KPMG

PSAK 74 Insurance Contracts

PSAK 74 adopts the final version of IFRS 17, Insurance Contracts, as amended in June 2020, that is effective for IFRS reporters on 1 January 2023. PSAK 74 will be the single standard for insurance contracts, replacing existing guidance under SAK that is dispersed in various standards (e.g. PSAK 62, PSAK 28, and PSAK 36).

This new insurance contracts standard aims to increase transparency and to reduce diversity in the accounting for insurance contracts as it brings new level of transparency, giving users more insight into an insurer's financial health than ever before. Investors will be able to draw on more information on the profitability of new and in-force business; the separate presentation of underwriting and financial results will provide added transparency about sources of profits and quality of earnings. The new standard will drive greater consistency globally, allowing for increased comparability between insurers.

With PSAK 74, the temporary exemptions from PSAK 71, Financial Instruments will soon expire for insurers. The implementation of PSAK 71 will allow insurers' investment activities to be compared with other entities' once again.

PSAK 74 introduces the general measurement model, which is based on a risk-adjusted present value of future cash flows that will arise as the insurance contract is fulfilled. The new measurement model aims to provide relevant information about the future cash flows.

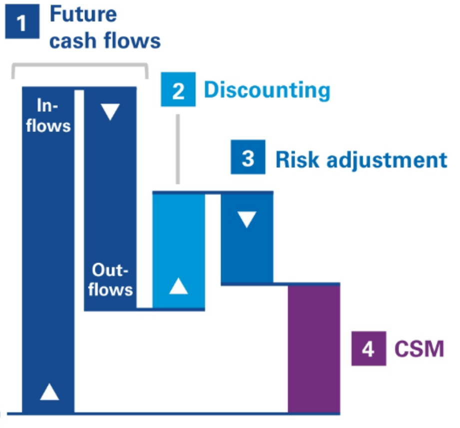
Key components of the general measurement model

Fulfillment cash flows (1, 2, 3)

Risk-adjusted present value of future cash flows – e.g. premiums, claims

Contractual service margin (CSM) (4)

Represents unearned profit – results in no gain on initial recognition



When net cash outflows result in no CSM, a loss is recognized immediately

A company applying PSAK 74 will need to remeasure its estimates each reporting period using current assumptions, which could require significant effort and new processes and controls.

The aggregation of contracts into 'groups' as defined by PSAK 74 is required at initial recognition and is not reassessed subsequently. Contract grouping is performed in a manner that limits the offsetting of profitable contracts against loss-making ones and cannot include contracts issued more than one year apart; however, exceptions apply in certain circumstances on transition. Generally, this will result in the grouping of contracts for presentation purposes below the portfolio of insurance contracts level.

While the general measurement model applies to all groups of insurance contracts in the scope of PSAK 74, a simplified approach – the premium allocation approach (PAA) – may be used (optional) to measure contracts that meet certain criteria. Separately, the general measurement model is modified (mandatory) for the measurement of reinsurance contracts held, direct participating contracts and investment contracts with discretionary participation features.

PSAK 74 requires companies to present separately insurance revenue (excluding receipts of any investment component), insurance service expenses (excluding repayments of any investment components) and insurance finance income or expenses. PSAK 74 also includes new disclosure requirements aimed to deliver clarity and transparency for users of financial statements. Companies will have to consider the level of detail necessary to satisfy the disclosure requirements, which may result in some companies disclosing information at a more granular level. The required reconciliations help to explain drivers of change in the contract liability and different types of information about the insurance service results.

PSAK 74 is effective for annual reporting periods beginning on or after 1 January 2025. It is applied retrospectively unless this is impracticable. A company can apply different transition approaches to different group of contracts, as appropriate. Early adoption is permitted only when a company applies PSAK 71 on or before the date of initial application of PSAK 74. The option to early adopt is mainly for the benefit of subsidiaries of IFRS reporters, so as to avoid the need to maintain separate records/systems as a result of different effective dates between IFRS 17 and PSAK 74.

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