

## Paper 2 – Local Submission: Employees Compensation Insurance

### Potential implementation question

1. Employees' Compensation Insurance Residual Scheme Bureau Limited ("ECIRSB") has a market agreement with all insurers writing Employees Compensation Insurance ("EC Insurers"). The purpose of ECIRSB is to ensure that insurance coverage is provided to policyholders that cannot get that insurance in the market. ECIRSB appointed a service provider (an insurance company) to issue policies for Employee's Compensation Insurance ("EC Insurance") to qualified employers with a service fee.
2. Participation in the ECIRSB is based on Applicable Proportions based on provisional statistics for Gross Written Premiums for EC Insurance provided to the ECIRSB by the Insurance Authority for the most recent preceding years.
3. ECIRSB Appointed Service Provider issues a co-insurance policy on behalf of EC Insurers and ECIRSB Administrator provides information to members on a monthly basis. The EC Insurers record the underwriting result allocated to them as direct business. Each EC Insurer reports premiums, claims and expenses incurred and pays a service fee to the Appointed Service Provider.
4. Each financial year end, ECIRSB will engage an independent actuary to conduct Actuarial Reserve Review (similar to GL9 requirements) ("Actuarial Review") but EC Insurers are not required to account based on the review result.
5. The question is whether the fact pattern is similar to Pool 1 under AP 09 (Annex 2.1 of this paper) and hence the risk adjustment for non-financial risk should be determined by individual member entity?
6. The fact pattern of pool 1 under AP09 is:

"All entities issuing automobile insurance contracts in a specific jurisdiction are required by law to be a member of an association. The purpose of the association is to ensure that insurance coverage is provided to policyholders that cannot get that insurance in the voluntary market. The association manages two types of industry pools:

  - (a) Pool 1—in which some members are appointed to issue contracts on behalf of all of the members; and
  - (b) Pool 2—to which members can choose to transfer some insurance contracts they have issued.

The results of each industry pool are allocated to all the members of the association based on a specific sharing formula (generally based on market share). Applying existing practice each member accounts for their share in the pool in their own financial statements as direct business."
7. The full extract of relevant section from Market Agreement is included in appendix A to this Paper.

### Paragraph of HKFRS/IFRS 17 Insurance Contracts

8. Please refer to AP09 (Annex 2.1 of this paper)
9. Paragraphs of HKFRS/IFRS 11 Joint Arrangements:
  - 4 A joint arrangement is an arrangement of which two or more parties have joint control.
  - 5 A joint arrangement has the following characteristics:
    - (a) The parties are bound by a contractual arrangement (see paragraphs B2–B4).

(b) The contractual arrangement gives two or more of those parties joint control of the arrangement (see paragraphs 7–13).

6 A joint arrangement is either a joint operation or a joint venture.

7 Joint control is the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require the unanimous consent of the parties sharing control.

### **Analysis of the question**

10. Please refer to AP09 (Annex 2.1 of this paper) and TRG meeting summary for AP09 (Annex 2.2 of this paper), which observes that:
  - "- IFRS 17 applies to insurance contracts issued by an entity and does not have specific requirements for insurance contracts issued by more than one entity.
  - Entities should assess whether an arrangement under which an insurance contract is issued by more than one entity is also within the scope of another
  - IFRS Standard, for example IFRS 11 Joint Arrangements.
  - IAS 8 includes requirements for an entity to apply in the absence of a Standard that specifically applies to a transaction, other event or condition.
  - In relation to the risk adjustment for non-financial risk, TRG members observed that paragraph B88 of IFRS 17 requires the risk adjustment for non-financial risk to reflect the degree of diversification benefit included in the compensation required for bearing non-financial risk.
  - AP09 distinguished between contracts issued by an individual member entity of an industry pool and contracts issued by the collective comprised of all members. In the former case, the risk adjustment for non-financial risk is determined by individual member entity. In the latter case it is determined by the collective.
  - Some TRG members expressed the view that applying paragraph B88 of IFRS 17, each entity would consider the compensation it would require for bearing the non-financial risk, rather than the compensation required by the association."
11. For ECIRSB, ECIRSB is managed by its Board which its composition is based on (i) market share and (ii) election from EC Insurers. The liability of each EC Insurer is specified in the schedule of the policy. We view it does not fit the joint control definition of Paragraph 7 of HKFRS/ IFRS 11 and does not fall within scope of HKFRS/ IFRS 11.
12. Since the issuer of the contract is the party that recognizes revenue from the contract, the component of which is the amounts related to the risk adjustment for non-financial risk. EC Insurance contracts issued under ECIRSB by Appointed Service Provider are co-insurance policies, that is each Individual Insurer is the issuer of the contract.
13. In practice, individual EC Insurer's risk adjustment for non-financial risk will base on their own assessment and may not be its share of the risk adjustment determined by the Actuarial Review. It would also reflect the diversification benefits available to each of the EC Insurers on their own.