IFRS 17 affects more than just insurance companies

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IFRS 17 for non-insurers

At a glance

The existing requirements for insurance contracts (IFRS 4) allow flexibility to follow the measurement principles of other standards. The replacement accounting standard for insurance contracts, IFRS 17, is more prescriptive, and so it is critical to identify insurance contracts, to determine whether they are within the scope of IFRS 17 and, if so, to determine the accounting implications.

This publication considers examples of common contracts that might be within the scope of IFRS 17.

1. Introduction

IFRS 17, 'Insurance Contracts', applies to insurance contracts, regardless of the entity that issues them. It applies more widely than contracts issued by traditional insurance entities. IFRS 17 defines an insurance contract based on whether the contract transfers significant insurance risk. Although the definition of an insurance contract is similar to IFRS 4, the accounting consequences of IFRS 17 are very different from IFRS 4. In particular, while under IFRS 4 many entities were able to 'unbundle' the insurance elements of contracts and apply the measurement principles in other standards, IFRS 17 applies to the whole contract (with limited exceptions) and has detailed measurement requirements.

This publication reflects the June 2020 amendments to IFRS 17. The amended IFRS 17 is mandatory for annual reporting periods beginning on or after 1 January 2023, with restatement of comparatives for the previous reporting period (that is, from 1 January 2022 for calendar year-ends).

PwC Observation: Implementing IFRS 17 can be challenging and might require significant time and resources

Although IFRS 17 is not yet mandatory, identifying which contracts are within the scope of IFRS 17 now allows sufficient time to work through the implementation.

Where IFRS 17 applies, an entity might have to:

- identify portfolios of insurance contacts, and then disaggregate each portfolio into groups;
- decide which measurement approach to apply - the general model, premium allocation approach or variable fee approach;
- apply the relevant measurement approach(es), which will include determining the cash flows expected to be received, the cash flows expected to be paid, risk adjustments and, in many cases, discounting;
- update the calculations each reporting period to reflect updated information (including the expected cash flows, risk adjustments and, if relevant, discounting);
- give the disclosures required by IFRS 17; and
- assess whether new systems, processes and controls are required to accurately perform these calculations and give the necessary disclosures.

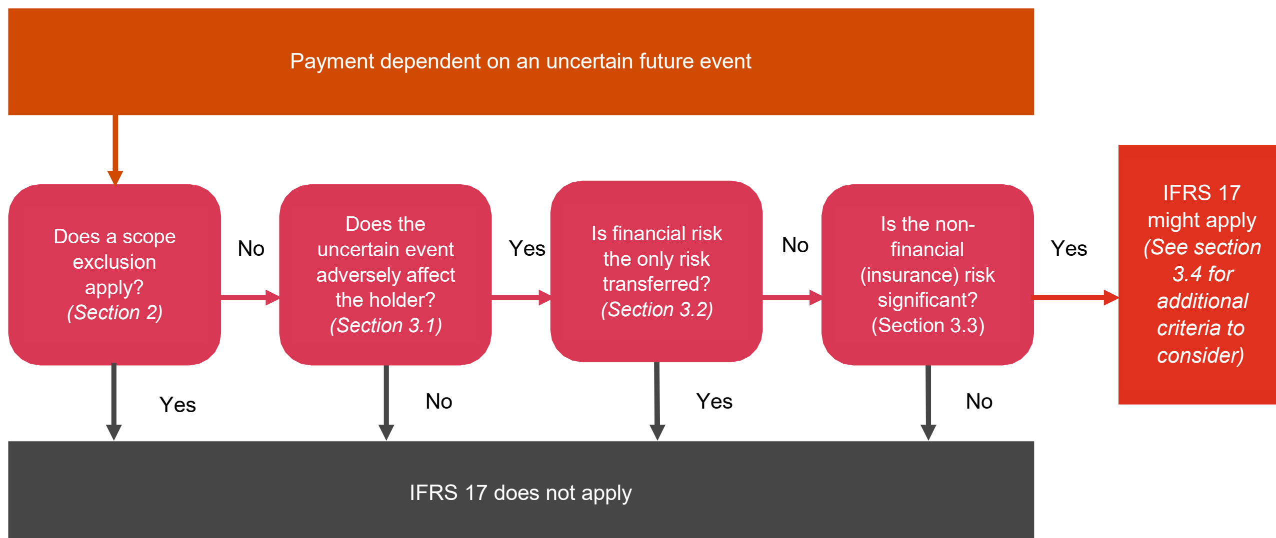
IFRS 17 defines insurance contracts as contracts under which one party (the issuer) accepts significant insurance risk from another party (the policyholder) by agreeing to compensate the policyholder if a specified uncertain future event (the insured event) adversely affects the policyholder. The compensation could be a cash payment or a payment in kind (for example, repairing or replacing a broken product).

Uncertainty (or risk) is the essence of an insurance contract. At least one of the following is uncertain at the inception of an insurance contract:

- the probability of an insured event occurring (for example, car breakdown cover has risk that the car will break down);
- when it will occur (for example, a life-contingent annuity has risk that an individual will live longer than expected); or
- how much the entity will need to pay if it occurs (for example, health insurance has risk relating to the magnitude of medical costs incurred).

IFRS 17 typically applies to the issuer, and not the holder, of insurance contracts. An entity which owns a building and takes out buildings insurance is the holder, and it does not apply IFRS 17 to that purchased insurance contract. The only situation where the holder applies IFRS 17 is when an entity holds a reinsurance contract to transfer the insurance risk arising from an underlying insurance contract that it has issued.

The flowchart below shows the criteria that are most relevant, for entities that are not insurers, in identifying whether a contract that it has issued is an insurance contract that is within the scope of IFRS 17:



2. Scope exclusions from IFRS 17

Even if a contract is an ‘insurance contract’ as defined in IFRS 17, it will not be accounted for under IFRS 17 if it meets a scope exclusion. These exclusions cover various common contracts that a non-insurer might enter into, and so they are useful to be aware of before going into further detail on the criteria for identifying ‘insurance contracts’.

Some scope exclusions are mandatory and apply to all contracts of a particular kind; these are covered in section 2.1. Other scope exclusions are optional or apply only if certain conditions are met; these are covered in sections 2.2 to 2.5.

2.1 Contracts within the scope of other standards

Standards other than IFRS 17 apply to the following (even if the definition of an insurance contract is met):

- Product warranties provided by a manufacturer, retailer or dealer in connection with the sale of its products (either a good or a service) to a customer are within the scope of IFRS 15 and IAS 37.
- Employers’ assets and liabilities from employee benefit plans (see IAS 19 and IFRS 2), and retirement benefit obligations reported by defined benefit retirement plans, are within the scope of IAS 26.
- Contractual rights or obligations that are contingent on the future use of, or the right to use, a non-financial item is within the scope of IFRS 16, IFRS 15 and IAS 38.
- Residual value guarantees provided by a manufacturer, dealer or retailer are within the scope of IFRS 15.
- Residual value guarantees for lessees embedded in a lease are within the scope of IFRS 16.
- Contingent consideration payable on a business combination is within the scope of IFRS 3.
- Insurance contracts in which the entity is the policyholder, unless those contracts are reinsurance contracts held.
- Credit card contracts (or similar contracts that provide credit or payment arrangements) that meet the definition of an insurance contract if, and only if, the entity does not reflect an assessment of the insurance risk associated with an individual customer in setting the price of the contract with that customer.

Example – Scope exclusion for warranty contracts

A consumer electronics company provides its customers, at the time of the sale of its electronics products, with a three-year free of charge warranty to cover repairs due to manufacturing defects. In addition, for a fixed price, the customer can purchase a further two-year extended warranty repair cover, which is offered through a warranty subsidiary of the manufacturing company.

Question 1: Is either of these two warranty products an insurance contract within the scope of IFRS 17 in the consolidated group's financial statements?

No. From a group perspective, the electronic products, the three-year warranty, and the two-year extended warranty are provided by the same reporting entity. There will be insurance risk in the contract, because either the number of services to be performed or the nature of those services, or both, is uncertain. Both the warranty and the extended warranty contracts provide protection to the customer against an 'uncertain future event' and, assuming that the risk is significant, would meet the 'insurance contract' definition. However, since both types of warranty are available at the time of the sale, they will meet the scope exclusion for warranties provided by a manufacturer, dealer or retailer in connection with the sale of its goods or services to a customer.

Question 2: Would the answer change if the extended warranty contract is provided at a later date, and the terms of the original sale did not provide for the future purchase of the warranty at a fixed price?

Yes. If the extended warranty is provided at a later stage and not in conjunction with the sale (that is, the terms of the original sale did not provide for the future purchase of the warranty at a fixed price), it will not meet the scope exclusion in IFRS 17, because it is not 'in connection with the sale'. However, this product might meet the fixed fee contract criteria in section 2.2.

Question 3: Would the answer change at the level of the subsidiary providing the extended warranty services?

Yes. For the separate financial statements of the subsidiary that provides the extended warranty cover, the scope exclusion in paragraph 7(a) of IFRS 17 would not apply, because the repairs and maintenance are provided by a party other than the manufacturer, retailer or dealer. The fixed-fee contract considerations in section 2.2 would apply at the subsidiary level.

2.2 Fixed-fee contracts

An entity can choose to apply either IFRS 15 or IFRS 17 to some contracts that provide a service for a fixed fee. Examples of such contracts are maintenance contracts under which the service provider is obliged to repair specified equipment after a malfunction, or car breakdown services in which the provider is obliged to provide roadside assistance or tow the car to a nearby garage. Because the level of service, and thereby the obligation of the service provider, depends on an uncertain future event, these kinds of contracts might meet the definition of an insurance contract.

An entity can choose to apply IFRS 15 only if all of the following criteria are met; otherwise, IFRS 17 must be applied:

- the price of the contract does not reflect an assessment of the risk with an individual customer;
- the contract compensates the customer by providing a service; and
- the insurance risk arises primarily from the customer's use of services rather than from uncertainty over the cost of the service.

The choice can be made on a contract-by-contract basis, but the choice made for each contract is irrevocable.

Example – Optional scope exemption for fixed-fee contracts

When is a fixed-fee property maintenance contract an insurance contract within the scope of IFRS 17?

Entity P owns a portfolio of properties. It outsources its property maintenance and repair on all of these properties to entity S, a property management entity, for a five-year period for a fixed fee. This fee covers both property management and the cost of repair work. All repairs and maintenance required to maintain the properties to an agreed standard, based on the condition on inception of the contract, are now the responsibility of entity S. In entering into this contract, entity S made an assessment of the risks and likely repairs that would be required in respect of the specific portfolio of properties owned by entity P. This included normal wear and tear and certain other conditions (such as dry rot and damp, should they be discovered in the course of any remedial work). The price was fixed at the outset. Repairs required as a result of external events, such as fire or storm damage, continue to be covered by entity P's property insurance arrangements with a regulated insurance entity.

Where either the number of services to be performed over a period or the nature of those services is not pre-determined, there can be significant insurance risk. There is uncertainty in the situation above in the following areas:

- whether any particular repair will be required;
- when any particular repair will be required; and
- how much any particular repair will cost.

There is a specified uncertain event, because it is uncertain when or if any particular repair will be required and how much it might cost. The significance of the insurance risk for entity S is assessed, on a contract-by-contract basis, under IFRS 17. Insurance risk could be significant, even though there might be a minimal probability of material losses for entity S arising from all of its property management contracts, because a significant loss could arise on any one contract, such as the contract with entity P. If the insurance risk is significant, IFRS 17 will apply. Since entity S priced the contract based on an assessment of the risk associated with entity P's properties, this contract is not eligible for the fixed-fee contract scope exemption, and it is within the scope of IFRS 17.

2.3 Loans with death waivers

Provided that no other scope exclusions apply, an entity can choose to apply either IFRS 9 or IFRS 17 to contracts which limit the compensation to the amount otherwise required to settle the policyholder's obligation created by the contract. An example of such contracts is a loan with a death waiver.

The choice can be made for each portfolio of insurance contracts, and the choice made for each portfolio is irrevocable.

PwC Observation: IFRS 9 might be easier than IFRS 17 to apply to loans with death waivers

The scope choice for loans with death waivers applies to contracts such as equity release mortgages (see section 3.2 for an example). Today, under IFRS 4, many entities account for these mortgages using IAS 39 principles, and so electing IFRS 9 on transition to IFRS 17 might be operationally less disruptive.

2.4 Financial guarantee contracts

Financial guarantee contracts that require the issuer to make specified payments, to reimburse the holder for a loss that it incurs because a specified debtor fails to make a payment when due, meet the definition of an insurance contract. They are, however, outside the scope of IFRS 17, unless the issuer has previously asserted explicitly that it regards such contracts as insurance contracts and has used the accounting guidance applicable to insurance contracts.

2.5 Credit cards and other payment arrangements

Some credit card contracts (or similar contracts that provide credit or payment arrangements) meet the definition of an insurance contract, because they make payments to the card holder in circumstances that meet the definition of insurance risk. Examples include if the holder uses the card to purchase goods or services that turn out to be faulty or are not delivered, or if the holder is 'duped' or 'scammed' into making an invalid payment. Where the contract pricing does not reflect an assessment of the individual customer's insurance risk, IFRS 17 does not apply to the contract in its entirety.

Example – Credit card with insurance coverage

A bank issues a credit card (or other similar contract) to a customer. Under the credit card contract, the bank provides protection for purchases of goods or services that are faulty or not delivered to the customer, including any costs incurred, as well as fraud protection for the cardholder against the misuse of the card. The bank does not charge any fees to the cardholder that reflects an assessment of the cardholder's individual risk associated with the protection provided.

The scope exclusions in IFRS 9 have been amended for financial instruments arising under credit card contracts, or similar contracts that provide credit or payment arrangements (effective 1 January 2023).

Does the bank apply IFRS 17 to the contract with the cardholder?

The bank will need to assess whether the contract is an insurance contract as defined in IFRS 17. Both the faulty goods or services / failure to deliver goods or services and potential fraud are uncertain future events which adversely affect the cardholder. The risk transferred to the bank is an insurance risk. If there is significant insurance risk as defined in IFRS 17, the contract meets the definition of an insurance contract in IFRS 17.

The bank will typically consider the following in determining the accounting for credit card contracts, or similar contracts that provide credit or payment arrangements.

Does the bank reflect an assessment of the insurance risk associated with the individual customer in setting the price of the credit card contract with the customer?

The bank will need to consider the IFRS 17 scope exclusion relating to credit card contracts that meet the definition of an insurance contract. This example meets the criteria for the scope exclusion, because the bank does not charge any fees to the cardholder that reflect an assessment of the cardholder's individual risk.

Is the insurance coverage a contractual term of the financial instrument?

Applying IFRS 9, the bank will need to determine whether the insurance coverage is a contractual term of the financial instrument. The interpretation of 'contractual term' should be consistent with IFRS 9 (since the contract is within the scope of IFRS 9). In particular the interpretation should be consistent with that applied in interpreting paragraph B4.1.13 of IFRS 9 that clarifies that, where payments arise only as a result of legislation that gives the regulatory authority power to impose changes to an instrument, they should be disregarded when assessing the SPPI criterion, because that power is not part of the contractual terms of a financial instrument. Instrument E in paragraph B4.1.13 specifically refers to bail-in instruments as an example that might meet the SPPI criterion.

A clause should not be taken into account, when assessing the SPPI criterion, where the clause merely acknowledges the existence of legislation (that is, the clause does not create additional rights or

obligations that would not have existed in the absence of such a clause). Applying that conclusion to insurance coverage, the insurance coverage clause should not be considered to be part of 'contractual terms of such a financial instrument' where the clause merely acknowledges the existence of the insurance coverage legislation. For this to be the case, it is necessary for:

the insurance coverage regulations themselves to specify all of the key terms, including what the insurance coverage trigger is and the effects of the trigger being met; and
the contract terms to be drafted such that, if the regulations change, the insurance coverage terms of the instrument change in exactly the same way.

In some situations, it might be appropriate to obtain legal advice to determine whether or not the contractual terms included create additional rights or obligations that would not have existed in the absence of such a clause.

If the bank concludes that the insurance coverage is a contractual term of the financial instrument, IFRS 9 requires the insurance coverage component to be separated from the contract and accounted for under IFRS 17.

However, if the insurance coverage is not a contractual term of the financial instrument, it will not be within the scope of IFRS 9, and the bank will need to consider other applicable IFRS standards.

Is there a separate service under IFRS 15?

In paragraph BC94C of the Basis for Conclusions on IFRS 17, the IASB noted that other IFRS standards, such as IFRS 15 or IAS 37, might apply to other components of the contract, such as other service components or insurance components required by law or regulation.

Under IFRS 15, promises in a contract can be explicit, or implicit if they create a valid expectation that the entity will provide a good or service based on the entity's customary business practices, published policies or specific statements [IFRS 15 para 24]. Warranties might be written in the contract, or they might be implicit as a result of either customary business practices or legal requirements. The bank will need to assess whether the insurance coverage for faulty goods or services / failure to deliver goods or services and fraud are separate performance obligations to be accounted for under IFRS 15. This assessment requires judgement; however, we think that generally:

Faulty goods or services / failure to deliver goods or services. The insurance coverage is likely not a separate performance obligation, since it only provides assurance that a product will function as expected and in accordance with certain specifications. The warranty is generally intended to safeguard the customer against existing defects, and it does not provide any incremental service to the customer.
Fraud protection. In our view, the insurance coverage for fraud protection might also be viewed as an assurance-type warranty. The bank is providing assurance that it will execute a transaction that was appropriately authorised by the credit card holder, and funds will be transferred to a valid merchant account. [IFRS 15 App B paras B28–B33].

As a result, where the insurance coverage for fraud and for faulty goods or services / failure to deliver goods or services is not part of the contractual terms of the financial instrument, the insurance coverage will generally be accounted for under IAS 37. [IFRS 15 App B para B30].

3. The criteria for identifying insurance contracts

Sections 3.1 to 3.3 explain the three most relevant criteria included in the flowchart on page 3 for identifying whether a contract that it has issued meets IFRS 17's definition of an insurance contract. Section 3.4 then summarises additional criteria that are typically less relevant to a non-insurance entity, but would also need to be considered to reach a conclusion.

3.1 Does the uncertain event adversely affect the holder?

A contract can only be an insurance contract within the scope of IFRS 17 if the uncertain event would adversely affect the holder. For example, insurance that compensates a building owner for damage to its building would meet this criterion, because the building owner would otherwise be adversely affected by damage to its building.

Example – Weather derivatives

An entity has a contract under which it will receive payments if rainfall is below average during monsoon months. Could this be an insurance contract?

No. Contracts that require a payment based only on climatic variables (sometimes described as 'weather derivatives'), or on other geological or other physical variables, are not insurance contracts, even if the policyholder uses the contract to mitigate an underlying risk exposure. Such contracts do not require an adverse effect on the policyholder as a precondition of payment, and the risk transferred arises from a non-financial variable that is not specific to either party to the contract. Examples of contracts based on climatic variables that are not insurance contracts include a weather derivative that is triggered by its 'underlying' and pays even if the holder has not suffered any damage from the weather (for example, a contract under which an entity will receive payments if rainfall is below average during the monsoon months).

In contrast, if the contract was based on a climatic variable that is specific to a party to the contract (for example, reduced crop yields from land that is owned and farmed by the holder of the contract as a result of below-average rainfall in the region during the monsoon months), the contract might be within the scope of IFRS 17, and the issuer should proceed as in section 3.2 below.

Example – Savings plan with cash prizes

An entity issues a contract whereby the customer pays monthly deposits of CU100 under a 60-month saving plan, with a guaranteed annual interest of approximately 6% (equivalent to market rates applicable to saving accounts or other inflation index). Interest is only accrued for those monthly deposits which are not withdrawn after the first 12 months of the plan. These plans are sometimes referred to as 'capitalisation plans'.

Customers are entered, during the term of the plan, into monthly lotteries that award a cash prize equivalent to 1,000 times the amount of the last deposit made (that is, cash prize equals CU100,000). Each customer receives a certificate with a numerical identification that might coincide with the winning numbers from the National Lottery. Every month, there will be one winner amongst all participants in the plan.

The deposits are redeemable in full, plus interest, only after one year. If the customer redeems the monthly deposits before one year, it will be subject to a surrender penalty. Surrender penalties are applied during the whole term of the contract, and they vary from 90% at inception of the contract to 0% after the 60 months, in order to encourage customers to keep their funds with the entity for a longer period of time.

At the inception of the contract, all customers nominate a beneficiary that will receive the prize or the accumulated surrender value of the deposits in the event of the customer's death.

Is the saving plan, with rights to receive cash awards based on lottery-type draws, an insurance contract under IFRS 17?

No, this is not an insurance contract, as defined in Appendix A to IFRS 17. Although it is clear that there is a substantial benefit to be paid to a customer who wins the monthly lottery, the fact that the customer has the winning lottery numbers does not qualify as an insured event, because the event does not affect the customer adversely. This is a gambling contract.

3.2 Is financial risk the only risk transferred?

Insurance risk is any risk other than financial risk transferred from the holder of the contract to the issuer.

IFRS 17 defines financial risk as *“the risk of a possible future change in one or more of a specified interest rate, financial instrument price, commodity price, currency exchange rate, index of prices or rates, credit rating or credit index or other variable, provided in the case of a non-financial variable that the variable is not specific to a party to the contract*”.

Examples of non-financial variables that are specific to a party to the contract, and hence do not give rise to financial risk, include:

- the occurrence or non-occurrence of a fire that damages or destroys an asset of a party to the contract;
- EBITDA;
- revenue; or
- a measure of regulatory capital of a financial institution (for example, core tier 1 capital of a bank), including non-viability clauses included in some debt instruments issued by banks.

PwC Observation: If a contract does not transfer insurance risk, it might be a derivative

The definition of financial risk above is consistent with part of the definition of a derivative in IFRS 9. If a contract does not meet the definition of an insurance contract in IFRS 17 because it transfers financial risk rather than insurance risk, it might contain a derivative within the scope of IFRS 9. In some cases, it will not be a derivative either (for example, if there is a significant initial net investment), but this should be considered further.

Example – Credit insurance

Entity A has a receivable balance from entity B, and a bank agrees to reimburse entity A if entity B fails to make payment when due under the original terms of the receivable balance.

Although the receivable balance is a financial asset, the risk that entity A fails to receive payment when due is not a financial risk as defined in IFRS 7, because the risk is specific to entity A, and so it is insurance risk rather than a financial risk.

This contract is a financial guarantee contract, for which the scope exclusion explained in section 2.4 might apply. If the scope exclusion does not apply, the contract might be within the scope of IFRS 17, and the bank should proceed as in section 3.3 below.

Example – Embedded EBITDA guarantee

An entity agrees to provide hotel management services to the owner of a hotel for 20 years, in return for a variable fee determined as a percentage of gross hotel revenue. In addition, the contract contains an embedded guarantee that guarantees the hotel owner a specified level of earnings before interest, tax depreciation and amortisation ('EBITDA'). To the extent that actual EBITDA is below 85% of projected EBITDA, the service provider is obligated to make payments to the owner of the hotel to cover the shortfall.

There are no limitations relating to the events that might give rise to an eligible EBITDA shortfall other than material disruption to business (such as force majeure, or refurbishment). Accordingly, the service provider is exposed to risks other than its own poor performance – for example, an over-supply of hotel accommodation in that location and other general market risks. Furthermore, the amount payable under the guarantee might exceed the amount of the revenue-based fee receivable, such that the service provider might be required to make a net payment to the hotel owner.

The embedded EBITDA guarantee compensates the hotel owner if EBITDA is lower than expected, which is an uncertain event that adversely affects the hotel owner; also it is not a financial risk, because it is specific to the hotel owner. The transferred risk is therefore insurance risk. The contract might be within the scope of IFRS 17 and the service provider should proceed as in section 3.3 below.

If a contract transfers only financial risk, it is not within the scope of IFRS 17 and would be accounted for applying other standards such as IFRS 9, 'Financial Instruments'. Contracts can contain both financial and non-financial risk; such contracts are not excluded from being insurance contracts, provided that the insurance risk is significant. See section 3.3 for assessing whether insurance risk is significant.

Example – Equity release mortgage

An entity issues an equity release mortgage (also commonly referred to as a 'lifetime' or 'reverse' mortgage) with a 'no negative equity' guarantee. The contractual terms secure the mortgage against the borrower's property. Interest is accrued. Principal and accrued interest are payable when the borrower dies or moves into long-term care. The property is then sold, and the proceeds are used to repay the mortgage balance (including any accrued interest). The entity is not entitled to any excess of the sales proceeds over the amount due, but it bears any shortfall where the sales proceeds are not sufficient to repay the principal and accrued interest. Assume that the entity holds the equity release mortgage within a 'hold to collect' business model, and that the contract contains no other features that could cause it to fail the SPPI test in IFRS 9.

Does the contract transfer insurance risk?

Yes. The contract exposes the entity, amongst other risks, to the risk of changes in fair value of the borrower's property (a non-financial asset). That is not a financial risk, because the fair value of the property reflects not only changes in market prices for properties in general (a financial variable) but also the physical condition of the specific asset (a non-financial variable). The contract therefore transfers insurance risk, as well as financial risk, from the borrower to the entity.

This contract might meet the optional scope exclusion explained in section 2.3, because the maximum shortfall is the mortgage balance (that is, the benefit to the borrower is limited to the amount otherwise required to settle their obligation). If the entity does not elect to apply IFRS 9, the contract might be within the scope of IFRS 17 and the entity should proceed as in section 3.3 below.

3.3 Is the non-financial (insurance) risk significant?

Insurance risk is 'significant' only if the occurrence of an insured event could cause the entity to pay additional amounts that are significant in any scenario, excluding scenarios that lack commercial substance (that is, that have no discernible effect on the economics of the transaction). The additional amounts refer to the present value of amounts that exceed those that would be payable if no insured event had occurred.

Unlike IFRS 4, IFRS 17 specifies that there is a transfer of significant insurance risk only if there is a scenario that has commercial substance in which the issuer has a possibility of a loss on a present value basis. The one exception to this principle is reinsurance contracts – even if a reinsurance contract does not expose the issuer to the possibility of a significant loss, that contract is deemed to transfer significant insurance risk if it transfers to the reinsurer substantially all of the insurance risk relating to the reinsured portions of the underlying insurance contracts.

A scenario with commercial substance can be one that is extremely unlikely.

Example – Unlikely scenario

An entity has a contract which requires an insurer to reimburse it for the value of a property that it owns in the event of the property being destroyed by a hurricane. The likelihood of a hurricane destroying a building is low (although the scenario has commercial substance), but the payment by the insurer would be substantial. In all other scenarios, a similar payment would not be made. The contract therefore contains significant insurance risk.

PwC Observation: Liabilities might be recognised earlier under IFRS 17 than under some other accounting standards

A liability might be recognised under IFRS 17, even if the adverse event is very unlikely. This might result in liabilities being recognised sooner than would be the case applying IAS 37. Where the entity does not have a class of similar items, under IAS 37 it might only recognise a liability when an outflow is probable.

If an insured event does not cause a significant loss to the policyholder, that scenario is ignored when assessing whether there is significant insurance risk.

Example – Is the policyholder's loss insignificant?

A contract requires the issuer to pay CU1 million to the holder if an asset suffers physical damage causing an insignificant economic loss of CU1 to the holder. The holder transfers to the insurer only the insignificant loss of losing CU1. In addition, the requirement in the contract for the issuer also to pay CU999,999 if the physical damage occurs creates non-insurance risk. Because the issuer does not accept significant insurance risk from the holder, this contract is not an insurance contract.

3.4 Additional criteria to consider

In the preceding sections, we have focused on the three criteria that are most relevant to a non-insurance entity when deciding whether a contract that it has issued is an 'insurance contract' as defined in IFRS 17. This section summarises additional criteria that are typically less relevant to a non-insurance entity, but they would also need to be considered to reach a conclusion.

Criteria	Explanation
Does a contract exist?	A contract is an agreement between two or more parties that creates enforceable rights and obligations. Contracts can be written, oral or implied by customary business practices. Contractual terms can be either explicit or implicit, including those terms that are imposed by law or regulation. An entity should consider its substantive rights and obligations arising from a contract, law or regulation.
Is the transferred risk a pre-existing risk?	Insurance risk must be a pre-existing risk that is transferred from the policyholder to the entity as a result of the contract, and it must not be a new risk created by the contract. For example, an entity leases a car to a customer, and the contract provides insurance coverage for damage to third-party vehicles caused by the customer driving the leased car. The transferred risk relates to damage caused by the customer driving the car, which is not created by the contract, and so it will meet the definition of insurance risk.
Is the transferred risk from a third party?	Entities must accept risk from another party (a separate entity) in order for insurance risk to exist.

4. Conclusion

The scope of IFRS 17 will include some contracts issued by entities that are not traditional insurance entities. Unless a scope exclusion applies, any entity issuing insurance contracts will need to apply IFRS 17 to account for those contracts.

Under IFRS 4, many entities were able to 'unbundle' the insurance elements of contracts and to apply the measurement principles in other standards to the non-insurance elements of the contract. In contrast, IFRS 17 applies to the whole contract (with limited exceptions) and has detailed measurement requirements. Applying IFRS 17 can be challenging and time-consuming in practice. So it is critical that entities identify insurance contracts, determine whether they are within the scope of IFRS 17 and, if so, analyse the accounting implications in good time for the mandatory adoption of IFRS 17 in 2023.

We hope that you find this Spotlight useful in addressing some of your questions. For more information, please visit www.pwc.com/ifrs17 or refer to the PwC Manual of Accounting. PwC clients who have questions about this Spotlight should contact their engagement partner.

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