



HM Treasury

IFRS 17 Insurance Contracts application guidance:

Month 20XX

IFRS 17 Insurance contracts Application guidance:



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Executive Summary

IFRS 17 Insurance contracts

IFRS 17 Insurance Contracts (IFRS 17) is being applied by HM Treasury in the Government Financial Reporting Manual (FReM) from 1 April 2025 (with limited options for early adoption).

IFRS 17 sets out the principles for the recognition, measurement, presentation and disclosure of insurance contracts within the scope of IFRS 17 and replaces the previous standard IFRS 4 Insurance Contracts.

IFRS 4 was an interim standard which was meant to be in place until the IASB completed its project on insurance contracts. IFRS 4 permitted entities to use a wide variety of accounting practices for insurance contracts. IFRS 17 significantly changes the accounting treatment for insurance contracts, and will increase the transparency of entities' financial positions and performance, and make financial statements more comparable.

As discussed in **Chapter 2**, the scope of IFRS 17 is broad and can apply to a wider range of contracts than expected. IFRS 17 applies a current value approach to measuring insurance contracts. Income, expenditure, and profit is recognised as insurance services are provided to the policyholder. Losses on insurance contracts (onerous contracts) are recognised immediately in the SoCNE.

Detailed disclosures are required to explain amounts recognised on the statement of financial position and income and expenditure, risks and significant judgements. Entities will need to apply judgement in deciding upon the information to disclose in order to meet the objective of providing a basis for users of financial statements to assess the effect that insurance contracts have on the financial position, financial performance and cash flows of the entity. Entities are reminded to use the principles of materiality that flow through all accounting standards to ensure they provide relevant and reliable information about insurance contracts in the financial statements.

IFRS 17 is a complex accounting standard. Preparers should consider whether engagement with experts such as actuaries and corporate finance professionals is required. The changes from IFRS 4 to IFRS 17 will affect both preparers of financial statements and users. Users will receive more and different information; preparers will need to help users interpret this new information.

FReM Interpretation and adaptations

The FReM interprets and adapts IFRS 17 in several ways. IFRS 17, as adapted and interpreted by the FReM, will be effective from 1 April 2025, unless an entity has elected to adopt IFRS 17 earlier, with the permission from the relevant authority.

The FReM **interprets** IFRS 17 in the following ways, as set out in FReM Chapter 8:

- For the purpose of applying IFRS 17 in central government, legislation and regulations, in isolation, **are not** equivalent to insurance contracts. Legislation and regulations can include binding rights or obligations,

can facilitate the creation of arrangements that fall within the definition of a contract and can form part of the implied terms of a contract, but in themselves are not agreements between parties. [Section 2.2]

- The accounting policy choice to account for contracts meeting the criteria set out in IFRS 17 paragraph 8 under has been withdrawn. All entities applying the FReM shall account for contracts meeting the criteria in IFRS 17 paragraph 8 under IFRS 15. [Section 2.5]
- The accounting policy choice in IFRS 17 paragraph 7(e) is withdrawn. All entities shall account for financial guarantee contracts using IAS 32, IFRS 7 and IFRS 9. [Section 2.6]
- ~~The definition of a contract (and therefore, of an insurance contract) is expanded to include intra-UK government agreements that are not legally enforceable. [Section 2.7]~~
- The accounting policy choice under IFRS 17 paragraphs 88 and 89 has been withdrawn. All entities shall follow IFRS 17 paragraphs 88(a) and 89(a) and recognise insurance finance income and expense for the period in the SoCNE. [Section 3.2.7]
- For insurance contracts that limit the compensation for insured events to the amount otherwise required to settle the policyholder's obligation created by the contract (for example, loans with death waivers), entities shall account for these contracts under IFRS 9. [Section 3.4]
- If an entity has reasonable and supportable information to conclude that a set of contracts will all be in the same group applying IFRS 17 paragraph 16, it shall measure the set of contracts to determine if the contracts are onerous and assess the set of contracts to determine if the contracts have no significant possibility of becoming onerous subsequently. [Section 3.4]
- In applying the premium allocation approach, an entity shall recognise any insurance acquisition cash flows as expenses when it incurs those costs, provided that the coverage period of each contract in the group at initial recognition is no more than one year. [Section 3.4]
- Entities shall include the entire change in the risk adjustment for non-financial risk as part of the insurance service result. [Section 3.4]
- An entity shall present the income or expenses from a group of reinsurance contracts held (see paragraphs 60–70A), other than insurance finance income or expenses, as a single amount. [Section 3.4]
- Entities shall include insurance finance income or expenses for the period in the SoCNE. [Section 3.4]
- On transition entities shall restate retrospectively following the requirements of IFRS 17 paragraphs C3-C4. If full retrospective restatement is impracticable, entities shall apply the fair value approach per IFRS 17 paragraphs C20-C24. [Section 4.2]

- The transition relief noted in IFRS 17 paragraph C28 is mandated. [Section 4.45]

The FReM **adapts** IFRS 17 in the following ways, as set out in FReM Chapter 8:

- There is a rebuttable assumption that the financial instrument discount rate provided in PES papers will be used to discount IFRS 17 insurance liabilities, except for insurers regulated by the Prudential Regulation Authority (PRA) and entities whose principal business activity is insurance or reinsurance. [Section 3.2.3]
- Where entities use the financial instrument discount rate stated in PES papers, reporting entities do not need to disclose the yield curve used to discount cash flows as required by IFRS 17 paragraph 120. [Section 3.2.3]
- The requirement of IFRS 17 paragraph 119 to disclose the confidence level used to determine the risk adjustment for non-financial risk has been withdrawn. [Section 3.2.4]
- ~~Where the application of IFRS 13 at transition would result in an excessive premium, entities should instead measure the contractual service margin (CSM) at transition as £nil and the insurance liability measured at value of fulfilment cash flows. For insurance contracts where a £nil premium is charged and the fair value approach is being used to transition to IFRS 17 for those contracts, entities must measure the transition value of those contracts at fulfilment cashflows.~~ [Section 4.3]
- ~~Where full retrospective transition per IFRS 17 paragraph C4(a) is impracticable, for groups of insurance contracts which are breakeven or onerous (or priced to be breakeven or onerous), entities may measure the transition value of these groups of contracts at fulfilment cashflows at the transition date.~~ [section 4.4]

Note on this application guidance

This guidance sets out the basis for the central government adaptations and interpretations of IFRS 17 and does not focus on the application of IFRS 17 itself. It does not seek to duplicate the extensive guidance already included in IFRS 17, nor take away the judgements each entity will be required to make when applying IFRS 17.

Chapter 1 – introduction, purpose and context

1.1 Introducing IFRS 17 Insurance Contracts

1.1.1 International Financial Reporting Standard (IFRS) 17 Insurance Contracts (IFRS 17) is the new accounting standard for insurance contracts issued by the International Accounting Standards Board (IASB). It replaces IFRS 4 Insurance Contracts for accounting periods starting on or after 1 January 2023. Government bodies should apply IFRS 17 for the first time in the financial year commencing 1 April 2025, unless approval has been received from HM Treasury to implement IFRS 17 before this financial year.

1.1.2 IFRS 17 establishes the principles for the recognition, measurement, presentation and disclosure of insurance contracts issued by an entity, and for reinsurance contracts held or issued. It does not address how to account for insurance contracts purchased by an entity.

1.1.3 This application guidance is intended to support those applying IFRS 17 in the UK central government. It discusses the nature and purpose of IFRS 17, the definition of an insurance contract for accounting purposes, and how to apply IFRS 17. It includes further guidance on specific issues such as transition arrangements, remote contingent liabilities, the impact of IFRS 17 on the Whole of Government Accounts, and the impact on budgets and estimates.

1.2 The purpose of IFRS 17

1.2.1 IFRS 4 (the standard IFRS 17 is replacing) defined what an insurance contract is but did not give a full accounting treatment for those contracts. Instead, it set out parameters to limit unhelpful practices. Entities were free to adopt any accounting treatment that fell within those parameters.

1.2.2 IFRS 17 sets out, for the first time in IFRS Standards, comprehensive accounting requirements for insurance contracts. Applying IFRS 17, entities that issue insurance contracts produce more comparable financial reporting that provides useful information about the entity's economic resources, claims against the entity and changes in those resources and claims, in line with the objectives of general purpose financial reporting as set out in the IASB's Conceptual Framework.

1.2.3 The key principles in IFRS 17 itself are summarised on the IFRS website. The text of IFRS 17 can be viewed or downloaded from the same page by those who have registered for a free account.

1.2.4 In brief, IFRS 17 requires entities providing insurance contracts to:

- identify those contracts,
- separate out contract elements that are accounted for separately from the insurance contracts,
- sort the insurance contracts into groups that share similar characteristics,

- recognise and measure these groups of contracts in a specified way,
- recognise any profit over the period the organisation is providing insurance contract services, and recognise any loss immediately,
- present insurance revenue, insurance service expenses, and insurance finance income or expenses separately, and
- make disclosures that enable users of their financial statements to assess how these insurance contracts impact on their financial position, performance, and cash flows.

1.2.5 IFRS 17 applies a consistent methodology for recognising, measuring, and disclosing the financial impact of insurance contracts. This allows users of central government financial statements to see how public money has been committed to cover insurance risks by government entities issuing insurance contracts. It is for these reasons HM Treasury consider it important IFRS 17 is adopted by central government entities who issue insurance contracts.

1.3 Why central government entities issue insurance contracts

1.3.1 Some central government entities issue and manage large portfolios of insurance contracts. These generally address situations where the risk is too great for a profit-making organisation to absorb it alone.

1.3.2 A central government entity may also issue insurance contracts as part of contracting with private sector suppliers in the form of guarantees built into contracts that transfer some insurance risk in from the supplier. For example, a department may need to commission a private sector organisation to carry out work that gives rise to risks that private sector insurance companies will not cover, including contracts in defence and transport.

1.3.3 Insurance contracts, or guarantees that meet the definition of insurance contracts, may also be issued on an ad hoc basis to meet specific needs, encourage specific behaviours, or address specific responsibilities. For example, a department might provide guarantees to encourage investment in a region or might commit to make good any losses caused by a specified project.

1.3.4 These situations commit the government to making future payments if certain specified events take place. Transferring insurance risk into central government has an impact on future central government finances. Applying IFRS 17 empowers central government entities to consistently quantify that impact and ensure that they receive value for money when taking on insurance risk. Carrying the insurance liability in their financial statements also means that they can be more prepared when risks crystallise.

Chapter 2 – The Scope of IFRS 17

2.1 Definition of an insurance contract

2.1.1 For a transaction to be within the scope of IFRS 17 a contract must be in place. The description of a contract is included in the box after this paragraph. A

contract does not need to be explicitly described as insurance, or as a contract, to be deemed an insurance contract. What matters is the substance: does it meet the description of a contract as used in IFRS 17, and does it transfer insurance risk?

Description of a contract

A contract is described in IFRS 17 as an agreement between two or more parties that creates enforceable rights and obligations. Enforceability of the rights and obligations in a contract is a matter of law. Contracts can be written, oral or implied by an entity's customary business practices.¹

2.1.2 Any entity can issue an insurance contract if it has taken on insurance risk from another party. It does not have to charge a fee for the service (the insurance coverage), or to define itself as an insurance provider. The arrangement does not need to be described as insurance and does not need to be in writing. IFRS 17 only applies, however, if there is a contract as described below:

Definition of an insurance contract

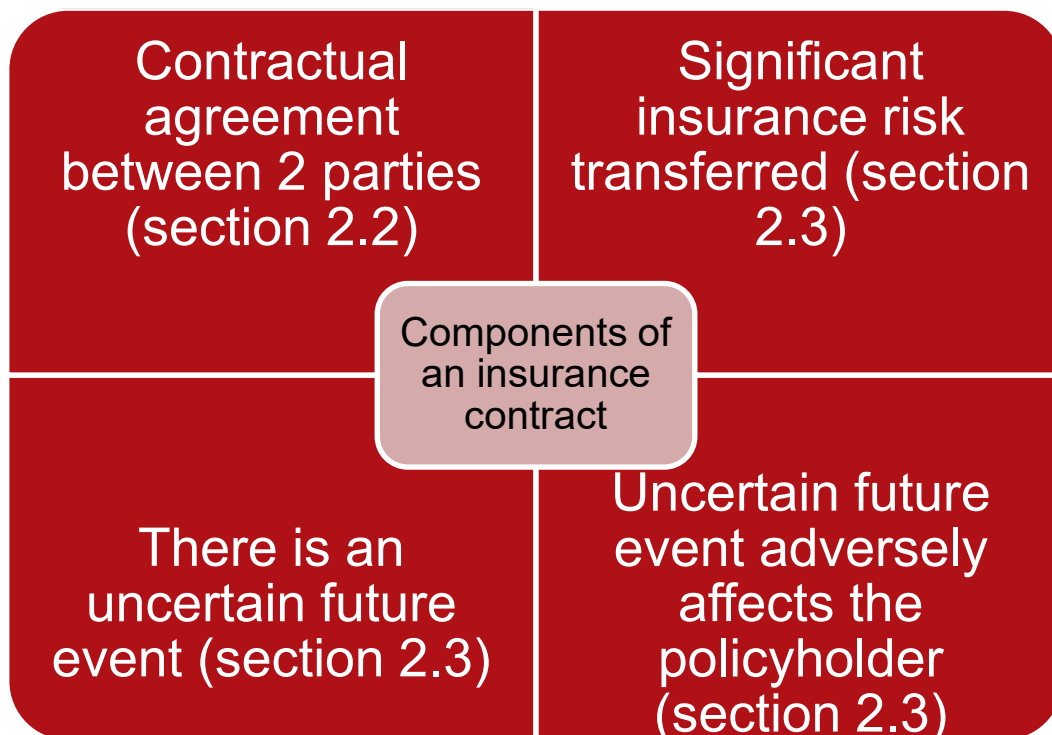
An insurance contract is a contract under which one party (the issuer) accepts significant insurance risk from another party (the policyholder) by agreeing to compensate the policyholder if a specified uncertain future event (the insured event) adversely affects the policyholder.²

2.1.3 Based on the definitions of an insurance contract in IFRS 17 entities should consider the following questions when determining whether a transaction is in scope of IFRS 17:

- Is there an agreement between two or more parties? (refer to **section 2.2** below for further discussion of contracts in central government)
- Is there a transfer of risk from the issuer of the contract to the policyholder? If so, is the transferred risk insurance risk and does it meet the definition of significant insurance risk under IFRS 17? (refer to **section 2.3** below)
- Does the contract cover an uncertain insured event which, if occurred, would adversely affect the policyholder? (refer to **section 2.3** below)

¹ Refer to IFRS 17 paragraph 2 for a full discussion of what a contract is under IFRS 17.

² Refer to defined terms in IFRS 17 for a full definition of an insurance contract, significant insurance risk, policyholder and insured event.



2.1.4 One area where central government differs to the private sector is how responsibilities set out in legislation interact with the concept of a contract in IFRS 17. Specifically, do legislative responsibilities equate to contractual obligations under IFRS 17? The next section provides guidance on this question.

2.2 When a responsibility is not a contract

2.2.1 Determining whether there is a contract (as described in IFRS 17) in place is the first step entities should undertake when assessing whether they provide insurance within the scope of IFRS 17. Many arrangements transfer significant insurance risk (see the next section) but do not meet the description of a contract in IFRS 17 (see paragraph 2.1.1). These arrangements are accounted for under another appropriate standard or using accounting policies developed applying the Conceptual Framework.

2.2.2 As noted above, legislation can confer responsibilities on central government organisations, but these are not necessarily contractual. For the purpose of applying IFRS 17 in central government, legislation and regulations, in isolation, **are not** equivalent to insurance contracts. The key difference is that legislation and regulations enabling, for example, the NHS to provide healthcare free at the point of delivery or social benefits are not agreements between government and specific individual citizens or businesses. Rather, legislation and regulation can enable or oblige entities to provide services or make certain payments. They can include binding rights or obligations, can facilitate the creation of arrangements that fall within the definition of a contract and can form part of the implied terms of a contract, but in themselves are not agreements between parties.

Central government interpretation: For the purpose of applying IFRS 17 in central government, legislation and regulations, in isolation, **are not** equivalent to

insurance contracts – legislation and regulations do not fall within the scope of the definition. They can include binding rights or obligations, can facilitate the creation of arrangements that fall within the definition of a contract and can form part of the implied terms of a contract, but in themselves are not agreements between parties.

2.2.3 To provide an example, legislation such as the NHS Act 2006 and Health and Care Act 2022 are not contracts between all NHS entities and a specific party; it is legislation setting out how NHS bodies should operate.

2.2.4 A useful comparison is with commercial health insurance in the private sector. A party purchasing commercial health insurance will have a contract with the private healthcare provider- e.g., a policyholder could have a 10-year insurance contract with a private healthcare provider, which will obligate the private healthcare provider to provide care- in accordance with the insurance contract- for those 10 years. This is an explicit agreement between policyholder and issuer setting out what is being covered and the duration of the cover which is legally enforceable.

2.2.4.2.5 Entities should also note that a contract falls into the scope of IFRS 17 only where the rights and obligations in the contract are enforceable by law. Contracts which are not legally enforceable would therefore not fall within the scope of IFRS 17 (though they could fall into the scope of another accounting standard).

2.3 Insurance risk vs financial risks, significant insurance risk and uncertain future events

2.3.1 Once it has been determined a contract is in place another consideration is the type of risk transferred from the policyholder to the issuer. A central concept of IFRS 17 is the transfer of risk. However, to be within the scope of IFRS 17, the risk transferred must be **insurance risk**.

2.3.2 IFRS 17 defines **insurance risk as any risk which is not a financial risk**. A financial risk is defined in IFRS 17 below:

What is a financial risk?

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.³

2.3.3 Therefore, if the risk transferred is not a financial risk, it is an insurance risk. The next question to ask is whether the insurance risk is significant or not. Significant insurance risk is a key term in IFRS 17 as an insurance contract cannot exist without the entity accepting significant insurance risk from the policyholder.

What is significant insurance risk?

³ Refer to IFRS 17 defined terms.

Insurance risk is significant if, and only if, an insurance event could cause the issuer to pay additional amounts that are significant in **any single scenario**, excluding scenarios which have no commercial substance.⁴

It is important to note that significant insurance risk can exist even if the insured event is extremely unlikely or the expected present value of the contingent cashflows is a small proportion of the expected present value of the remaining cash flows from the insurance contract.⁴

Paragraphs B17-B23 of IFRS 17 discusses significant insurance risk in more detail.

2.3.4 The final part of the definition of an insurance contract is that compensation is provided by the issuer to the policyholder for an uncertain future event which adversely affects the policyholder. This part of the definition is relatively straightforward and IFRS 17 paragraphs B3-B5 discussed this in further detail.

2.3.5 Entities should also be aware that IFRS 17 applies where the transferred risk (from policyholder to issuer) is a pre-existing risk. Any new risk created by a contract for the entity or policyholder is not insurance risk⁵.

2.3.6 To apply this principle, consider this 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. In this example, the transferred risk relates to damage caused by the customer driving the leased car (the adverse event), which is not created by the contract and therefore meets the definition of insurance risk⁶.

2.3.7 To further understand how to apply paragraph B11 of IFRS 17, entities should also refer to this [IFRS Foundation staff paper](#)⁷.

2.4 Insurance and reinsurance contracts between central government bodies

2.4.1 Entities in the UK central government will generally self-insure against risks as this achieves better value for money. Entities within the same group may provide insurance to each other, for example a department providing insurance to one or more of its agencies or ALBs.

Is self-insurance within the scope of IFRS 17?

The answer to this is no except for single entity financial statements where an entity provides insurance to another entity within the group. The following examples will illustrate this point:

- Instead of purchasing commercial insurance, an entity chooses to bear the risk of an uncertain future event adversely affecting them. This arrangement would be outside of the scope of IFRS 17 as there is

⁴ IFRS 17 paragraph B18

⁵ IFRS 17 paragraph B11

⁶ Example taken from [this PwC publication](#).

⁷ [AP7: Premium waivers \(ifrs.org\)](#)

no agreement with another party. Any related expenditure (e.g., if the risk crystallises) will be accounted for under another IFRS standard or using accounting policies developed applying the Conceptual Framework.

- A department provides an insurance service [via contract](#) to its ALBs by agreeing to cover claims to damage incurred or loss of computer equipment. At the group level the transactions between the two entities associated with this service ~~net off~~ [eliminate](#) on consolidation. However, at the single entity level (i.e., at the core department only level) there may be an insurance contract if it is determined there is a contract in place between the department and its ALBs, with the department taking on significant insurance risk.

IFRS 17 paragraph B27(c) explains this further.

2.4.2 IFRS 17 requires that **reinsurance contracts** are accounted for separately from the underlying insurance contracts to which they relate. The reason for this is that reinsurance contracts do not normally allow the entity the right to reduce amounts owed to the underlying policyholder by amounts they expect to receive from the reinsurer.

What is reinsurance?

If a parent department has agreed to provide cover to one of its agencies or other bodies that has issued an insurance contract, so that the cost of any risk that crystallised would be passed on to the department, then the insurance risk has been transferred again. Under IFRS 17 this second transfer constitutes a reinsurance contract.

The definition of a reinsurance contract under IFRS 17 is an insurance contract issued by one entity (the reinsurer) to compensate another entity for claims arising from one or more insurance contracts issued by that other entity (underlying contracts)⁸.

2.4.3 An entity which has purchased reinsurance would recognise both the insurance contract and the reinsurance contract in its financial statements. If the insurance contract was a liability on the agency's statement of financial position, and the parent department had agreed to cover the whole cost of the risk crystallising, then the reinsurance contract would be a corresponding asset and the net impact would be zero (assuming there are no timing differences in recognition of the insurance contract and reinsurance contract).

2.4.4 There are two key differences when measuring reinsurance contracts, being the risk adjustment for non-financial risk and the contractual service margin (CSM)⁹ for a group of reinsurance contracts held.

⁸ IFRS 17 defined terms.

⁹ [Section 3](#) discusses the risk adjustment for non-financial risk and CSM in more detail.

- For reinsurance contracts held, the risk adjustment for non-financial risk represents the amount of risk being transferred by the holder to the issuer of reinsurance contracts¹⁰.
- For reinsurance contracts held, the CSM is modified to represent a net cost or net gain on purchasing the reinsurance rather than representing unearned profit (as with normal insurance contracts)¹¹.

2.4.5 The parent department's individual accounts would show only the insurance contract issued. As the reinsurance contract would be an intragroup arrangement, it would net off in the consolidated accounts. The consolidated accounts would only show the agreement with a third party (i.e., the original insurance contract.)

2.5 Fixed-fee service contracts

2.5.1 IFRS 17 provides a scope exception for fixed fee service contracts so that such contracts may be accounted for under either IFRS 15 or IFRS 17, at the discretion of the entity and subject to certain criteria¹².

2.5.2 An example could be a maintenance contract where the provider agrees to fix equipment after malfunction and the fee charged for the contract is fixed rather than variable based on the work to be performed. Such contracts could meet the definition of an insurance contract.

2.5.3 IFRS 17 allows entities to account for fixed fee contracts under IFRS 15 rather than IFRS 17 if the three conditions noted in IFRS 17 paragraph 8 are met:

- the entity does not reflect an assessment of the risk associated with an individual customer in setting the price of the contract with that customer;
- the contract compensates the customer by providing services, rather than by making cash payments to the customer; and
- the insurance risk transferred by the contract arises primarily from the customer's use of services rather than from uncertainty over the cost of those services.

2.5.4 To improve consistency of central government annual reports and accounts and consolidation of entities within the Whole of Government Accounts (WGA), IFRS 17 in central government has been interpreted to mandate use of IFRS 15 where the criteria in IFRS 17 paragraph 8 are met.

Central government interpretation: the accounting policy choice to account for contracts meeting the criteria set out in IFRS 17 paragraph 8 has been withdrawn. All entities applying the FReM shall account for contracts meeting the criteria in IFRS 17 paragraph 8 under IFRS 15.

¹⁰ IFRS 17 paragraph 64

¹¹ IFRS 17 paragraph 65

¹² IFRS 17 paragraph 8

2.6 Financial guarantee contracts

2.6.1 Prior to the implementation of IFRS 17 entities may have financial guarantee contracts, which have similar features to insurance contracts. Financial guarantee contracts can be accounted for under IFRS 9 and are defined in IFRS as contracts which require the issuer to make specified payments to reimburse the holder for a loss it incurs due to the debt repayments not being received¹³.

2.6.2 Financial guarantee contracts transfer credit risk. IFRS 17 explicitly excludes from its scope financial guarantee contracts **unless** the issuer has previously asserted explicitly that it regards such contracts as insurance contracts and has used accounting applicable to insurance contracts¹⁴.

2.6.3 To improve consistency of central government annual reports and accounts and consolidation of entities within the Whole of Government Accounts (WGA), the accounting policy choice to account for these contracts has been withdrawn; all entities shall account for financial guarantee contracts using IAS 32, IFRS 7 and IFRS 9.

Central government interpretation: the accounting policy choice in IFRS 17 paragraph 7(e) is withdrawn. All entities shall account for financial guarantee contracts using IAS 32, IFRS 7 and IFRS 9.

2.7 ~~Intra government agreements~~

~~2.7.1—The FReM makes an adaption to the definition of an insurance contract in IFRS 17 for central government, concerning intra government agreements.~~

~~**Central government adaptation:** The definition of a contract (and therefore, of an insurance contract) is expanded to include intra UK government agreements that are not legally enforceable.~~

~~2.7.2—This adaptation is intended to capture insurance like arrangements between Crown bodies, or other governmental bodies, that are not legally enforceable but are in substance akin to an enforceable contract. It also aligns the definition of a contract with adaptations made to IFRS 16 in the FReM regarding intra government agreements.~~

~~2.7.3—Although this adaptation broadens the definition of an insurance contract, it does not mean that all insurance like intra UK governmental agreements will meet this definition. Any such agreements made should be carefully analysed to determine whether they meet the definition of an insurance contract as discussed in the sections above.~~

¹³ Refer to IFRS 9 defined terms for the full definition.

¹⁴ IFRS 17 paragraph 7(e)

Chapter 3- Applying IFRS 17

The IFRS Foundation have published a range of implementation tools to support those applying IFRS 17 Insurance Contracts, including a one-page summary of the accounting model with an accompanying short animation to explain each element. The landing page for these resources is [here](#).

3.1 Portfolios and groups of insurance contracts

3.1.1 IFRS 17 defines the terms ‘**group of insurance contracts**’ and ‘**portfolio of insurance contracts**’. These terms are used throughout IFRS 17 and this guidance.

3.1.2 Contracts that are subject to similar risks and are managed together form a **portfolio**¹⁵ of insurance contracts. If an entity has a single insurance contract that cannot be bundled together under IFRS 17 with any similar contracts, then it can be treated as a portfolio of one.

3.1.3 Portfolios of insurance contracts are then divided into groups. The entity applies the accounting treatment to each group rather than to each individual contract. IFRS 17 does require a minimum level of portfolio division into the following groups¹⁶:

- 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.

3.1.4 IFRS 17 includes guidance on how to aggregate insurance contracts and the guidance is not adapted or interpreted by the FReM.

¹⁵ IFRS 17 paragraph 14

¹⁶ IFRS 17 paragraph 16.

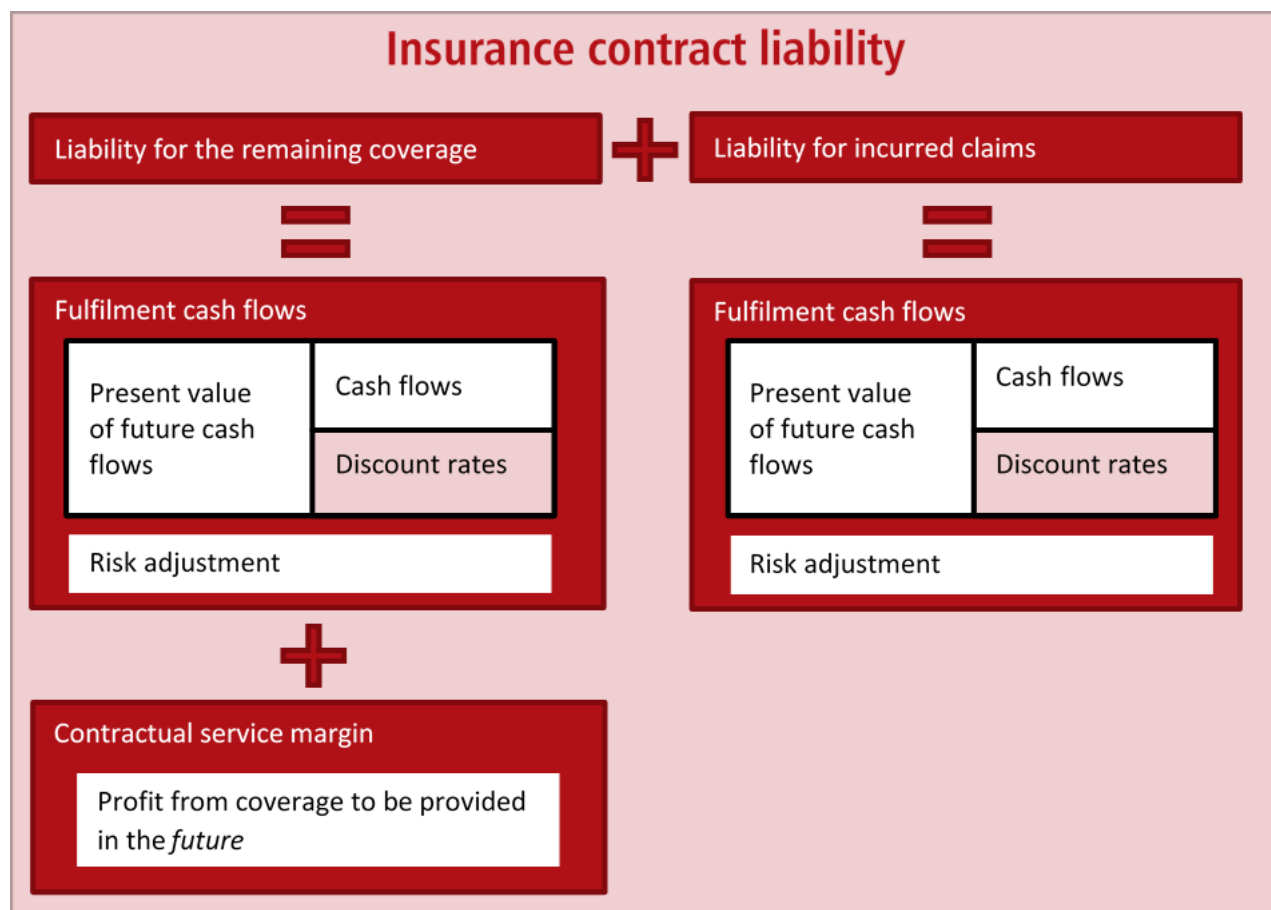
3.2 Accounting elements for insurance contracts

The IFRS Foundation has produced the following document to summarise the IFRS 17 accounting model: [The accounting model explained on one page \(ifs.org\)](https://www.ifs.org)

This section explains each element of the accounting model in more detail.

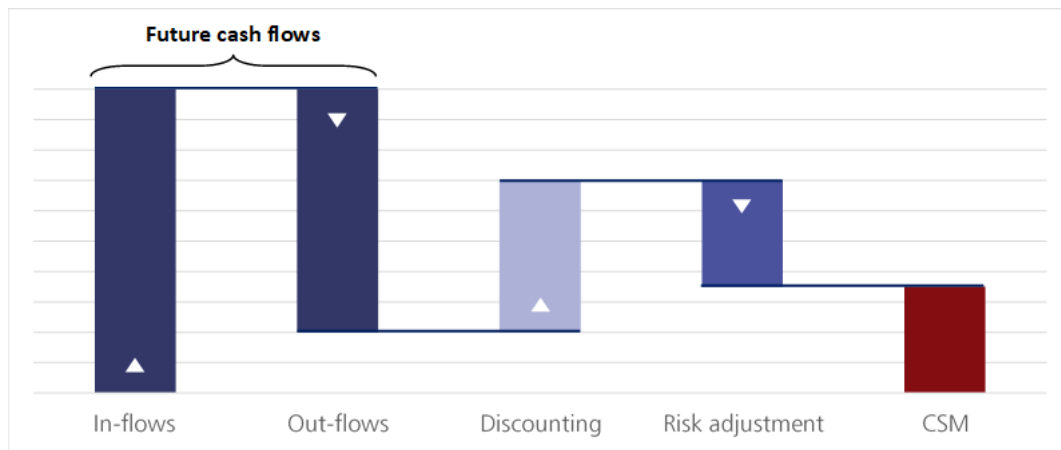
3.2.1 Statement of financial position (SoFP)

3.2.1.1 The SoFP model from the IFRS Foundation's publication has been reproduced below for reference:



3.2.1.2 The value of the IFRS 17 insurance contract liability on the SoFP is made up of several separate moving parts. Each element contributes to creating a full, updated picture of the insurance provider's commitments.

3.2.1.3 Both the liability for incurred claims and the liability for the remaining coverage are measured at current value at every SoFP date. In both cases this is achieved by calculating the present value of future cash flows and then making a risk adjustment. This is graphically represented below:



3.2.2 Cash flows

3.2.2.1 Both insurance and reinsurance contracts are measured using a probability-weighted average estimate of all future cash flows within the contract boundary with a risk adjustment to reflect the uncertainty in the timing and amount of cash flows that arises from non-financial risk. Determining which cash flows should be included is an area of judgement.

3.2.2.2 The contract boundary defines which cash flows are included in the measurement of an insurance contract (or group of insurance contracts). Further, the contract boundary places a limit on future cash flows that would not be included as they fall under subsequent insurance contracts which are still to be issued.

3.2.2.3 Cash flows are within the contract boundary if they arise from substantive rights and obligations arising from the contract (or imposed by law or regulation) that exist during the reporting period in which either¹⁷:

1. the insurer can compel the insured entity to pay premiums; or,
2. the insurer has a substantive obligation to provide the policyholder with services.

3.2.2.4 Cash flows within the boundary of an insurance contract are those that relate directly to the fulfilment of the contract¹⁸. Entities must refer to IFRS 17 for further guidance on the cashflows to include in the calculation of insurance liabilities.

3.2.3 Discount rate

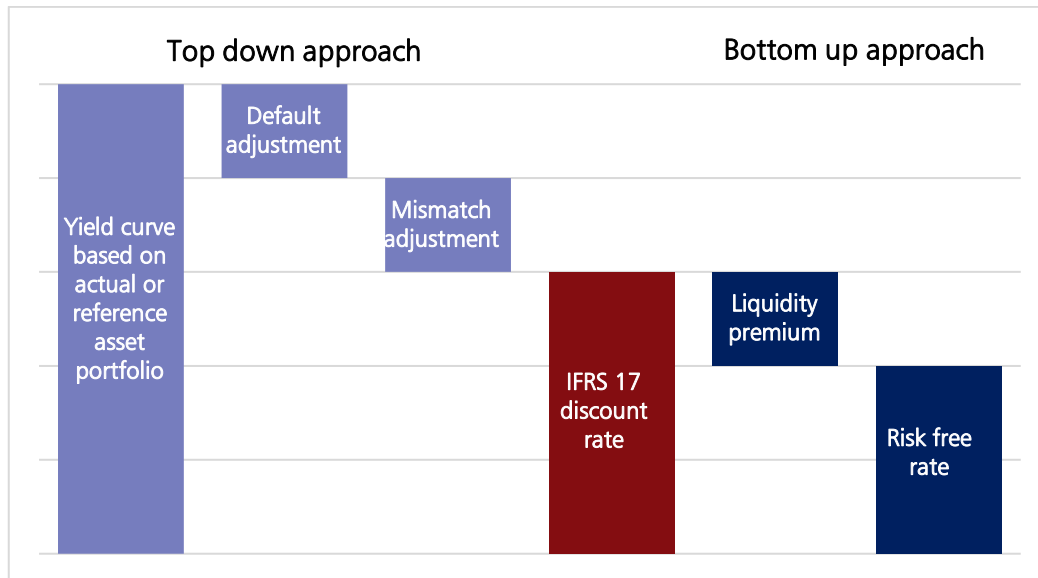
3.2.3.1 Under IFRS 17 the discount rates used to adjust future cash flows needs to reflect not just the time value of money but also the characteristics of those cash flows and the liquidity characteristics of the insurance contracts themselves.

3.2.3.2 Entities should refer to IFRS 17 paragraph B72 for instances where discounting is required. Entities should also note that IFRS 17 sets out instances where the 'current' discount rate is used and instances where the discount rate used at initial recognition is used.

¹⁷ IFRS 17 paragraph 34

¹⁸ IFRS 17 paragraph B65

3.2.3.3 There are two methodologies which can be used to determine discount rates: the top down approach and the bottom up approach:



The top-down approach (IFRS 17 para B81-B83):

- Starts with a yield curve based on the current market rates of return from either an actual portfolio of assets held by the company or a reference portfolio.
- Then adjusts the yield curve to eliminate any factors which are not relevant to the insurance contracts.

The bottom-up approach (IFRS 17 para B79, 80):

- Starts with a risk-free yield curve;
- Then add an illiquidity premium to adjust for differences between the liquidity characteristics of risk-free assets and those of the insurance contracts.

3.2.3.4 Under the bottom-up approach, discount rates need to take into account liquidity characteristics of the insurance contracts. As such discount rates may differ between groups or portfolios of insurance contracts within a single entity.

3.2.3.5 As noted in paragraph B79 of IFRS 17: 'For cash flows of insurance contracts that do not vary based on the returns on underlying items, the discount rate reflects the yield curve in the appropriate currency for instruments that expose the holder to no or negligible credit risk, adjusted to reflect the liquidity characteristics of the group of insurance contracts. That adjustment shall reflect the difference between the liquidity characteristics of the group of insurance contracts and the liquidity characteristics of the assets used to determine the yield curve.'

3.2.3.6 That being said, central government is different to the private sector in terms of how insurance liabilities which have crystallised are funded and the portfolio of assets which would back insurance liabilities. Most government entities do not hold assets to back insurance liabilities. Instead, entities would draw down

cash from the Consolidated Fund and have budgetary cover via the estimates process to fund insurance liabilities.

3.2.3.7 HM Treasury currently provide central discount rates to be used in the accounting for financial instruments, leases, provisions, and pensions. Reasons for doing this include consistency between central government annual reports and accounts and ease of implementation.

3.2.3.8 HM Treasury therefore adapts IFRS 17 in respect of discount rates to have a rebuttable presumption that the **financial instrument discount rate** is used to discount IFRS 17 liabilities, except for regulated insurers and entities whose principal business is insurance or reinsurance activities. The rebuttable presumption to use the HMT discount rate means the HMT discount rate is not mandated in central government.

3.2.3.9 The reason the financial instrument discount rate is used is for consistency between and comparison purposes between IFRS 9 and IFRS 17 liabilities.

Central government adaptation: There is a rebuttable assumption that the financial instrument discount rate (as stated in PES papers) will be used to discount IFRS 17 insurance liabilities, except for insurers regulated by the Prudential Regulation Authority (PRA) and entities whose principal business activity is insurance or reinsurance.

3.2.3.10 Paragraph 120 of IFRS 17 requires entities to disclose the yield curve used to discount cash flows which do not vary based on the returns on underlying items. Per the IFRS 17 Basis for Conclusions¹⁹, the reason for including this disclosure was because IFRS 17 allows different approaches to determine discount rates (which could give rise to different rates) and the disclosure of the yield curve will allow financial statement users to understand how those yield curves might differ between entities.

3.2.3.11 However, as noted above, IFRS 17 has been adapted to include a rebuttable presumption to use the financial instrument discount rate stated in PES papers. The financial instrument discount rate is a single rate rather than a range of rates on a yield curve. Therefore, the scenario of entities using different discount rates is no longer an issue if the financial instrument discount rate stated in PES papers is used. Therefore, the FReM is adapted to remove the requirement to disclose the yield curve used to discount cash flows in accordance with IFRS 17 paragraph 120, where the financial instrument discount rate stated in PES papers used.

Central government adaptation: Where entities use the financial instrument discount rate stated in PES papers, reporting entities do not need to disclose the yield curve used to discount cash flows as required by IFRS 17 paragraph 120.

3.2.4 Risk adjustment for non-financial risk

3.2.4.1 To account for the uncertainty associated with insurance contract cash flows, IFRS 17 includes a risk adjustment. In IFRS 17, this is referred to as the risk adjustment for non-financial risk and it distinguishes it from the financial risk

¹⁹ IFRS 17 paragraph BC198

element addressed by the discount rate (IFRS 17 paragraphs 37 and B87-B92 includes more guidance on the risk adjustment for non-financial risk).

3.2.4.2 The risk adjustment for non-financial risk is defined as the compensation an insurer requires for bearing uncertainty over the amount and timing of future cash flows as it fulfils the contract.

3.2.4.3 IFRS 17 does not specify the estimation techniques that an entity should apply when calculating the risk adjustment. IFRS 17 does, however, set out a list of characteristics that this adjustment should have in paragraph B91.

3.2.4.4 The reasons for including this adjustment are explained further in the IFRS 17 Basis for Conclusions but to summarise the adjustment was included in the calculation of the insurance liability for the following reasons²⁰:

- The adjustment results in an explicit measurement of non-financial risks, providing clearer insight into the obligation created by insurance contracts.
- It provides useful information about the entity's view of the economic burden imposed by non-financial risk associated with insurance contracts.
- The adjustment results in profit recognition pattern reflecting profit from bearing risk and from providing insurance services.
- The adjustment highlights instances where the entity has charged insufficient premiums for bearing the risk that claims exceed premiums.
- The adjustment will report changes in risk promptly and in an understandable way.

3.2.4.5 IFRS 17 includes the principle of what the risk adjustment should represent. It does not set how to calculate the adjustment. One key thing to note is that the risk adjustment is calculated from the **perspective of the issuer- not the market**.²¹ This means the risk adjustment for non-financial risk can differ between entities for similar groups of contracts.

3.2.4.6 To calculate the risk adjustment for non-financial risk, there are three common methods discussed by corporate finance professionals:

- Value at Risk (VaR) [also known as the confidence level technique]
- Tail Value at Risk (TVaR)
- Cost of Capital

3.2.4.7 As noted above, IFRS 17 does not prescribe a method for calculating the risk adjustment, so there may be additional methods to measure the risk adjustment for non-financial risk such as explicit loading for prudence (e.g., a 5% risk adjustment is used based on management's judgement). There are, however, certain characteristics the risk adjustment for non-financial risk must meet, which are stated in IFRS 17 paragraphs B89-B92. This guidance does not go into the above methods in any detail.

²⁰ IFRS 17 BC211

²¹ IFRS 17 BC215

3.2.4.8 There are several disclosure requirements associated with the risk adjustment, one of which is paragraph 119 of IFRS 17, requiring entities to disclose the confidence level used to determine the risk adjustment for non-financial risk. Where a technique other than the confidence level technique is used, entities should disclose the technique used and the confidence level corresponding to the results of that technique.

3.2.4.9 IFRS 17 Basis for Conclusions notes that this disclosure is burdensome to prepare and may not provide information that is directly comparable²². On this basis it has been concluded that the costs of preparing the disclosure outweigh the benefits in central government context, and the disclosure requirement in IFRS 17 paragraph 119 has **been withdrawn**.

Central government adaptation: the requirement of IFRS 17 paragraph 119 to disclose the confidence level used to determine the risk adjustment for non-financial risk has been withdrawn.

3.2.5 Contractual service margin

3.2.5.1 The contractual service margin (CSM):

- represents the unearned profit on an insurance contract or group of insurance contracts;
- relates to future service to be provided under the insurance contracts issued by the entity; and
- represents the margin the entity has charged for the insurance services it is providing in addition to bearing risk (the charge for bearing risk is represented by the risk adjustment for non-financial risk discussed above).

3.2.5.2 This unearned profit is recognised over the coverage period of that contract (or group of contracts) as and when insurance services are provided by the insurer to the policyholder. In other words, as with other IFRS accounting treatments, the entity only recognises the profit (the CSM) when it has carried out the services that earn that profit.

3.2.5.3 At initial recognition, if the expected present value of cash inflows related to a group of insurance contracts are greater than the expected present value of cash outflows (adjusted for the time value of money, non-financial risk and financial risk), that difference is the profit for that group of contracts. That profit is recognised as it is earned. The unearned element, updated at each SoFP date, is the contractual service margin. It forms part of the insurance contract liability.

3.2.5.4 In very simple terms, the CSM is the balancing figure included on the SoFP to avoid profit being recognised on day 1 of the contract being issued.

3.2.5.5 Note that entities will need to put into place processes to track the CSM on groups of contracts. One reason is to track the amount of CSM left to release in profit and loss in future periods. Another reason is because subsequent measurement of insurance contracts can impact the CSM recognised on the SoFP. For example, experience adjustments for premiums received for future coverage

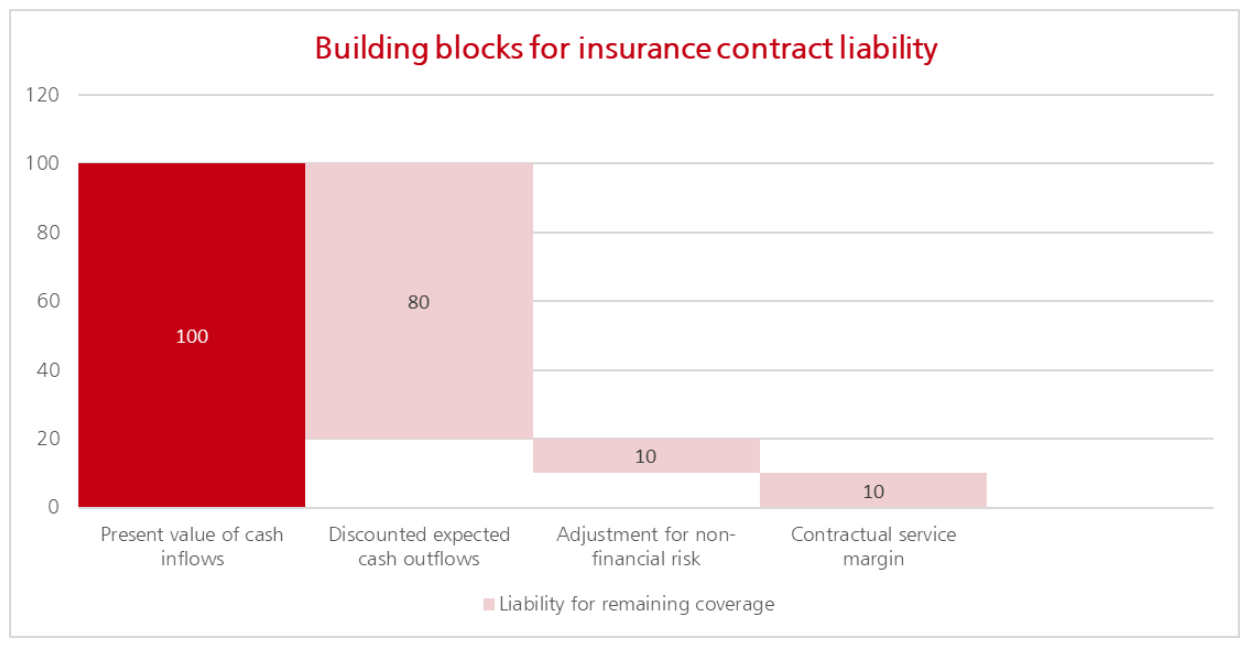
²² IFRS 17 BC216

relate to future service and may therefore require an adjustment to the CSM on the SoFP. IFRS 17 paragraphs 44 and 45 provides a list of reasons why the carrying amount of CSM should be adjusted.

Example 3.A: calculating the CSM

On 1 April 20XY the entity has issued 100 insurance contracts charging £1k each.

- Discounted expected future cash outflows are £80k
- The risk adjustment for non-financial risk has been calculated at £10k
- The CSM is therefore £10k on 1 April 20XY (£100k - £80k - £10k)



3.2.5.6 After calculating the CSM at inception of the insurance contracts it is subsequently recognised in profit and loss as noted above.

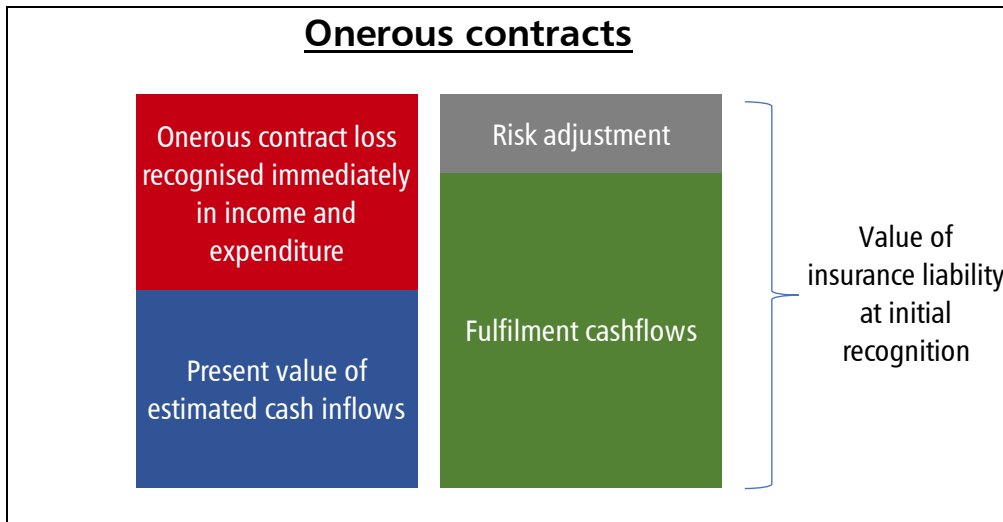
3.2.5.7 It is important to note that insurance service is provided over the whole of the coverage period rather than when an entity incurs a claim. Therefore, IFRS 17 requires the CSM to be recognised over the coverage period in a pattern reflecting the provision of insurance coverage as required by the insurance contract.²³

3.2.6 Onerous contracts

3.2.6.1 IFRS 17 also has specific guidance concerning onerous contracts. When an insurance contract is issued and the expected cash outflows are expected to exceed inflows, the insurance contract is **onerous**. The CSM cannot depict unearned losses. If a contract or group of contracts is onerous from inception or becomes onerous so that no profit is ever anticipated, then there is no contractual service margin. In the case of onerous contracts, the loss on the contracts is recognised through income

²³ IFRS 17 BC279

and expenditure **immediately** as insurance service expenditure²⁴. This is illustrated below:



3.2.6.2 As one can see from the diagram above, the value of the insurance liability (liability for remaining coverage) contains a loss component.

3.2.6.3 It is important entities keep a record of the loss component of the liability for remaining coverage for an onerous group. This is because subsequent changes in the liability for remaining coverage are allocated differently to the loss component based on the nature of the change:

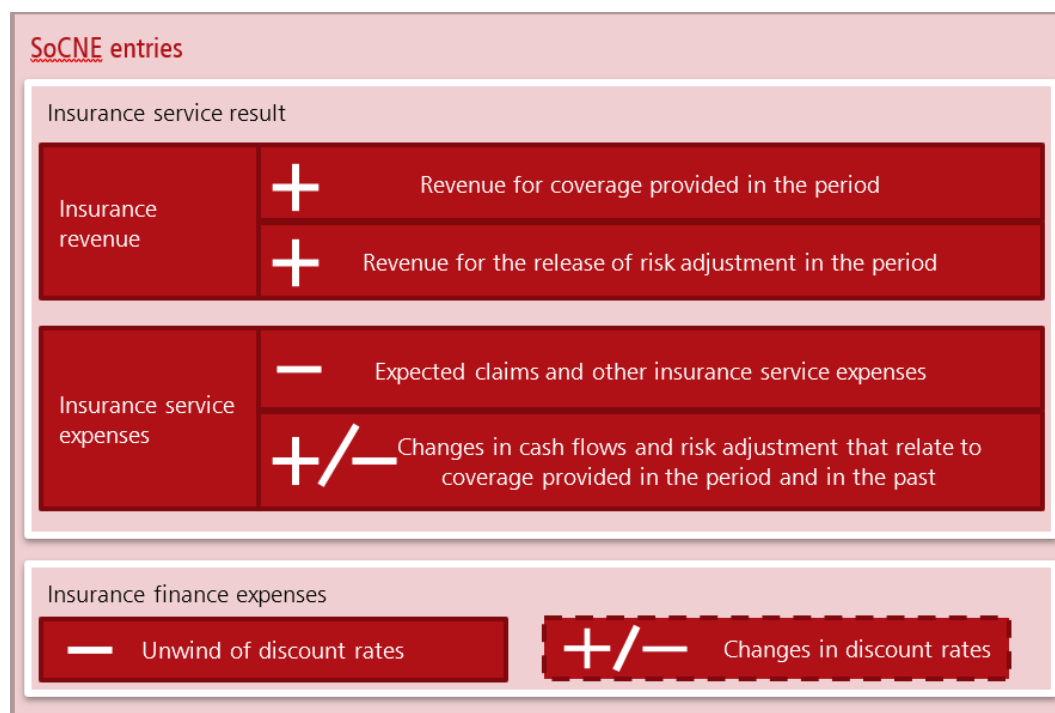
- Subsequent changes- as specified in IFRS 17 paragraph 51- in fulfilment cashflows of the liability for remaining coverage are to be allocated on a systematic basis **between** the loss component and the remainder of the liability for remaining coverage²⁵.
- Subsequent decreases relating to future service in fulfilment cash flows allocated to the group, arising from changes in estimates of future cash flows and the risk adjustment for non-financial risk are allocated wholly to the loss component (until the loss component is £nil).
- Subsequent increases in the amount of the entity's share of the fair value of underlying items is allocated wholly to the loss component (until the loss component is £nil).

²⁴ IFRS 17 paragraph 47

²⁵ IFRS 17 paragraph 50(a)

3.2.7 Statement of Consolidated Net Expenditure (SoCNE) entries

3.2.7.1 In each period the entity recognises the revenue for the coverage provided in that period, as well as any expenses incurred in that period. As time passes some of the uncertainty associated with the original insurance contract(s) is reduced, and the risk adjustment is accordingly released. IFRS 17 paragraphs 41 and 42 set out the amounts recognised as income and expenditure, and are summarised in the graphic below:



3.2.7.2 Under IFRS 17 paragraphs 88 and 89, entities make an accounting policy choice between:

- including insurance finance income and expenses for the period in profit or loss; or
- recognising part in profit or loss and part on other comprehensive income based on a systematic process²⁶.

3.2.7.3 To ensure consistency of accounting, the option in IFRS 17 paragraphs 88(b) and 89(b) to split insurance finance income and expenses between profit and loss and other comprehensive income **has been withdrawn**; all entities shall follow IFRS 17 paragraphs 88(a) and 89(a) and recognise insurance finance income and expense for the period in the SoCNE.

Central government interpretation: the accounting policy choice under IFRS 17 paragraphs 88 and 89 has been withdrawn. All entities shall follow IFRS 17 paragraphs 88(a) and 89(a) and recognise insurance finance income and expense for the period in the SoCNE.

²⁶ Also refer to IFRS 17 paragraph 90.

3.3 IFRS 17 disclosures

3.3.1 The disclosure requirements in IFRS 17 are more extensive than those in IFRS 4. In addition to referring to the disclosure requirements in IFRS 17, entities may find it useful to refer to the following publication from the IFRS Foundation for some illustrative disclosures (refer to Appendix B of the linked document):

<https://cdn.ifrs.org/-/media/project/insurance-contracts/ifrs-standard/ifrs-17-effects-analysis.pdf>

3.3.2 Additionally, there are a number of IFRS 17 illustrative statements issued by major professional services firms which can be referred to when preparing IFRS 17 disclosures.

3.3.3 Note that the requirement to disclose the confidence level used to measure the risk adjustment for non-financial risk has been withdrawn (refer to section 3.2.4 above). The requirement to disclose the yield curve used to discount cash flows has also been withdrawn where entities use the financial instrument discount rate stated in PES papers (refer to section 3.2.3 above).

3.3.4 Accounts preparers are reminded that entities need only include disclosures where the information therein is material to the users of the accounts (with the key user being Parliament).

3.4 General Measurement Model (GMM) and the Premium Allocation Approach (PAA)

3.4.1 There are three models for accounting for insurance contracts in IFRS 17, being:

- The General Measurement Model (GMM).
- The Premium Allocation Approach (PAA).
- The Variable Fee Approach (VFA).

3.4.2 IFRS 17 sets out the key accounting requirements for the GMM and includes additional guidance where the PAA or VFA models are used.

3.4.3 The **VFA approach** is used for groups of investment contracts with discretionary participation features. Such contracts are unlikely to be common in central government entities, so the approach will not be discussed any further this guidance.

3.4.4 For groups of insurance contracts which meet certain criteria, entities can use the **PAA** instead of the GMM. The PAA is a simplified model for accounting for groups of insurance contracts. IFRS 17 requires the following criteria are met to use the PAA for accounting for groups of insurance contracts

- The entity reasonably expects that such simplification would produce a measurement of the liability for remaining coverage for the group that would not differ materially from the one that would be produced applying the requirements of the GMM; **or**
- the coverage period of each contract in the group (including insurance contract services arising from all premiums within the contract boundary

determined at that date applying paragraph 34 of IFRS 17) is one year or less.

3.4.5 The decision regarding whether to apply the PAA or GMM to a group of insurance contracts meeting any of the criteria in paragraph 53 of IFRS 17 is an accounting policy choice.

3.4.6 Though the PAA is a simplified method of accounting, this may not always be the most efficient or cost-effective method. Entities who have already developed accounting models complying with the GMM may find that accounting for all insurance contracts using the GMM is the most efficient and cost-effective approach.

3.4.7 Consequently, this accounting policy choice will remain in central government to allow entities to choose the method most appropriate to their circumstances and each group of insurance contracts.

3.54 Other accounting policy choices

IFRS 17 also has many other accounting policy choices entities can take advantage of when applying IFRS 17. These have been summarised below, with a note as to whether a choice has been mandated to improve consistency of central government annual reports and accounts and consolidation of entities within the Whole of Government Accounts (WGA), all of which are central government interpretations of IFRS 17:

IFRS 17 paragraph	Choice available	Leave choice open/ mandate or hybrid option
8A	For insurance contracts that limit the compensation for insured events to the amount otherwise required to settle the policyholder's obligation created by the contract (for example, loans with death wavers), entities can account for these contracts under IFRS 9.	Mandate IFRS 9.
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.	Mandate measuring as a set of contracts to determine if onerous if the ' <i>reasonable and supportable</i> ' test is met.
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	No mandated approach

	contracts in the same group. The entity shall not apply this paragraph by analogy to other items.	
53	Measure insurance contracts under the premium allocation approach (PAA) if: <ul style="list-style-type: none"> • The measurement for the LRC does not differ materially from the general model; or • The coverage period for each contract in the group is one year or less. 	No mandated approach.
59 (a)	In applying the premium allocation approach, an entity: <ul style="list-style-type: none"> • may choose to recognise any insurance acquisition cash flows as expenses when it incurs those costs, provided that the coverage period of each contract in the group at initial recognition is no more than one year. 	Mandate this accounting policy choice.
69	Measure reinsurance contracts under the premium allocation approach (PAA) if: <ul style="list-style-type: none"> • The measurement does not differ materially from the general model; or • The coverage period for each contract in the group is one year or less. 	No mandated approach.
81	An entity is not required to disaggregate the change in the risk adjustment for non-financial risk between the insurance service result and insurance finance income or expenses. If an entity does not make such a disaggregation, it shall include the entire change in the risk adjustment for non-financial risk as part of the insurance service result.	Mandate not disaggregating and including the entire change in the risk adjustment for non-financial risk as part of the insurance service result.
86	An entity may present the income or expenses from a group of reinsurance contracts held (see paragraphs 60–70A), other than insurance finance income or expenses, as a single amount; or the entity may present separately the amounts recovered from the reinsurer and an allocation of the premiums paid that together give a net amount equal to that single amount.	Mandate presenting as a net amount.
88	In applying paragraph 87A(b), unless paragraph 89 applies, an entity shall make an accounting policy choice between: <ol style="list-style-type: none"> a) including insurance finance income or expenses for the period in profit or loss; or b) disaggregating insurance finance income or expenses for the period to include in profit or loss an amount determined by a 	Mandate IFRS 17 paragraph 88(a).

	systematic allocation of the expected total insurance finance income or expenses over the duration of the group of contracts, applying paragraphs B130–B133.	
89	<p>In applying paragraph 87A(b), for insurance contracts with direct participation features, for which the entity holds the underlying items, an entity shall make an accounting policy choice between:</p> <ul style="list-style-type: none"> a) including insurance finance income or expenses for the period in profit or loss; or b) disaggregating insurance finance income or expenses for the period to include in profit or loss an amount that eliminates accounting mismatches with income or expenses included in profit or loss on the underlying items held, applying paragraphs B134–B136. 	Mandate IFRS 17 paragraph 89(a), for the reasons noted for paragraph 88 above.

Chapter 4 – Transition Arrangements

4.1 Transition guidance

4.1.1 There are several considerations to evaluate as part of the transition to IFRS 17. These include the transition arrangements around retrospective application and disclosure considerations.

4.1.2 The date of initial application is the date when an entity first applies the transition requirements of IFRS 17 and must be the beginning of a reporting period after IFRS 17 is issued. For central government entities this will usually be 1 April 2025, unless the entity is early adopting as described in the executive summary. Entities must have made certain key assessments by this date including (the below is not an exhaustive list):

- Identifying all contracts which transfer significant insurance risk and meet the definition of an insurance contract as defined by IFRS 17.
- Determining how to communicate and educate all relevant stakeholders as to the impact of IFRS 17, including commercial, legal and finance teams.
- Considering which disclosure requirements are material, and where the necessary information is held to provide sufficient disclosures to meet the disclosure requirements.
- Determining how to group insurance contracts.

4.1.3 Entities should be aware of the following terms, as they are regularly used in IFRS 17 and this section of the application guidance:

- The **date of initial application** is the beginning of the annual reporting period in which IFRS 17 is first applied²⁷. In central government the **date of initial application is 1 April 2025**, unless an entity adopts IFRS 17 earlier.
- The **transition date** is the beginning of the annual reporting period immediately preceding the date of initial application²⁸. In central government the **transition date is 1 April 2024**, unless an entity adopts IFRS 17 earlier.

4.2 Approach to transition

4.2.1 IFRS 17 requires entities to restate fully retrospectively unless impracticable. To apply IFRS 17 retrospectively, at the transition date (1 April 2024) entities need to²⁹:

²⁷ IFRS 17 paragraph C2(a)

²⁸ IFRS 17 paragraph C2(b)

²⁹ IFRS 17 paragraph C4

- identify, recognise and measure each group of insurance contracts as if IFRS 17 had always applied;
- identify, recognise and measure any assets for insurance acquisition cash flows as if IFRS 17 had always applied (except that an entity is not required to apply the recoverability assessment in paragraph 28E before the transition date);
- derecognise any existing balances that would not exist had IFRS 17 always applied; and
- recognise any resulting net difference in equity.

4.2.2 If it is not practicable to retrospectively apply the requirements of IFRS 17, two alternative approaches are available:

- The modified retrospective approach (MRA).
- The fair value approach.

4.2.3 Entities applying the fair value approach determine the contractual service margin, or loss component, of insurance contracts by measuring the difference between the fair value of that group of contracts at the transition date and the fulfilment cash flows of those contracts. Fair value is measured using the requirements of IFRS 13.

4.2.4 IFRS 17 paragraphs C20-C24 set out the fair value approach in more detail.

4.2.5 In order to achieve consistency across central government, entities should retrospectively apply IFRS 17 in full if they have the information available to do so (as required by IFRS 17).

4.2.6 If full retrospective application is not practicable, central government bodies should use the **fair value** approach to improve consistency of central government annual reports and accounts and consolidation of entities within the Whole of Government Accounts (WGA).

4.2.7 The fair value approach was chosen over the MRA to make IFRS 17 transition less burdensome. Though the MRA has a number of modifications to retrospective restatement, there was a consensus that if retrospective restatement was judged impracticable by a central government entity, then it was likely the MRA would also be impracticable, and entities will be applying the fair value approach more often than not. As such, mandating the fair value approach if retrospective restatement is impracticable should enable entities to come to a decision on which transition approach to use more quickly and easily, whilst allowing for a more consistent transition approach across central government.

Central government interpretation: on transition entities shall restate retrospectively following the requirements of IFRS 17 paragraphs C3-C4. If full retrospective restatement is impracticable, entities shall apply the fair value approach per IFRS 17 paragraphs C20-C24.

What is impracticable?

4.2.8 The concept of impracticability of applying requirements of accounting standards is set out in IAS 8 paragraph 5. Specifically, IAS 8 defines impracticability scenarios where the entity cannot apply a requirement after making every reasonable effort to do so. It then goes on to set out some of the scenarios where retrospective application may be impracticable.

4.2.9 The IASB concluded that the following amounts needed for retrospective application would often (though not always) be impracticable³⁰:

- the estimates of cash flows at the date of initial recognition;
- the risk adjustment for non-financial risk at the date of initial recognition;
- the changes in estimates that would have been recognised in profit or loss for each accounting period because they did not relate to future service, and the extent to which changes in the fulfilment cash flows would have been allocated to the loss component;
- the discount rates at the date of initial recognition; and
- the effect of changes in discount rates on estimates of future cash flows for contracts for which changes in financial assumptions have a substantial effect on the amounts paid to policyholders.

4.2.10 IAS 8 paragraphs 50-53 provide further guidance on what impracticable means in the context of retrospective restatement.

4.2.11 As noted in IAS 8 entities must make every reasonable effort to apply a new standard retrospectively before concluding impracticability.

4.3 The Fair Value Approach

4.3.1 The fair value approach is fundamentally different from the full retrospective and modified retrospective approaches in that the calculation of the CSM is performed on a prospective basis.

4.3.2 The fair value approach is a method of determining the ~~{CSM}~~ at the transition date (1 April 2024). As noted above, the fair value approach can only be used when the full retrospective approach is impracticable.

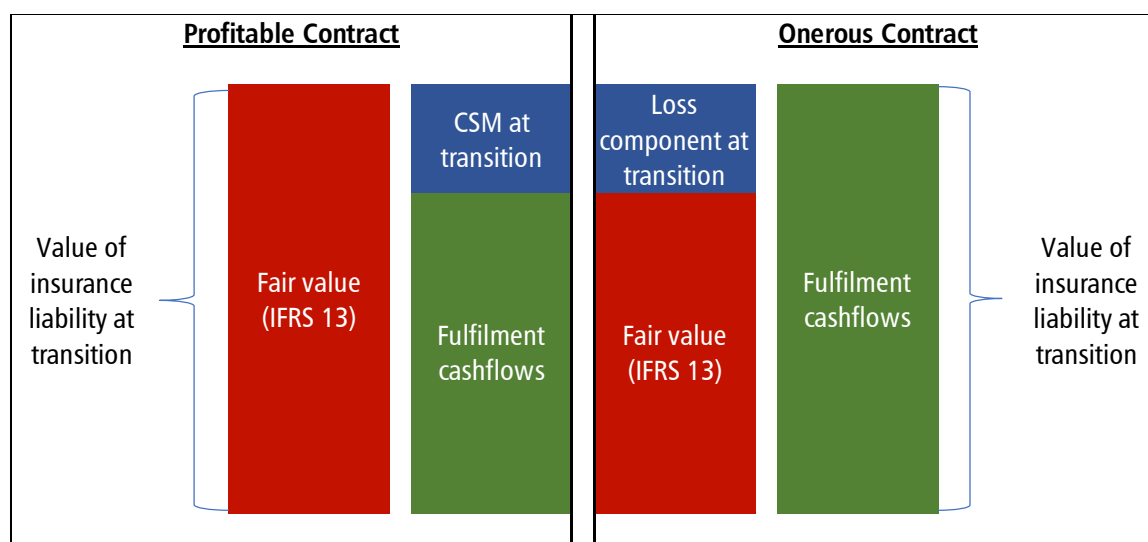
4.3.3 Fair value is defined in IFRS 13 as ‘**the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date**’³¹. Applying fair value requirements to insurance contracts is likely to be complex and require the exercise of significant professional judgement.

4.3.4 The insurance liability at transition using the fair value approach is measured at the higher of the fulfilment cashflows and fair value amount (these are illustrated in graphical form below):

³⁰ IFRS 17 Basis for Conclusions BC378

³¹ IFRS 13 paragraph 9

- If the fair value amount is higher than the fulfilment cashflows at transition, then the insurance liability is measured at the fair value amount. There is a CSM in this scenario, being the difference between the fair value and the fulfilment cashflows at transition.
- If the fair value is less than the fulfilment cashflows then the insurance liability at transition is measured at the fulfilment cashflows amount. There is a loss component in this scenario, being the difference between the fair value amount and the fulfilment cashflows at transition.



4.3.5 One of the key differences between the use of fair value and IFRS 17 is that the liability is measured from the perspective of the market participant rather than the entity, i.e.:

- IFRS 17 measures the liability based on the amount that will likely be paid over the life of the contract plus a risk premium.
- IFRS 13 measures the liability based on the exit price from the perspective of the market participant.

4.3.6 Consequently, this could result in some central government contracts recognising some very large CSM values for contracts where the market is not willing to take on many central government risks without charging a very significant market premium (hence why government often steps in).

4.3.7 Central government entities often do not charge a premium for issuing these types of contracts. Where a premium is not charged to issue a contract, that contract will be onerous and would not become profitable in the future.

4.3.8 Insurers operating in the commercial market would not take on these contracts for no premium, and as mentioned above, would likely demand a very significant premium for taking these on.

4.3.64.3.9 Therefore, there is a risk of measuring the transition value of contracts where no premium is charged, using the fair value approach, with a very significant CSM. This would not be reflective of reality and distort the entity's balance sheet.

4.3.74.3.10 To avoid situations where the transition value of insurance contracts with a £nil premium charged results in a significant CSM being recognised on transition for central government contracts, IFRS 17 is adapted in the FReM as follows:

Central government adaptation: Where the application of IFRS 13 at transition would result in an excessive premium, entities should instead measure the CSM at transition as £nil and the insurance liability measured at value of fulfilment cash flows. For insurance contracts where a £nil premium is charged and the fair value approach is being used to transition to IFRS 17 for those contracts, entities must measure the transition value of those contracts at fulfilment cashflows. -

~~4.3.8—Whether a theoretical premium calculated under IFRS 13 is excessive is a matter of judgement for entities to make. However, this judgement should be made in the context of the purpose of the adaptation, which is to avoid scenarios where the transition value under IFRS 17 has a large CSM when the contract is either breakeven, onerous or expected to generate a much lower level of profit.~~

~~4.3.94.3.11~~ Entities should also be aware of the disclosure requirements in IFRS 17 paragraph 114, relating to the effect of groups of insurance contracts measured using the fair value approach at the transition date on the CSM and insurance revenue in subsequent periods.

4.4—Optional Practical Expedient

~~4.4.1—The FReM includes a practical expedient when using the fair value approach to transition to IFRS 17. The practical expedient allows entities to measure onerous contracts breakeven contracts (or contracts priced to be onerous or breakeven) at fulfilment cashflows at transition. The rationale for this is:~~

- ~~● Entities in central government are not expected to issue profit making insurance contracts. Generally, government will issue insurance contracts where the market is unwilling or unable to provide the cover. These contracts are issued to cover the costs of issuing the contract or at a loss. Therefore, a large scale of contracts which are profitable is not expected.~~
- ~~● The fair value of a group of contracts is expected to be more than the IFRS 17 liability measurement, resulting in the recognition of CSM at transition. This includes onerous contracts as a market participant would require compensation above the risk adjustment to take on the contracts.~~
- ~~● Scenarios where the fair value of an insurance contract is less than the fulfilment cashflows are expected to be extremely rare. A scenario where the fair value calculated under IFRS 13 is less than the fulfilment cash flows could be where a market participant thinks they can fulfil the contract at a lower cost than government and require no risk margin.~~

~~4.4.2—This practical expedient should only be used for insurance contracts which are breakeven or onerous at the transition date (or priced such that they are onerous or breakeven). Contracts which are profitable or priced to generate a profit should be measured using the fair value approach at transition, noting that there is an~~

adaptation to measure the CSM at £nil if the fair value approach would result in an excessive CSM being recognised.

Central government adaptation: Where the full retrospective transition per IFRS 17 paragraph C4(a) is impracticable, for groups of insurance contracts which are breakeven or onerous (or priced to be breakeven or onerous), entities may measure the transition value of these groups of contracts at fulfilment cashflows at the transition date.

4.45 Transition Reliefs

4.4.34.4.1 On transition to IFRS 17, entities must retrospectively apply the new standard to prior periods. This means that the entity must identify, measure, and recognise all their portfolios of insurance contracts as if IFRS 17 has always applied. There are, however, reliefs reporting entities can take advantage of:

- a. IAS 8 paragraph 28 requires several disclosures on the effect of the initial application of a new Standard. However, an entity is not required to present the quantitative information required by paragraph 28(f) of IAS 8 to disclose the amount of the adjustment for each financial statement line affected (and earnings per share) for the current period and each prior period presented³².
- b. An entity need not disclose previously unpublished information about claims development that occurred earlier than five years before the end of the annual reporting period in which it first applies IFRS 17. However, if an entity does not disclose that information, it shall disclose that fact³³.
- c. There are additional reliefs regarding insurance contracts with direct participation features (IFRS 17 paragraph C3(b)) and insurance contracts acquired as part of a business combination within the scope of IFRS 3 before the initial application of IFRS 17 (IFRS 3 paragraph 64N). Entities may choose to apply these reliefs should they meet the qualifying criteria.

Central government interpretation: To improve consistency of central government annual reports and accounts and consolidation of entities within the Whole of Government Accounts (WGA) both transition relief noted in IFRS 17 paragraph C28 is mandated. On transition entities shall not disclose previously unpublished information about claims development that occurred earlier than five years before the end of the annual reporting period in which it first applies IFRS 17.

4.6 Summary of transition approach

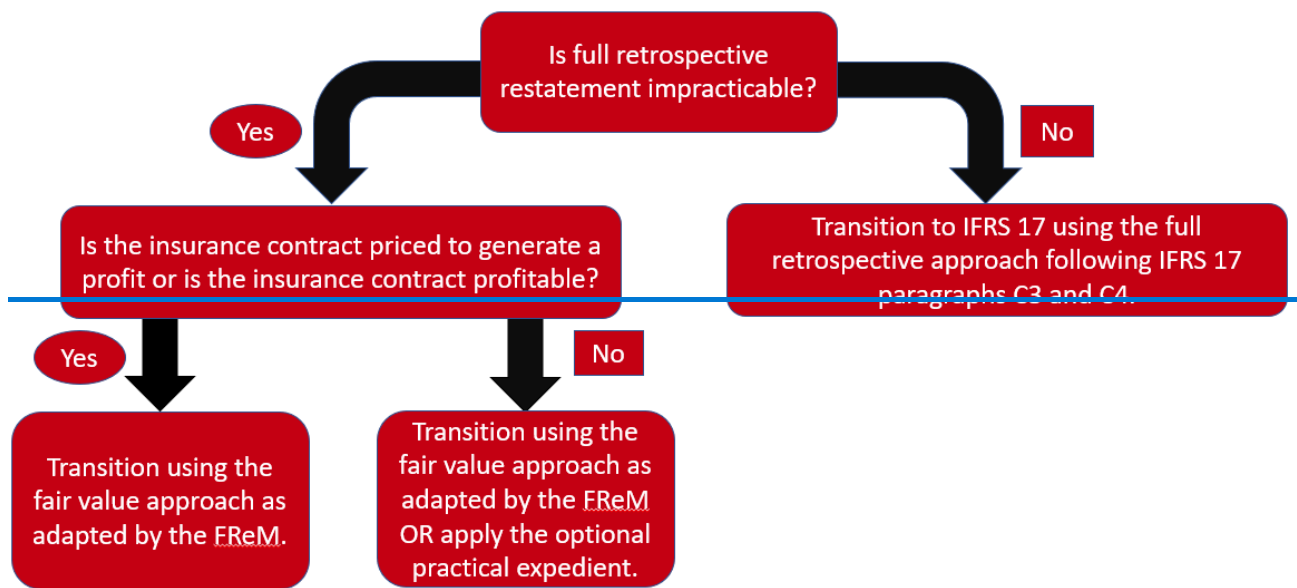
4.6.1 To summarise, the approach to transition to IFRS 17 for entities applying the FReM is as follows:

³² IFRS 17 paragraph C3(a)

³³ IFRS 17 paragraph C28

- a) ~~Restate fully retrospectively per IFRS 17 paragraphs C3 and C4 if practicable.~~
- b) ~~If full retrospective restatement is impracticable, entities should apply the fair value approach as adapted by the FReM.~~
- c) ~~If full retrospective restatement is impracticable and the insurance contract (or group of insurance contracts) is breakeven or onerous (or priced to be breakeven or onerous) then, as a practical expedient, entities may measure the transition value at fulfilment cashflows at the transition date.~~

4.6.2—This is further shown in the flow diagram below:



Chapter 5 – Whole of Government Accounts

~~5.1.1~~

~~5.1.25.1.1~~ Implementation of IFRS 17 presents some challenges to the Whole of Government Accounts (WGA). Disclosures in the WGA will require more detail in the transition year to allow users of the financial statements to understand the impact of IFRS 17 implementation. Both the accounting and disclosure requirements of IFRS 17 are more extensive than IFRS 4, so will require more data to be provided to HM Treasury for WGA purposes.

~~5.1.35.1.2~~ IFRS 17 implementation increases the volume and complexity of eliminating intra-government transactions. The data collection and accounts preparation process will require changes to address this issue.

~~5.1.45.1.3~~ IFRS 17 data collection will be built into the WGA data collection process and entities will need to understand which insurance contracts they hold with other bodies within the WGA boundary (from both the insurer and policyholder perspective). This data will be collected and stored in separate account codes, allowing for intra-governmental transactions to be identified and eliminated.

~~5.1.55.1.4~~ Supplementary data may need to be collected as part of the transition process, particularly to support adjustments to opening balances, and to demonstrate that IFRS 17 has been implemented in a materially consistent fashion across WGA.

~~5.1.65.1.5~~ Entities with intra-group insurance contracts will likely need to consider similar issues for their group financial statements, particularly with respect to eliminations.

Chapter 6 – Budgets and Estimates

6.1 Planned treatment under IFRS 17

6.1.1 Under IFRS 17, insurance liabilities ~~recognised in the SoFP may become more common and~~ will be accounted for ~~differently and~~ in a more consistent way than under IFRS 4. This will affect budget control totals going forward and improve the management of insurance-type arrangements in government. The guiding principle is that the budgeting impacts of insurance transactions should align to the accounting.

6.1.2 The initial budgetary impact for insurance contracts differs based on whether the contract is profitable, break even, partly onerous or wholly onerous (as the accounting transactions also differ). Within central government, many insurance contracts will be often be partly onerous or wholly onerous as they are not provided on commercial terms and are often provided for policy reasons.

6.1.3 The key difference between profitable/ breakeven contracts and onerous contracts is that, for onerous contracts the onerous element of the contract is recognised as expenditure at recognition of the contract. For example, if a contract issued charged £100 but had an expected loss of £120, £20 would be recognised at initial recognition of the contract with the remaining £100 recognised as expenditure over the life of the contract.

6.1.4 That being said, the overall outcome is that net insurance expenditure should be recognised in Resource DEL at the end of the contract when all risks have crystallised (or dissipated).

6.1.5 It is expected that most insurance contracts will be treated as one-off guarantees by the ONS so the budgeting also reflects the [National Accounts](#) impact, but for those treated as standardised guarantees or insurance, a different budgeting treatment may be needed to ensure the budgeting impact also aligns to the fiscal impact of the transactions.

[6.1.6](#) The budgeting treatment reflects both IFRS and national accounts impacts, in a very similar way to provisions. The budgeting treatment recognises the movements of the liability on the SoFP as well as the initial recognition and any movements that appear in the SoCNE. This dual recognition is because in the national accounts the initial recognition of the provision does not score, rather the actual transfer scores when the liability becomes certain- [an insurance liability becomes certain whenever the cash payment is made, or the liability is reclassified from a liability for remaining coverage to a liability for incurred claims \(whichever is earlier\)](#).

~~6.1.6~~[6.1.7](#) Scoring the separate elements to the transaction in this way ensures that the information required for the national accounts is available and allows HM Treasury to control spending in support of the fiscal framework.

~~6.1.7~~[6.1.8](#) In summary, the budgetary impacts are as follows:

- Recognition of losses on onerous insurance contracts: **RAME**

- Payment of incurred claims, [reclassification of the liability from liability for remaining coverage to liability for incurred claims](#), or recognition of expenditure from provision of insurance services: **RDEL**, with a reversal of any **previously recognised** hit to **RAME**.
- Insurance income: **RDEL**
- Revaluations and unwinding of the discount: **RAME**

~~6.1.8~~[6.1.9](#) 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 here will apply where is no previously agreed budgeting approach with HM Treasury.

~~6.1.9~~[6.1.10](#) There are three worked examples at the end of this section showing the budgeting in practice.

6.2 Estimates

6.2.1 Where there is a change in accounting standards there is no net impact on budgets and the Supply sought at the time was correct. Parliament is therefore content not to see a Prior Period Adjustment (PPA) on the voted part of the Estimate (i.e. Part I, Part II).

6.2.2 However, Parliament does require departments to identify the change due to adopting a new accounting standard and the impact on prior years in the 'Note F to an Estimate - Accounting Policy changes'. Further details can be found in paragraphs 3.39 – 3.40 of the Supply Estimates guidance manual.

Budgeting Example 1: Onerous Contract

Scenario:

- entity issues insurance contracts in Y0 for coverage in Y1 and Y2
- £nil premiums charged
- total discounted outflows = £80k, expected to be incurred equally over Y1 and Y2
- for the purpose of this example please ignore experience adjustments, discounting and assume the risk adjustment for non-financial risk crystallises and forms part of the insurance expenditure.

Period	Transaction	SoCNE		SoFP		Budgeting impact	
		DR	CR	DR	CR	DEL	AME
Y0	Recognise £80k loss on contract	80 (insurance expenditure)			-80 (Liability for remaining coverage)		80
Y1	50% of claims occur in Y1 as expected and are fully paid out before the year end			40 (Liability for remaining coverage)	-40 (Cash)	40	-40
Y2	50% of claims occur in Y2 as expected and are fully paid out before the year end			40 (Liability for remaining coverage)	-40 (Cash)	40	-40

N.B. in Y1 and Y2 the switches from AME to DEL due to the insurance risk crystallising and being paid out- similar to provisions.

Budgeting Example 2: Partly Onerous Contract

Scenario:

- entity issues insurance contracts in Y0 for coverage in Y1 and Y2
- premiums charged = £50k, charged in Y0 for full coverage period
- total discounted outflows = £80k, expected to be incurred equally over Y1 and Y2
- for the purpose of this example please ignore experience adjustments, discounting and assume the risk adjustment for non-financial risk crystallises and forms part of the insurance expenditure.

Period	Transaction	SoCNE		SoFP		Budgeting impact	
		DR	CR	DR	CR	DEL	AME
Y0	Entity issues 100 insurance contracts at charging £0.5k each			50 (Cash)	-50 (Liability for remaining coverage)		
Y0	Recognise £30k loss on contract	30 (Insurance expenditure)			-30 (Liability for remaining coverage)		30
Y1	50% of claims occur in Y1 as expected and are fully paid out before the year end	40 (Insurance expenditure)			-40 (Cash)	40	
Y1	Recognise 50% insurance revenue		-25 (Insurance income)	25 (Liability for remaining coverage)			-25

Y1	Reversal of 50% of loss component		-15 (Reversal of contract losses)	15 (Liability for remaining coverage)			-15
Y2	50% of claims occur in Y2 as expected and are fully paid out before the year end	40 (Insurance expenditure)			-40 (Cash)	40	
Y2	Recognise 50% insurance revenue		-25 (Insurance income)	25 (Liability for remaining coverage)		-25	
Y2	Reversal of 50% of loss component		-15 (Reversal of contract losses)	15 (Liability for remaining coverage)			-15

N.B. in Y1 and Y2 the switches from AME to DEL due to the insurance risk crystallising and being paid out- similar to provisions.

Budgeting Example 3: Profitable Contract

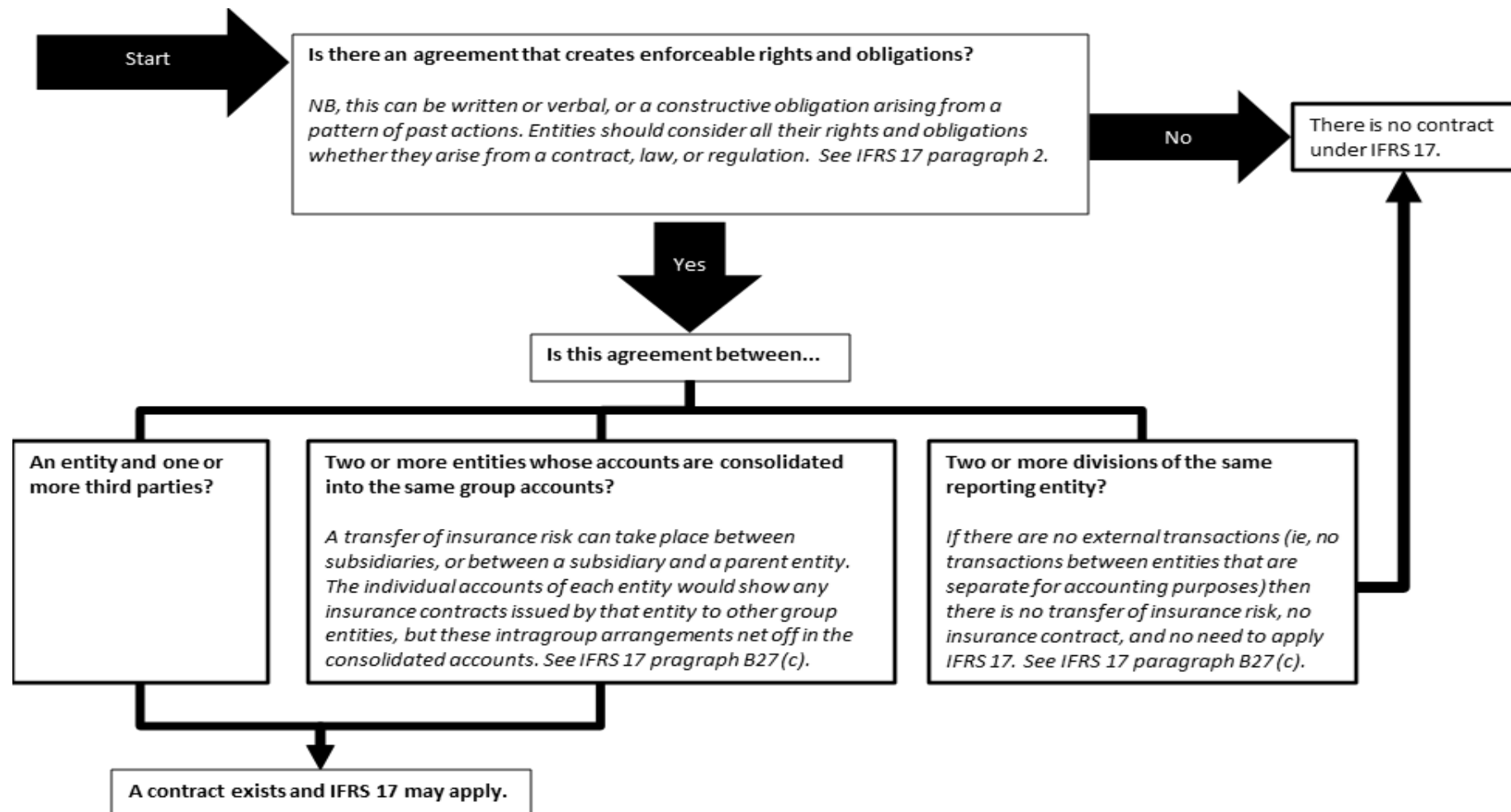
Scenario:

- entity issues insurance contracts in Y0 for coverage in Y1 and Y2
- premiums charged = £100k, charged in Y0 for full coverage period
- total discounted outflows = £80k, expected to be incurred equally over Y1 and Y2
- for the purpose of this example please ignore experience adjustments, discounting and assume the risk adjustment for non-financial risk crystallises and forms part of the insurance expenditure.

Period	Transaction	SoCNE		SoFP		Budgeting impact	
		DR	CR	DR	CR	DEL	AME
Y0	Entity issues 100 insurance contracts at charging £1k each, with expected claims being £80 over the life of the contract			100 (Cash)	-100 (Liability for remaining coverage)		
Y1	50% of claims occur in Y1 as expected and are fully paid out before the year end	40 (Insurance expenditure)			-40 (Cash)	40	
Y1	Recognise 50% insurance revenue		-50 (Insurance income)	50 (Liability for remaining coverage)		-50	
Y2	50% of claims occur in Y2 as expected and are fully paid out before the year end	40 (Insurance expenditure)			-40 (Cash)	40	

Y2	Recognise 50% insurance revenue		-50 (Insurance income)	50 (Liability for remaining coverage)		-50
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Appendix 1 - IFRS 17 Decision Tree



A contract exists. Does it require one party to make a payment to a second party, depending on the outcome of a future event?

NB the payments can be in money, or in kind. For example, this would include an agreement to arrange for an engineer to come and fix a broken machine, or an agreement to replace the machine, as well as an agreement to make a cash payment to support the purchase of a replacement machine. See IFRS 17 paragraph B6.



Is the future event that would trigger payments *uncertain*?

Without uncertainty, there is no risk. IFRS 17 paragraph B3 states that "at least one of the following is uncertain at the inception of an insurance contract: (a) the probability of an insured event occurring; (b) when the insured event will occur; or (c) how much the entity will need to pay if the insured event occurs."

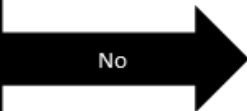


Does the *specified* uncertain future event adversely affect the second party to the contract?

For example, flood damage to a building owned or used by one party to the contract is specific to that party. In contrast, if a contract requires a payment if there is a general increase in floods in a region, the variable is not specific to a party in the contract.



The contract requires one party (the issuer) to compensate a second party when a specified, uncertain future event adversely affects that second party (the policyholder). IFRS 17 may apply.



The first party to the contract has no requirement to compensate the second party when a specified, uncertain future event adversely affects that second party. IFRS 17 does not apply.

The agreement is a contract that transfers insurance risk and IFRS 17 may apply. Is the insurance risk significant?

IFRS 17 paragraph B17: "Insurance risk is significant if, and only if, an insured event could cause the issuer to pay additional amounts that are significant in any single scenario, excluding scenarios that have no commercial substance (ie no discernible effect on the economics of the transaction)."

NB 'significant' here has a different meaning from 'significant' or 'material' in other accounting contexts. The scenario that leads to the issuer paying significant additional amounts does not have to be probable, it only has to have commercial substance. If the scenario is very unlikely, then its impact on the valuation of the insurance contract may be immaterial, but significant insurance risk may still be transferred and IFRS 17 would still apply.

Note also that the significance must be assessed on a contract-by-contract basis.

No

The agreement is in a category specifically excluded from IFRS 17. IFRS 17 does not apply.

Yes

Does one of the exceptions set out in IFRS 17 paras 7 and 8 apply (as adapted by the FReM):

7 (a): "warranties provided by the manufacturer, dealer, or retailer in connection with the sale of its goods or services to a customer"

7 (b): "employers assets and liabilities from employee benefit plans ... and retirement benefit obligations from defined benefit pension plans"

7 (c): "contractual rights or contractual obligations contingent on the future use of, or the right to use, a non-financial item" (eg licence fees, royalties)

7 (d): "residual value guarantees provided by a manufacturer, dealer or retailer and a lessee's residual value guarantees when they are embedded in a lease"

7 (e): "financial guarantee contracts" (IFRS 9 is applied)

7 (f): "contingent consideration payable or receivable in a business combination"

7 (g): "insurance contracts in which the entity is the policyholder, unless those contracts are reinsurance contracts held"

8: If an entity has a contract which meets the definition of an insurance contract but is primarily intended to provide services for a fixed fee, it must apply IFRS 15 instead of IFRS 17.

8A: Contracts that limit the compensation for insured events to the amount otherwise required to settle the policyholder's obligation created by the contract. (IFRS 9 is applied)

Yes

No

There is "a contract 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 agreement should be treated as an insurance contract under IFRS 17.