

STAFF PAPER

January 2016

IASB Meeting

Project	Insurance Contracts		
Paper topic	Level of aggregation - addendum		
CONTACT(S)	Anne McGeachin	amcgeachin@ifrs.org	+44 (0)20 7246 6486
	Andrea Pryde	apryde@ifrs.org	+44 (0)20 7246 6491

This paper has been prepared for discussion at a public meeting of the International Accounting Standards Board (the "Board") and does not represent the views of the Board or any individual member of the Board. Comments on the application of IFRS Standards do not purport to set out acceptable or unacceptable application of IFRS Standards. Technical decisions are made in public and reported in IASB Update.

Purpose of this paper

1. This paper:
 - (a) summarises the key discussion points on the level of aggregation for the allocation of the contractual service margin at the Board's meeting on 19 January 2016, and
 - (b) provides a revised staff recommendation.

Key discussion points***What is the objective for allocation?***

2. When insurance contracts in a group have different expected durations, then it is expected that the coverage period for some contracts will end earlier than the average coverage period for the group and the coverage period of other contracts will end later than the average coverage period for the group.
3. For those contracts for which the coverage period ends earlier than the average coverage period for the group, paragraph 24 of agenda paper 2A observes:

- (a) Measuring the contracts on an individual basis would mean that the contractual service margin associated with those contracts would be fully recognised in profit or loss over the shorter period up to the point when the coverage period ends.
 - (b) Measuring the contracts on a group basis would not necessarily mean that the contractual service margin associated with those contracts would be recognised in profit or loss when the coverage period ends.
4. The Board discussed whether the objective was to allocate the contractual service margin on an individual contract basis.
5. The staff proposes to be clear that the objective is to allocate the contractual service margin on an individual contract basis, whilst acknowledging that the objective could be satisfied when contracts are grouped (see paragraphs 6 and 7).

Permitting groupings

6. The Board discussed whether an entity could achieve the objective described in paragraph 3(a) by considering groups of contracts. In particular, the Board discussed:
- (a) whether specifying only the objective would force entities to apply an individual contract basis for allocation;
 - (b) whether it should provide explicit guidance that would permit entities to group contracts for the purpose of allocation, provided that appropriate boundaries were set; and
 - (c) the need for an entity to use more sophisticated (eg weighted) allocation techniques to ensure the objective is met if it considers groups of contracts.
7. The staff proposes to state explicitly that an entity is permitted to group contracts for the allocation of the contractual service margin and to specify boundaries for the permitted groupings.

Role of expected duration and lapses

8. The Board discussed whether an entity would need to consider the effect of different duration and lapse times when grouping contracts to ensure that the objective is met.
9. In the staff's view, the objective of allocating the contractual service margin to profit and loss over the coverage period of the contract in a way that best reflects the remaining transfer of services provided by the insurance contract implies that there should be no remaining contractual service margin recognised in the balance sheet when the related contracts have no more coverage to provide. Accordingly, the staff proposes to specify that an entity should consider the effect of expected duration and lapses.

Single level of aggregation

10. The Board discussed the desirability of applying a single level of aggregation for both determining onerous contracts and the allocation of the contractual service margin.
11. However, the staff notes that the objective for allocating the contractual service margin is different from that for determining onerous contracts and so the same level of aggregation may not be appropriate. Nonetheless, as the Board noted, an entity could apply the same grouping used for onerous contracts provided that it applied more sophisticated allocation methods that reflected the expected duration and size of contracts.

Staff recommendation

12. The staff recommends:

- (a) The objective for the allocation of the contractual service margin is to recognise the contractual service margin for an individual contract in profit and loss over the coverage period of the contract in a way that best reflects the service to be provided by the contract. Hence, if there is no more service to be provided by a contract after the end of the reporting period, the contractual service margin for that contract should have been fully recognised in profit or loss.
- (b) An entity can group contracts for allocating the contractual service margin provided that the allocation of the contractual service margin for the group meets the objective in (a).
- (c) An entity that groups contracts is deemed to meet the objective in (a) provided that:
 - (i) the contracts in the group:
 1. have cash flows that the entity expects will respond in similar ways to key drivers of risk in terms of amount and timing; and
 2. on inception had similar expected profitability (ie similar contractual service margin as a percentage of the premium); and
 - (ii) the entity adjusts the allocation of the contractual service margin for the group in the period to reflect the expected duration and size of the contracts remaining after the end of the period.