Facility Association IFRS 17 Frequently Asked Questions (FAQ)

Facility Association (FA) began reporting its results on an IFRS 17 basis beginning on November 1, 2022. Reports for FA's 2022 Fiscal Year (November 2021-October 2022) are also provided for comparative purposes.

FA members can access reports regarding their share of FA's balance sheet and operating results through the **FA Portal**.

Commentary and reporting on overall Facility Association Residual Market (FARM) and Risk Sharing Pool (RSP) results are available monthly through the **Member Bulletins** and quarterly through the **Quarterly Reports** on our website. We strive to provide reports that serve the needs of as many members as possible, and your questions have been critical to our ongoing improvement process.

For your ease of reference, please find below the FAQ document, which provides a reference for some of the most commonly asked questions about the reports.

Please note that the IFRS 17 calculations in our report rely on assumptions about the level of aggregation, risk adjustment, discount rate, cash flows, and contract boundary that may differ from the members' own assumptions. Members are advised to assess the impact of any differences in FA's assumptions compared to the Members. For more information on these assumptions and accounting policy papers, please refer to FA's **IFRS17 Documents** available on the website.

General questions

1. What reports are available to members?

Reports on the IFRS 4 accounting basis are still available in the following formats from the FA Portal, until we determine through member consultation that they are no longer required:

- Monthly Operational Report:
  - PDF format
  - Web format
  - CSV format
  - All years (extended) CSV format
- Monthly Government Line Report:
  - PDF format
  - Web format
  - CSV format

Please note that we will give significant advance notice to members before the IFRS 4 reports are discontinued, to avoid any impact to member financial reporting processes.

Reports on the IFRS 17 accounting basis are available from the FA Portal starting from November 2021:

- Monthly Operational Report:
  - PDF format
  - Web format
  - CSV format
  - All years (extended) CSV format
- Monthly Government Line Report:
  - PDF format
  - Web format
  - CSV format
  - All years (extended) CSV format

The RSP and FARM calendar year Outlooks under IFRS 17 standards are available beginning Calendar Year 2023 on the FA website at **Outlook.**

Monthly Bulletins on the IFRS 17 basis for RSP and FARM are available beginning with the December 2022 accounting month on the FA website at **Member Bulletins**.

YTD Summary of Operations on the IFRS 17 basis for RSP and FARM are available starting from the January 2023 accounting month on the FA website at **Summary of Operations**.

2. **How does IFRS 17 affect the monthly settlement process of the risk sharing pools?**
IFRS 17 does not affect the monthly settlement of the pools, which is still based on the member's share of written premium - expense allowance - paid losses and expenses – administrative expenses, as per page 9 of the operational report. IFRS 17 only affects the liabilities of the pools and the presentation of the operating results.

3. **What is the Expense Allowance?**
The expense allowance is a payment from the RSP to the member companies who cede risks to the RSP. It is a percentage of the written premium ceded to the RSP. It is intended to compensate the member for all expenses incurred including acquisition costs, operating costs and loss adjustment costs, but not including professional fees (such professional fees to be stipulated in the Risk Sharing Pool Claims Guide with compensation to be as therein directed). You can find additional information about the expense allowance in the Accounting and Statistical Manual on our website: **Broker Resources**.

A helpful way to conceptualize the expense allowance under IFRS 17 is as a ceding commission for quota share reinsurance. The expense allowance is not a new concept under IFRS 17, and has always been a part of the RSP operations. However, its accounting treatment has changed as the earned expense allowance is now netted from the earned premium to determine the insurance revenue.

For more information on the impact of IFRS 17 on the Expense Allowance, please refer to Question 16.

4. **Why is the FARM loss component blank/zero in the operational reports?**
   FARM business is priced to provide a fair return on the capital members are providing to support the FARM business. The FA Board of Directors provides FA Management direction and approval on the target level to be used in FA rating plan to receive a fair return on their capital. Based on current indications, none of our FARM segments are expected to be onerous. We will continue to monitor these indications on an ongoing basis to determine if any segments become onerous and require loss component.

5. **Why does the RSP loss ratio/combined operating ratio appear significantly different now under IFRS 17?**
   The denominator of the loss ratio/combined operating ratio presented in the bulletins is now the **insurance revenue** (earned premium minus earned expense allowance), rather than earned premium, which results in more significant changes to the ratios in the bulletins.

6. **Are members obligated to book the liabilities from the operational report in their financial statements?**
   Members are not obligated to book the amounts from the operational report in their financial statements. The financial statements in the operational report represent the best estimate of the liabilities of the RSPs and FARM based on the analysis completed by FA staff and our Appointed Actuary. These financial statements are prepared in accordance with GAAS/IFRS accounting standards, and the underlying data processes are subject to audit under the Canadian Standard on Assurance Agreements framework (CSAE 3416 – Reporting on Controls at a Service Organization). However, some members may take an alternate view on the assumptions underlying these insurance contracts, such as the discount rate, risk adjustment, onerousness, expected loss ratio, timing of cash flows, and level of aggregation of contracts.

   FA encourages members to discuss with their actuaries (particularly their Appointed Actuary), accountants and/or auditors regarding the treatment of the assumed liabilities of the RSPs and FARM.

   FA provides supplementary data sources through our quarterly reports to support members with data needed to unwind FA's assumptions from the numbers in the operational reports.

Data questions

7. **Where can I find the Earned Premium and Earned Expense Allowance for the RSP?**
   Prior to the December 2022 IFRS 17 RSP operational report, Earned Expense Allowance was netted from Earned Premium in the calculation of Insurance Revenue in the report. Starting with the December operational report, these items are shown explicitly.

8. **Where can I find the Written Premium?**
   Written premium is not a metric directly used in the IFRS 17 financial reporting, and therefore it has been excluded from the operational report. However, many members have inquired about this item as they still wish to track this metric for their own reporting purposes; the RSP monthly settlement amounts and share ratios are also still based on Written Premium as per the Plan of Operations, which makes it an important metric for the mechanism. For now, members can find the written premium in the IFRS 4 operational report. The written premium is available in the IFRS 17 Government Line monthly reports.

9. **Where can I find the Written Expense Allowance?**
   Written Expense Allowance is not a metric directly used in the IFRS 17 financial reporting, and therefore it has been excluded from the operational report. However, many members have inquired about this item as they still wish to track this metric for their own reporting purposes; the RSP monthly settlement amounts are also still based on Written Expense Allowance (referred to simply as "Expense Allowance") as per the Plan of Operations, which makes it an important metric for the mechanism. For now, members can find the Written Expense Allowance in the IFRS 4 operational report under the item named "Expense Allowance". The Written Expense Allowance is available in the IFRS 17 Government Line monthly reports.

10. **How can I understand the structure, format, and terminology of the IFRS 17 Reports?**
    There is both a User Guide and Glossary of Terms available for both RSP and FARM. Please refer to the IFRS 17 Resource section on our website.

Accounting questions

11. **I require additional information to calculate the Unexpired Coverage for reinsurance contracts held for the OSFI PC4 (Minimum Capital Test) relating to Margin Required for Unexpired Coverage. Where can I find this information?**
    The LRC in our operational report for the RSPs includes underlying insurance contracts within the contract boundary that have not yet been issued, as per the OSFI Clarification dated December 2023. It is our opinion that the LRC including Loss Component in our operational report is similar to OSFI's definition of Unexpired Coverage, except that the Loss Component is inclusive of the risk adjustment for non-financial risk, whereas the Unexpired Coverage as per the OSFI Guideline explicitly excludes the risk adjustment.

    A detailed breakdown of the LRC calculation is provided in the quarterly reports available on our website.

12. What is the IFRS 17 transition adjustment?

Because members are adopting IFRS 17 at different times, and may also choose different assumptions when accounting for their share of FA's business in their own financial statements, we have not calculated a transition adjustment explicitly in our operational reports. Members are advised to use the balances available on both IFRS 4 and IFRS 17 basis, as well as the calculated Member's share of life-to-date operating results and funds held by members also available on both IFRS 4 and IFRS 17 basis, in order to calculate the transition adjustment applicable to their own IFRS 17 transition.

13. Why is there a large increase to the RSP LRC in the January (actual or projected) accounting month results?

The increase to the LRC in the accounting month of January each year is due to initial recognition of the loss component on onerous contracts for the subsequent accident year, as per our accounting policy.

RSPs are considered a single accident year reinsurance contract of which members are assuming their share, and they are onerous. As per Plan of Operations, all companies who do business in these jurisdictions are obligated to participate in their share of the RSPs. As soon as any member writes a 12 month policy which has exposure in AY 2023, they are obligated to take their share of the AY 2023 RSP results. For example, if a company writes a policy on Jan. 2, 2022, that policy ends on Jan. 1, 2023, and so the member is a participant in the AY 2023 RSP Contract. Since it is onerous, members are required to recognize the loss upfront. Therefore, as of Jan. 2, 2022, the RSP must book the loss component for the entire AY 2023 (the expected losses on the 2023 Accident Year contract). The amount of this loss component is based on our latest projection of premium and losses for that accident year.

14. How can I reconcile the change in the LRC (excluding loss component) with the income statement/cash flow amounts?

In general, we can reconcile the change in LRC (excluding loss component for onerous contracts) as:

Opening LRC (ex onerous)

Less: Insurance revenue recognized in the period = earned premium (for RSP, earned premium net of earned expense allowance)

Add: Net Premium received in the period = Received premium (for RSP, premium received net of paid expense allowance)

Add: Change in unamortized insurance acquisition cash flows (IACFs) (Note, in RSP there are no IACFs)

Closing LRC (ex onerous)

Some members have noted difficulty in reconciling this calculation from our reports. This is due to limitations in the LRC calculation tool concerning the data used to calculate the "Unearned Premium Received" (change in premium received less insurance revenue recognized). The LRC calculation tool cuts off a small amount of data (typically, fluctuations in insurance revenue or premium received due to data corrections etc.) from older periods, but the insurance revenue and premium received lines do include these. Therefore, this roll-forward may not perfectly reconcile at this time.

Regarding the change in unamortized IACFs, this can also be challenging to reconcile. The reconciliation is as follows:

Opening Unamortized Insurance Acquisition Cash Flows

Add: insurance acquisition cash flows written during the period (these are the "Agents Commissions" and "Driver Record Abstracts" on the IFRS 4 member report – note that these amounts are not included on the IFRS17 report)

Subtract: amortization of insurance acquisition cash flows

Closing Unamortized Insurance Acquisition Cash Flows

15. How can I reconcile the change in the LIC balance sheet item with the corresponding expense in the statement of Operations for FARM?

For FARM, the LIC balance includes:

- The present value of future cash flows or "PV FCF", which is the discounted estimate of unpaid incurred claims and expenses
- The Risk Adjustment (which is also a discounted amount)
- The Current Payable, which refers to liabilities for expenses that have already been incurred in the operating results but have not yet been paid to the vendor by the FARM. Examples include operating and service fees owed to FARM servicing carriers.

In the FARM statement of operations, any changes in the PV FCF and risk adjustment flow through the Claims Incurred and/or Adjustments to Liabilities for claims incurred. **The exception to this is that the change in the effect of the time value of money arising from the passage of time and the effect of changes in financial assumptions on the carrying amounts of insurance contracts** are recognized through Finance income/expense from insurance.

Taken together, the change in PV FCF and change in Risk Adjustment from the Insurance Service Expenses, minus the Insurance Finance income/expense from PV FCF and Risk Adjustment, are equal to the change in PVFCF and Risk Adjustment on the balance sheet.

Changes to the Current Payable, although they do affect the LIC balance, do not impact the statement of operations. The expenses related to the current payable have already been recorded in the expenses previously. When the invoices related to Current Payable are paid, the balance in Current Payable is reduced and the balance in Facility Association's Cash account is reduced.

16. What is the appropriate accounting treatment of premium tax and health levy for policies ceded to the RSP?

Premium tax and health levies are assessed against the direct written premium.

In the past, when a policy was transferred to the RSP, the transferred premium was classified as negative direct written premium, and the assumed premium from the member's share of RSP results was classified as direct written premium in the member's financial statements.

Under IFRS 17, the RSP is classified on the members' financial statements as reinsurance ceded/assumed, rather than direct written premium. This means that the amounts ceded/assumed do not impact the members' premium tax and health levies, which will henceforth be based only on the business directly written by the members.

To ensure this change does not have a financial impact on users of the pool, we have increased our expense allowance to compensate members for the premium tax and health levies on policies ceded to the RSP. Members will then assume their share of the cost of these reimbursements. In this way, the impact of the change will be neutral.

17. How are changes in the RSP Loss Component recorded in the operating statement?

Changes in the loss component are recorded in three different lines of the operating statement:

- "Losses on Onerous Contracts"
- "Reversals of Losses on Onerous Contracts"
- "Finance income/expense from Loss Component"

Losses on Onerous Contracts includes initial recognition of the loss component (occurs in January each year), as well as changes in valuation assumptions on the remaining coverage, such as loss ratios, expense assumptions, timing of future cash flows and changes in assumptions of future premium amounts.

Reversals of Losses on Onerous Contracts is the unwinding of the loss component as the remaining coverage is earned.

Finance income/expense from Loss Component is the change in the effect of the time value of money arising from the passage of time and the effect of changes in financial assumptions on the carrying amounts of the loss component.

18. How is the finance income/expense calculated?

For reports prior to June 2023, Finance income/expense only considered the impact on the liabilities that arises from updating the yield curve. The discount unwind was incorrectly allocated to the insurance service results for these reporting periods. In June 2023, there was a special one-time adjustment to the year to date income classification between Insurance Services Expenses and Insurance Finance Income (Expense). The total operating result is unaffected – this is purely a reclassification of the discount unwind from insurance service result to insurance finance result. For further information, please see the June 2023 bulletin issued for RSP and FARM.

From July 2023 onwards, the finance income correctly captures the discount unwinding and yield impacts.