow more advance disclosures for future reporting. In some countries, related party transactions are disclosed separately, hence the counterparty behind the treaty is a critical data requirement to further split the treaty into participants level. In some circumstances, credit risk exposures for reinsurance contracts assets may require further disclosures by group of counterparties of similar credit rating. Details will be covered in the guidance note for reinsurance contract held.





## 5.0 Frequently Asked Questions

### 5.1 Level of Aggregation-Onerous Group

#### Background

For contracts accounted for under the PAA, an entity shall assume no contracts in the portfolio are onerous at initial recognition, unless “facts and circumstances” indicate otherwise.

An entity needs to assess facts and circumstances for existing portfolios and identify changes to facts and circumstances in subsequent years during the coverage period in order to identify whether there are indications for onerous contracts in the portfolio. This applies similarly for new business portfolios.

#### Question 1:

Determination of facts and circumstances is a qualitative assessment. Then if onerous contracts are identified from the qualitative assessment, entities are required to take a quantitative approach (OCT) to determine the loss component at initial recognition and subsequent measurement. If the OCT results in no loss component at initial recognition, should the grouping of the contracts be revised to other profitability bucket?

**View A:** Yes, re-visit the composition of the contracts.



**View B:** No, do not re-visit the composition of the contracts.

#### Explanation

##### *View A*

The situation is not impossible due to the difference between qualitative and quantitative approaches due to the simplification of facts and circumstances. In some circumstances, the variances in OCT are caused by coverage period and allocated acquisition cash flows to the group of insurance contracts.

Practically, re-visit the composition of the sets of contracts in a group is challenging and not viable. Therefore, an entity shall assess whether contracts that are not onerous at initial recognition have no significant possibility of becoming onerous subsequently by assessing the likelihood of changes in applicable facts and circumstances. The application of IFRS17.18 will greatly reduce the possibility of reclassifying onerous sets of contracts to profitable group of insurance contracts at initial recognition as we can certainly be more conservative in setting the metric for onerous group used in the qualitative assessment.

#### Question 2:

In determine the loss component of the onerous group, is it necessary to consider the discounting and risk adjustment in addition to the combined operating ratio?

**View A:** Discounting and risk adjustment are required in OCT.



**View B:** Discounting and risk adjustment are not required in OCT.

#### Explanation

##### *View A*

The methodology of the calculating fulfilment cash flows is the same as the general measurement model in terms.

For discounting, IFRS17.57b and IFRS17.59b provides practical expedient for company to calculate fulfilment cash flows on undiscounted basis for short term contract if claim is settled fast.

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**Question 3:**

Can the company set the IFRS17 group similar to the classes for the RBC reporting?

**Explanation**

Currently RBC reporting doesn't require the insurance contracts to be measured by underwriting year for the direct insurance contracts and reinsurance held. So this is the first noticeable difference between RBC statistical reporting and IFRS17.

Secondly, IFRS 17 requires "Facts and Circumstances" to be ascertained for evidence of onerous contracts within the cohort at the inception of the group. It is understood that loss ratio assumptions would be available without undue cost and efforts according to the classes of RBC, however it is also observed that acquisition expenses accounting policy choice and maintenance expenses ratio may be set at a broader level. Hence this would result further divergence views among the auditors on grouping of contracts based on a RBC class within any underwriting year. Companies are recommended to maintain the calculation at risk classes used in management reporting (which is more granular than RBC class) during the IFRS17 implementation phase.

**5.2 Level of Aggregation for Aggregation Cover****Background**

In aggregate cover, Minimum Deposit Premium (MDP) is usually the consideration paid by installment.

MDP form part of the total reinsurance ceded premium for the company. It refers to the minimum amount the insurer is prepared to pay to the reinsurer for the proportion of the risks shared to them. It is calculated based on the reasonable expectation of the low end of the turnover estimated (Gross Net Premium Income) on a specific period.

The MDP is recognised, reported by respective class on a monthly basis and paid on a quarterly basis. The recognition and posting are in lump sum (total amount) without issuance of individual treaty contract by the respective class.

**Question 1:**

What will be the view on the presentation in FS for aggregate cover with regard to IFRS17?

**View A:** Present the reinsurance results by the respective underlying portfolio (set of reinsurance contracts).

**View B:** Present the reinsurance results by the reinsurance portfolio. ☒

**Explanation*****View B***

The presentation of financial results is required by the reinsurance portfolio level as set out in IFRS17.78 and IFRS17.79.



**Question 2:**

How is the measurement, grouping and cohort to be reported?

**View A:** Group and measure the reinsurance contract by each contract. ☒

**View B:** Group and measure the set of reinsurance contract by more granular than the contract, split by underlying insurance portfolio.

**Explanation****View A**

The reinsurance contract is not unbundled given the substance is not a separate contract.

However, operationally the reporting entity can allocate the results by GNPI and/or measure the results at more granular level to meet the statutory reporting requirement in Thailand.

**Question 3:**

Profitability Group - Auto. Voluntary (Motorcar) in the entity is loss making, but other classes for Auto. are all profitable, which result in a profitable Auto. portfolio. In the case, do we need to separate the Auto. Comprehensive class as Onerous from the other profitable Auto. classes?

**View A:** Yes ☒

**View B:** No

**Explanation:**

Yes, you need to separate them.

In addition to that, the entity shall also assess whether contracts that are not onerous has no significant possibility of becoming onerous.

**Question 4:**

Travel - Pricing for Travel insurance is based on the region of countries, for example premium for Japan is cheaper than Africa's. If Africa is loss making, do we need to separate Africa as Onerous Contract?

**View A:** Yes

**View B:** No

**View C:** Depends ☒

**Explanation:**

If the entity does not split the risk in different risk classes by region, then it is doubtful that the company can draw conclusion that the Africa trip is onerous solely based on premium class info because other information such as claim, expense, commission and risk adjustment may be measured at risk class level instead of premium class.

Under PAA, company can use "facts and circumstances" to determine whether a contract is onerous or otherwise. Typically the facts are available at the risk class level instead of premium class level for travel insurance due to its messy nature of premium register

**Question 5:**

Health - Health price will be readjusted year by year usually. For example, if it is a loss-making year, the insurance company will increase the price in the renewal year, while if it is a profitable year, the insurance company will give a discount on the premium. In this case, how do we justify if this is an Onerous contract or not?

**View A:** Yes

**View B:** No

**View C:** Depends

**Explanation:**

It depends, judgement is permitted.

Assume that the health insurance is eligible for measurement under PAA, company can use “facts and circumstances” to determine whether a contract is onerous or otherwise, at the risk class level, for each renewal year. In short, judgement call has to be made early of the underwriting year (cohort).

Assume that the health insurance is not eligible for measurement under PAA, instead of qualitative method, company must assess quantitatively at the contract/sets of contract to determine whether a contract is onerous or otherwise. In short, judgement call has to be made as early as the recognition of the policy.

**Question 6:**

Health insurance, similar to travel insurance, premium pricing is different by the health insurance industry. In this case, if some industry is loss making, do we need to separate it to Onerous Contract group?

**View A:** Yes

**View B:** No

**View C:** Depends

**Explanation:**

It depends, judgement is permitted.

If the entity does not split the risk in different risk classes by industry, then it is doubtful that the company are able to analyze the onerousity solely based on premium class info because other information such as claim, expense, commission and risk adjustment may be measured at risk class level instead of premium class.

Analysis of onerousity should be determined at the risk class level.

**End of document**