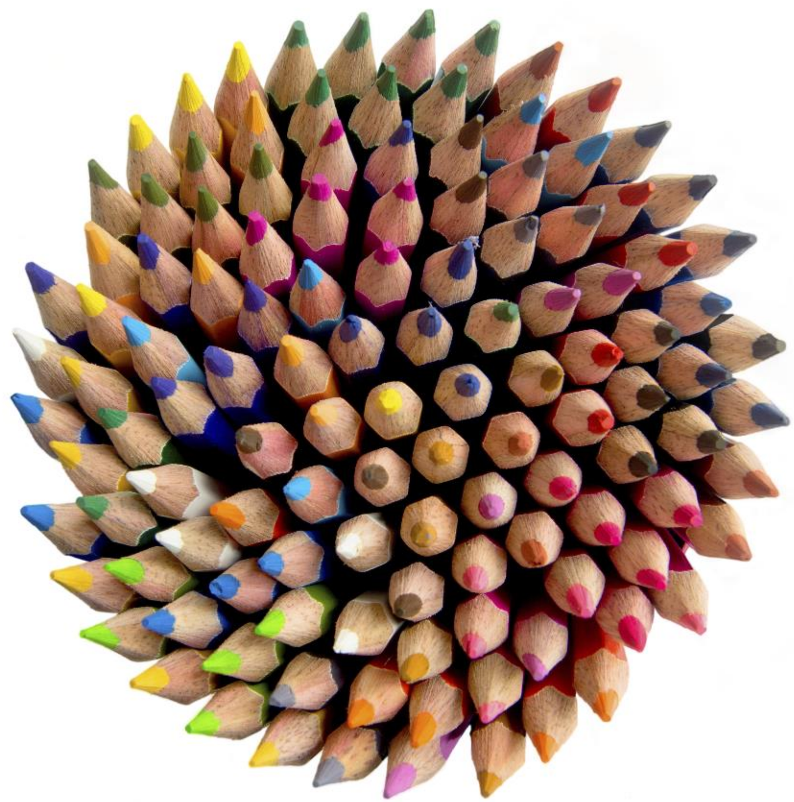

Hong Kong Insurance Implementation Support Group

Brief on IASB TRG papers for 2 May meeting

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Agenda

Summary of the TRG 2 May papers

1. AP01 – Combination of Insurance Contracts

When is it necessary to treat a set or series of insurance contracts as a whole? (para 9)?

Potential factors of a set or series of insurance contracts that are in substance a single contract:

01 the contracts are priced as a single risk

02 the lapse of one contract changes the rights and obligations of the other contract(s); and

03 measuring the contracts separately would result in one/some of the contract(s) being onerous whereas when measured as a whole the contract is profitable.

Staff views

- Interdependency of risks is a factor for consideration; i.e. if one risk offset another it could lead to combination of contracts. For example longevity and mortality risk are interdependent.
- When the lapse or maturity of one contract causes the lapse or maturity of another contract; there is a strong indication that the contracts achieve an overall commercial effect; i.e. need to be combined. **The existence of a discount does not in itself achieves an overall commercial effect.**

No single factor is determinative in applying this assessment, significant judgement and careful consideration of all relevant facts and circumstances are required.

2. AP02 – Risk adjustment in a group of entities

At which level is the risk adjustment (RA) for non-financial risk required to be determined?

Staff view

Individual financial statements

- Risk diversification at the group level may be taken into account, only if the entity has taken this into account when determining the compensation required for bearing non-financial risk related to insurance contracts issued by the entity.

Consolidated financial statements

- **The RA at the consolidated level is the same as the RA at the individual entity level.**
- The determination of the risk adjustment is a single decision that is made by the entity which chooses the factors to consider; for example the degree to which diversification benefits at the group level are included.

3. AP05 - Coverage units (1/2)

What is the quantity of benefits?

Coverage units (CU) reflect the likelihood of insured events occurring if they affect the:

1	**Expected duration of the contracts in the group**
2	**Expected claim amount in the period**
3	**Variability across period in the level of cover?**

Staff view

General observations

- Sources of profit are more than the CSM release. They also include RA release and experience adjustments
- The insurance risk period is not necessarily equal to the insurance coverage period
- The CU's for a group of contracts is based on the sum of the benefits and expected coverage duration for each contract
- Lapse assumptions are included in the CU determination because they affect the expected coverage duration
- CSM allocation to P&L is to reflect services in the period

Contracts without investment components

- Because the CSM allocation to P&L revenue is to reflect services in the period; **different levels of service across periods should be reflected**
- The quantity of benefits depends on the amount that can be claimed by the policyholder (not the entity's expectation).

Possible approaches could uses the following basis:

- Maximum contractual cover
- Entity's expectation of the policyholder's valid claim in each period if an insured event occur

Approaches considered inappropriate would be based on:

- The entity's performance of its assets
- Premiums; unless they are a reasonable proxy
- Expected cash flows; unless they are a reasonable proxy

3. AP05 - Coverage units (2/2)
What is the quantity of benefits?

Staff view (cont')

Contracts with investment components

VFA contracts
BC 280 only refers to the coverage period as the insurance services are provided

- Both insurance and investment related services are provided; hence the quantity of benefits + expected coverage duration should refer to both
- **A narrow amendment to IFRS 17 is proposed** to modify the definition of coverage period of VFA contracts such that **the coverage period includes investment-related services.**

General model (indirect par.) contracts
- **The coverage unit only refers to insurance services, and not to investment services**
- The amounts promised to policyholders other then insurance benefits, are a form of financial instrument and not related to service

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