Online Webinar

Takaful & Insurance Contract Under IFRS-17

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Discussion Topics:

- Background of IFRS-17
- Objective and scope of IFRS-17
- Significant judgements in applying IFRS -17
- Financial accounts and reports under IFRS-17
- General presentation and disclosure in financial statement of takaful
- Other disclosure requirements of regulator under ICP-20
- Conceptual framework for financial reporting of Islamic Insurance/Takaful
- The qualitative characteristics of accounting information
- Basic Requirements of Takaful

Background of IFRS -17

What IS IFRS foundation?

- The IFRS Foundation is a not-for-profit, public interest organization.
- It develops a single set of high-quality, understandable, enforceable, and globally accepted accounting standards—IFRS Standards.
- It promotes and facilitate the adoption of the standards.
- IFRS Standards are set by the IFRS Foundation's standard-setting body, the International Accounting Standards Board.

What is IFRS-17?

- IFRS 17 is the first truly international, comprehensive accounting standard for insurance contracts;
- IFRS 17 replaces interim standard –IFRS-4 – which requires consistent accounting for all insurance contracts based on current measurement model.
- Provides useful information about the profitability of insurance contracts;
- provides - updated information about obligations, risks and performance of insurance contracts.
- Increases transparency in financial information reported by insurance companies;
- IFRS 17 applies to all entities that issue insurance contracts and hence primarily going to affect the entities in the insurance industry.

International Financial Reporting Standards (IFRS) in Practice

1.First-time Adoption of International Financial Reporting Standards - One (|FRS1).

2. Share-based Payment (IFRS-2).

3. Business Combinations (IFRS-3).

4. Non-current Assets Held for Sale and Discontinued Operations (|FRS-5).

5. Exploration for and Evaluation of Mineral Resources (IFRS-6).

6. Financial Instruments: Disclosures (|FRS-7).

7. Operating Segments (IFRS-8).

8. Financial Instruments (IFRS-9).

9. Consolidated Financial Statements (IFRS-10).

10. Joint Arrangements (IFRS-11).

11. Disclosure of Interest in Other Entities (|FRS-12).

12. Fair Value Measurement (|FRS-13).

13. Regulatory Deferral Accounts (IFRS-14).

14. Revenue from Contracts with Customers (IFRS-15).

15. Leases (|FRS-16).

16. Insurance Contracts (IFRS-17).

Why IFRS?

- IFRS Standards bring transparency by enhancing the international comparability and quality of financial information, enabling investors and other market participants to make informed economic decisions.
- IFRS Standards strengthen accountability by reducing the information gap between the providers of capital and the people to whom they have entrusted their money.
- Standards provide the information needed to hold management to account. As a source of globally comparable information.
- IFRS Standards are also of vital importance to regulators around the world.
- IFRS Standards contribute to economic efficiency by helping investors to identify opportunities and risks across the world, thus improving capital allocation.

Evolution of IFRS-17

- In March 2004 the International Accounting Standards Board (Board) issued IFRS 4 Insurance Contracts. IFRS 4 was an interim standard.
- IFRS 4 permitted entities to use a wide variety of accounting practices for insurance contracts, reflecting national accounting requirements.
- In May 2017, the FAS Board completed its project on insurance contracts with the issuance of IFRS 17 Insurance Contracts. IFRS 17 replaced IFRS 4.
- In June 2020, the Board issued Amendments to IFRS 17. The objective of the amendments was to assist entities implementing the Standard.
- In December 2021, the Board issued Initial Application of IFRS.

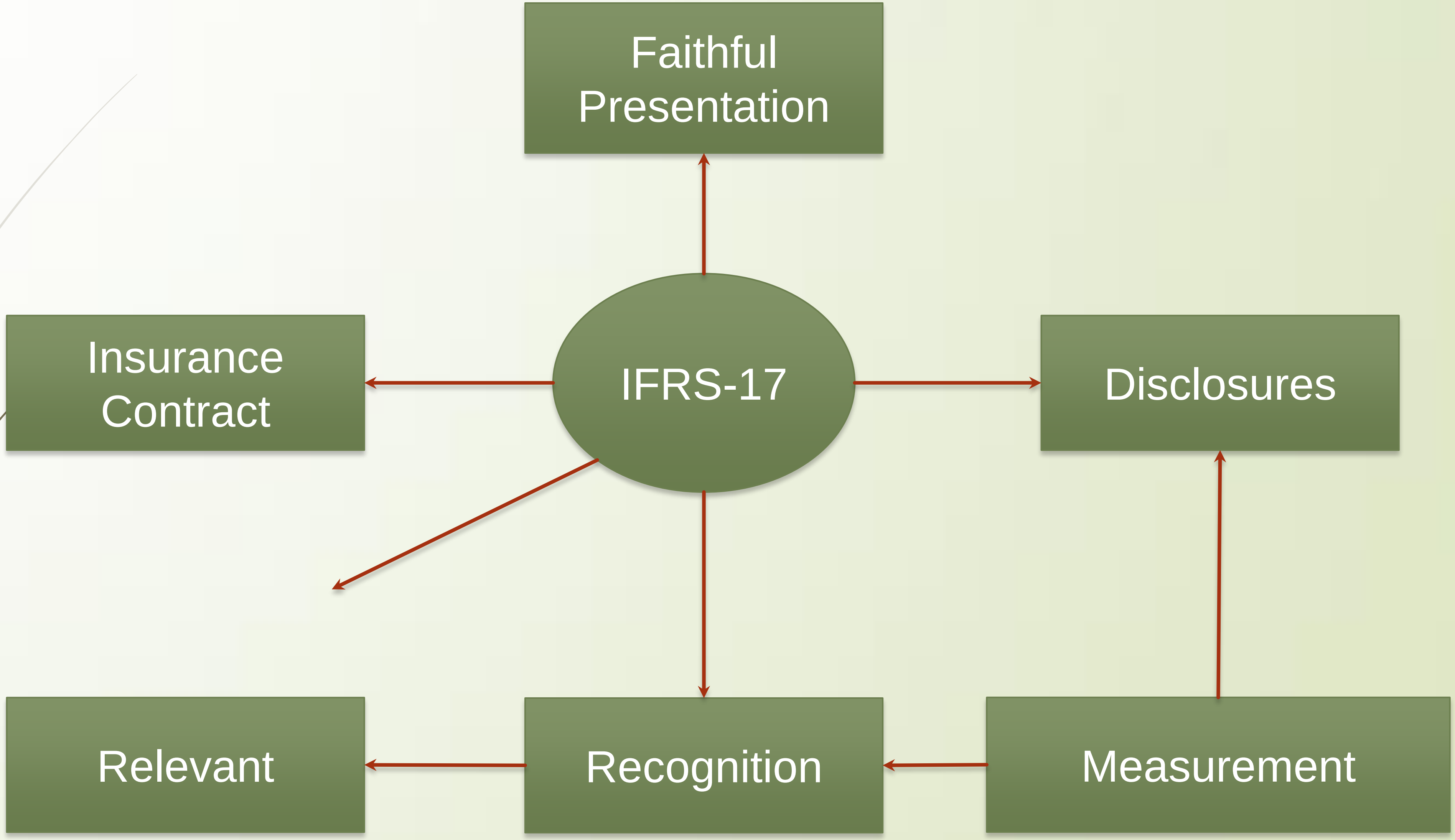
Key principles of IFRS- 17

- Identify risks which an insurer accept from policyholders in order to indemnify or provide financial assistance if and when a future uncertain event adversely affects the policyholders.
- Divide the contracts into groups for recognition and measurement
- Present separately insurance revenue, insurance service, expenses insurance finance (income/ expenses)
- Disclose information to enable users of financial statements. To assess the effect of the contracts have on the financial position, financial performance and cash flows of the insurer/operator.

Objective and scope of IFRS-17

Objectives of IFRS-17

- IFRS 17 Insurance Contracts established principles for the recognition, measurement, presentation and disclosure of insurance contracts within the scope of the Standard.
- The objective of IFRS 17 is to ensure that an entity provides relevant information that faithfully represents those contracts.
- A contract is 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.
- An entity shall identify portfolios of insurance contracts. A portfolio comprises contracts subject to similar risks and managed together.

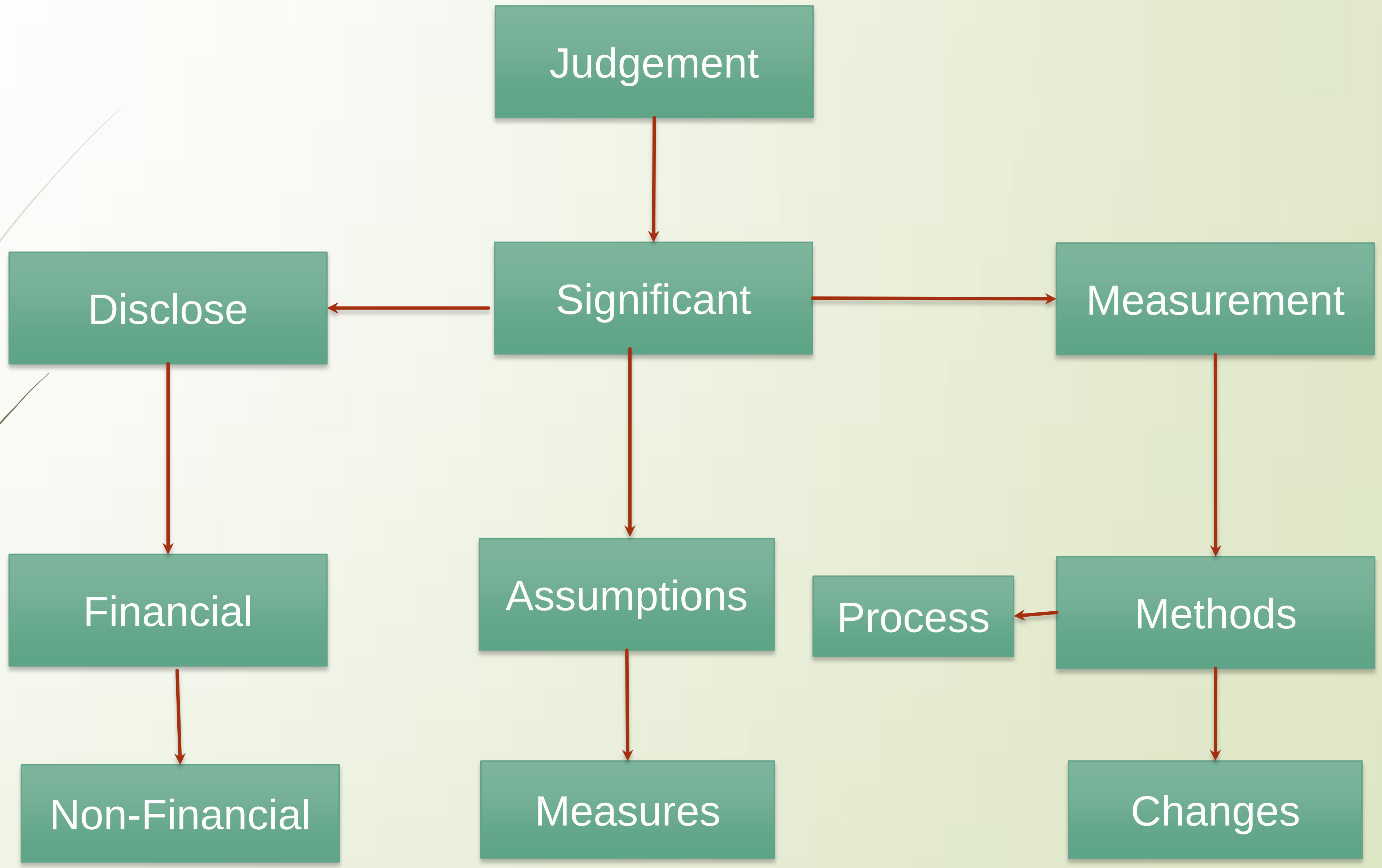

Faithful Presentation
Insurance Contract
IFRS-17
Disclosures
Relevant
Recognition
Measurement

What need to be Disclosed?

- An entity shall disclose information that enables users of its financial statements to evaluate the nature, amount, timing and uncertainty of future cash flows.
- For each type of risk arising from contracts within the scope of IFRS 17, an entity shall disclose:
  - the exposures to risks and how they arise;
  - the entity’s objectives, policies and processes for managing the risks and the methods used to measure the risks; and
  - any changes in (a) or (b) from the previous period.

Significant judgements in applying IFRS -17

- An entity shall disclose the significant judgements and changes in judgements made in applying IFRS 17.
- the methods used to measure insurance contracts within the scope of IFRS 17 and the processes for estimating the inputs to those methods.
- any changes in the methods and processes for estimating inputs used to measure contracts, the reason for each change, and the type of contracts affected.
- to determine the risk adjustment for non-financial risk.
- to determine investment components.


Judgement
Significant
Disclose
Measurement
Financial
Assumptions
Process
Methods
Non-Financial
Measures
Changes

Disclosure of Significant Accounting Policies

- Accounting policies refer to the accounting principles, bases rules and methods which have been adopted by the Islamic Insurers management for the preparation and publication of the financial statement.
- The financial statements must contain a clear and precise description of the significant accounting policies used for the preparation and publication of the financial statements.
  - The accounting policies that represent a choice among acceptable alternative accounting methods (e.g., the depreciation method used).
  - The accounting policies adopted by the management of the Islamic insurers but which are not consistent with the concepts of financial accounting for Islamic Insurers, if any.
  - The accounting policies adopted by the management of the Islamic insurers for revenue, gain and loss recognition.
  - The accounting policies adopted by the Islamic Insurers management for the recognition and determination of doubtful receivables and the policies of writing-off debts.
  - The policies, bases and methods adopted by the insurers management for the revaluation of assets, liabilities and restricted investments to their cash equivalent value, if applicable.
  - The accounting policies adopted by Islamic insurer management for the consolidation of the financial statements of subsidiaries, if any.

Financial Accounts and reports under IFRS-17

Balance Sheet:

- IFRS 17 requires a current measurement model, where estimates are re-measured in each reporting period.
- The measurement is based on the general measurement model of discounted, probability-weighted cash flows, a risk adjustment, and a contractual service margin (‘CSM’) representing the unearned profit of the contract.

Income statement:

- Requirements in IFRS 17 align the presentation of revenue with other industries.
- Investment components are excluded from insurance revenue.
- Under IFRS 17, entities have an accounting policy choice to recognize the impact of changes in discount rates in profit or loss or in other comprehensive income (‘OCI’) to reduce some volatility in profit or loss.

Disclosures:

- IFRS 17 disclosures will be more detailed than required under current reporting frameworks.
- Disclosures will provide additional insight into key judgements and profit emergence.
- Disclosures are designed to allow greater comparability across entities.

Measurement Models

	General measurement model (GMM) or Building Block Approach (BBA)	Premium allocation approach (PAA)	Variable fee approach
Why needed?	Default model for all insurance contracts	To simplify for short term contracts with little variability	To deal with participating business where payments to policyholders are linked to underlying items like assets
Types of contract	• Long-term and whole life insurance, protection business • Certain annuities • Universal life • Reinsurance written • Certain general insurance contracts	• General insurance • Short-term life and certain group contracts	• Unit-linked contracts and equity index-linked contracts etc.
Mandatory	Mandatory	Optional	Mandatory

Disclosures

Accounts

- Detailed roll forward schedules and reconciliations
- Reconciliation of sources of profit
- Contracts written in the period
- Relationship interest and investment return

Significant judgments

- Processes to estimate inputs to methods
- Effect of changes in methods and inputs
- Confidence level for determining risk adjustment
- Yield curve(s) used to discount cash flows

Nature & Extent of Risks

- Nature and extent of risks
- Insurance risk on gross/net basis
- Concentrations of insurance risk and claims development
- Quantitative disclosures about non-insurance risks

Objectives of Financial Accounting Reports

- Information about the IFI's compliance with the Sharia and its objectives and to establish such compliance; and information regarding the manner in which prohibited earnings and expenditures, if any, were recorded and dealt with.
- This information should be directed principally at assisting the user in evaluating the adequacy of the IFI's capital to absorb losses and business risks.
- Limitations: Limitations of information provided by financial accounting and reports. Financial reports are incapable of providing all relevant information that might be required by those who use them.
- Financing accounting is concerned mainly with measuring the financial effect of transactions and order events on the IFI's financial position, results of operations and cash flows.
- The information currently provided by financial accounting is predominantly historical in nature which may or may not be indicative of the future.
- Limitations resulting from cost and benefit consideration – Information which financial accounting produces has costs associated with its preparation, presentation and usage.

Summary of Financial Accounting & Reporting

- In financial accounting, transactions are recorded classified, summarized, and finally, reported by way of financial statements.
- The financial statements of business entity presents the financial performance of the entity over a specified period of time and show the position of the entity's assets, liabilities and equities at the end of that period.
- From the financial statements, the user of the statements will be aware of the income generated and expenses incurred by the entity over the period of time.
- A user can identify the key income generating function of the business entity, and the expenses that have the most impact on the performance of the business.
- The financial performance of the entity, that is, whether it is a profit or loss making concern, is communicated through the entity's financial statements.
- The liquidity position including the amount of cash the entity holds as at end of the period can also be known from the financial statements.
- The financial reporting process commences with the recording of transactions by way of journal entries. In journal entries, the debits are always equal to the credits. The convention of journal entries is the same in both conventional and Islamic accounting. They differ in recognition, measurement, presentation and disclosures of the financial transactions.

Objectives of Financial Accounting Reporting

- The Objectives of general purpose financial reporting is to provide financial information about the reporting entity that is useful to existing and potential investors, lenders and other creditors in making decisions about providing resources to the entity.
- Those decisions involve buying, selling, or holding equity and debt instruments, and providing or setting loans and other forms of credit.
- Main objectives are:
  - To communicate with the various users of financial statements by fulfilling their general and specific information needs.
  - To allow the existing investors to determine the reporting entity's profitability and cash generating ability to decide whether to maintain or divest their investment.
  - To attract potential investors by allowing them to reliably estimate further performance of the reporting entity based on its past performance.
  - To demonstrate creditworthiness of the reporting entity by presenting the assets and liabilities position of the entity.
  - To comply with the requirements set by the regulatory authorities, such as the securities commission, tax authority or central bank, by providing general and specific information as required by them.

Limitations of Financial Accounting Reporting

- Investors, regulators, employees, and the general public rely on the financial reporting system which requires companies to disclose details of their financial condition annually but IFRS is less detailed.
- Other significant disadvantages of IFRS relate to implementation costs. The cost for businesses that operate only at the national level.
- One of the disadvantages of adopting a single standard is that capital markets are not the same in different countries. Businesses in a country may depend primarily on bank financing to raise capital; their financial statements may want to emphasize prudence and a strong balance sheet, as banks only want repayment with interest; they do not speculate.
- By following single standards and guidelines, businesses risk losing flexibility in part of their financial statement.

Information needed by IFI stakeholders

Financial reports of the IFIs should provide the following types of information.

- Information about the IFI's compliance with the Islamic Shariah and its objective, and to establish such compliance.
- Information regarding the manner in which prohibited earnings and expenditure, if any, where recorded and dealt with.
- Information about IFI's economic resources and related obligations, and the effect of transactions other events and circumstances on the IFI's economic resources and related obligations.
- Information to assist in determining *zakah*.
- Information about the IFI's discharge of its fiduciary responsibilities.
- Information about the IFI's discharge of its social responsibilities.

Preparation and Presentation of Accounting Information

Materiality:

- Information is material if its omission or misstatement could influence the decisions that users make on the basis of an IFI’s financial information.
- Materiality and adequate disclosure are interrelated and relate also to the concepts or relevance and reliability. Materiality and adequate disclosure are interrelated.
- In general, an item is regarded material if its omission, non-disclosure or misstatement would result in distortion of the information being presented in the financial statements.

Cost of information – The benefits of providing financial reporting information should justify the costs of providing that information. Information, like any other commodity, has a cost either for the IFI or society as a whole.

IFRS 17 – what is happening

(in Bangladesh)?

- Back in September 2015, GoB (Government of Bangladesh) promulgated an Act titled as 'Financial reporting Act 2015'.
- It was decided that separate regulatory body will be established in the name - Financial reporting council.
- This council will be constituted by eleven members headed by Chairman, who will act as chief executive.
- Councils objectives powers and functions have been prescribed in the Act.
- It will have four executive divisions as follows :
  - ➔ Standard setting divisions
  - ➔ Financial reporting and monitoring divisions
  - ➔ Audit practices review divisions
  - ➔ Enforcement divisions

Responsibilities of each division has been fixed by the Act.

Why IFRS 17 need urgent implementation?

- It is more transparent
- Ensure fair treatment of transactions
- Provides more information for decisions
- Reflects features of insurer’s cash funds
- Reflects different components if profitability
- It helps to frame consistent accounting framework for all insurance contracts
- Provide ways to frame Takaful reporting principles

General Presentation and Disclosures in Financial Accounting of Takaful

General Disclosures of Takaful

- shall appoint a Shariah Advisor in accordance with the provisions of these Rules;
- shall appoint a Shariah compliance auditor in accordance with the provisions of these Rules;
- shall appoint a Shariah compliance officer in accordance with the provisions of these Rules;
- carrying on Family Takaful business shall set up one or more statutory funds exclusively for Takaful business;
- carrying on Family Takaful business shall divide each statutory fund set up for Takaful business into a number of sub-funds namely Participant Takaful Funds, an Operator sub-fund and in case of investment contracts a Participant Investment Funds;

- carrying on General Takaful business shall set up one or more Participant Takaful Funds and an Operator Fund;
- shall ensure that all investments made for the purposes of Takaful business are made in accordance with the investment policy approved by its Shariah Advisor;
- shall ensure that assets and liabilities of each Participant Takaful Fund and each Participant Investment Fund are segregated from its other assets and liabilities;
- shall ensure that receipts to and payments from each Participant Takaful Fund are made in accordance with the provisions of these Rules;
- shall ensure that the Participant Takaful Fund, at all times, carry reserves as may be specified by the Commission;
- shall ensure that in case of General Takaful each Participant Takaful Fund, at all times, has admissible assets in excess of its liabilities.

Establishment of Participant Takaful Fund

Takaful Operator shall establish for each Participant Takaful Fund, formulate Participant Takaful Fund Policies defining:-

- risks being covered, specifically with reference to classes of business;
- the events upon which amounts would be payable from the Participant Takaful Fund to a participant and the method of determination of the amount payable;
- expenses which may be charged to the Participant Takaful Fund;
- the method and frequency of determining surpluses or deficits of the Participant Takaful Fund;
- the method of disposing of any surplus;
- the method of extinguishing any deficit; and
- the procedure of dissolution of Participant Takaful Fund.

Establishment of Participant Investment Funds.- An Operator carrying on Family Takaful business and issuing contracts which have an investment component shall establish one or more Participant Investment Funds.

Segregation of Contributions and Funds – General Takaful

- All Contributions recognized under General Takaful contracts, net of any Government levy, shall be credited to one or more Participant Takaful Funds.
- All Contributions into a Participant Takaful Fund shall be deposited in a bank account designated as belonging to the Participant Takaful Fund.
- All income received on assets of a Participant Takaful Fund and receipts from Re-Takaful operators relating to the Participant Takaful Fund shall be deposited in bank.
- All assets, liabilities, income and expenditure of a General Takaful Operator which do not relate to a Participant Takaful Fund shall be deemed to be part of the Operator's Fund.

Establishment of Participant Takaful Fund

Establishment of Investment Fund

Segregation of Contributions and Fund – Family Takaful

- Contributions under Family Takaful Contracts, net of any Government levy, shall be segregated into the risk component and takaful operator's fee, and, if relevant, the investment component.
- The risk component shall be credited to one or more Participant Takaful Funds; the takaful operator's fee to an Operator sub-fund and any investment component to one or more Participant Investment Funds.
- The determination of each component shall be in accordance with provisions of each Family Takaful Contract.

Segregation of Contributions and Fund – Family Takaful

- All Contributions credited to a Participant Takaful Fund or Participant Investment Fund shall be deposited in a bank accounts designated as belonging to Participant Takaful Fund and Participant Investment Fund or paid across to such account within seven days of receipt.
- All income received on assets of a Participant Takaful Fund and receipts from Re-Takaful operators relating to the Participant Takaful Fund shall be deposited in bank account designated as belonging to the Participant Takaful Fund or be paid across within seven days of receipt.
- All income received on assets of a Participant Investment Fund shall be deposited in bank account designated as belonging to the Participant Investment Fund or be paid across within seven days of receipt.

Disclosure of Related Party Transactions

- **Definition of related parties are:-**
  - Members of the board of directors, its external auditors, Sharia advisor or members of its Sharia board, its general manager and his deputies and equivalent.
  - Relatives of those mentioned in (a) above to the second degree there is vested interest between the two parties.
  - Any natural person or entity which directly or indirectly owns a percentage of the relative of the natural person to the second degree. Changes in the percentage used by the Islamic insurers should be disclosed.
  - An entity is considered an affiliate of another if they are controlled by an entity that owns not less than 51 percent of the shares of each entity.
  - Any entity in which the Takaful organization directly or indirectly owns a sufficient percentage of its voting ownership units to enable the insurance to influence its operations.

Other Disclosure Requirements of Regulator under ICP-20

Public Disclosure-

- The supervisor requires insurers to disclose relevant and comprehensive information on a timely in order to give policyholders and market participants a clear view of their business activities, risks, performance and financial position.
- Public disclosure may include a description of how information is prepared, including methods applied and assumptions used.
- In establishing disclosure requirements for its jurisdiction, the supervisor should consider the need for disclosures that deliver key information rather than unnecessary volumes of data.
- Subject to their nature, scale and complexity, insurers make audited financial statements available at least annually.

Public Disclosure-

In developing disclosure requirements, the supervisor may consider whether such disclosure are:

- Easily accessible and up-to-date;
- Comprehensive, reliable and meaningful;
- Comparable between different insurers operating in the same market;
- Consistent over time so as to enable relevant trends to be discerned; and
- Aggregated or disaggregated so that useful information is not obscured.

- Disclosure requirements may also have to balance the interests of reliability against those of relevance or usefulness.
- Disclosures may include information about company objectives, strategies and timeframes for achieving those objectives.
- Key resources available may include both financial and non-financial resources. For non-financial resources the insurer may, for example, provide information about its human and intellectual capital.
- Information should, so far as practicable, reflect the economic substance of events and transactions as well as their legal form. The information should be neutral (i.e, free from material error or bias) and complete in all material respects.

Disclosures include information about the insurer’s company profile such as:

- The nature of its business;
- Its corporate structure;
- Key business segments;
- The external environments in which it operates; and
- Its objects and the strategies for achieving those objectives.

The supervisor requires that disclosures about the insurers technical provisions are presented by material insurance business segment and include, where relevant, information on:-

- The future cash flow assumptions;
- The rationale for the choice of discount rates;
- The risk adjustment methodology where used; and
- Other information as appropriate to provide a description of the method used.

Conceptual Framework for Financial Reporting of Islamic Insurance/Takaful

- The conceptual framework introduces the main objectives as well as the concepts underlying financial accounting and reporting by Islamic financial institutions (IFIs).
- The objective of financial accounting and reporting is the foundation of the conceptual framework.
- The concepts flow from the objectives and represent a framework of principles underlying financial reporting of Takaful.
- Three important reasons underpin the development of the conceptual framework and separate financial accounting standards for IFIs.
- The relationship between IFIs and the parties that deal with them differs from the relationship of those who deal with conventional entities, insurance firms, mutual funds, and other organizations.

- IFIs are prohibited from the use of interest in their investment and financing transactions from entering into highly speculative transactions and also prohibited from entering into transactions that are not permissible by the Sharia.
- The conceptual framework promotes harmonization by providing a basis for selecting the most appropriate accounting treatment permitted by the financial accounting standards.
- The conceptual framework is a guide for the development of financial accounting standards.
- The conceptual framework assists users of financial reports in interpreting the information contained in financial statements prepared in conformity with financial accounting standards.

Disclosure of Shariah

- The principles of Sharia strike a balance between the interests of the individual and society. It is known that investment is the foundation of economic activities in any society.
- Islamic Insurance play an important role by acting as a vehicle to attract the savings of individuals and investing those savings for the benefit of the individual and society.
- General Disclosures in the Financial Statements of Takaful Operator
- The financial statements should disclose all material information that is necessary to make those financial statements adequate, relevant and reliable for their users.
- The financial statements should disclose, to the extent applicable, the following information about the insurer:
  - The name if the Islamic Insurance;
  - The country of incorporation;
  - Formation date and legal form;
  - Location of headquarters and number of branches in each country where the insurers operates;

Disclosure of earnings or expenditures prohibited by Sharia

- The financial statements should disclose the amount and nature of earnings that have been realized from sources or by means which are not permitted by Sharia.
- Disclosures should be made of the amount and nature of expenditures for purposes not permitted by Sharia.
- The Islamic insurers should also disclose how it intends to dispose of the assets generated by the prohibited earning or acquired through prohibited expenditures.

Disclosures of concentrations of asset risks

Disclosure should be made in the financial statements of the magnitude of assets invested or deposited in any of the following concentrations:

- An economic sector (e.g., the agriculture sector, the service sector, the manufacturing sector, the real estate sector, etc.).
- A customer, including another insurer or a financial institution without stating the customer’s name.
- A domestic geographical area with unique economic characteristics.
- Foreign countries.

Disclosure should be made in the financial statements of the distribution of assets in accordance with their respective periods to maturity or expected periods to cash conversion from the date of the balance sheet.

The Qualitative Characteristics of Accounting Information

- True and fair view
- Decision usefulness
- Transparency
- Relevance
- Understandability:
- Reliability
- Representational faithfulness

- Neutrality
- Substance and form
- Completeness
- Verifiability
- Consistency
- Comparability
- Prudence

Basic Requirements of IFRS

Detailed disclosure is needed broadly in respect of the following items :

- Accounting Policies
- Assets, Liabilities, Income and Expense
- Changes in assumptions.
- Changes in insurance liabilities and related items.
- Nature and extent of risks arising from insurance contracts.
- Risk management objectives and policies for mitigating risks arising from insurance contracts.

- Insurance Risk.
- Sensitivity to insurance risks.
- Concentration of Insurance risk.
- Claims development
- Credit risk, liquidity risk and market risk.
- Exposure to market risk under embedded derivatives.
- Key performance indicators.

Actions to be taken

- Decide the timeframe for implementation
- Engalge/create new regulator for the purpose
- Professionals be given responsibility to frame standards based on IFRS-17
- Red Tapism be avoided
- Arrange more study/ seminar etc for quik dissemination of purpose
- Beneficial effects of transparency to enhance market penetration and create confidence of customers/ sales. People be focused by policy makers and market players.
- IFSB and AAOIFI and or IAIS may jointly formulate guidelines as has been suggested above.

Q&A

Thank you