



Institute  
and Faculty  
of Actuaries

# What will IFRS 17 mean in practice?

Alice Boreman, Deloitte  
Simon Sheaf, Grant Thornton

# What is IFRS 17?

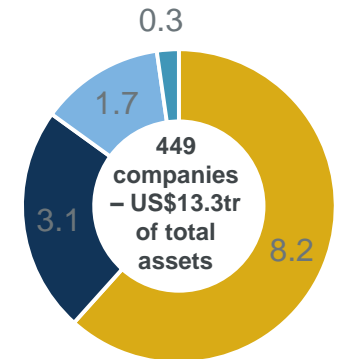
**IFRS 17 is the first truly international, comprehensive accounting Standard for insurance, replacing IFRS 4 – an interim Standard that results in widely divergent practices.**

## **The IASB aimed for IFRS 17 to bring:**

- Consistent accounting for all insurance contracts
- Updated information about obligations, risks and performance of insurance contracts
- Increased transparency in financial information reported by insurance companies

## **Total assets of listed IFRS insurers (in US\$ trillions)\***

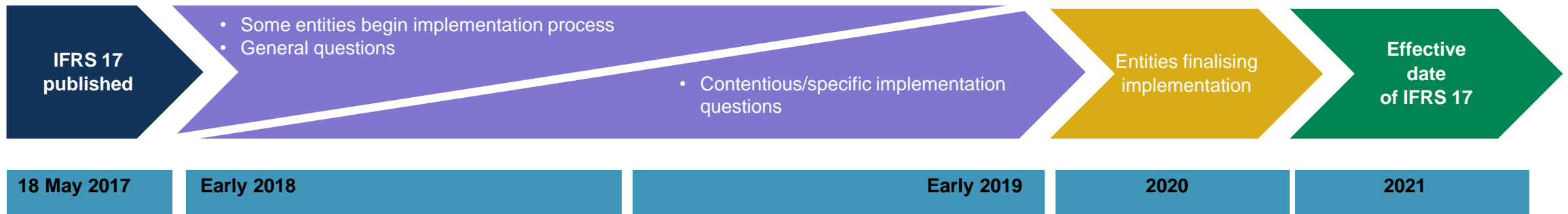
- Europe - 87 companies
- Asia Pacific - 156 companies
- Canada - 10 companies
- Africa, Middle East and Latin America - 196 companies



Institute  
and Faculty  
of Actuaries

# IFRS 17 is now published

- The standard was published by the IASB on **18<sup>th</sup> May 2017** with an effective date of **1 January 2021**
- IFRS 17 replaces IFRS 4 – an Interim Standard that allowed widely divergent practices in different regions



\* Source: <http://www.ifrs.org/news-and-events/2017/05/live-presentations-on-new-insurance-standard/>



Institute  
and Faculty  
of Actuaries

# IFRS 17 Technical Overview

IFRS 17 starts with a few **key principles**:

- Current market-consistent valuation of expected future cash flows
- Reflects risk associated with those cash flows  
=> discounted, risk-adjusted cash flows
- No recognition of profit until services are provided, losses recognised immediately
- Transparency through disclosures
- Revenue metrics consistent with other non-insurance industry revenue metrics

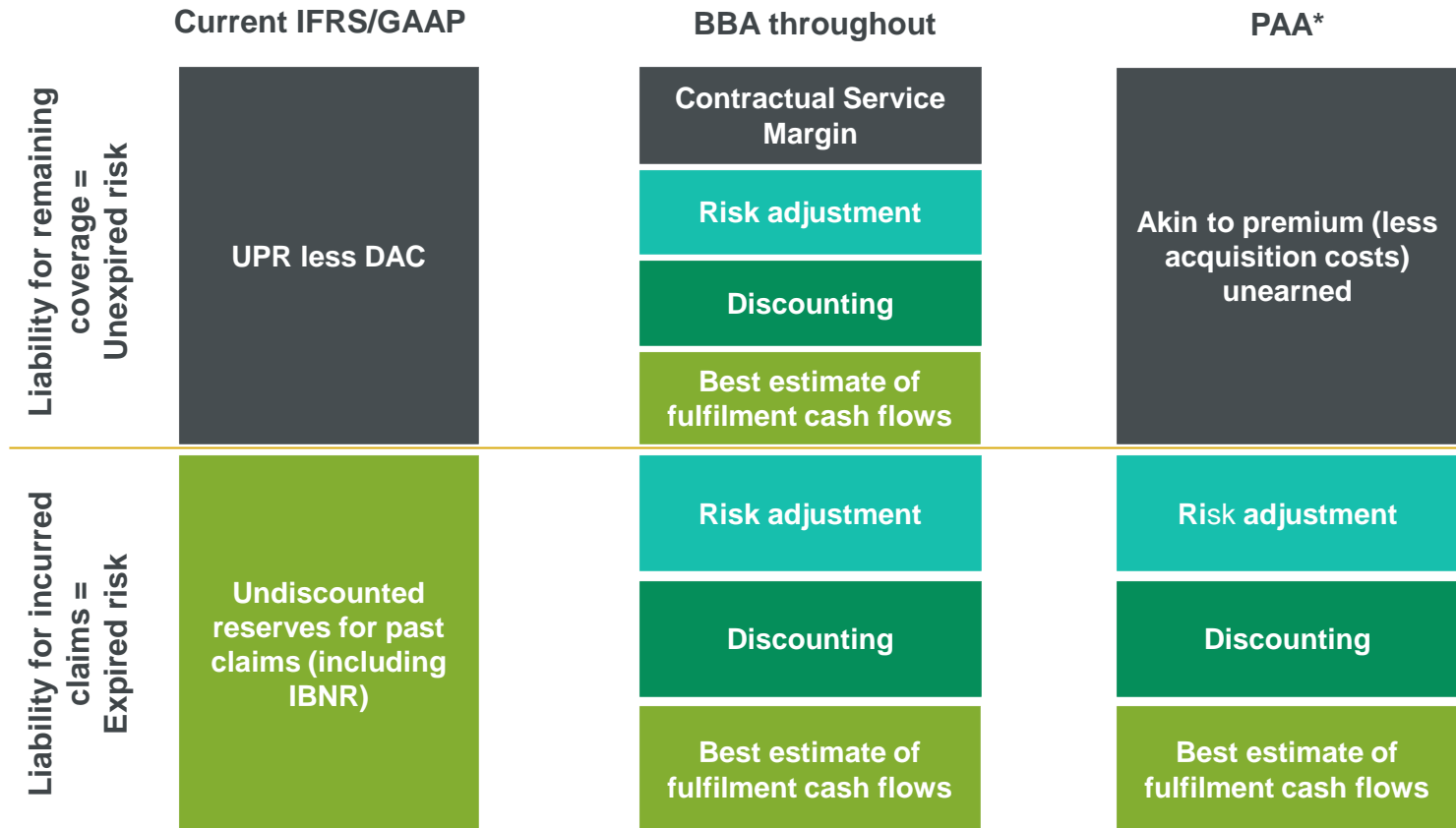
## Overview:

- General measurement model often referred to as the Building Block Approach (BBA)
- Simplifications exist for eligible contracts:
  - Premium Allocation Approach (PAA) for unexpired risk component
  - PAA with undiscounted expired risk
- Recognition of contracts - earliest of start of coverage and premium receipt (plus onerous contract test)
- Applies to outwards reinsurance too
- More granularity required (level of aggregation)
- Detailed disclosure requirements



Institute  
and Faculty  
of Actuaries

# IFRS 17 Technical Overview



There are a number of **key changes**:

- Move to a best estimate basis, no reserve margins will be permitted instead an explicit risk adjustment will be required
- Driver of profit and recognition of profit over time will change due to new best estimate valuation model, unwind of discount, release of risk adjustment and release of CSM (unearned profit under BBA only)
- Underwriting result and finance result will have a new 'feel' and presentation.
- New KPIs, strategy, incentives and education are required as well as system changes
- Expansion of disclosure requirements

Size of boxes for illustrative purposes only. Specific conditions must be met for PAA (\*)



Institute  
and Faculty  
of Actuaries

# Key areas of the standard

**Simplified  
approach  
(PAA)**



**Best estimate  
cash flows**

**Discounting**

**Risk  
adjustment**



**Level of  
aggregation /  
onerous  
contracts**



**Contractual  
service margin  
(BBA only)**

**Reinsurance  
measurement**

**Acquired  
portfolios**

**Presentation  
and disclosure**



**Transition**



Institute  
and Faculty  
of Actuaries



# Simplified approach (PAA)

**Objective:**  
Practical expedient for short-term contracts

Applies equally to insurance and reinsurance (*both inwards and outwards*) contracts, but they will need to be assessed separately

When are contracts eligible for the PAA?

OR

If at inception the coverage period is **one year or less**

If at inception, reasonably expect that measurement would not differ materially from applying the BBA

Not met if expect **significant variability** in the fulfilment cash flows before a claim is incurred

Variability increases with

Length of contract coverage

Embedded derivatives

- Expected to be adopted for the majority of general insurance contracts.
- Multi-year policies such as construction, retrospective reinsurances (LPTs / ADCs), risk attaching RI etc may not be eligible. Also need to consider contract boundaries.
- Key features which may restrict PAA eligibility:
  - the difference between the incidence of risk earning pattern used under PAA vs CSM earning pattern based on “coverage units”.
  - Exposure to discount rates driven by the level of discount rates and the length of the claims payout pattern over time.
  - The impact of positive and negative shocks which would change the unearned profitability assumptions.



Institute  
and Faculty  
of Actuaries

# Risk Adjustment

## Objective:

Adjustment to make insurer indifferent between the PV of the uncertain cash flows and the PV of certain cash flows.

Possible methods...?

Value at Risk  
(VaR)

Tail Value at Risk  
(tVaR)

Cost of Capital  
(CoC)

- No prescribed approach
- Risk adjustment required on a gross and reinsurance basis separately
- Re-measured at each reporting period
- Allows for effect of diversification between portfolios within a reporting entity
- Regardless of the method chosen, a confidence level equivalent must be calculated and disclosed (i.e. VaR percentile)



Institute  
and Faculty  
of Actuaries



## Level of aggregation / onerous contracts

### Objective:

Separate profitable and loss making contracts  
No CSM at end of coverage period

### Step 1: Identify portfolios

= insurance contracts subject to similar risks and managed together as a single pool




Contracts in different products lines would be in different portfolios.



### Step 2: Divide each portfolio into groups:

- contracts issued within the same 12-month period
- information about the contracts' resilience (considered on a gross basis)
- consistent with internal reporting
- exemption for regulatory pricing
- group not reassessed after inception

Fulfilment cash flows may be estimated at a **higher level of aggregation** than the group or portfolio => then need to **allocate estimates to groups of contracts**

Profitable contracts		Contracts that at inception have no significant possibility of becoming onerous subsequently, if any	Unearned profit is recognised as liability and is released as insurance services are provided
		Other profitable contracts, if any	
Onerous contracts		Contracts that are onerous at inception, if any	A loss is recognised in P/L

**PAA:**  
**At inception:** Assume no contracts in the portfolio are onerous, unless **facts and circumstances** indicate otherwise



Institute  
and Faculty  
of Actuaries

# Presentation and disclosure

## Objective:

Transparency through disclosures

Revenue metrics consistent with other non-insurance industry revenue metrics

### Statement of comprehensive income

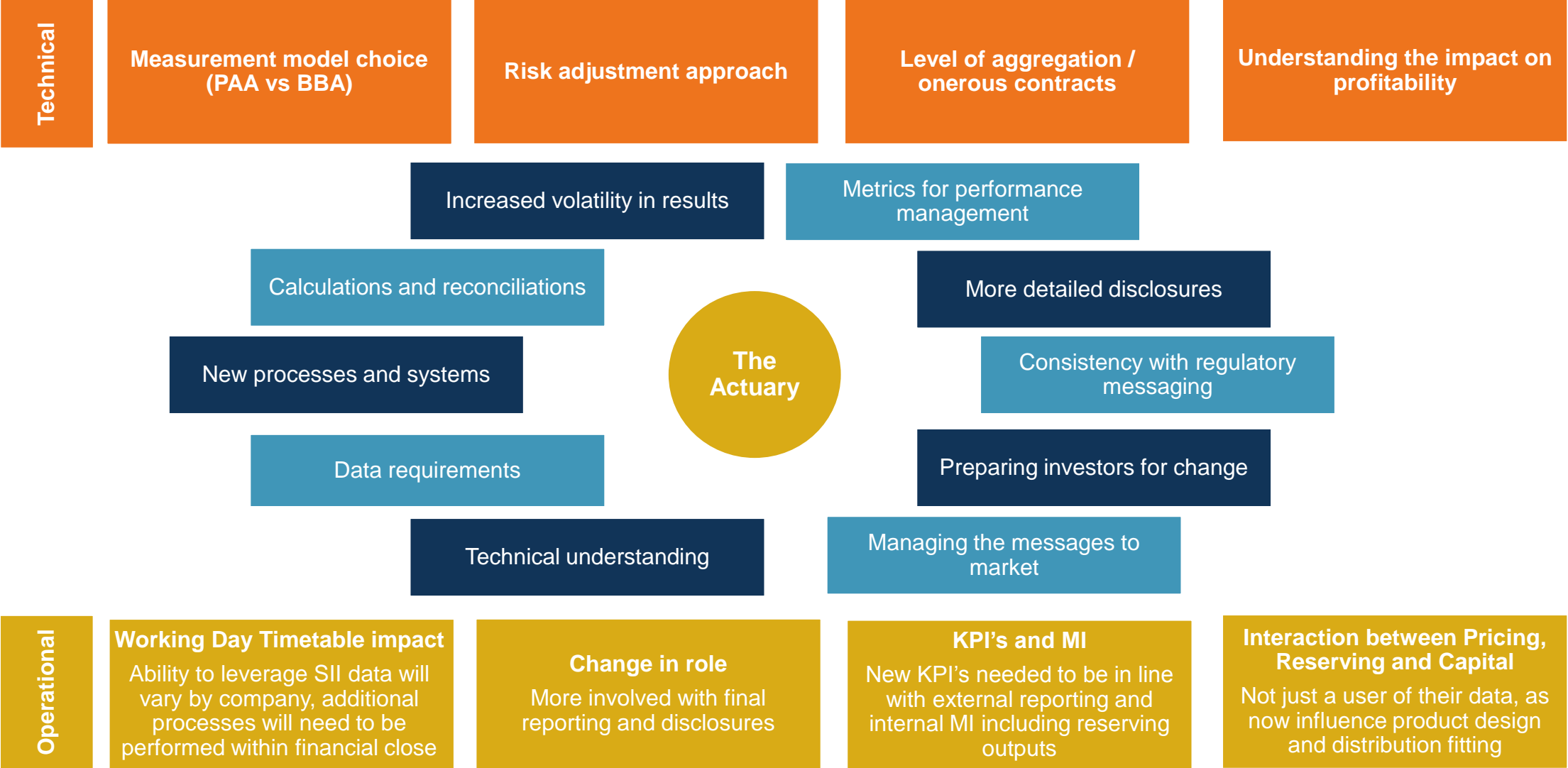
Insurance revenue	X
Insurance service expenses	(X)
Reinsurance expenses	(X)
<b>Insurance service result</b>	<b>X</b>
Insurance finance income / (expense)	X/ (X)
Investment income	X
Investment expenses	(X)
<b>Net financial result</b>	<b>X</b>
Administrative expenses	(X)
Other expenses	(X)
<b>Profit or loss</b>	<b>X</b>
Effect of discount rate changes on insurance liabilities	X
<b>Total comprehensive income</b>	<b>X</b>

- New look and feel to financial statements including:
  - Volume based metric of reporting premiums as income is replaced with an insurance revenue line item
  - Insurers will now split out insurance service result and net financial result when explaining profitability of insurance policies to stakeholders
- Additional quantitative reconciliations will are likely to require actuarial input
- Additional qualitative disclosures including:
  - Risk adjustment method and confidence level
  - Yield curves used to discount cashflows



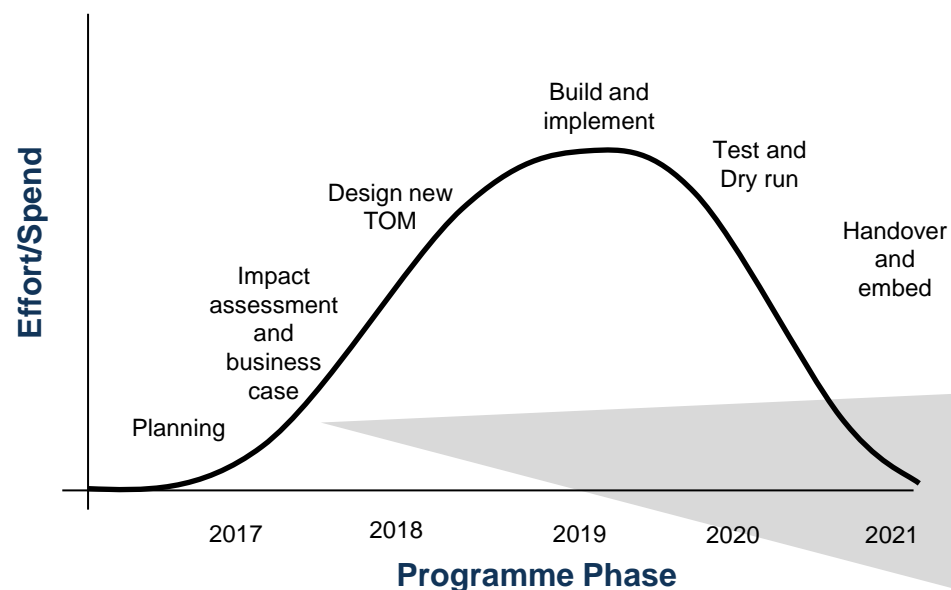
Institute  
and Faculty  
of Actuaries

# How does this impact the actuary?



# IFRS 17 project timeline

The ideal timeline for implementing IFRS 17 will depend on the complexity of the changes required to the underlying systems and processes for financial reporting.



## Focus for 2017

- Identify and agree key design decisions
- Deep dive in operational and financial impact of key design decisions
- Define systems and data requirements
- Design target state operating model and gaps from current state
- Develop implementation plan and business case

***Don't forget lessons learned from Solvency II...***

Silos need to be broken - Actuaries need to be integrated and integral to Finance process

Controls and documentation need to be updated

Leaving things to the last minute can be expensive and painful

Reconciliations can be time consuming

Technical issues can be surprisingly time consuming

Train, train and train again

Training the Board early, as well as other stakeholders is key

# Get involved...!

*How does this impact the company you work for or your client?*

*What is the operational impact (data, systems, processes, people)?*

*Is there a working group already set up in your company? Who is on that?*

*Are there projects already underway to transform finance / actuarial processes? Are they thinking about IFRS17?*

**Stakeholder management**  
*Knowledge*

- Increase awareness
- Technical training

**Impact studies**  
*Identify hot spots*

- Financial and operational impact assessment
- Assessment of system, modelling, data flow and process implications
- Product assessment – establish PAA eligibility
- Identify relevant existing and planned projects to leverage

**Implementation planning**  
*Plan for a plan*

- Identify key stakeholders and create project governance structure
- Cost estimation for business case
- Search for skilled resources
- Detailed impact assessment across your business



Institute  
and Faculty  
of Actuaries

# Where to find out more...?

- IFoA working party papers, industry events:
  - <https://www.actuaries.org.uk/practice-areas/general-insurance/research-working-parties/ifrs-17>
- The Actuary article on the implications for General Insurers:
  - <http://www.theactuary.com/features/2017/06/the-wide-ranging-implications-of-ifrs-17/>
- IASB website publishes lots of detail on Board deliberations, there is also a series of webinars delving into the different elements of the standard
  - <http://www.ifrs.org/Current-Projects/IASB-Projects/Insurance-Contracts/Pages/Insurance-Contracts.aspx>



# Questions

# Comments

Expressions of individual views by members of the Institute and Faculty of Actuaries and its staff are encouraged.

The views expressed in this presentation are those of the presenter.



Institute  
and Faculty  
of Actuaries