IFRS 17 for WSIB:

Assessing "Contract Boundary"

May 2019

IFRS 17 at a Glance

Background:

- Effective on January 1, 2022*
- Supersedes IFRS 4 , an interim standard which used legacy reporting methods

Objective of new IFRS 17:

- Comparability
- Transparency
- Relevant and useful financial information

* Deferral of IFRS 17 to 2022 (from 2021) is pending exposure draft process, that being said expectation is for amendment to standard to be finalized by late 2019

Why was IFRS 17 Introduced?

IFRS 4 – Criticisms

- Lack of comparability across countries
- Lack of comparability of insurance vs. non- insurance companies
- Different accounting policies per insurance contract
- Difficult to see key drivers of profit
- Discount rate based on investments

IFRS 17 – Responses

- Uniform accounting practice across countries
- Similar accounting methods based on consistent principles for insurance and non- insurance companies
- One accounting policy for all insurance contracts
- Key drivers of profit (investment vs. underwriting) made transparent
- Discount rate based on cash flows of the contract

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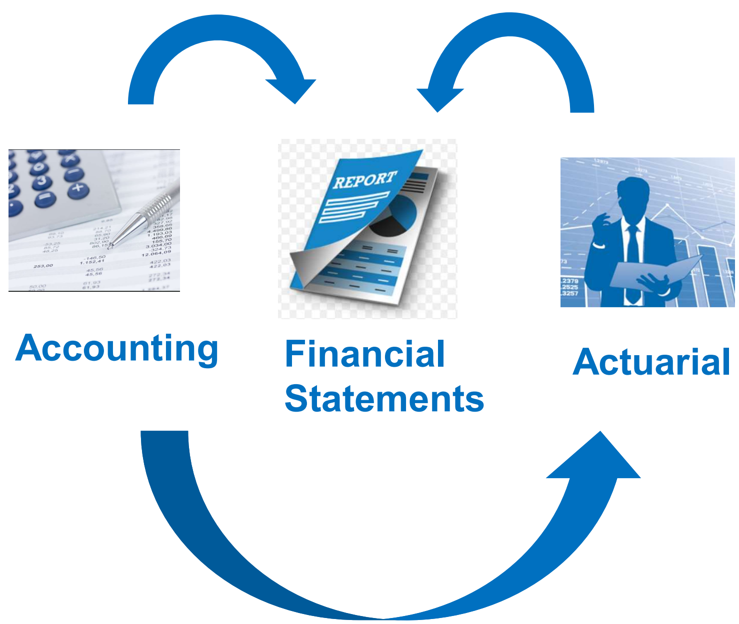
The Accounting/Actuarial Partnership

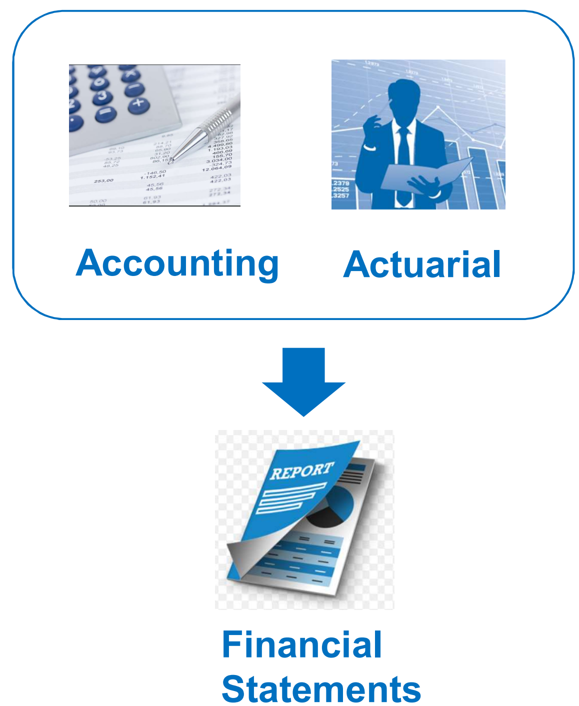
IFRS 4

- In Canada, IFRS 4 largely leveraged the Actuarial Standards of Practice



IFRS 17

- An accounting framework in which actuarial approaches are inputs into the standard



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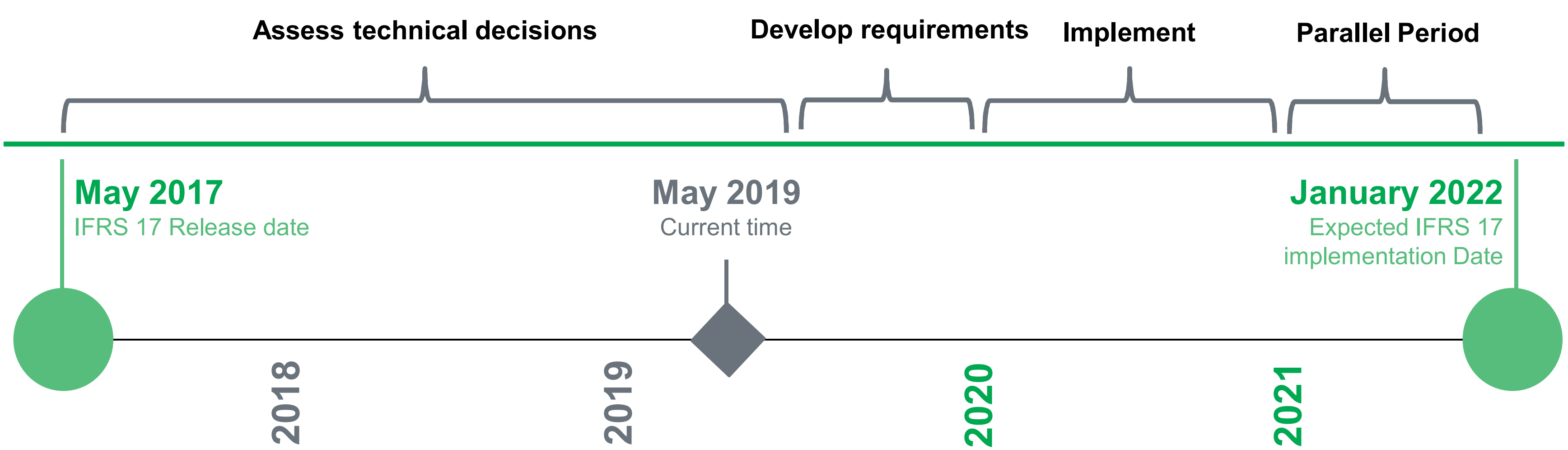
WSIB's IFRS 17 Journey

Subset of topic areas under IFRS 17

- **Contract evaluation and defining the contract boundary**
- Best estimates of cash flows
- Portfolio determination / grouping
- Discounting approaches
- Explicit adjustments for non-financial impacts
- Liability for remaining coverage
- Presentation / disclosure and transition

Focus of today's discussion

Where are we on this journey



IFRS 17 – Contract Evaluation and Defining Contract Boundary

Why is this important?

- Establish measurement approach
- Significant impacts on
  - Financial statement presentation
  - Operational considerations

The two views:

- ***View A***
  - Insurance contract is **1 Year**
  - Simplified approach – Premium Allocation Approach (PAA)
- ***View B***
  - Insurance contract is **lifetime**
  - General approach – Building Block Approach (BBA)
  - An interpretation of View B is that assets = liabilities at all times for WCBs

Summary of Approach

Step 1:
Define the contract

Step 2:
Assess whether contract meets the definition of an "insurance contract"

Step 3:
Determine contract boundary for "insurance contract"

Step 1: Define a Contract

Step 1: Define the contract | **Step 2: Assess if contract meets definition of an 'insurance contract'** | **Step 3: Determine contract boundary for insurance contract**

- **Definition of Contract**
  - Legislative requirements
  - Arrangement between WCB and employers
  - Contract identification criteria under IFRS 15 (Appendix A)
- **View A (1 Year):**
  - "Agreement" exists for 1 year on coverage (per legislation) and payment terms (premium rates set annually)
- **View B (Lifetime) :**
  - Not explicitly assessed
  - Assumes that "agreement" exists between WCB and employer indefinitely
  - Considerably more judgment around coverage and payment terms

Step 2: Does Contract Meet the Definition of an "Insurance Contract"

Step 1: Define the contract → **Step 2**: Assess if contract meets definition of an 'insurance contract' → **Step 3**: Determine contract boundary for insurance contract

- **Is there significant insurance risk transfer?**
- **View A (1 Year):**
  - Expected that definition of an insurance contract would be met
- **View B (Lifetime):**
  - Complexities to be contemplated:
    - WCB's ability to reprice within a given "contract"
    - The assets = liabilities interpretation would further contradict significant insurance risk transfer
  - If insurance contract definition is not met → outside of IFRS 17
    - Directly contradicts current application of IFRS 4
    - Broader ramifications on the recognition/measurement of assets/ liabilities, and potential derecognition if in an agency relationship

Step 3: Determining Contract Boundary for Insurance Contract

Step 1: Define the contract

Step 2: Assess if contract meets definition of an 'insurance contract'

Step 3: Determine contract boundary for insurance contract

- **View A (1 Year):**
  - Cash flows beyond 1 year not relevant for boundary evaluation
  - Ability to reprice and compel premiums would be limited to 1 year
  - Simplified approach would apply

- **View B (Lifetime):**
  - Assumes step 1 and 2 are met
  - WCB has a life long relationship with employers and the ability to compel premiums indefinitely
  - Contract boundary would be the life time of the employer relationship – general approach would be required

Impact to Financial Statements

- **Simple illustrative example of View A & B (Slide 12 &13)**
- **View B (Lifetime) – two contemplated recognition approaches**
  - Interpretation B.1 General Approach (BBA application)
  - Interpretation B.2 Assets = Liabilities
    - Not a prescribed method under IFRS 17
- **Impact illustrated assumes surplus position of the WCB**
  - Illustrative example assuming a deficit position included in Appendix B

Assessing Impact from Financial Statement Presentation

	View A: Simplified Approach	View B: B.1 General Approach	View B: B.2 Assets = Liabilities
Insurance Revenue	Similar to Premiums today	Significantly different concept than Premiums today	
Contractual Service Margin (CSM)	N/A	Complex calculation	N/A
Loss component (onerous contract)	Less significant	Significant	
Insurance Contract Liability	Similar concept to Benefit Liability	Significantly different concept than Benefit Liability today	
Net Asset/Deficit	Financial position/ funded status	Nil	

Illustrative impacts to Financial Statements – Income Statement

Assumes a Surplus Position	View A PAA Application	View B.1: BBA Application	View B.2: Assets = Liabilities
Income Statement			
Insurance Revenue	90	89	89
Insurance Service Expense	84	84	84
Insurance Service Result	6	5	5
Insurance Finance Expense	###	###	###
Investment Income	###	###	###
Administration and other expenses	###	###	###
Expenses	###	###	###
Excess of revenues over expenses	(2)	(3)	(3)

* Breakout has been shown for illustrative purposes, details noted will be shown in disclosure and not on face of financial statements

Illustrative Impact to Financial Statements – Balance Sheet

Assumes a Surplus Position	View A PAA Application	View B.1: BBA Application	View B.2: Assets = Liabilities
Balance Sheet			
Assets			
Cash and Receivables	###	###	###
Investments	1,000	1,000	1,000
Other Assets	###	###	###
Total Assets	**1,210**	**1,210**	**1,210**
Liability			
Payables and Debt	###	###	###
Contingent Liability (Asset)			(280)
Premiums received	-		
Loss Component	10	400	300
Best Estimate Liability	700	1,140	1,140
Risk Adjustment	###	###	###
Contractual Service Margin		20	-
Insurance Contract Liability	710	1,560	1,440
Total Liabilities	760	1,610	1,210
Net surplus (deficiency of) assets			
Deficit/Surplus	450	(400)	-
Total net surplus (deficiency of) assets	450	(400)	-
Total liabilities and net (deficiency of) assets	**1,210**	**1,210**	**1,210**

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Assessing Impact from Financial Statement Presentation

- ***Comparability, transparency and usefulness of financial statements***
  - The assets = liabilities interpretation of View B poses significant challenges
    - Not a prescribed method under IFRS 17
    - "Contingent asset/ liability" likely would not meet recognition criteria
    - Comparability amongst WCBs and with other insurers
    - Comparability with non-insurers/ consistency with other IFRS standards
    - Usefulness of financial statements in general
  - View B with full BBA application
    - Significant loss component as a result of onerous contracts over lifetime of employers may be difficult to rationalize
  - The simplified approach would be the easiest to understand, largely in line with current recognition

Assessing Impact from Financial Statement Presentation

- ***Operational Considerations***
  - The general approach requires a significant amount of administrative effort
  - The general approach may require a new/updated actuarial system/process
  - The general approach also requires the most extensive disclosures
- ***Other considerations***
  - Public perception on funding status and premium rates
  - Characterization of WCBs as an insurer vs. flow-through administrator

Appendices

Appendix A – IFRS 15 Guidance on Contract Identification

- The definition of “contract” is consistent between IFRS 17 and IFRS 15
- IFRS 15 paragraph 9 contains a list of criteria for identifying the contract:
  - Approved contract between both parties
  - Each entities rights related to goods/services can be identified
  - Payment terms for goods and services can be identified
  - Contract has commercial substance
  - Probable collection of consideration

Appendix B - Illustrative impacts to Financial Statements – Deficit

Assumes a Deficit Position	View A	View B.1: BBA Application	View B.2: Assets = Liabilities
Income Statement			
Insurance Revenue	90	89	89
Insurance Service Expense	84	84	84
Insurance Service Result	6	5	5
Insurance Finance Expense	###	###	###
Investment Income	###	###	###
Administration and other expenses	###	###	###
Expenses	###	###	###
Excess of revenues over expenses	(2)	(3)	(3)

Balance Sheet			
Assets			
Cash and Receivables	###	###	###
Investments	400	400	400
Contingent Asset			280
Other Assets	###	###	###
Total Assets	**610**	**610**	**890**
Liability			
Payables and Debt	###	###	###
Premiums received	-		
Loss Component	10	400	300
Best Estimate Liability	700	540	540
Risk Adjustment	###	###	###
Contractual Service Margin		20	-
Insurance Contract Liability	710	960	840
Total Liabilities	760	1,010	890
Net (deficiency of) assets			
Deficit/Surplus	(150)	(400)	-
Total net (deficiency of) assets	(150)	(400)	-
Total liabilities and net (deficiency of) assets	**610**	**610**	**890**

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