

## CHAPTER 2

# Ind AS 117- Insurance contracts for non-insurers

### This article aims to:

Explain applicability and scope of Ind AS 117 to all companies, especially for non-insurer companies.

## Introduction

IFRS 4 was issued in 2004 as an interim IFRS Standard that permitted issuers to continue their accounting practices and focused on enhanced disclosures. The International Accounting Standards Board (IASB) issued IFRS 17, *Insurance Contracts*, a comprehensive standard that prescribes recognition, measurement and disclosure requirements, to avoid diversities in practice for accounting insurance contracts. Final amendments for IFRS 17 were issued by IASB on 25 June 2020. The exposure draft of the standard under Ind AS, Ind AS 117, was issued by the Institute of Chartered Accountants of India (ICAI) on 12 February 2018.



## Background

The Ministry of Corporate Affairs (MCA) issued Ind AS 117, *Insurance Contracts* on 12 August 2024.

Ind AS 117 applies to all companies i.e. it applies to 'insurance contracts', regardless of the issuer, and therefore all companies could be affected, not just insurance companies registered with the Insurance Regulatory and Development Authority of India (IRDAI).

Indian Accounting Standards (Ind AS) currently do not apply to entities registered with IRDAI as insurance companies. These companies apply accounting standards notified under the Companies Act, 2013 read with relevant guidelines issued by the IRDAI. While the IRDAI re-constituted an Expert Committee in the month of February 2024 to address implementation issues of Ind AS/IFRS in the insurance

sector, the expert committee is yet to recommend on timelines for implementation of Ind AS.

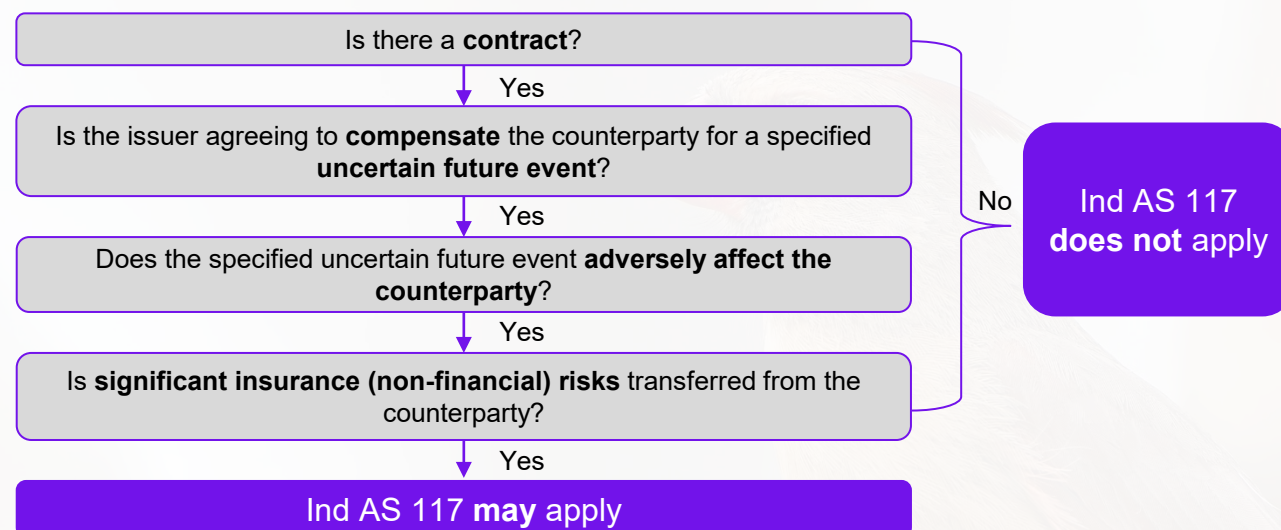
Accordingly, the MCA, vide its notification dated 28 September 2024, has clarified that an insurer or insurance company may provide its financial statement as per Ind AS 104 for the purposes of consolidated financial statements of its parent or investor or venturer till the IRDAI has notified Ind AS 117. This amendment provides relief to insurance companies who otherwise were required to apply Ind AS 117 for submission to their parent, investor or venturer for inclusion in their respective consolidated financial statements.

It appears that for entities which are not insurers/ insurance companies Ind AS 117 will continue to apply with effect from 1 April 2024.



## Identification of Insurance contracts:

When determining if a contract is an insurance contract, there are four main steps in the assessment.



(Source: IFRS 17 for non-insurers issued by KPMG IFRG Limited, May 2022)

**Step 1** is to assess whether there is a contract.

- 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.
- Contracts can be written, oral or implied by an entity's customary business practices.
- An entity shall also consider its substantive rights and obligations that arise from law or regulation.

Hence, scope of rights and obligations considered for Ind AS 117 accounting are wider in scope to include contract, law, or regulation.

**Step 2** requires there to be an agreement to compensation for a specified uncertain future event:

- **Compensation** could be cash payment or a payment in kind – e.g. repairing or replacing broken product.
- The **future event** for which the policyholder is being compensated is required to be uncertain at the inception of the contract.
- This **uncertainty** surrounding the event is the essence of the insurance contract. Uncertainty can be with respect to probability of occurrence, timing of occurrence or possible compensation.

**In Step 3**, a specified uncertain future event needs to adversely affect the counterparty. This means that:

- **Ind AS 117 might apply:** For example, a policy that compensates a building owner for earthquake damage to its building would meet this criterion, because the building owner would be adversely affected by damage to their building.
- **Ind AS 117 would not apply:** A weather derivative contract where an entity will receive payments if there is an earthquake would not meet this criterion because the derivative contract does not require the earthquake to adversely effect the policyholder.

**Step 4** requires evaluation of significant insurance risk being transferred:

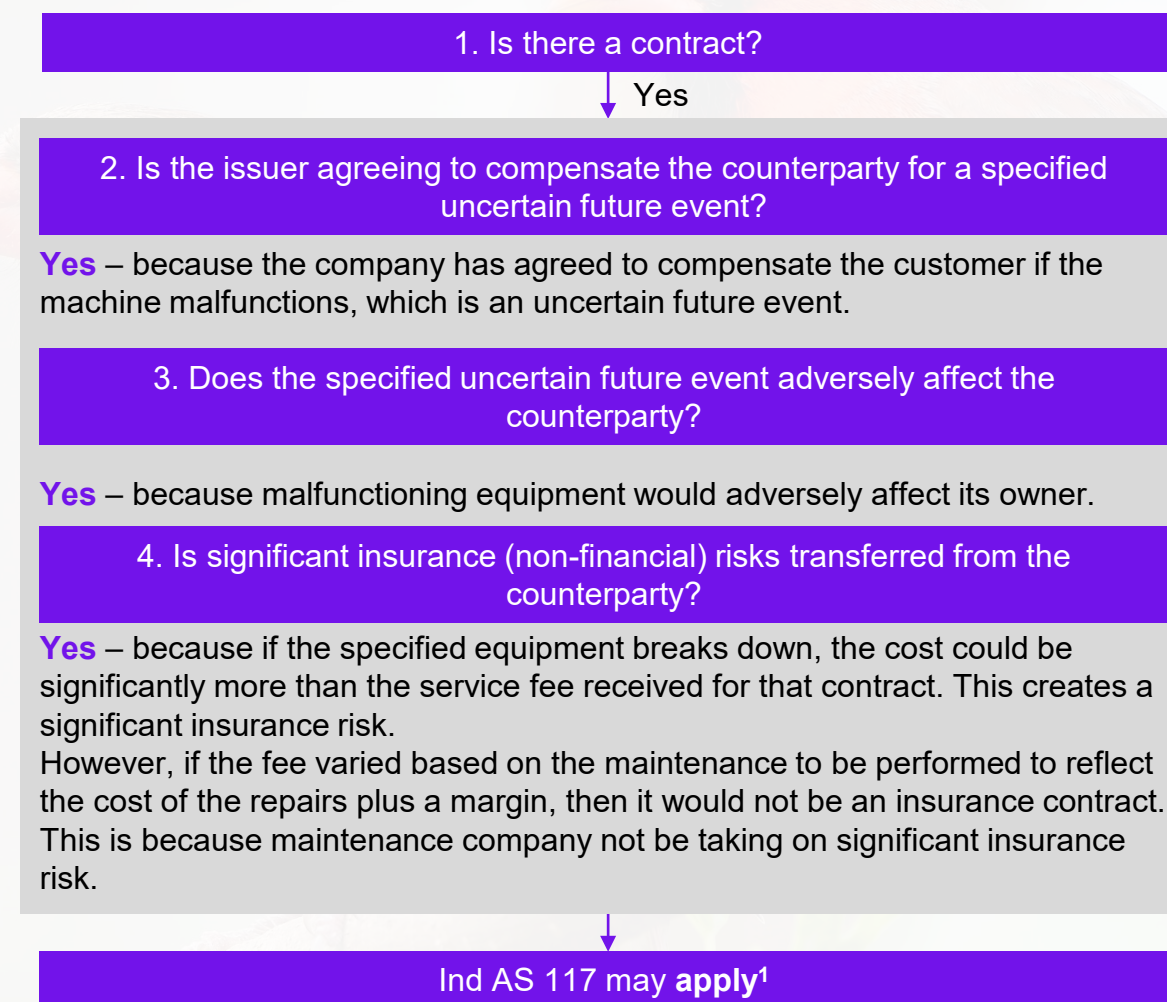
- Insurance risk: Risk, other than financial risk, transferred from the holder of a contract to the issuer.
- The risk of a possible future change in non-financial variables that are specific to the party to the contract.
- Example of financial variables are specified interest rate, financial instrument price, commodity price, currency exchange rate, index of prices or rates, credit rating or credit index.

## Illustration: Applying the four-step process<sup>1</sup>

### Maintenance contract

- A company provides a maintenance contract in which it agrees to repair specified equipment after a malfunction for a fixed fee. This agreement is between two or more parties and creates enforceable rights and obligations.
- The fixed service fee is based on the expected number of malfunctions for the customer's specified equipment.
- The cost of repair of the specified equipment could significantly exceed the fixed service fee received in some circumstances.

<sup>1</sup> Fixed-fee service fee contracts that are determined to be insurance contracts can be accounted for under Ind AS 115 Revenue from contracts with customers, if certain conditions are met ( Page reference for optional exceptions). This is a contract-by-contract assessment.



(Source: IFRS 17 for non-insurers issued by KPMG IFRG Limited, May 2022)



## Scope of Ind AS 117 Insurance contracts

Once we determine that a contract has a component of an 'insurance contract' next step is to evaluate mandatory exemptions and optional exceptions to determine whether principles of recognition, measurement and disclosures prescribed under Ind AS 117 would be applicable to such components.



### A. Mandatory exemptions

Ind AS 117 has a broad scope and may bring contracts into scope that are issued by non-insurers. Following contracts are not in the scope of Ind AS 117:

Product	Considerations
Warranties	Warranties provided by a manufacturer, dealer or retailer in connection with the sale of its goods or services to customer (Ind AS 115 and Ind AS 37).
Employer's assets and liabilities	Employers' assets and liabilities from employee benefit plans (Ind AS 19 and Ind AS 102) and retirement benefit obligations reported by defined benefit retirement plans.
Contractual rights and obligations	Contractual rights or contractual obligations contingent on the future use of, or the right to use, a non-financial item (for example, some licence fees, royalties, variable and other contingent lease payments and similar items: (Ind AS 115, Ind AS 38 and Ind AS 116).
Residual value guarantees	Residual value guarantees provided by a manufacturer, dealer or retailer and a lessee's residual value guarantees when they are embedded in a lease (Ind AS 115 and Ind AS 116).
Financial guarantees	Financial guarantee contracts, unless the issuer has previously asserted explicitly that it regards such contracts as insurance contracts and has used accounting applicable to insurance contracts (Ind AS 32, Ind AS 107 and Ind AS 109).
Contingent consideration	Contingent consideration payable or receivable in a business combination (Ind AS 103).
Policyholder	Insurance contracts in which the entity is the policyholder, unless those contracts are reinsurance contracts held (Ind AS 37 addresses the accounting for reimbursement rights arising from insurance contracts for expenditure required to settle a provision. Ind AS 16 addresses some aspects of reimbursement under an insurance contract for the impairment or loss of property, plant and equipment).
Credit cards	Credit card contracts, or similar contracts that provide credit or payment arrangements, that meet the definition of an insurance contract if, and only if, the entity <b>does not reflect</b> an assessment of the insurance risk associated with an individual customer in <b>setting the price</b> of the contract with that customer (Ind AS 109 and other applicable Ind AS). However, if, and only if, Ind AS 109 requires an entity to separate an insurance coverage component that is embedded in such a contract, the entity shall apply Ind AS 117 to that component.

(Source: KPMG in India's analysis 2024 based on Ind AS 117)

# Scope of Ind AS 117 Insurance contracts

## B. Optional Exceptions

In addition, Ind AS 117 allows a number of specific accounting choices for contracts that meet the definition of an insurance contract. Under the accounting choice provided, either Ind AS 117 or another standard can be applied (shown between brackets):

Product	Consideration
Financial guarantees	Financial guarantee contracts for which the issuer has <b>previously asserted explicitly</b> that it regards such contracts as insurance contracts and has used accounting applicable to insurance contracts. Only in this situation a choice applies (Ind AS 32, Ind AS 107 and Ind AS 109 or Ind AS 117 on contract-by-contract basis). When this has not been asserted, Ind AS 109 applies. On transition to Ind AS 117, entities can however elect to apply Ind AS 109 or 117.
Fixed-fee services	Fixed-fee service contracts (Ind AS 115 or Ind AS 117 on contract-by-contract basis) that meet the following conditions: <div><div>a)</div><div>The entity does not reflect an assessment of the risk associated with an <b>individual customer</b> in setting the price of the contract with that customer;</div><div>b)</div><div>The contract <b>compensates the customer by providing services</b>, rather than by making cash payments to the customer; and</div><div>c)</div><div>The insurance risk transferred by the contract arises primarily from the <b>customer's use of services</b> rather than from uncertainty over the cost of those services.</div></div>
Loans	Loan contracts that meet the definition of an insurance contract but limit the compensation for insured events to the amount otherwise required to <b>settle the policyholder's obligation created by the contract</b> . (Ind AS 109 or Ind AS 117 on portfolio of insurance contracts basis)

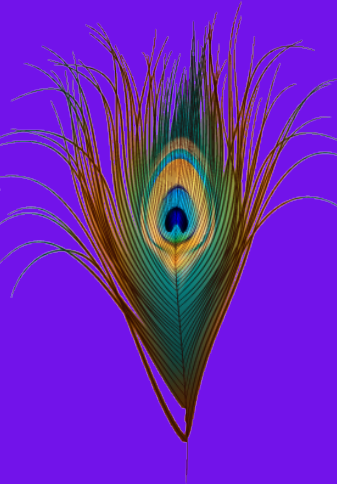
(Source: KPMG in India's analysis 2024 based on Ind AS 117)

Considering the definition of an insurance contract and additional scope exemptions and exceptions under the new standard, accounting for contracts in the scope of Ind AS 117 may be challenging for many companies. It is important for a company to determine now whether it issues any insurance contracts in the scope of Ind AS 117.



# Applicability

An entity shall apply Ind AS 117 for annual reporting periods beginning on or after 1 April 2024. Ind AS 117 also prescribes various transition options for smoothly implementation.



# Next steps

For entities to implement this standard, following are the next steps.

Understand the terms of the contract	<ul style="list-style-type: none"><li>Companies should evaluate whether they have contracts that might meet the definition of an insurance contract.</li></ul>
Accounting policies/elections	<ul style="list-style-type: none"><li>Evaluate whether these contracts are in the scope of Ind AS 117</li><li>Understand how they might be affected by Ind AS 117</li><li>Evaluate the ‘elections’ as given in the standard when deciding how to account for those contracts</li></ul>
Accounting systems and processes	<ul style="list-style-type: none"><li>Evaluate whether appropriate controls and processes are in place</li><li>Consider whether there are accounting implications under Ind AS 117 for any new contracts.</li></ul>

