



THE 13th ANNUAL AOSSG MEETING

Joining hands in regional cooperation and the development of IFRS

November 22-24, 2021, Virtual Meeting

Islamic finance: Adoption of IFRS 17 and Takaful

**Malaysian Accounting Standards Board
AOSSG Islamic Finance Working Group Leader**

Islamic Finance Working Group

- Malaysia (Leader)
- Bangladesh
- Indonesia
- Pakistan
- Saudi Arabia
- Syria

Objectives

- To ascertain member jurisdiction's implementation phase of IFRS 17 *Insurance Contracts*
- To understand any major implementation issues in applying IFRS 17 to takaful
- Sharing Malaysia's approach and 'main' discussions in relation to applying IFRS 17 to takaful; and whether other member jurisdictions share the same issues

Overview of Takaful

- Takaful is established on the concepts of *tabarru'* (donation) and *ta'awun* (mutual cooperation)
- There is co-operation among participants.
 - Participants **contribute (donate) to a fund and mutually indemnify co-participants** by agreeing to compensate a participant if a pre-specified event adversely affects the participant.

Takaful operator

- Operator receives a fee which may or may not be linked to performance of the Takaful fund (eg wakalah fee (fixed) and mudarabah (profit sharing))
- The operator has an obligation to make good any deficits through return free, non-recourse loan or other form of financial support

Underlying Takaful fund(s)*

- Underlying Takaful funds are set up to be distinct
- Takaful fund may or may not be separate legal entity, however legal framework creates distinct rights and obligations
- Assets and liabilities, and surplus and deficits of the fund are first and foremost those of the policyholders

Takaful operator and takaful funds are set-up to be distinct. From a financial reporting perspective, these are separate “reporting entities”

FINDINGS

Memo to WG members

- A Memo containing 5 Questions was sent to WG members
- Responses received from 5 members:
 - Malaysia
 - Indonesia
 - Pakistan
 - Saudi Arabia
 - Syria

Q1: Adoption plan of IFRS 17

Q1: Has your jurisdiction approved IFRS 17 *Insurance Contracts* for adoption?

Respondent	Response
Malaysia	Yes
Indonesia	Yes
Pakistan	Under active consideration by Securities and Exchange Commission of Pakistan (SECP) - ICAP has recommended adoption of IFRS 17 to the SECP with same effective date as IFRS 17 issued by IASB
Saudi Arabia	Yes
Syria	Yes

Q2: Adoption of IFRS 17 as 'national standard'

Q2: If your jurisdiction has adopted IFRS 17:

- (a) is it adopted **word-for-word** IFRS 17 or there are modifications made for national GAAP? If there are modifications, please elaborate.
- (b) does it have the same **mandatory effective date** of 1 January 2023? If not, please state the effective date and why you have chosen a different date.
- (c) is there any **scope exclusion being provided for entities engaged in takaful or Islamic insurance** from applying the IFRS 17 as adopted?
- (d) has there been any **local discussion or guidance issued** in applying IFRS 17 to takaful or Islamic insurance? If yes, please provide further details on the topics discussed and/or the guidance issued.

Q2: Adoption of IFRS 17 as 'national standard' (cont'd)

Respondent	Response
Malaysia	<ul style="list-style-type: none">• Adopted as MFRS 17, word-for-word IFRS 17, with mandatory effective date of 1.1.2023. No scope exclusion for takaful• MASB issued Technical Pronouncements to accompany the application of IFRS 17 to Takaful:<ol style="list-style-type: none">(1) Applicability of IFRS 17 to Takaful(2) Presentation using columns vis-à-vis IFRS 17(3) Qard (loan) accounting under IFRS 17
Indonesia	<ul style="list-style-type: none">• Adopted as PSAK 74, with mandatory effective date of 1.1.2025• PSAK 74 is not applicable to takaful, but local GAAP is, i.e. PSAK 108 <i>Accounting for Sharia Insurance Transactions</i>

Q2: Adoption of IFRS 17 as 'national standard' (cont'd)

Respondent	Response
Pakistan	<ul style="list-style-type: none">• Under consideration by SECP for word-for-word adoption of IFRS 17 by 1.1.2023. No scope exclusion for takaful is presently under consideration. SECP is currently engaged with takaful industry to deliberate and decide on the application of IFRS 17 to takaful• No guidance has been issued thus far
Saudi Arabia	<ul style="list-style-type: none">• Adopted IFRS 17, with mandatory effective date of 1.1.2023. No scope exclusion for takaful• IFRS 17 (as adopted) included additional disclosures to cater for entities applying the principles of cooperative or takaful insurance or reinsurance [details in Appendix 1]
Syria	<ul style="list-style-type: none">• Adopted IFRS 17, word-for-word with mandatory effective date of 1.1.2023. No scope exclusion for takaful• No guidance has been issued thus far

Q3: Presentation of takaful financial information

- It is common for takaful entities to present separately financial information of the takaful fund (TF) (comprises both risk fund and investment fund) from the takaful operator (TO)
- The work of the WG aimed to establish whether such presentation is common among WG member jurisdictions and whether there had been discussion on it upon the application of IFRS 17

**STATEMENT OF FINANCIAL POSITION
AS AT 31 DECEMBER 2020**

		31.12.2020		
	Note	Shareholder's fund RM'000	Family takaful fund RM'000	Company RM'000
ASSETS				
Property, plant and equipment	3	203	-	203
Right-of-use assets	4	518	-	518
Intangible assets	5	5,589	-	5,589
Investments	6	2,447,377	12,024,957	14,444,717
Financing receivables	7	15,011	-	15,011
Retakaful assets	8	-	162,030	162,030
Takaful receivables	9	-	140,095	140,095
Other assets	10	185,842	118,429	158,955
Deferred tax assets		-	-	-
Current tax assets	11	63,042	20,416	83,458
Cash and bank balances		38,893	193,264	232,157
Total Assets		2,756,475	12,659,191	15,242,733

Example of presentation of financial information of takaful fund and takaful operator in columns

Q3: Presentation of takaful financial information (cont'd)

Q3: Do takaful entities in your jurisdiction need to demarcate the assets and liabilities as well as financial performance of the takaful funds separately from the takaful operator on the face of the statement of financial position and statement of financial performance respectively, for example, by way of **columnar presentation** on the face of such statements? If yes, is it intended that such demarcation on the face of financial statements will continue when IFRS 17 is applied?

Yes

- Malaysia
- Syria

Presentation using columns are expected to continue when IFRS 17 is applied

No

- Indonesia
- Saudi Arabia; but additional disclosures are required

Under consideration

- Pakistan; but currently takaful companies do present information in columns

Q4: Qard-Regulatory requirement and its accounting

- By definition, Qard is a 'loan'
- In the context of the WG discussion, Qard is a loan from the takaful operator to the takaful fund to support deficit of the takaful fund
- The work of the WG aimed to establish whether:
 - qard is part of the regulatory requirement of takaful in the respective member jurisdiction; and
 - there has been discussion or a conclusion on how to account for qard under IFRS 17

Q4: Do local regulations require takaful operators to provide financial support, such as in the form of Qard (loan contract from the takaful operator to the takaful fund(s)) to takaful funds that are in deficit? If yes, has there been discussion or a conclusion as to how Qard would be accounted for under IFRS 17?

Q4: Qard-Regulatory requirement and its accounting (cont'd)

Qard forms part of local regulatory requirements

- **Yes:** Malaysia, Indonesia & Pakistan
- **No:** Saudi Arabia & Syria

Guidance on accounting for Qard under IFRS 17?

- **Yes:** Malaysia
- **No:** Indonesia, Pakistan, Syria
- **Others:** Saudi Arabia - additional disclosures (including about Qard) are required in IFRS 17 (as adopted)

Summary

- **Malaysia, Saudi Arabia and Syria:** adopted IFRS 17 word-for-word, with no scope exclusion for takaful
- **Indonesia:** IFRS 17 (adopted as PSAK 74) is not applicable to takaful; local GAAP is
- **Pakistan:** Regulator is considering the adoption of IFRS 17, word for word as issued by the IASB, including the effective date, for insurance and takaful entities
 - Phase-based implementation strategy has been rolled out by the SECP to prepare the industry for the adoption of IFRS 17
- **Guidance/specific requirements** relating to the application of IFRS 17 to takaful
 - Malaysia: Technical Pronouncements accompanying the application of IFRS 17
 - Saudi Arabia: IFRS 17 (as adopted) added a list of additional disclosures
- Members did not raise any specific issue for further discussion

MALAYSIA: IMPLEMENTATION OF MFRS 17 TO TAKAFUL

Adoption of IFRS 17

- MFRS 17 was issued by MASB in August 2017
 - MFRS 17 is word-for-word from IFRS 17 including the effective date
 - In August 2020, MASB issued Amendments to MFRS 17 (similar to Amendments to IFRS 17 issued by IASB in June 2020)
- To support implementation of MFRS 17:
 - MASB established several workstreams, including **MFRS 17 Implementation Task Force**. The Task Force discussed issues that are unique to local facts and circumstances and provided recommendations to the industry [see **Appendix 2** for the list of issues discussed by this Task Force]
 - MASB issued 3 Technical Pronouncements

MASB Technical Pronouncements



Issues Bulletin 1

MFRS 17 Insurance Contracts: Definition and Scope for Takaful



Issues Bulletin 2

Columnar Presentation of Takaful Funds in Takaful Entity Financial Statements



Issues Bulletin 3

Reporting Qard in the Takaful Fund Column within Takaful Entity Financial Statements

Issues Bulletin 1: Scope

MFRS 17 (IFRS 17) applies to 'insurance contracts', which involve:

Acceptance of significant 'insurance risk' by one party

Agreement to compensate another party for adverse consequences of an insured event

Based on IFSA 2013 and BNM TOF – takaful is a 'contract' between participants and the Takaful Fund (TF):

Mutuality aspect of a takaful fund is consistent with the TF accepting "insurance risk" from participants

TF is the party agreeing to compensate a participant if an insured event adversely affects that participant

Issues Bulletin 1: Scope (cont'd)

- Definition of an insurance contract
 - “A contract under which one party (the issuer) accepts significant insurance risk from another party (the policyholder) by agreeing to compensate the policyholder if a specified uncertain future event (the insured event) adversely affects the policyholder.”
- Current takaful arrangements are designed to offer participants protection that is economically similar to insurance whilst adhering to Shariah principles
- MFRS 17 applies to those contracts that fall within the ‘insurance contract’ definition, regardless of their legal form or the legal form of the entity accepting insurance risk.

Issues Bulletin 1 does not provide a new conclusion on the applicability of MFRS 17 to Takaful but serves as a “refresher” on the earlier consensus that MFRS 4 *Insurance Contracts*, adopted by MASB in 2008 applies to takaful contracts

Issues Bulletin 2: Presentation

- It is common for takaful entities in Malaysia to present separate information for TF and TO in columns, because it helps to demonstrate that:
 - the takaful entity is conducting its business in a Shariah-compliant manner i.e., to differentiate the rights and obligations between the TO and TF
 - risk is shared among participants for the mutual benefit of participants; while the TO is a “manager” and administrator of the TF
- Columnar presentation could be made in the takaful financial statements under MFRS 17 and that, each column is considered as a reporting entity that would produce MFRS-compliant numbers.
- Based on cost-benefit consideration, MASB recommended columns of the TF and Takaful entity be presented on the primary financial statements

Issues Bulletin 2: Presentation (cont'd)

Columns as separate reporting entities

Conceptual Framework acknowledges that other entities, which may not be legal entities, can also be reporting entities

Columns provide relevant information to users

Information presented would provide faithful representation

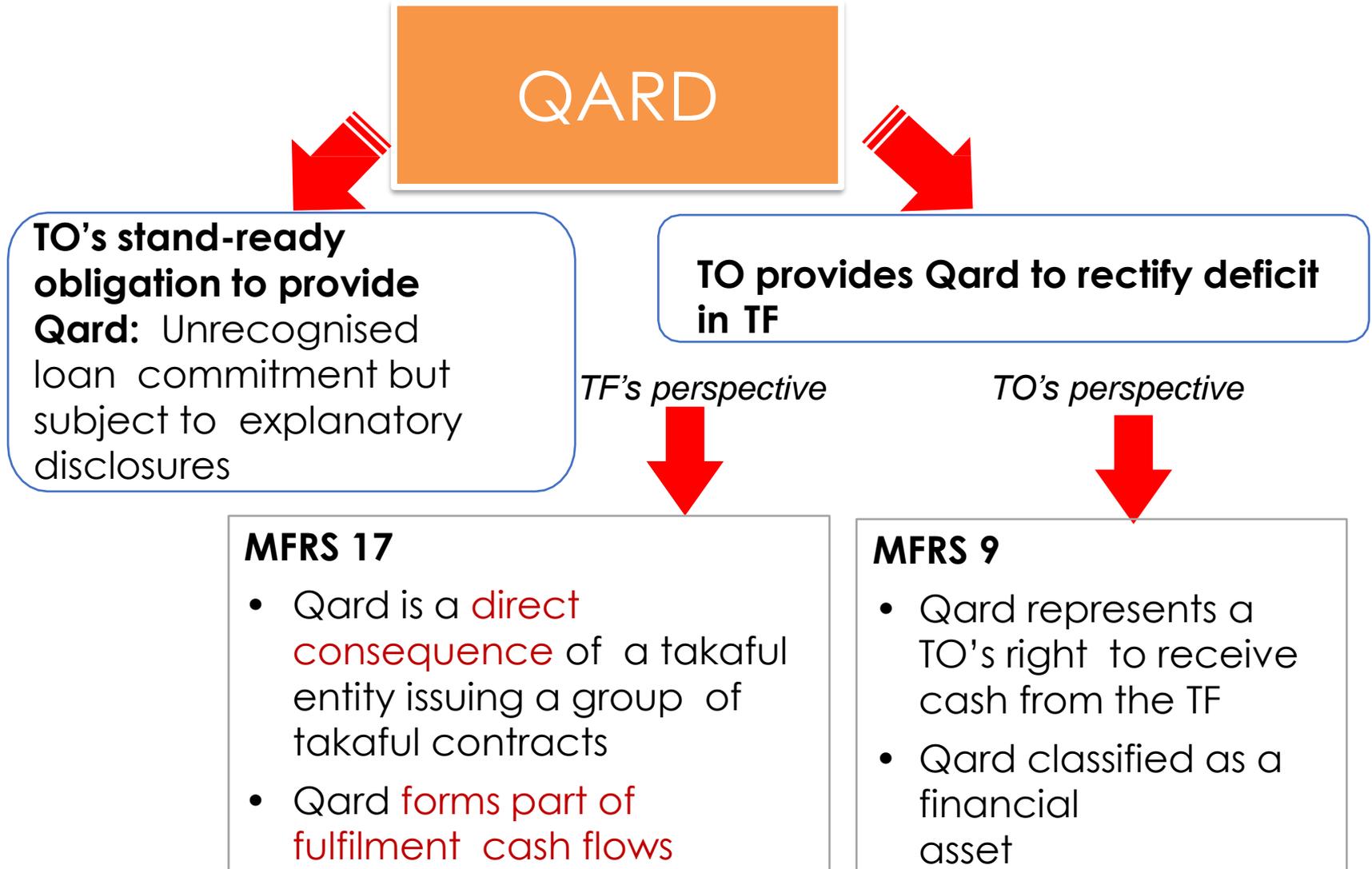
Prominence

Information about TF would not be more prominent than the information for the takaful entity as a whole

Issues Bulletin 3: Qard

- Scope: Qard as required by the Islamic Financial Services Act 2013 to provide financial support to fund deficit of takaful funds
 - Issues Bulletin 3 does not consider other application of qard
- Terms of takaful contracts include the implied terms within the legal and regulatory framework that governs those contracts, and this includes the requirement for the takaful operators to contribute qard
 - These terms are mutually known and accepted by the contracting parties, namely the takaful participants and the takaful operator
- Thus, the potential contribution of qard from a TO in these circumstances is a **direct consequence of the issuance of a group of takaful contracts**
- Conclusion: Qard arises as a direct consequence of the takaful entity issuing takaful contracts, and hence forms part of fulfilment cash flows under IFRS 17

Issues Bulletin 3: Qard (cont'd)



THANK YOU

Appendix 1: Additional disclosure requirements in IFRS 17 as adopted in Saudi Arabia

Disclosures related to entities that enter into transactions of cooperative or Takaful insurance or reinsurance:

In case that the entity applies principles of cooperative or Takaful insurance or reinsurance that is based on the separation between insurance operations and shareholders' operations, it shall disclose that fact and disclose:

- a. Assets, liabilities, income, expenses and other components of comprehensive income of insurance operations in a manner that distinguish them from those of shareholders' operations;
- b. The contractual capacity of the entity and the insured (for example, statement in the policy that the entity is a manager of insurance operation, agent or mudhareb, or that the entity itself is the insurer);
- c. Nature of contracts transferred from other insurers, or through business combinations, that is different from that of contracts entered by the entity;
- d. Financial guarantee contracts (if the entity chooses to treat them as insurance contracts, as permitted by IFRS 17), and whether they are contracts for insurance operations or shareholders' operations;
- e. Contracts that constitute a group or series of contracts, that might be necessary to deal with as a whole as per paragraph 9 of IFRS 17;

Appendix 1: Additional disclosure requirements in IFRS 17 as adopted in Saudi Arabia (cont'd)

- f. If an insurance contract includes non-insurance components, the entity shall disclose such components and whether they relate to insurance operations or shareholders' operations;
- g. Allocation of discretionary participation features (referred to in paragraph 71), if any, to insurance operations and shareholders' operations;
- h. Contractual arrangements related to management services and its fees, the entity's share in insurance operation surplus (for example, agent fees deducted after transferring a percentage from the surplus to the policy holders' fund, agent fees or mudharaba that is considered an expense of the insurance operation, or performance bonus as a percentage of the surplus) and amounts related thereto;
- i. Contractual arrangements between insurance operations and shareholders' operations related to the bases upon which deficit in insurance operations shall be treated (for example, providing finance or qardh hasan (interest-free loan) from shareholders to the insurance operations and the way it shall be amortized or repaid, or bearing such deficit by shareholders) and the amount of deficit; and
- j. Nature of reinsurance contracts entered into by the entity and whether they are concluded with entities that provide reinsurance services on cooperative insurance basis or conventional trading bases.

Appendix 2: Issues discussed by the Task Force (January-July 2021) - Conventional

No	Issue
1	Cash flows: Interaction between MFRS 17 and other MFRSs
2	Contract modification: The exercise of right included in the terms of a contract
3	Reinsurance: Treatment of reinsurance cash flows for the participating contracts - presentation of the direct and reinsurance contract held revenue and service expense
4	Contract Boundary issue for insurers that has unilateral right to cancel policy
5	Investment component for participating product – determining non-distinct investment component
6	Application of mutualisation for participating products in accordance with IFRS 17.B67-B68
7	Application of IFRS 17.B128(c) for participating products for the difference between the expected asset share balance and actual asset share balance
8	Treatment of orphan estate in relation to IFRS 17.B71



Appendix 2: Issues discussed by the Task Force (January-July 2021) - Conventional

No	Issue
9	Treatment of orphan estate as Liability for Remaining Coverage or Liability for Incurred Claims?
10	Reinsurance cash flow and CSM in participating products – how to reflect claims/bonus from underlying item variances from reinsurance contract in underlying contract.
11	Treatment of bancassurance upfront payments – is it an IFRS 17 acquisition cash flows?
12	Insurance acquisition cash flows – How should an entity recognise insurance acquisition cash flows as expenses when incurred applying IFRS 17.59(a)?
13	Premium allocation approach optionality in IFRS 17.59(a) to expense or defer acquisition cash flows for transition calculation purposes
14	Calculation of the Loss Recovery Component for losses-occurring reinsurance contracts held (application of IFRS 17.66A in conjunction with IFRS 17.B119C)
15	Coverage units determination for annuities contracts to appropriately reflect the service provided

Appendix 2: Issues discussed by the Task Force (January-July 2021) - Takaful

No	Issue
1	Wakalah* fee expense – Acquisition or maintenance expense from the Takaful Fund perspective
2	Application of risk adjustment for Liability for Remaining Coverage for takaful contracts – in relation to columnar presentation of takaful company
3	Treatment of unallocated surplus – Liability for Remaining Coverage or Liability for Incurred Claims?
4	Application of IFRS 17.B128(c) for takaful – presentation of non-investment component experience variance in Takaful Fund