



APPLICATION OF IFRS 17 INSURANCE CONTRACTS ON CENTRAL GOVERNMENT

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ICAEW welcomes the opportunity to respond to HM Treasury's consultation on the application of IFRS 17 Insurance Contracts across central government published on 5 January 2023, a copy of which is available from this [link](#).

ICAEW agrees with the proposals in HM Treasury's Exposure Draft on IFRS 17 Insurance Contracts that clarify how IFRS 17 should be implemented by government entities and that seek to simplify the transition to and application of IFRS 17.

We believe the proposed approach reduces the burden on preparers to adopt and apply IFRS 17 whilst still maintaining high-quality financial reporting within the public sector. We welcome:

- The clarification that laws and regulations do not in themselves constitute contracts within the meaning of IFRS 17.
- The restriction of accounting choices provided by IFRS 17 to provide a consistent approach across central government.
- The full application of IFRS 17 in the small number of government entities that provide insurance as part of their normal course of operation.
- Other proposals that reduce burdens on other government entities with transactions that could fall within the scope of IFRS 17.

We broadly agree with the questions asked in the consultation, with the following exceptions:

- We recommend remote contingent liabilities be reported as the difference between the maximum exposure and the amount recorded in the balance sheet under IFRS 17.
- We agree that a practical expedient may be appropriate in calculating fair values on transition where applying the retrospective method is not possible. However, this should distinguish between onerous contracts using a fulfilment cash flow basis, and insurance contracts entered into on a commercial basis (or priced off a commercial basis) where we believe fair value calculated under IFRS 13 is more appropriate.

Adopting this standard provides an opportunity to review and improve how risks are managed within government and we recommend that insurance contracts form part of UKGI contingent liabilities team's remit.

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As a regulator of the accountancy and audit profession, ICAEW is currently the largest Recognised Supervisory Body (RSB) for local audit in England. We have ten firms and over 85 Key Audit Partners registered under the Local Audit and Accountability Act 2014.

This response has been prepared by ICAEW's Public Sector team in consultation with ICAEW's Public Sector Advisory Group. ICAEW's Public Sector team supports members working in and with the public sector to deliver public priorities and sustainable public finances, including over 10,500 in ICAEW's Public Sector Community. ICAEW engages with policy makers, public servants, and others to promote the need for effective financial management, audit and assurance, financial reporting and governance and ethics across the public sector to ensure public money is spent wisely.

For questions on this response please contact our Public Sector team at representations@icaew.com quoting REP 16/23.

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KEY POINTS

We welcome HM Treasury's guidance on IFRS 17 Insurance Contracts

1. IFRS 17 seeks to ensure that insurance contracts are accounted for consistently and in line with the objectives set out in the International Accounting Standards Board's Conceptual Framework. The standard principally affects the insurance industry, where accounting for the complex commercial arrangements inherent in insurance contracts can be challenging.
2. We concur with HM Treasury that by applying a consistent methodology for recognising, measuring, and disclosing the financial impact of insurance contracts, IFRS 17 will enable users of central government financial statements to better understand how public money has been committed to cover insurance risks by government entities issuing insurance contracts.
3. We anticipate that many users of the standard will not be insurance experts and we therefore commend HM Treasury for what we found to be a clear, concise, and easy to follow exposure draft.

Simplification and consistency are key

4. We share HM Treasury's view that a consistent approach across central government will aid comparability and understandability. We therefore welcome the proposals in the exposure draft to restrict accounting choices so that differing approaches are not adopted by central government entities.
5. Applying this standard by entities who have contracts that might fall in scope but whose primary activity is not insurance related will be challenging given the technical expertise required to apply the requirements of IFRS 17. We therefore concur with opting to apply other standards where this is permitted in order to make application of the standard simpler.
6. We welcome the stress placed in the guidance on the importance of materiality in preparing financial statements and ensuring that disclosures do not contain excessive detail on immaterial items that obscures rather than enhances understanding. It is also important that preparers avoid the use of 'boilerplate' disclosures and instead provide useful information relevant to their particular circumstances.

Fair Value approach on transition

7. Upon transitioning to IFRS 17, we recommend that those insurance contracts entered on a commercial basis are either adopted using the full retrospective approach or, if that is not practical, the fair value approach based on IFRS 13.
8. For those contracts not entered on a commercial basis, we support the alternative adaptation to measure all insurance liabilities at fulfilment cash flows. See responses to questions 14 and 15 for more detail.

Benefits of IFRS 17

9. Managing risk is essential to how public bodies operate and implementing IFRS 17 will strengthen accountability by ensuring insurance risks are accounted for and reported consistently and transparently across central government. This will complement existing accounting requirements on how financial risks and exposures are accounted for and reported.
10. IFRS 17 will help Parliament and other stakeholders to better understand the extent to which government is being compensated for the insurance risks that it assumes. This is particularly important to being able to understand whether public money is being used wisely, especially in circumstances where insurance is provided for no cost or at below market rates for public policy reasons.

11. We believe the adoption of IFRS 17 provides a good opportunity for public bodies to evaluate the insurance risks to which they are exposed and whether they are being used effectively to deliver on objectives. Better disclosure should provide Parliament and the public with sufficient detail to evaluate the financial exposures to which central government entities are exposed and whether they represent value for money.

ANSWERS TO SPECIFIC QUESTIONS

Question 1: Do you agree with the interpretation for the definition of a contract? If so, why? If not, why not and what alternatives do you propose? [Section E.2]

12. We agree that IFRS 17 should only apply in instances where a contract exists as defined in the standard. It should not be expanded to include non-binding arrangements between two public sector entities or to cover binding arrangements that are enforceable by non-legal means (see paragraph 15 below).
13. We also concur with HM Treasury's view that legislation and regulation, in isolation, are not equivalent to insurance contracts. This clarification is important in ensuring that public bodies providing public services in compliance with relevant laws and regulation are not inadvertently caught by accounting requirements intended to apply to commercial insurance arrangements, even where there may be 'equivalent means' (whether or not analogous to contract law) by which arrangements can be or are enforced.
14. The fundamental difference between the definition of a contract in IFRS 17 and the definition of binding arrangements more broadly is that contracts are enforceable only between the parties to that contract. This contrasts with binding arrangements enforceable by equivalent means, so both within and outside the legal system. Compliance through equivalent means includes laws and regulations, including legislation, executive authority, cabinet decisions, ministerial directives, ombuds or regulator decisions, or judicial review.
15. Our experience of International Public Sector Accounting Standards (IPSAS) applied outside the UK suggests that it is important for public sector accounting frameworks to provide clear guidance on whether to analyse transactions into binding and non-binding elements. We therefore agree with the proposals to limit the scope of when transactions fall within IFRS 17 to those where a contract is in place.
16. The proposed guidance of when agreements are contracts and when not (section E.2) should clarify that only transactions that are enforceable by law are within scope. This should avoid risk sharing between government entities that does not take the form of an enforceable contract being accidentally captured by IFRS 17.

Question 2: Do you agree with the requirement to disclose and include insurance liabilities in both the remote contingent liabilities note and the financial statements - where the insurance liabilities meet the definition of both a remote contingent liability and insurance contract under IFRS 17- is the right approach to maintain high quality parliamentary reporting?

If so, why? If not, why not and what alternatives do you propose? [Section E.4]

17. Yes, we agree that including insurance liabilities in both the remote contingent liabilities note and the financial statements is the right approach if the criteria are met, even if this means there is some duplication.
18. It is important that Parliament is apprised of remote contingent liabilities that could impact the public finances, especially where the maximum exposure is higher than the probability weighted value recorded in the balance sheet. Both values provide decision useful information and transparency on the risk to which the government is exposed.

19. However, a financial exposure that is recorded as a liability in the balance sheet is by (accounting definition) not 'remote', and we suggest that the remote contingent liability would more appropriately be measured at an amount equal to the difference between the maximum exposure and the amount recorded in the balance sheet as an insurance risk liability. Arguably this would provide Parliament with a better understanding of the financial exposures facing the public finances by avoiding double counting between balance sheet liabilities and remote contingent liabilities, provided there are appropriate disclosures to enable readers to understand that the maximum exposure is the combination of two numbers.

Question 3: Does the proposed wording explaining the difference between the value of insurance liabilities included in the remote contingent liabilities note and in the financial statements provide sufficient clarity on the difference between these values?

If so, why? If not, why not and what alternatives do you propose? [Section E.4]

20. If your proposed approach is followed then we believe the proposed wording is reasonable, assuming preparers have already provided the disclosures required under IFRS 17 describing the underlying contract, why the government is providing insurance cover and the principal risks. It is important that users of the financial statements are provided with a clear explanation of the specific risks relating to insurance contracts rather than just a technical explanation of the accounting standards.
21. If our suggestion for a different approach (see paragraph 19 above) were to be adopted, consequential amendments would be needed to the proposed wording, perhaps along the lines of:

"The following remote contingent liabilities arise from insurance contracts accounted for under IFRS 17 represent the difference between the maximum exposure under these contracts and the amounts recorded as insurance contract liabilities (see note X): [provide a list of the liabilities, with maximum exposure (A), insurance contract liability recorded under IFRS 17 (B), and remote contingent liability reported to Parliament (A-B)].

The value of insurance contract liabilities recorded in the statement of financial position is measured under the requirements of IFRS 17 as adapted and interpreted by the FReM, which takes the probability weighted value of the cash flows, adds an adjustment for risk and can include any un-earned profit on the contract. This is different to amounts reported as remote contingent liabilities, which represent the extent to which the maximum financial exposure under the contracts concerned exceed insurance contract liabilities recorded in the statement of financial position."

Question 4: Do you agree with the interpretation for contracts meeting the criteria set out in IFRS 17 paragraph 8 to be accounted for under IFRS 15?

If so, why? If not, why not and what alternatives do you propose? [Section E.6]

22. Yes, we concur with eliminating the accounting choice provided by IFRS 17.8 that enables fixed fee service contracts to be accounted for under either IFRS 15 or IFRS 17 in order to ensure a consistent approach is adopted across central government in how these types of contracts are accounted for.
23. We believe IFRS 15 provides an appropriate method of accounting in the context of the public sector for fixed fee services even where there are insurance risks inherent in such arrangements, provided that those risks are appropriately described in the IFRS 15 disclosures.

Question 5: Do you agree with the interpretation to account for all financial guarantee contracts under IAS 32, IFRS 7 and IFRS 9?

If so, why? If not, why not and what alternatives do you propose? [Section E.7]

24. Yes, we agree with the proposal that financial guarantee contracts be accounted for as financial instruments under IAS 32, IFRS 7 and IFRS 9 rather than as insurance contracts under IFRS 17. Eliminating the accounting choice in IFRS 17 will ensure a consistent approach is adopted across central government and better enable the consolidated risk position relating to such contracts to be understood than if differing approaches were permitted.
25. Financial guarantees have grown in significance since COVID and are in many instances material, so it is important that there is a common approach adopted within central government in how they are accounted for. This should enable better reporting of exposures relating to financial guarantees in the Whole of Government Accounts (WGA).

Question 6: Do you agree with the adaptation to include a rebuttable assumption that the financial instrument discount rate (as stated in PES papers) is to be used to discount IFRS 17 liabilities?

If so, why? If not, why not and what alternatives do you propose? [Section F.2.3]

26. Yes, we support the adaptation to include a rebuttable assumption that the financial instrument discount rate (as stated in PES papers) should be used to discount IFRS 17 liabilities.
27. This approach should aid comparability across central government, as well as reflecting the position of government entities in being financed collectively through taxation and borrowing by HM Treasury. It will also ease implementation on the part of individual preparers, avoiding a need to calculate specific discount rates unless there is a clear reason to do so, such as where there is a portfolio of matching assets used to fund the payment of insurance claims.
28. We concur that there is a clear reason to divert from the use of a central discount rate in the case of regulated insurers or entities whose principal business activity is insurance or reinsurance.
29. While we don't believe the use of a central discount rate for other insurance contracts would materially distort the financial information provided to Parliament, it is important that readers of financial statements are able to understand the effect of discount rate choice on the values recorded, particularly on longer term contracts where discounting has a much greater impact. Movements in discount rates are often a significant contributor to changes in balance sheet liabilities within both individual accounts and the WGA from one year to the next, while at the same time being generally not well understood by users of public sector accounts. Preparers should provide comprehensible disclosures around the effect of the choice of discount rates in calculating significant estimates in the financial statements.

Question 7: Do you agree with the adaptation to withdraw the requirement to disclose the confidence level used to determine the risk adjustment for non-financial risk?

If so, why? If not, why not? [Section F.2.4]

30. Yes, we support adapting IFRS 17 within central government to withdraw the requirement to disclose the confidence level used to determine the risk adjustment for non-financial risk for reasons outlined in the ED.

31. We consider that this requirement is not essential in the context of central government, where the primary user of financial statements is Parliament, in contrast with the private sector where this is a more important disclosure of interest to investors.
32. Withdrawing the requirement should not prevent those entities that have calculated confidence levels from disclosing them if that is helpful to readers, however, it should reduce the burden placed on other central government entities applying IFRS 17.

Question 8: Do you agree with the interpretation to mandate accounting for insurance finance income and expenses for the period in the SoCNE?

If so, why? If not, why not? [Section F.2.7]

33. Yes, we agree that it is appropriate for central government entities to adopt a common approach in how income and expenses are recorded in the financial statements.
34. A common approach will provide consistency between government entities and with the WGA. While there might be arguments for a different approach in some entities given their individual circumstances, we believe the recording of insurance finance income and expenses for the period in the SoCNE is most appropriate, given that providing insurance is not a core activity for central government overall.

Question 9: Are there any disclosure requirements which you believe are not applicable to central government?

If so, why? If not, why not and what alternatives do you propose? [Section F.3]

35. No, we concur with HM Treasury's view that users of central government financial statements should be able to see how public money has been committed to cover insurance risks by government entities issuing insurance contracts. Providing the disclosures required by IFRS 17 should achieve this aim.
36. As with other areas of accounting, it is important that preparers assess the materiality of transactions and balances to ensure that disclosures are proportionate and comprehensible. It is important that government entities appropriately apply the requirement of IFRS 17 to account for insurance contracts on a group or portfolio basis and to provide a balanced analysis of risks relation to such contracts. There needs to be a focus on quality rather than quantity in the notes to financial statements, avoiding excessive disclosures around contracts or contract groups that are not material.

Question 10: Do you agree with the decision to keep the accounting policy choice of either using the PAA or GMM where the criteria to use the PAA are met?

If so, why? If not, why not? [Section F.4]

37. We agree that it can be appropriate to adopt the general measurement model even where the criteria to apply the premium allocation approach are met, for example to be consistent with the approach adopted for other insurance contracts or insurance contract groups within the same or related entities. We therefore concur with the proposal to permit entities to choose the method they consider most appropriate to their circumstances and each group of insurance contracts.

Question 11: For each of the accounting policy choices listed in the table in section F.5, do you agree with the decision of whether to mandate an approach or not?

If so, why? If not, why not? [Section F.5]

Question 12:

For each of the accounting policy choices mandated in the table in section F.5, do you agree with the choice mandated?

If so, why? If not, why not?

[Section F.5]

38. We concur with your proposed approach to limit many of the accounting policy choices available in IFRS 17 to ensure a consistent approach across central government.
39. With respect to the individual items listed in the table, we have no specific comments to add to those contained elsewhere in this response.

Question 13: Do you agree with the proposed date of initial application and transition dates for the central government implementation of IFRS 17?

If so, why? If not, why not and what alternatives do you propose? [Section G.1]

40. Yes, we believe the proposed initial application date of 1 April 2025 and transition date of 1 April 2024 are reasonable. This timetable should provide preparers with sufficient time to implement the standard in their financial statements for the year ending 31 March 2026.
41. This timeline should also enable preparers to benefit from the experience of private sector entities in their 2023 and 2024 disclosures, given that IFRS 17 is effective for their financial statements for annual reporting periods beginning on or after 1 January 2023.
42. The need to apply the requirements of IFRS 17 retrospectively and to include comparative information for the year commencing 1 April 2024 means that preparers should ideally start preparing for implementation this year. It is therefore important that the application date is confirmed as soon as possible.
43. Although outside the scope of this consultation, we believe that if possible IFRS 17 should be adopted by local government entities on the same timeline as proposed here. This is important to the preparation of the Whole of Government Accounts, while also ensuring that local authorities are providing high quality financial statements in line with best practice. However, it is important that any delays in local government adoption are not allowed to delay implementation by central government.

Question 14: Do you agree with the interpretation to mandate transitioning to IFRS 17 using the full retrospective approach where practicable, and then using the fair value approach if full retrospective restatement is impracticable?

If so, why? If not, why not and what alternatives do you propose? [Section G.2]

44. Yes, we agree with a consistent approach to implementing IFRS 17 across central government. Removal of the modified retrospective approach as an option to transition to this standard is therefore appropriate.
45. However, we also agree that there may be circumstances where sufficient information is not available to enable the full retrospective approach to be adopted by all government entities or with respect to specific contracts or contract groups.
46. In these instances, we concur with mandating the use of a single standard method to ensure there is a consistent approach across central government in how these circumstances are dealt with. This could be the fair value method or, as discussed in our response to questions 15 and 16 below, an alternative approach to calculating the deemed value at transition such as that proposed in G.3.9.

47. We agree with your comment in G.3.3 that applying fair value requirements to insurance contracts is likely to be complex and require the exercise of significant professional judgment. This is particularly the case in a public sector context where, for example, there may be no active market for some of the insurance contracts entered into, no premiums, or premiums not calculated on a commercial basis, or where market participants outside of government would not be willing to accept the level of risk concerned.
48. There may therefore be a need for specific support from the Government Actuarial Service to support entities in implementing IFRS 17, firstly to ensure that wherever possible the retrospective approach is adopted, and secondly to assist in calculating fair values when it is not.
49. The consultation highlights potential scenarios where the fair value calculated for an insurance contract calculated in accordance with IFRS 13 exceeds fulfilment cash flows by a significant amount, resulting in an 'excessive' contract service margin. We agree that there is a need for specific guidance and potentially an adaptation in such circumstances, as discussed in our responses to question 15 and 16 below.

Question 15:

Do you agree with the adaptation to measure the Contractual Service Margin (CSM) at £nil and the insurance liability at fulfilment cash flows where the liability calculated under IFRS 13 would result in an excessive premium?

If so, why? If not, why not and what alternatives do you propose? [Section G.3]

50. No, we do not support this adaptation. While it would simplify implementation it would involve an arbitrary assessment on what is meant by an 'excessive' CSM that we don't consider is appropriate.
51. It would also result in a perverse situation where the liabilities for insurance contracts or contract groups deemed to be 'non-excessive' would be recorded at higher amounts than more onerous equivalents where the CSM is decided arbitrarily to be 'excessive'.
52. As the consultation highlights, many of the contracts to which this adaptation would apply relate to onerous contracts where equivalent insurance is not available in the market and/or where premiums are not charged on a commercial basis.
53. We therefore suggest an approach that distinguishes between insurance contracts entered into on a commercial basis at inception (or priced off a commercial basis, for example where premiums are subsidised for public policy reasons), and onerous insurance contracts at inception where there is no intention to generate income or where the income that is generated was never intended to cover the risks being assumed.
54. In the former case, we believe fair value in accordance with IFRS 13 would be the appropriate basis to use on transition to IFRS 17 in circumstances where applying the retrospective method is not possible.
55. In the latter case, we would agree with a practical expedient to measure the insurance liabilities equal to the fulfilment cash flows necessary to meet the onerous obligation represented by the insurance contract or contract groups concerned.

Question 16: Do you agree with the rationale for the potential practical expedient to measure the insurance contract liability at fulfilment cashflows when using the fair value transition approach?

If so, why? If not, what are the reasons for this? [Section G.3]

56. Yes, with the proviso that it should not apply to insurance contracts or contract groups entered into on a commercial basis (or priced off a commercial basis), where we consider that fair value under IFRS 13 is the most appropriate basis for calculating the deemed value on transition to IFRS 17.

Question 17: If you agree with the rationale and inclusion of the practical expedient, should it be mandated or be included as an optional practical expedient? What are the reasons for your choice? [Section G.3]

57. If the practical expedient is adopted, we would recommend mandating its use, depending on the nature of the insurance contracts or contract groups concerned, as described in our response to question 16 above.
58. Such an approach would provide greater consistency across central government. Otherwise, there is a risk of significantly different valuations for similar insurance contracts or contract groups depending on the choices made by individual entities.

Question 18: Do you agree with the interpretation to mandate the transition reliefs stated in section G.4? If so, why? If not, why not? [Section G.4]

59. Yes, we agree on consistency grounds.

Question 19: Do you have any comments on the impacts IFRS 17 will have on consolidation (either at the individual reporting entity level or Whole of Government Accounts level)?

Please explain any comments, including providing alternatives HM Treasury should consider. [Section H]

60. One key component of good Public Finance Management (PFM) is risk management. WGA are the best place to bring together the risks the government is exposed to and to describe how those risks are being managed since it aggregates all material balances from across the public sector into one set of financial statements.
61. The adoption of IFRS 17 provides an opportunity to improve the reporting of risk both at the individual entity level and in the WGA. This will complement disclosures on other risks required by other accounting standards and should enhance the commentary on risk in narrative reports.
62. In addition, disclosing either the CSM or loss element of insurance contracts together with the purpose of issuing insurance contracts will provide Parliament and other readers with a better understanding of the costs and benefits of insurance provided by government.
63. Managing insurance alongside contingent liability risk will form an important overall risk management role. Contingent liabilities are currently overseen by a dedicated team within UKGI, we would recommend to either expand their remit to include insurance contracts. There is a role for the Government Actuarial Service to play in supporting central government entities in managing risks relating to insurance contracts and the premiums being charged for those risks as well in calculating insurance contract values.
64. The full external exposure will need to be disclosed on a consolidated basis in the WGA. Care will need to be given to those circumstances where one public sector entity has provided insurance to an external client but has used another public sector entity to spread the risk (re-insurance). Individual entity accounts, group accounts and WGA could all look different depending on whether the re-insurance is provided by an entity that is outside the original entity's accounting boundary or not.

Question 20: Do you agree with the proposed budgetary regime for insurance contracts within the scope of IFRS 17?

If so, why? If not, why not and what alternatives do you propose?

[N.b. where entities already have an agreed budgeting approach for their groups of insurance contracts it will be assumed that this will continue; the budgeting approach described in this Exposure Draft will apply to all other insurance contracts and new insurance contracts issued]. [Section I]

65. We have no further comments to add to those contained elsewhere in this consultation response.

Question 21: Are there any other areas not covered by the questions which you would like to comment on? Please explain any comments, including providing alternatives HM Treasury should consider.

66. We have no further comments to add to those provided elsewhere in this consultation response.