Coverage Unit

Version	Date	Comments
.0	23 Apr 2019	Draft for discussion
0.1	14 Jun 2019	Incorporate comments from SAS meeting discussions
1.0	17 Jun 2019	First circulation

This IFRS17 Working Paper aims to facilitate discussion among actuaries and other stakeholders to capture the range of opinions on the application of IFRS17 in the Singapore context and is not meant to serve as mandatory practice notes.

Any interpretation of IFRS17 set out in this Paper represents a plausible treatment given the text of IFRS17. However, it shall neither be construed as the only possible treatment nor the agreed interpretation for Singapore insurers. Users of this Working Paper shall be mindful that differences in the exact fact pattern and operating context facing each insurer may drive different interpretations. Users shall also be mindful that for the same fact pattern and operating context, there is scope for the substance of same transaction to be articulated differently depending on how the transaction is analysed. (For example, in substance, cash flows from a call option with strike price $X on an asset is equivalent to the combined cash flow from the underlying asset and a put option with strike price $X on the asset, less cash of $X.) Differences in articulation can give rise to a range of plausible treatments. An insurer remains responsible for justifying its choice of treatment after discussion with its auditor. Opinions expressed in the working papers are not representative of that of the Singapore Actuarial Society.

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1. IFRS17 Standards

The key passages in the IFRS17 standards that relate to the Coverage Unit are outlined below:

Paragraph 44

For insurance contracts without direct participation features, the carrying amount of the contractual service margin of a group of contracts at the end of the reporting period equals the carrying amount at the start of the reporting period adjusted for:

> (e) the amount recognised as insurance revenue because of the transfer of services in the period, determined by the allocation of the contractual service margin remaining at the end of the reporting period (before any allocation) over the current and remaining coverage period applying paragraph B119.

Paragraph 45

For insurance contracts with direct participation features (see paragraphs B101–B118), the carrying amount of the contractual service margin of a group of contracts at the end of the reporting period equals the carrying amount at the start of the reporting period adjusted for the amounts specified in subparagraphs (a)–(e) below. An entity is not required to identify these adjustments separately. Instead, a combined amount may be determined for some, or all, of the adjustments. The adjustments are:

> (e) the amount recognised as insurance revenue because of the transfer of services in the period, determined by the allocation of the contractual service margin remaining at the end of the reporting period (before any allocation) over the current and remaining coverage period, applying paragraph B119.

Paragraph B119

An amount of the contractual service margin for a group of insurance contracts is recognised in profit or loss in each period to reflect the services provided under the group of insurance contracts in that period (see paragraphs 44(e), 45(e) and 66(e)). The amount is determined by:

> (a) identifying the coverage units in the group. The number of coverage units in a group is the quantity of coverage provided by the contracts in the group, determined by considering for each contract the quantity of the benefits provided under a contract and its expected coverage duration.
>
> (b) allocating the contractual service margin at the end of the period (before recognising any amounts in profit or loss to reflect the services provided in the period) equally to each coverage unit provided in the current period and expected to be provided in the future.
>
> (c) recognising in profit or loss the amount allocated to coverage units provided in the period.

IASB has proposed several amendments to IFRS 17 and intends to issue an exposure draft in June 2019. The key amendments, which will affect the determination of coverage unit, include:

1) To clarify that the definition of the coverage period for insurance contracts with direct participation features include periods in which investment-related services are provided.

2) In the general measurement model the contractual service margin is allocated on the basis of coverage units that are determined by considering both insurance coverage and any investment return service.

3) To disclose the approach to assessing the relative weighting of the benefits provided by insurance coverage and investment-related services or investment return services, as part of the disclosure requirements in paragraph 117 of IFRS 17 related to significant judgements and changes in judgements made in applying IFRS 17.

2. Interpretation of Standards

The accounting requirements for selection of Coverage Unit has been analyzed and discussed in-depth in the February 2018 and May 2018 TRG meeting, supplemented by several IASB staff papers. Key outcome of these discussions is summarized below:

1) IFRS 17 does not prescribe the method to determine the quantity of benefits (i.e. CU). Determination of CUs involves judgements and estimates to best achieve the principle of reflecting the services provided in the period. Different methods can be used as long as they achieve the principle. Judgement and estimates should also be determined systematically and rationally.

2) Coverage units should be determined by considering the following services the contract provide to the policyholder:

   - the insurance and investment return services for contract without direct participating features. (As mentioned above, IASB has agreed to propose an amendment so that CUs in the GMM are determined by considering both insurance coverage and a newly defined investment return service.)

   - the insurance and investment related service for contract with direct participating features

   - the investment services for investment contract with discretionary participating features

3) The purpose of the quantity of benefits is to give more or less weight to contracts in a group depending on the level of service provided over time for a given contract. Any measure that allows for the appropriate representation of the relative level of service in an insurance contract within a group is acceptable.

4) The quantity of benefits provided in a period is based on the amount that the entity is standing ready to pay to the policyholder, rather than the likelihood of the payment occurring.

5) Coverage units should reflect the different levels of benefits provided by different contracts within a group and differing levels of cover across periods. Coverage units should be reassessed at the end of each reporting period.

6) The expected coverage duration and calculation of future coverage units should reflect the expected policy decrements. For life insurance contracts, to the extent that claims, lapses and other terminations impact the level of services provided in future period, such decrements should be reflected in future coverage units.

7) The Standard does not specify whether discounting is required in determining coverage units.

In addition, selection of coverage unit involves assessing the relative weighting of benefits provided by the contract between:

- Insurance service and investment-related service/investment-return service
- Multiple type of insurance coverages within insurance service

The approach to combining different services and insurance coverages would involve judgement and need to be disclosed.

3. How it applies to Singapore

Selecting the CU of each portfolio is a matter of judgement. It is likely that different industry players use different coverage unit measures even for the products with similar features. Companies might also adopt different approaches to assess the relative weighting of benefits of insurance and investment services.

The table below offers some possible choices of coverage unit measures for the common products sold in Singapore.

Product type	**Possible Coverage Unit Measure**
Term insurance	*Sum assured* for level term insurance *Increasing sum assured* for increasing term insurance For term with return of premium on maturity, CU might need to consider the investment return service as well as the insurance service. Where the contract provides multiple types of benefit (e.g. death claim + critical illness claims, fixed amount claim + variable/severity-based amount claims), judgement is required as to the appropriate approach of aggregating them. No industry consensus has yet formed around these areas. Several methods of assessing the relative weight of each component has been suggested, and the method that would best achieve the objectives would depend on the context and the portfolio in question: • Using the average claim size to assign relative weight between a fixed amount benefit and a variable amount benefit. • Using premiums or claim probability to assign relative weight between different benefit types. • Using the maximum amount payable among all components under each contract. • Taking simple sum of all benefits payable under each contract.
NonPar Endowment	*Death benefit / Maturity payout*
Universal life	*Max (Death benefit, Account Value)*

Medical reimbursement	There is no clear choice of coverage unit for these products, in particular, where there are multiple types of benefits being offered. Significant judgement may be required. Some of the possible coverage units include: • Claim limit for the period • Average claim size based on policyholders' risk profile • Premiums for the period (if it provides good representation of the quantity of benefit)
Critical Illness	Accelerated CI rider: *total claim benefit* Early stage CI Cover: *remaining SA* that policyholder could claim in the period Multiple CI Cover: *maximum claimable amount* in a period
Annuity	Immediate annuity: *the annuity amount* Deferred annuity: *total premium paid before vesting and the annuity amount after vesting*
Investment linked products	Investment linked contracts provide substantial investment service. Some regular premium products also offer significant protection benefit. *Total claim benefit* could be used as a simple measure that captures both investment and insurance services. The benefit payable from the unit fund represents the quantity of investment-related service provided, and the sum-at-risk measures the quantity of insurance service provided.
Participating products	Similar to investment linked contracts, participating contracts can provide significant investment as well as insurance services. *Total claim benefit* (including non-guaranteed benefit) might be used as a simple measure for total quantity of benefits.