


## IMPACTS OF IFRS 17 INSURANCE CONTRACTS

Rümeysa Karataş<sup>1,a\*</sup>

<sup>1</sup>*Karamanoğlu Mehmetbey University, Kamil Özdağ Faculty of Science, 70100  
Karaman, Turkey*

*\*Corresponding Author:  
E-mail: rumeysakaratas@kmu.edu.tr*

(Received 14<sup>th</sup> May 2022; Accepted 05<sup>th</sup> August 2022)

a:  ORCID 0000-0001-6810-3357

**ABSTRACT.** An insurance contract is a contract in which the insurer, in exchange for a premium, undertakes to compensate for the occurrence of a hazard, risk, or other act that damages a person's measurable interest in money, or to pay a sum or perform other acts due to the life span of one or more persons or certain events that have occurred in their lives. International Financial Reporting Standards 4 (IFRS 4) is the first application to regulate insurance contracts and is published in 2004. IFRS 17 is published by the International Accounting Standards Board (IASB). In this study, the changes that IFRS 17 proposes to be made to insurance contracts is explained.

**Keywords:** *IFRS, accounting standards, insurance contracts, financial statement*

### INTRODUCTION

Reasons such as the international level of trade and the rise of borders between countries, the increase in competition, the globalization of the world have shown that standard practice is mandatory in all areas. Today, the concept of national market is being replaced by the world market. This indicates that financial data and analytics must be in an internationally understandable state. Some standards have been introduced so that businesses can edit their financial statements under the same rules. International regulations are made to ensure compliance with a specific system. These regulations are the International Financial Reporting Standards (IFRS) published by the International Accounting Standards Board (IASB). The IFRS 17 Insurance Agreements Standard, which will take effect on January 1, 2023, replacing the IFRS 4, which is regulated by the standards developed by the Board, is highlighted by changes in the insurance accounting and financial reporting.

The amendments to the Insurance Agreements with IFRS 17 were published in the Official Gazette dated 31 December 2021 and numbered 31706. This study explains the changes IFRS 17 recommends to be made in insurance contracts.

On January 1, 2005, UFRS implementation is required in public enterprises in the European Union countries. Since 2005, the literature has started to include the developments in accounting policies and the implementation of the UFRS. In particular, the process of transition to UFRS has resulted in changes in the current financial structure in many countries around the world. Callao et al. [1] reviewed the impact of the transition to UFRS in Spain on the process of preparing financial reports. Hung et al. [2], international accounting of financial statements in an analysis on German firms between

1998 and 2002 they have investigated how and how it is affected by the transition to their standards. Lantto and Sahlstrom [3] analyzed the financial impact of the transition of businesses in Finland to the UFRS in 2004-2005. Silva et al. [4] in their work, they analyzed the impact of the transition to UFRS on the financial data of Portuguese companies. Iatridis and Rouvolis [5] analyzed the differences in financial reports along with the move to the UFRS in their work on companies traded on the Greek stock exchange. In 2017, the presentation prepared by Tucker and his friends [6] detailed the UFRS 17 process. The current flow of financial report preparation processes of companies and changes made with UFRS have been mentioned. This document also provides information on how to determine and apply measurement models. Yousuf et al. [7] study emphasized the new standard and the international understanding of financial statements and the quality of reports will increase. This study, where the current configuration and the new standard are examined with the insurance company data, indicates that the new standard will address many issues.

### **International Accounting Standards Committee (IASC) Organization**

The International Accounting Standards Committee (IASC) came up on 29 June 1973 as a result of the agreement of accounting organizations in various countries. The agreement was issued in 1975 and revised in March 1978. The revised agreement and regulation were revised in January 1983. The IASC main regulation was revised on October 11, 1992.

#### ***The Working Procedures of IASC***

To establish an accounting standard, the basis for obtaining the opinions of the financial statements of the preparers, auditors and users is adopted. In this framework, the formation of a standard takes about 3 years.

The IASC board selects a subject that requires the international accounting standard and is notified to a standards-setting committee. The situation is communicated to all IASC members and their views on this matter are taken. The standard identification committee does the required work and presents the documents prepared to the board. This process prepares the draft of the standard. The IASC board will review this draft and then send it to all member organizations for draft views. Once the views have been taken, a standard revised draft will be prepared, taking into account these views. This draft becomes a preliminary draft with the approval of at least two-thirds of the board. This preliminary draft is also sent to all member organizations, allowing members to provide the appropriate time for review and will be asked to provide feedback before this period expires. If the draft is approved with at least three-quarters of the board, it becomes the international accounting standard [8]. The version converted to international accounting standard is published in English and sent to all member organizations. Member organizations translate this standard into their national language and publish it to their members.

13 countries in IASC are represented for 5 years with professional accounting units who are IFAC members. A minimum of 3 developing countries are appointed to the Board. In addition, up to 4 organizations that are not a professional accounting professional organization, but are related to financial reporting and are designated by IASC are members of this board. The advisory group is formed with the participation of

international organizations representing most of the main preparers and users of the financial statements. The advisory group convenes regularly with representatives of the IASC Board, discussing issues related to accounting standards. IASC's work is recognized by financial institutions, securities stockbroker, financial analysts, OECD (Organization for Economic Co-operation and Development) and the United nations.

### **The Emergence Process of IFRS 17**

International Financial Reporting Standards (IFRS) are accounting standards prepared by the IASB to create a global common accounting scheme, eliminate differences [9].

The goal of creating a common accounting scheme with IFRS is to interpret financial statements that have emerged from different accounting practices by different countries and face confrontations at the point of analysis. The universalization of financial markets, the increasing volume of its movement to international spread, has led to the creation of these international standards and regulations. The financial reports of each company using the IFRS application, which was made a requirement by the European Union in 2005, can be clearly understood by other persons or institutions who know these standards.

### ***Roles of IFRS***

This section lists the tasks of the IFRS [10].

- The businesses can understand financial reports from businesses in other countries.
- Businesses with investments in different countries can track their investments wherever they are.
- Since the language of the tables used is the same, it provides investors with an easier and safer investment environment.
- It eliminates the time and labor costs associated with dealing with a different reporting standard for each country.
- It allows the control mechanism for the company to function more steady.
- The reports prepared with IFRS are prepared according to global standards. Having global standards prevents missing, incorrect or unnecessary information.

From mid-2011, in 98 countries, the quotable companies have to organize and report their financial statements in accordance with IFRS standards. It is also true that it is not easy for businesses to start implementing the IFRS process. In addition, the IFRS process will bring extra cost to companies. The Turkish Accounting Standards Board has translated all the documents published by the IFRS and declared them as Turkish Financial Reporting Standards.

### **IFRS and Insurance System**

#### ***Insurance and Insurance Contracts***

Insurance is the repository of these damages by transferring risks to insurance companies that agree to compensate insured for unexpected damage, provide other monetary benefits in the event of these damages, or provide services associated with risk [11]. Insurance has emerged because people and institutions need to ensure future economic damage. Insurance is an important part of society's economic and social life because it is a risk transfer and risk management tool. The oldest example of risk

management in literature is the method used by Chinese merchants in 3000 B.C. against the risk of destroying goods in their rivers as a result of their boat sinking. The merchants placed their goods on boats belonging to other merchants and shared risk rather than the loss of all property belonging to a single merchant in the event of a boat sinking. An insurance regulation must have features such as parsing damages, paying for unexpected damages, risk transfer and compensation.

The insurance contract is a contract under which the insurer, in exchange for a premium, is obliged to compensate for the danger, in the event of a risk, or in the event of a risk, or in the event of the occurrence of a risk, or in the event of life of one or several people, or in the event of some events in their lives. It is written and legal evidence of the agreement between the insurance company and the insured [12]. According to the Turkish Commercial Code, the information to be found on the policy is as follows: The name and surname of the insurance company, the insured and the beneficiary of insurance, if any, or the trade title and residence, the issue of the insurance, start and end date with the risks it takes on the insurance company, the insurance price, the amount of the premium and the payment time and place, all the cases that will fully determine the actual nature of the risks it takes on the insurance agent, the date of the arrangement.

The insurance policy includes the rights of the parties, provisions relating to the provision and general and special conditions, if applicable, and is regulated in a comfortable and easy way to read. If the contents of the policy and the attachments of the olive exchange are different from the offer or the agreed provisions, the provisions in the documents mentioned are invalid, which are different from the offer and which are stipulated against the insurance provider, the insured and the beneficiary. Unless otherwise convicted in the law, a change to the beneficiary, insured or beneficiary of the insurance shall be applied immediately and directly. However, if this change requires additional premium, the insurance agent may request a premium difference within eight days of the change. If the desired premium difference is not accepted within eight days, the contract will continue with the old general terms. In the insurance contract, the insurance agent's responsibility begins with the insurance provider's premium payment. If the premium is agreed to be paid in installments, it is sufficient that part of the premium is paid to begin the insurance agent's responsibility [13]. The contract and both parties are contractually obligated to each other. The feature that separates the insurance contract from other contracts is that the insurance agent's obligation depends on future unspecified facts. The main characteristics of the insurance contract can be listed as follows: A flow that loads responsibility and debt to both parties and the risk must be coincidental. One of the parties in insurance contracts is an insurance agent. The insurance agent is the institution that takes over the insurance contract period for a certain premium of the risks shown in the policy as a result of the insurance contract. The insurance contract is signed by the company's authorized person or agent on behalf of the policy insurance agent.

#### ***Insurance Contracts- IFRS 4***

The IFRS 4 Insurance Contracts Standard was first published in the Official Gazette dated 25/03/2006 and numbered 26119 to be applied for account periods beginning after 31/12/2005. The purpose of this IFRS is to determine the financial reporting of the insurance contracts of any operating operating company that organizes an insurance contract until the Board has completed the second part of its project for insurance contracts. The business applies this IFRS to its insurance agreements, reinsurance

agreements and optional participation-enabled financial instruments that it exports. Although the standard has been on the agenda for a long time, it has not been able to ensure that accounting practices in the insurance industry become monopoly. The IFRS 4 applies to all insurance contracts issued by an enterprise and all reinsurance contracts it holds. The IFRS 4-Insurance Contracts accounting financial instruments, while different from other standards, have gone to a distinction. This distinction covers the relationship of the financial vehicle with the insurance sector.

### ***Insurance Contracts- IFRS 17***

The IFRS 17 Insurance Agreements set the guidelines for the collection, measurement, presentation and disclosure of insurance agreements covered under Standard. The purpose of the IFRS 17 is to enable businesses to provide information that is relevant to the needs by demonstrating such agreements in a realistic manner. This information is essential in assessing the impact of insurance agreements on the financial situation, financial performance and cash flows of the business by financial table users. When implementing the IFRS 17, the business evaluates whether its original rights and taxpayers originate from a contract or a legislation. A contract is an agreement between two or more parties, which is a legally enforceable right and taxpayer. The fulfillment of rights and taxpayers in a contract is a legal matter. Contracts may be made in writing, verbal or implied by the business practices of the business. The terms of the contract include all explicit or implied provisions contained in a contract, but the business does not take into account any provisions that are not commercially qualified (in other words, without any significant impact on the economic conditions of the contract). The implied provisions in a contract include the provisions enforced by the legislation. The practices and processes for contracting customers differ according to the legal environment, industries and businesses. In addition, contracts may vary within a business (for example, contracts may depend on the customer class or the nature of the goods or services undertaken).

Amendments to the IFRS 17 and the initial Implementation of IFRS 9 with IFRS 17 to reflect and ensure full compliance with the IFRS as of January 1, 2023, in accordance with the IASB published by the IFRS — The Board decisions regarding Comparative Information dated December 31, 2021 and numbered 31706 (5. Repeated) published in the Official Gazette.

According to IFRS 17, there are three different measurement approaches to be taken in accounting and reporting insurance contracts. In the valuation of an insurance contract, it is recommended to use the most appropriate of these three approaches. These three approaches in IFRS 17 are expressed as the General Measurement Approach (Building Block approach), the Premium Allocation Approach and the Variable fee Approach. The general measurement model requires the anticipation of future cash flows first. These cash flows include any cash in and out that are bound to the insurance contract and will be assessed as part of the insurance activity and these cash flows are finalized and have today's values. In accordance with market conditions, this amount is defined as a service-based service margin if the balance is positive, taking into account the risk margin that will be determined regarding fluctuations in these cash flows. The General Measurement Model has four blocks: Expected cash flows, discount rate, risk adjustment, and contributitional service margin (CSM). The premium allocation approach of is an approach to short-term non-life insurance contracts. It is a close approach to the unearned

premium provision application in the current application. The variable fee approach is an approach that eliminates the effect of these fluctuations directly on the revenue table by evaluating the fluctuations in the service based service margin resulting from changes in market conditions.

### ***IFRS 4 versus IFRS 17***

The International Accounting Standards Board announced that IFRS 4 is a temporary standard that will be maintained until the new implementation is implemented in early 2017. This statement states that the development of various accounting practices within the insurance companies itself is complex. The general model approach to the measurement of IFRS 17 insurance contracts, the premium distribution approach, and the variable rate approach, however, IFRS 4 is not built to compare insurance businesses and contracts among themselves. With IFRS 4, the failure to apply current discount rates to all businesses prevents transparency and makes comparison difficult. IFRS 17 regulations contain significant regulations regarding the comparability and transparency of insurance agreements [14].

If we look at the differences between IFRS 4 and IFRS 17, it is summarized as follows: In IFRS 17, contrary to IFRS 4, a calculation policy is being prepared for all insurance contracts. The global regulations brought by IFRS 17 are becoming more comparable to those of insurance companies. Unlike IFRS 4 in IFRS 17, estimates are updated during each reporting period. With IFRS 17, you can clearly see which items and how the abdomen is obtained.

### ***Changes made in IFRS 17***

The IASB's IFRS was amended in June 2020 in 17 to assist in the implementation of such standard and in the disclosure of financial performance of companies. While the main principles of IFRS 17 are maintained, changes made have been aimed at achieving the following points as a result of feedback from companies: to reduce implementation costs by simplifying some provisions, to facilitate the explanation of financial performance, streamline the transition of businesses to the standard by postponing the effective date of the standard to 2023 and by granting exchanges. The changes made in IFRS 17 to meet these objectives are summarized in this study.

The changes made to the IFRS 17 are summarized as follows:

#### 1. Changes to reduce application costs:

IFRS 17 applies to all insurance agreements except for some specific exceptions. The first amendment is to expand the exceptions. This amendment has excluded some credit card agreements (and similar agreements) from the scope of IFRS 17 and allows the implementation of IFRS 17 or IFRS 9 to be applied to some debts.

With IFRS 17, companies should consolidated their insurance contracts at sub-portfolio level and these levels should be called “group”. The group of insurance agreements regulated as assets in IFRS 17 is offered separately from the insurance agreements regulated as obligations. The amendment requires that the assets and obligations of the insurance contract be presented as portfolios instead of groups.

Accounting estimates made in the previous interim financial statements under IFRS 17 cannot be changed in the following interim financial statements or in the annual reporting period. This change has provided the right to choose and facilitate the transition

to businesses that do not use this right to change the accounting forecasts made in the previous mid-term reporting in the following periods.

## 2. Changes made to facilitate the explanation of the results:

In IFRS 17, acquisition costs that can be attributed to insurance contracts must be distributed directly to the contract group. However, some of these costs are related to contract renewal costs and are actually expected to be recorded in the coming periods. With this change, companies should be distributed to contracts that are expected to renew the relevant part of acquisition costs, renewal contracts should be recorded as assets until reflected in financial statements, assessing whether there are any circumstances that indicate the recovery and value of these assets at the end of each reporting period, and the information about those assets should be disclosed.

The reinsurance contract is an insurance contract that a company has issued to compensate for damages arising from one or more insurance contracts issued by another company. The amendments made in IFRS 17 have no effect on the basis agreements, as the reinsurance agreements obtained in IFRS 17 are expected to be accounted for separately from the basis agreements.

For the first time in financial statements, the loss of insurance contracts expected to be damaged is projected immediately on the IFRS 17 for profit or loss. IFRS 17 also requires that parts of such losses recovered through the obtained reinsurance agreements be reflected in profit or loss as they receive the guarantee of company reinsurance. The amendment is that companies that record losses during the first time insurance contracts are taken into financial statements should also reflect the recovery of the damages made during or before the registration of the contract that is damaged - from the reinsurance agreements obtained. However, if the company does not know the date of the reinsurance contract, some conveniences have been provided in the transition.

IFRS 17 explains how to project the abdominal insurance contract into financial statements throughout its lifetime. The standard general model applies to agreements that do not have direct participation capability and requires the company to reflect profit into financial statements as long as it provides insurance guarantees. The change in this issue is that the insurance contract issuing company that does not have direct participation must take the profits into financial statements as it provides insurance guarantees or provides any service related to investment activities.

In IFRS 17, a company using derivative tools is allowed to use the risk reduction option to reduce the financial risk due to insurance agreements with direct participation. The change allows the option to reduce risk through the use of the specified tools when using the mitigation of risk option: Obtained reinsurance contracts, realization of value change reflected in profit or loss, and non-derivative financial instruments.

## 3. Changes made to facilitate the transition:

IFRS 17 was foreseen to take effect during the annual reporting periods that started on or after January 1, 2021. However, with the change, the effective date of IFRS 17 was moved to reporting periods on or after January 1, 2023. IFRS 9 entered into force as of reporting periods beginning on or after January 1, 2018. However, some insurance parties are allowed to apply the IFRS 9 later in IFRS 4. The exception for implementation of IFRS 9 will be extended for another two years and will end in reporting periods starting on or after January 1, 2023.

A company that has implemented IFRS 17 for the first time must account for it as if IFRS 17 had been implemented from the beginning. If this is not possible, alternative approaches are allowed to be used to measure contractual service margin. These approaches are: Retrospectively modified approach and a true value approach. The change has been recognized in IFRS 17 as some of the ease of the transition related to the following. These conveniences are agreements acquired before the transition, the option to reduce risk in transition and the investment contract with optional engagement.

In some cases, a company that implements IFRS 17 addresses the "remaining collateral liability" for contracts where it has obtained an obligation to compensate for damages and the "liability for damages that occur" for its contracts. Under the amendment, companies are allowed to account for damages as "liability for damages that occur" instead of "remaining collateral liability" for agreements acquired before the transition to IFRS 17.

In IFRS 17, retro implementation of the option to reduce risk is prohibited. Two modifications have been made to this issue. The first is to allow the option to reduce risk to be applied forward from the beginning of the previous period, which is presented comparatively. The second is to allow a group of insurance contracts to be retrospectively accounted for to be measured using the true value approach in the transition. When implementing IFRS 17, it is first necessary to determine the contracts to which IFRS 17 will be implemented. The amendment allows companies to use information available at the time of transition, in some cases, instead of information at the beginning of the agreement or the date of registration, to determine whether an investment agreement has optional participation.

## RESULTS AND DISCUSSION

In this part of the study, the differences in IFRS 4 and 17 are explained through the income chart example.

*Table 1. Income table for IFRS 4 and IFRS 17 Regulation*

Net earned premiums	17,302		Gross insurance revenue	12,191
Technical interest income	11,824		Gross insurance expense	10,342
Gross incurred claims	10,127		Gain/loss from reinsurance	776
Gross expenses	6,912		Insurance finance income	11,757
Acquisition costs	1,542		Insurance finance expenses	11,015
Change in liability	11,093			
Net investment income	238		Net investment income	392
Other operating components	747		Other operating components	803

IFRS 17 has introduced a different financial situation table arrangement than IFRS 4. The values in the first two columns in Table 1 contain the values for the accounts of the IFRS 4 arrangement. The calculations for IFRS 17 regulation are made using the values in the last two columns in Table 1. Net earned premiums and technical interest income are collected to generate total income. The total income is found as 29,126 units. The total expense is obtained by subtracting ceded incurred claims, benefits and expenses (602



units) from the sum of gross incurred claims, gross expenses, acquisition costs and change in liability value. Total expense is found 28,352 units. After calculating total income and total expense, the technical result is available as 774 units. Using net investment income and other operating components values, the nontechnical result value is available as 509 units. The operating result value is derived from the difference between the technical result and nontechnical result and is 265 units. The calculations described so far include the calculations contained in IFRS 4.

The calculations for IFRS 17 are then explained. The insurance service result is obtained by subtracting sum of gross insurance service expense and gain or loss value from the gross insurance contracts revenue. The insurance service result is found as 1,073 units. The insurance finance result is derived from the difference between insurance finance income and insurance finance expenses and is 742 units. The nontechnical result is 401 units. The operating result is calculated as 1,404 using the values found as a result of the operations carried out.

The income table created with IFRS 17 regulations can be said to be more suitable for the needs in terms of comparability.

## **CONCLUSION**

Financial outputs must be internationally assessed and readable with markets reaching international dimensions. The financial statements of insurance contracts, which are a key part of the market, must be clearly understood by all investors and all institutions and organizations in the market. For these reasons, it is deemed appropriate to set a standard for insurance contracts. Insurance contract items with this standard are transparent and comparable.

The IFRS 4 Insurance Contracts Standard was first published on 25/03/2006. IFRS 4 has become difficult for investors to interpret, as it has resulted in a wide range of approaches, while ensuring accounting of insurance contracts. The IFRS 4 is not implemented as intended, and new regulations have been developed and the IFRS 17 has been introduced. IFRS 17, published by IASB after Solvency II, which took effect in 2016, redefines the accounting standards of insurance companies. IFRS 17 regulations have highlighted comparability and transparency. Compared to IFRS 4, there are also some innovations. IFRS 17 requires a complete review of the workflow between the actuarial, risk and accounting departments of insurance companies. IASB decided on March 17, 2020 to postpone the validity date of the IFRS 17 standard to January 1, 2023.

IASB's standards on insurance contracts is a long-term work for companies. It will have a wide impact on standard international financial markets. Companies must begin their analysis on this issue and pass both technical and operational changes.

## REFERENCES

- [1] Callao, S., Jarne, J.I., Lainez, J.A. (2007): Adoption of IFRS in Spain: Effect on the Comparability and Relevance of Financial Reporting. *Journal of International Accounting, Auditing and Taxation* 16: 148-178.
- [2] Hung, M., Subramanyam, K. (2007): Financial Statement Effects of Adopting International Accounting Standards: The Case of Germany. *Review of Accounting Studies* 12(4): 623-657.
- [3] Lantto, A.M., Sahlstorm, P. (2009): Impact of International Financial Reporting Standard Adoption on Key Financial Ratios. *Accounting and Finance* 49: 341-361.
- [4] Silva, F.J.F., Do Couto, G.M.M., Corderio, R.M., (2009): Measuring the Impact of International Standards to Financial Information of Portuguese Companies. *Revista Universo Contabil* 5(1): 129-144.
- [5] Iatridis, G., Rouvolis, S. (2010): The Post-Adoption Effects of Implementation of International Financial Reporting Standards in Greece. *Journal of International Accounting, Auditing and Taxation* 19(1): 55-65.
- [6] Tucker, G., Sedelnikova, I., Saslow, M., Meurer, H., Coughlan, A. (2017): IFRS 17 Marks on New Epoch for Insurance Contract Accounting. *Pricewaterhousecoopers INT2017-04*.
- [7] Yousuf, W., Stansfield, J., Malde, K., Mirin, N., Walton, R., Thorpe, B., Thorpe, J., Iftode, C., Tan, L., Dyble, R., Pelsser, A., Ghosh, A., Qin, W., Berry T., Er, C. (2021): The IFRS Contractual Service Margin: A Life Insurance. *British Actuarial Journal* 26(e2): 1-105.
- [8] Mirza, A. (2011). *Practical Implementation Guide and Workbook*. Wiley and Sons Inc, New Jersey
- [9] Ball, R. (2006): International Financial Reporting Standards (IFRS): Pros and Cons for Investors. *Accounting and Business Research* 36(1): 5-27.
- [10] Mackenzie, B., (2013). *Interpretations and Applications of International Financial Standards*. Willey Inc, Somerset
- [11] Ayhan, R., Çağlar, H., Özdamar, M. (2019): *Sigorta Hukuku Ders Kitabı*. Yetkin Yayıncılık
- [12] Atalay, M. (2019): *Türk Hukukunda Sigorta Sözleşmeleri*
- [13] Light, A.D. (2012): Sigorta sözleşmesi süresi içinde sigorta ettirenin yükümlülükleri. *İstanbul Ticaret Üniversitesi Sosyal Bilimler Dergisi* 1-8
- [14] Gültekin, M.S. (2021): IFRS 17 Sigorta Sözleşmeleri Standardının İncelenmesi, Standart kapsamındaki Hesaplar ve Muhasebesi Üzerine Uygulama