

Transforming Insurance Reporting: Challenges of IFRS 17 Implementation*

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Abstract

The new reporting standard, IFRS 17 – Insurance Contracts, replaces the previous IFRS 4 and introduces significant changes in how insurance companies measure, recognize, and report their insurance contracts. IFRS 4 had become partly outdated and inefficient, prompting the need for a more transparent, standardized approach. Key challenges of IFRS 17 include adjusting accounting policies for revenue, profit, and liability measurement, as well as assessing risk and reserves. Additional difficulties arise from the complexity of contract measurement, alignment with regulatory requirements, and technological upgrades needed for compliance. The implementation of IFRS 17 affects management, staff, and external users, enabling clearer, more transparent, and comparable reporting of insurance company performance.

Keywords: insurance, reporting, IFRS 17

Introduction

The International Accounting Standards Board (IASB) developed the International Financial Reporting Standards (IFRS) to harmonize financial reporting globally, enhancing transparency, comparability, and informed decision-making (IASB, 2017). IFRS 17 – Insurance Contracts, issued in 2017 and effective from January 1, 2023 (postponed due to COVID-19), replaced IFRS 4, introducing comprehensive requirements for recognition, measurement, presentation, and disclosure of insurance contracts (IASB, 2017). The standard aims to provide clear insights into an insurer's financial position and performance, fostering investor confidence. IFRS 17 applies to insurance and reinsurance contracts issued and held by insurers, including certain investment contracts with direct participation features (IASB, 2017) so insurance contracts may be grouped if they achieve a commercial effect collectively. Components not closely linked to insurance must be separated and accounted for under IFRS 9 – Financial Instruments (Ernst & Young, 2021). Insurers must assess all contracts, including short-term policies and consider contract renewal options and historical experience. The standard introduces a single measurement model based on the present value of future cash flows, including expected cash flows, discount rates, risk adjustment and contractual service margin (CSM). A simplified Premium Allocation Approach (PAA) may be applied for short-duration contracts, typically one year or less (Radić Blažin, 2022). IFRS 17 emphasizes separating insurance revenue, service costs, and liabilities, ensuring transparent and comparable reporting. Risk management and market-based discounting are crucial for accurate liability assessment (KPMG, 2020).

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IFRS 4 allowed existing practices, leading to inconsistencies and limited comparability. On the other side IFRS 17 addresses these limitations by introducing a unified measurement model, recognizing revenue as insurance services are provided, mandating detailed disclosures on risks, assumptions and contract margins, incorporating risk adjustments for future cash flow uncertainty (International Association of Insurance Supervisors, 2022). Insurance contracts are recognized at the earliest of: the start of coverage, first premium payment, or when a contract becomes onerous (IASB, 2017). Derecognition occurs when all obligations are fulfilled, contracts are terminated or the insured risk ceases. This process ensures liabilities are removed from financial statements reflecting accurate financial positions and enhancing transparency. IFRS 17 significantly improves the quality, comparability, and transparency of insurance company financial statements, requiring adjustments to accounting systems, policies and staff training. While implementation is complex, the standard provides long-term benefits through consistent reporting, better investor confidence, and a clearer depiction of profitability and risk exposure.

Challenges in Implementing IFRS 17 – Insurance Contracts from an Accounting Perspective

The introduction of IFRS 17 has presented significant accounting challenges for insurance companies, affecting the recognition of liabilities, revenue, expenses and reserves. This section highlights the key challenges insurers face when adapting existing accounting policies, measuring insurance contracts, collaborating with regulators and provides illustrative accounting examples.

Regarding measurement of insurance contracts there are three models:

1. General measurement model (GMM)

The GMM provides a consistent framework for measuring insurance liabilities by considering the present value of future cash flows and recognizing profit over time. It consists of four elements: estimating future cash flows, discounting for time value of money, risk adjustment and the Contractual Service Margin (CSM) which reflects expected profit. Future cash flows include premiums received, claims, administrative costs and other service-related expenses. Cash flows are discounted to present value using market-consistent rates, which may follow a top-down or bottom-up approach. The CSM prevents premature profit recognition and adjusts for changes in expected future cash flows, mitigating financial statement volatility. Loss-making contracts are recognized immediately as losses. Liabilities are split into *remaining coverage* – future services including CSM and *incurred claims* – payments and related costs already incurred. Factors like inflation, market conditions, and legal changes must be considered in ongoing evaluations (Ernst & Young, 2021).

2. Variable fee approach (VFA)

VFA is used for contracts with direct participation in underlying assets. It adjusts the CSM for changes in the fair value of underlying assets, recognizing profit gradually. This approach reduces volatility and aligns insurer and policyholder interests but requires sophisticated models and high-quality data (Ernst & Young, 2021). Advantages of this model are that it stabilizes financial statements, it is transparent to users, it enables fair profit allocation and flexibility in risk management. Some disadvantages can be connected to complex measurement, data-intensive model, regulatory alignment challenges and it also requires continuous monitoring.

3. Premium allocation approach (PAA)

PAA simplifies liability measurement for short-term or simpler contracts, mostly under one year. Revenue is recognized gradually over the coverage period without detailed future cash flow estimates. Long-term contracts can only use PAA if results closely approximate GMM outcomes. This approach reduces implementation complexity and costs (Ernst & Young, 2021). Advantages of this model are simplicity, also lower implementation costs and flexibility for longer contracts while disadvantages can be linked to limited to short-term contracts, discounting for long-term contracts and less detailed risk reflection. IFRS 17 replaces IFRS 4's flexible practices with a forward-looking approach. Future cash flows, including premiums, claims and administrative costs, must be regularly reviewed and discounted to present value using market-consistent rates. Non-financial risks are also incorporated, enhancing transparency and stability (International Association of Insurance Supervisors, 2022; KPMG, 2020). The CSM is dynamically adjusted for changes in expected cash flows, ensuring profit recognition aligns with services provided. Discount rates reflect the time value of money, liquidity and associated risks, calculated using top-down or bottom-up approaches.

Revenue is recognized over the contract period based on services provided, requiring detailed contract analysis and ongoing monitoring. Future cash flows are projected, discounted and adjusted for risk to ensure accurate and consistent profit recognition (KPMG, 2020). Risk adjustments reflect uncertainties in timing and amount of cash flows. Insurers must quantify risks, apply discounting and account for adverse events, ensuring adequate reserves. Two main approaches are used: GMM for long-term contracts and PAA for short-term contracts (BDO Global, 2023; KPMG, 2020).

In Croatia, insurers must align IFRS 17 with local regulations, including Solvency II and HANFA requirements (The Croatian Financial Services Supervisory Agency) which focus on capital adequacy, risk management and financial stability. Implementing IFRS 17 requires significant investment in systems, processes and personnel, particularly challenging for smaller insurers (Vašiček et al., 2020; HANFA, 2023).

To illustrate, for example the GMM model, according to IFRS 4 premium was recognized immediately as revenue but according to IFRS 17 premium is recorded as liability and recognized as revenue over the coverage period. Regarding claims and reserves according to IFRS 4 claims were recognized immediately but under IFRS 17 are recognized within insurance contract liabilities. Additionally, according to VFA model under IFRS 4 all premium and investment income were recognized immediately but under IFRS 17 fixed and variable fees are separated and revenue is recognized gradually based on asset performance. These changes ensure more accurate timing of revenue and liability measurement, enhancing transparency and financial statement reliability (Ernst & Young, 2021; KPMG, 2020).

Characteristics of Insurance Companies' Financial Reporting

Financial reporting for insurance companies differs from that of other businesses due to the nature of their assets, technical provisions, regulatory requirements and risk management practices inherent to insurance operations. Reports must comply with International Financial Reporting Standards (IFRS) and national insurance law, providing management, investors and other external users with insights into the company's financial position and performance (Zager et al., 2021). Key financial statements include:

1. **Statement of Financial Position (Balance Sheet)** – shows assets, liabilities and equity at a specific date, with particular attention to investments and technical provisions such as claims, mathematical reserves, and unearned premiums.
2. **Statement of Comprehensive Income** – reports total revenue, expenses, profit or loss, and comprehensive income over a period.
3. **Cash Flow Statement** – details cash inflows and outflows from operating, investing and financing activities.
4. **Statement of Changes in Equity** – presents equity changes, including transactions with owners and impacts on profit or loss.
5. **Notes to Financial Statements** – explain reported items, providing crucial context for understanding financial position, performance, and risk.

Insurance companies must also prepare regulatory and supervisory reports under Solvency II and national laws, including solvency and financial condition reports (SFCR), regular supervisory reports (RSR), own risk and solvency assessments (ORSA), capital requirement reports (SCR, MCR), reinsurance reports and risk management reports (Vašiček et al., 2020). HANFA regulates reporting formats and content, ensuring consistency with IFRS and national standards.

Impact of IFRS 17 – Insurance Contracts on Financial Statement Users

Internal users of financial statements primarily include company employees, particularly management and executives. IFRS 17 has significantly influenced financial accounting and actuarial systems, as well as operational reporting models. The standard provides more reliable data on current and future profitability of insurance contracts, increasing transparency and offering comparable information for management to assess the company's position relative to industry peers.

For management, IFRS 17 enhances decision-making by providing detailed analysis of financial performance by product type and business segment, allowing better identification of profitable contracts and high-risk areas. It improves cost and revenue control, aiding in pricing strategy and long-term financial planning. Accounting and

finance teams must now recognize revenue based on services provided, utilize advanced models to assess technical provisions and future cash flows and risk management teams gain better tools for evaluating long-term risks, capital reserves, and solvency planning (Ernst & Young, 2019).

External users include shareholders, investors, creditors, regulators, auditors, partners and the public. IFRS 17 increases transparency of profitability and financial results, offering shareholders clearer insights into company performance. Investors and shareholders benefit from more comparable and globally consistent financial statements, supporting informed investment decisions. IFRS 17 separates insurance service revenue from financial activity results, improving understanding of sources of profit and aligning with Solvency II principles. Regulators, reinsurers, and credit rating agencies gain better insights into technical provisions, capital requirements, and long-term risk management (Deloitte, 2020; EIOPA, 2017).

In following part of the paper and IFRS 17 – Presentation in financial statements of Croatia osiguranje d.d. will be analyzed. Croatia Osiguranje d.d. is the oldest and leading insurance company in Croatia, providing life and property insurance services, as well as reinsurance in the non-life insurance sector, operating in both Croatia and Slovenia. Its parent company, CO Group, also operates in North Macedonia, Bosnia and Herzegovina and Serbia. Since 2004, the company's shares have been listed on the official market of the Zagreb Stock Exchange, and since 2014, it has been majority-owned by the Adris Group from Rovinj. With centuries of experience, Croatia Osiguranje has stood by people through historical challenges, and thanks to its financial and asset strength, the company has become an important economic leader.

The company conducts activities related to entering into and fulfilling life insurance contracts, which include the following types of insurance: life insurance, annuity insurance where the policyholder bears the investment risk, supplementary life insurance, insurance for weddings, entering into a life partnership, or birth, tontines, insurance with capitalized payouts, and management of collective pension fund assets. The company also conducts activities related to entering into and fulfilling non-life insurance contracts, which include: accident insurance, health insurance (excluding mandatory health insurance), motor vehicle insurance, railway vehicle insurance, aircraft insurance, vessel insurance, cargo in transit insurance, fire and natural disaster insurance, other property insurance, motor vehicle liability insurance, aircraft liability insurance, vessel liability insurance, other liability insurance, credit insurance, guarantee insurance, various financial loss insurance, legal protection and assistance insurance.

In addition to the above, the company also performs activities directly or indirectly related to insurance operations, including offering investment fund units and voluntary pension fund and pension insurance programs in accordance with laws regulating such offerings, distributing insurance for other insurance companies and acting as a credit intermediary in accordance with relevant regulations. Part of the assumed risk is ceded to reinsurance domestically and abroad for additional protection. As of December 31, 2023, the company's share capital amounts to €79,923,642.00, consisting of 429,697 shares with a nominal value of €186.00 each, fully paid in cash.

The company is organized so that all key and administrative processes are centralized, while the insurance sales process is strengthened through organizational adaptation to different client categories. The organizational structure is established according to the following functions: support functions, business development and asset management, finance, insurance operations, and sales. This organizational approach aims to accelerate business operations and maintain a strong client focus.

Statement of Financial Position

The statement of financial position systematically presents assets, liabilities, and equity, allowing assessment of the company's financial standing. IFRS 17 significantly changed how insurance contract-related items are measured and presented. Assets and liabilities from insurance contracts are now clearly separated, simplifying comparison with other companies and standardizing reporting (IASB, 2017).

Under IFRS 4, deferred acquisition costs, business acquisitions, and premiums receivable were shown separately, often without a clear link to insurance obligations. IFRS 17 now requires aggregation of rights and obligations within portfolios, including insurance coverage, claims receivable, and contract service margins. This enhances transparency and comparability, linking assets directly to obligations. For example, Croatia osiguranje's insurance contract liabilities increased from €702,494 million in 2022 (IFRS 4) to €861,986 million in 2023 (IFRS 17), a 22.72% increase, reflecting more precise liability measurement and recognition of future cash flows (Croatia osiguranje d.d., 2022–2023).

Statement of Comprehensive Income

IFRS 17 separates revenue into *insurance service results* and *financial investment results*, aligning revenue recognition with the provision of services. Premiums are no longer recognized immediately upon receipt but are spread over the contract duration. Expenses, including claims and service costs, are recognized simultaneously with revenue, providing a more stable and accurate view of profitability. Croatia osiguranje's insurance revenue increased from €357,229 million in 2022 to €395,384 million in 2023 (+10.68%), while insurance expenses rose from €325,508 million to €375,931 million (+15.51%). The net financial result turned negative (€-4,723 million in 2023) due to adjustments in contract liabilities and risk provisions (Ernst & Young, 2021).

Cash Flow Statement

The cash flow statement now links cash flows to insurance service coverage rather than premium receipt. IFRS 17 requires separation of insurance operational cash flows from financial cash flows, enhancing clarity of fund allocation. Croatia osiguranje experienced a significant negative cash flow from operating activities in 2023 (€-58,055 thousand) due to higher claims and expenses under IFRS 17, while investment cash flows improved slightly (€-7,753 thousand) and financing cash flows changed modestly (€-3,492 thousand), reflecting the impact of the new standard (KPMG, 2020; Žager et al., 2021).

Notes to the Financial Statements

Notes provide additional explanations and disclosures necessary for understanding financial statement items. IFRS 17 requires detailed explanation of revenue and liability recognition methods, including cash flow estimation, discounting and risk adjustments. Reinsurance effects and expectations from reinsurers must be disclosed, as well as changes in contract obligations during the reporting period. These notes enhance transparency, comparability, and provide insights into long-term financial obligations and risk management (IASB, 2017).

Conclusion

The application of IFRS 4 highlighted significant inconsistencies in accounting for insurance contracts, including measurement of liabilities, recognition of income and profit, and misalignment with accounting models used in other industries. Its provisions were outdated, insufficiently adapted for long-term contracts and market data, and often failed to reflect the financial effects or possible outcomes of certain contracts.

The introduction of IFRS 17 represents a major shift for insurance companies, focusing on the measurement, recognition, and reporting of insurance contracts to enhance transparency and comparability of financial statements within the industry. Unlike IFRS 4, which allowed diverse interpretations and inconsistent financial reporting, IFRS 17 provides a standardized approach based on discounted future cash flows that account for risk and the time value of money. This aims to improve the quality of financial information, disclosure, and decision-making for users of financial statements. The standard also brings challenges, requiring significant adjustments in accounting systems, technological upgrades, and employee training, as well as alignment with local regulatory frameworks such as Solvency II and national supervisory authorities like HANFA. The example of Croatia osiguranje d.d. demonstrates how IFRS 17 affects balance sheets, statements of comprehensive income, cash flows, and notes, showing improved transparency and precision in 2022 and 2023 compared to the previous standard.

While IFRS 17 presents complex implementation demands, it delivers long-term benefits, including higher-quality financial reporting, better risk and liability understanding and increased trust among financial statement users. Globally operating insurers can more effectively manage financial risks, align with international accounting practices and also communicate results transparently to investors and regulators. Ultimately, IFRS 17 is a crucial step toward modernizing insurance accounting standards. Though resource-intensive, it contributes to financial stability, comparability, and sustainability, offering insurers not just regulatory compliance but a strategic opportunity to enhance internal processes, financial management, and stakeholder confidence, forming a foundation for long-term success.

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