

IFRS Interpretations Committee (IFRIC) Tentative Agenda Decision

Multi-currency Groups of Insurance Contracts (IFRS 17 *Insurance Contracts* and IAS 21 *The Effects of Changes in Foreign Exchange Rates*)

The IFRIC received a request about how to account for insurance contracts that generate cash flows in more than one currency.

The request asked:

- a. whether an entity considers currency exchange rate risks when applying IFRS 17 to identify portfolios of insurance contracts; and
- b. how an entity applies IAS 21 in conjunction with IFRS 17 in measuring a group of insurance contracts that generate cash flows in more than one currency (a multi-currency group of insurance contracts).

Identifying portfolios of insurance contracts

IFRS 17 requires an entity to recognise and measure groups of insurance contracts. The first step in establishing groups of insurance contracts is to identify portfolios of insurance contracts. Paragraph 14 of IFRS 17 states that ‘a portfolio comprises contracts subject to similar risks and managed together’. The request asks whether currency exchange rate risks are among the risks an entity considers when assessing whether insurance contracts are ‘subject to similar risks’.

IFRS 17 defines financial risk and insurance risk (a non-financial risk). Financial risk is defined to include ‘the risk of a possible future change in ... [a] currency exchange rate’. When IFRS 17 requires an entity to consider or reflect only particular risks (for example, only non-financial risk), it explicitly refers to the risks to be considered or reflected. Consequently, the IFRIC concluded that, because paragraph 14 of IFRS 17 refers to ‘similar risks’ without specifying any particular types of risk, an entity is required to consider all risks—including currency exchange rate risks—when identifying portfolios of insurance contracts. However, ‘similar risks’ do not mean ‘identical risks’. An entity could therefore identify portfolios of contracts that include contracts subject to different currency exchange rate risks. The IFRIC observed that what an entity considers to be ‘similar risks’ will depend on the nature and extent of the risks in the entity’s insurance contracts.

Measuring a multi-currency group of insurance contracts

An entity measures a group of insurance contracts at the total of the fulfilment cash flows and the contractual service margin. Paragraph 30 of IFRS 17 states that ‘when applying IAS 21 ... to a group of insurance contracts that generate cash flows in a foreign currency, an entity shall treat the group of contracts, including the contractual service margin, as a monetary item’.

Paragraph 8 of IAS 21 defines monetary items as ‘units of currency held and assets and liabilities to be received or paid in a fixed or determinable number of units of currency’ and paragraph 20 describes a foreign currency transaction as ‘a transaction that is denominated or requires settlement in a foreign currency’. Paragraphs 21–24 of IAS 21 require an entity:

- a. to recognise on initial recognition a foreign currency transaction in the functional currency at the spot exchange rate at the date of the transaction;
- b. to determine the carrying amount of a monetary item in conjunction with other relevant Accounting Standards; and
- c. to translate at the end of the reporting period foreign currency monetary items into the functional currency using the closing rate.

The requirements in both IFRS 17 and IAS 21 refer to transactions or items that are denominated or require settlement in a single currency. IFRS Accounting Standards include no explicit requirements on how to determine the currency denomination of transactions or items that generate cash flows in more than one currency.

Therefore, the IFRIC observed that, in measuring a multi-currency group of insurance contracts, an entity:

- a. applies all the measurement requirements in IFRS 17 to the group of insurance contracts, including the requirement in paragraph 30 to treat the group—including the contractual service margin—as a monetary item.
- b. applies IAS 21 to translate at the end of the reporting period the carrying amount of the group—including the contractual service margin—at the closing rate (or rates).
- c. develops an accounting policy to determine on initial recognition the currency or currencies in which the group—including the contractual service margin—is denominated. The entity uses its judgement in developing and applying an accounting policy based on its specific circumstances and the terms of the contracts in the group. The accounting policy must result in information that is relevant and reliable (as described in paragraph 10 of IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*) and be applied consistently for similar transactions, other events and conditions (paragraph 13 of IAS 8). The entity could determine that the group—including the contractual service margin—is denominated in a single currency or in the multiple currencies of the cash flows in the group. The entity cannot simply deem the contractual service margin for the group to be denominated in the functional currency because simply deeming such a denomination would, in effect, fail to treat the contractual service margin as a monetary item as required by paragraph 30 of IFRS 17.

In applying IFRS 17, there is a single contractual service margin for the group of insurance contracts. Accordingly, if an entity were to determine that for the purpose of applying IAS 21 the contractual service margin is denominated in the multiple currencies of the cash flows in the group, the entity would:

- a. assess whether the group of contracts is onerous considering the contractual service margin as a single amount, after translation into the functional currency; and
- b. determine the amount of the contractual service margin to recognise in profit or loss by applying a single method of determining the coverage units provided in the current period and expected to be provided in the future.

In the light of its analysis, the IFRIC considered whether to add to the work plan a standard-setting project on how to account for the foreign currency aspects of insurance contracts. The IFRIC observed that it has not obtained evidence that such a project would be sufficiently narrow in scope that the International Accounting Standards Board (IASB) or the IFRIC could address it in an efficient manner. Consequently, the IFRIC [decided] not to add a standard-setting project to the work plan.

Invitation to comment

The MASB encourages interested parties to submit their responses by email to technical@masb.org.my before **27 July 2022**.

There are no specific questions raised but comments are most helpful if they contain a clear rationale and include any alternative the IFRIC should consider.