IFRS 17 for Non-life Insurers
The General Insurance Association

5 June 2018

The better the question. The better the answer.
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Agenda

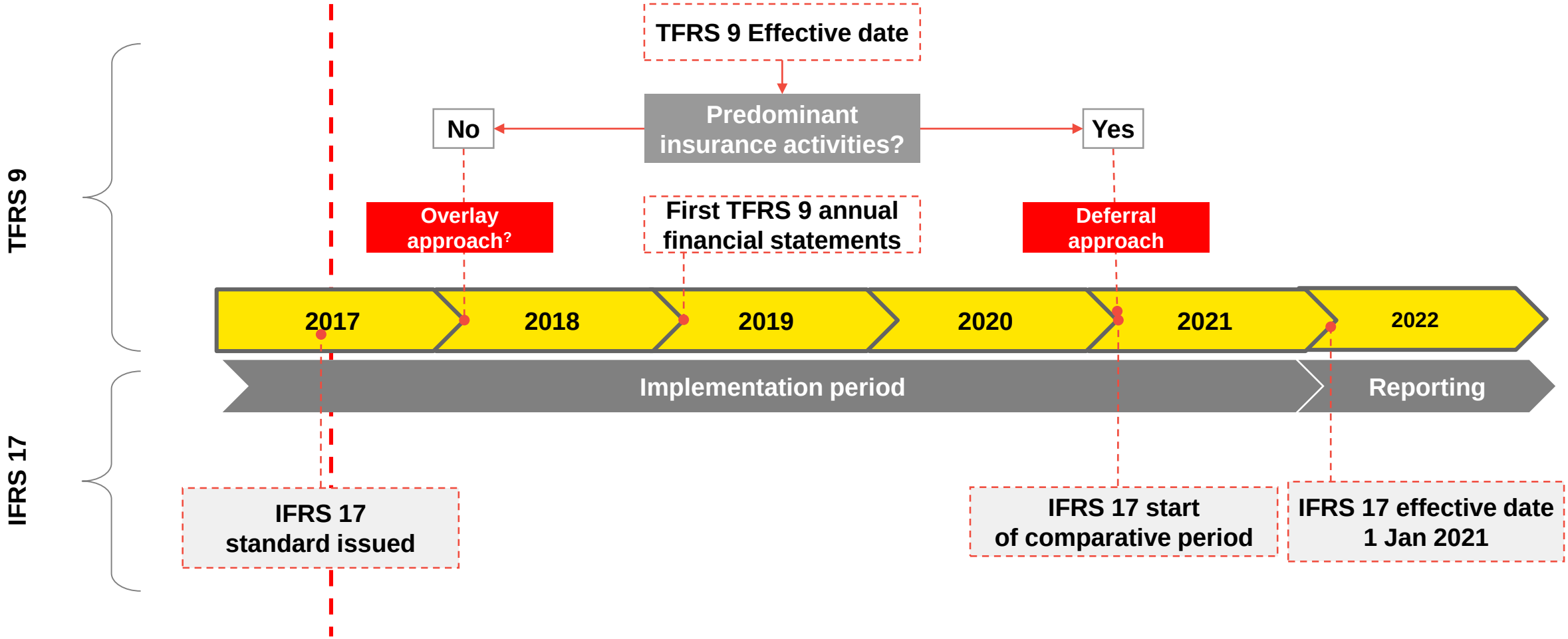
1. Overview of IFRS 17
2. Building block approach
3. Premium allocation approach
4. Reinsurance ceded
5. Presentation and disclosure
6. Transition
7. Issues from a general insurance perspective
8. Operational implications

Section 1

Overview of IFRS 17

Overview of IFRS 17

IFRS 17 and TFRS 9 –timeline



Overview of IFRS 17

IFRS 17 is expected to improve financial reporting by providing meaningful and comparable information

Provides up-to-date market consistent information of obligation including value of options and guarantees

Underwriting revenue and expenses are recognised over time in comparable way to other non insurance business

Reflects time value of money

Provides separate information about the investment and underwriting performance

Assumptions used in the valuation of insurance contact liabilities reflect the characteristics of the insurance contract rather than the risk related to asset / investment activity

Accounting model overview and step to apply the standard

The Standard describes a measurement and presentation model for insurance contracts. To apply the Standard, an entity would apply the following steps:

1. Identify and recognise the contract	• Defined by the presence of significant insurance risk • Some distinct non-insurance components should be separated • Recognise a contract when coverage periods begins, unless the contract is onerous
2. Measure the contract at initial recognition	• Incorporate all available information about the fulfilling CFs • Consistent with observable market information • May apply simplified approach (premium allocation approach)
3. Remeasure in subsequent periods	• In each reporting period, re-measure the insurance contract using updated assumptions • Recognise the effect of changes in estimates relating to future services in the periods in which the service is provided, rather than in the current period
4. Present results in financial statements	• Revenue and expense is consistent with that for non-insurance contracts • Present cost-based interest expense in P/L and the effect of discount rate changes either in P/L or OCI • Disclosure, e.g. amount recognized in the financial statements, significant judgement and the risks that arise from the insurance contract

Scope and contract components: Scope

Scope	❑ IFRS 17 applies to: ❑ an insurance contract (including reinsurance); ❑ a reinsurance contract entity holds; and ❑ investment contract with a discretionary participation feature that entity issues, provided that the entity also issues insurance contracts
Insurance contracts	❑ 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
Significant insurance risk	❑ Significant if and only if an insured event could cause an additional amount that has commercial substance in any single scenario; consider in a present value basis, but not the probability of the event. ❑ Significant insurance risk only occurs when there is a possibility that an issuer will incur a loss on a present value basis.

Scope and contract components: Recognition and de-recognition

Recognition

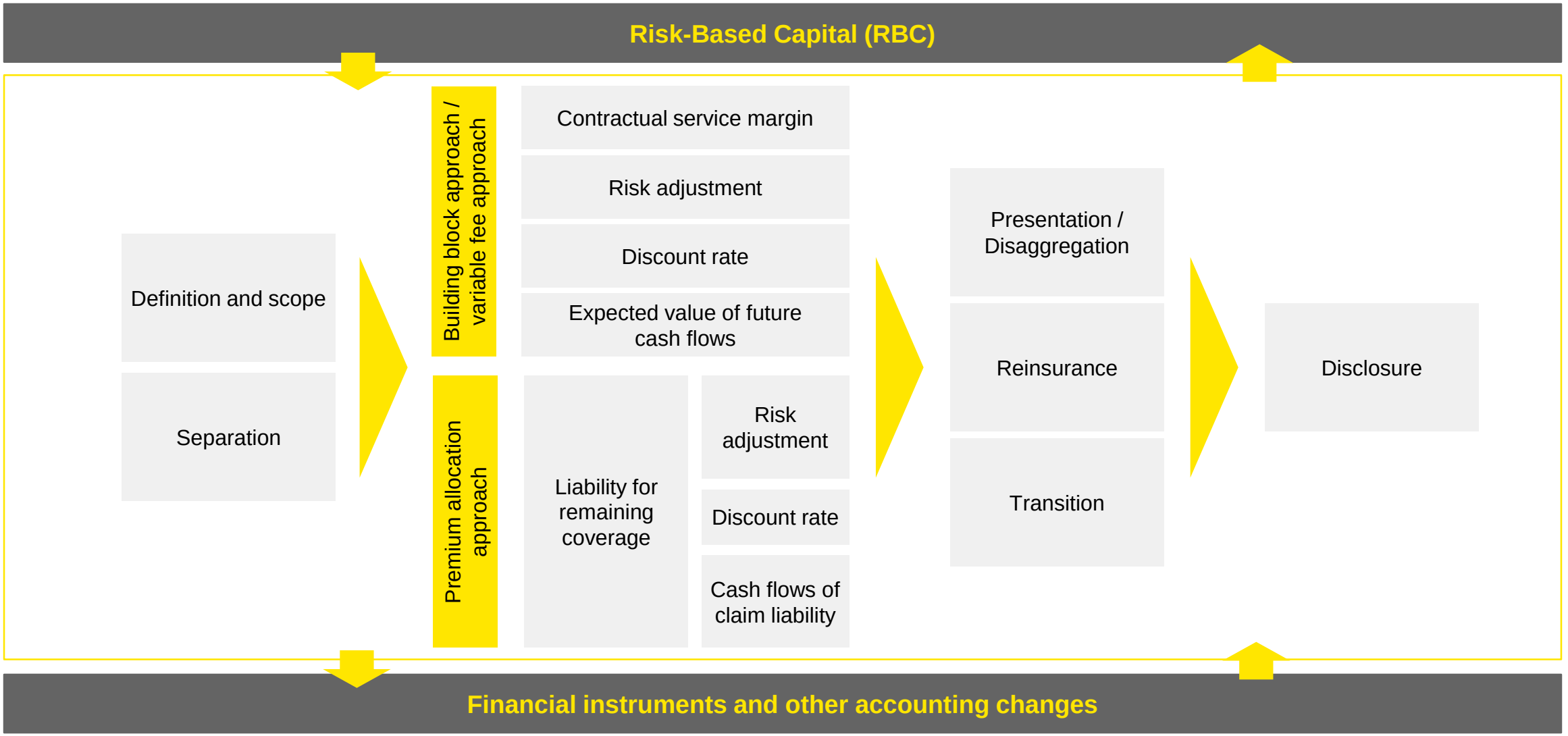
- Shall recognise an insurance contract that an entity issues from the earliest of the following:
  - the beginning of the coverage period
  - the date on which the portfolio of insurance contracts to which the contract will belong is onerous
- Shall recognise any acquisition cost

De-recognition

- When the obligation specified in the insurance contract is discharged, cancelled or expires
- At that point, the entity is no longer at risk and is therefore no longer required to transfer any economic resources to satisfy the insurance contract

Overview of IFRS 17

Key focus areas of the standard

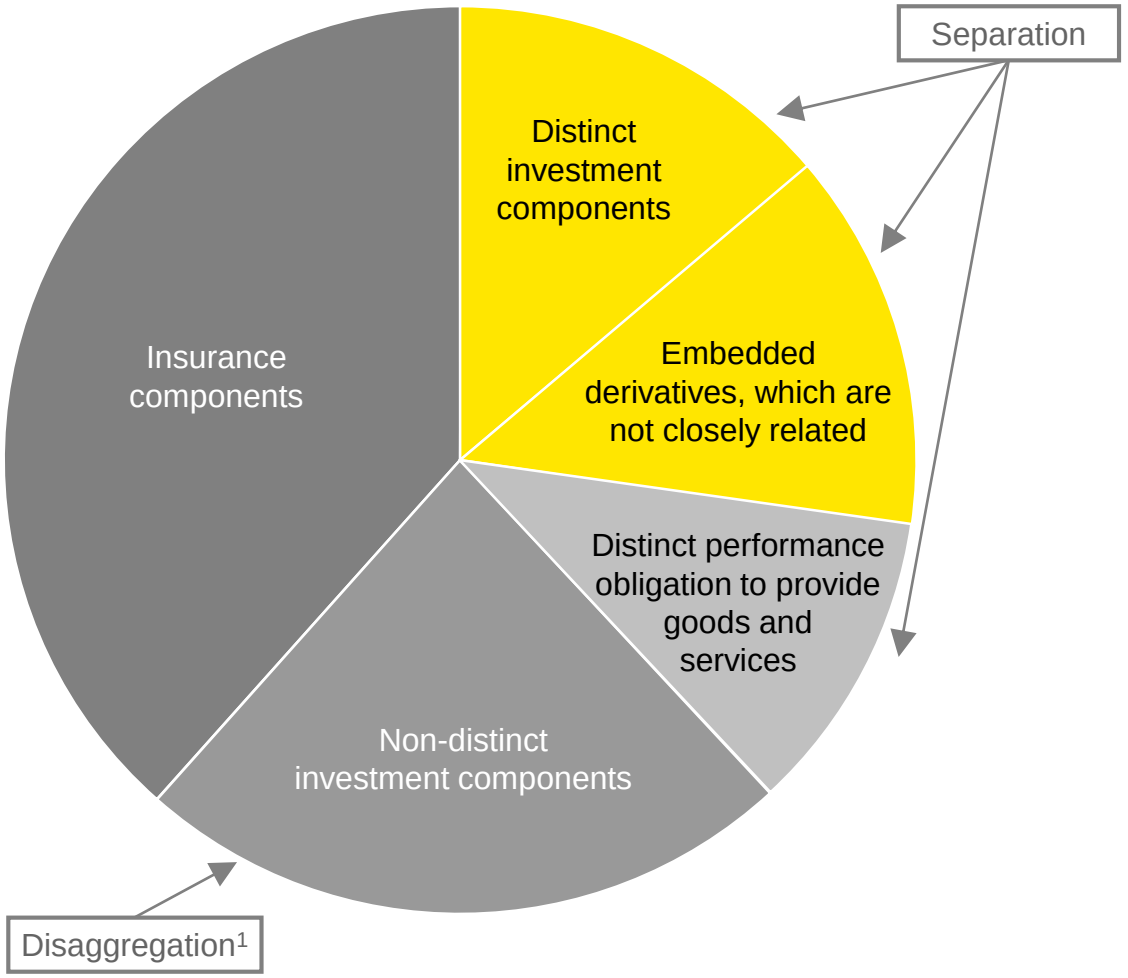


Overview of the measurement models

	Key features	Example products
Building block approach (BBA)	▸ Default model in IFRS 17 ▸ Probability weighted discounted cash flows ▸ Market-based valuation of options and guarantees ▸ Contractual service margin (CSM): to spread recognition of profit and impact of changes ▸ Risk adjustment	▸ Annuities ▸ Protection ▸ Long-duration non-life business
Variable fee approach (VFA)	▸ Based on the building block approach, but with additional features for direct participating contracts ▸ Market volatility passes through CSM vs Statement of Comprehensive Income (P&L/OCI) for building block approach	▸ With-profit business ▸ Unit-linked business
Premium allocation approach (PAA)	▸ Optional approach for short duration contracts (pre-claims liability) ▸ BBA approach used to determine remaining exposure	▸ Short-duration contract (mostly non-life insurance)

Overview of IFRS 17

Separated components



Accounting under IFRS 17

Accounting under TFRS 9

Accounting under TFRS 15

Accounting under IFRS 17, disaggregation for presentation in income statement notes

[1] ***Disaggregation*** is the exclusion of an unseparated investment component from insurance contracts revenue

Overview of IFRS 17

Level of aggregation

At Contract Inception

1 **Portfolio**

Portfolio = A group of contracts
(a) subject to similar risks
(b) managed together

2 **Cohorts**

Permitted to group only contracts issued no more than one year apart

3 **Onerous contracts at inception**

Contracts not onerous at inception

Other profitable contracts

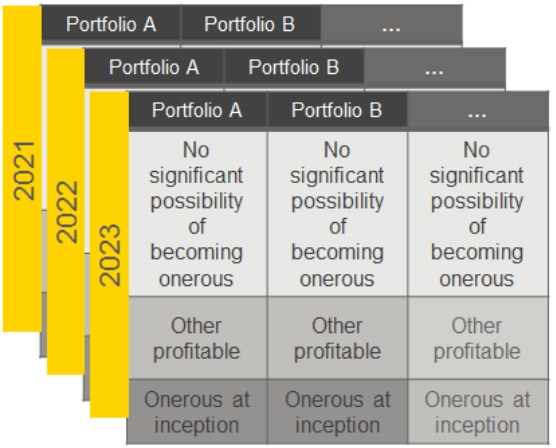
No significant possibility of becoming onerous

Assessment based on:
(a) Likelihood of changes in estimates which, if they occurred, would result in the contracts becoming onerous
(b) Using internal information about changes in estimates

A loss is recognized in the P&L at inception

CSM is recognized and released as insurance service is provided

Assessment is done at contract inception – no subsequent re-assessment

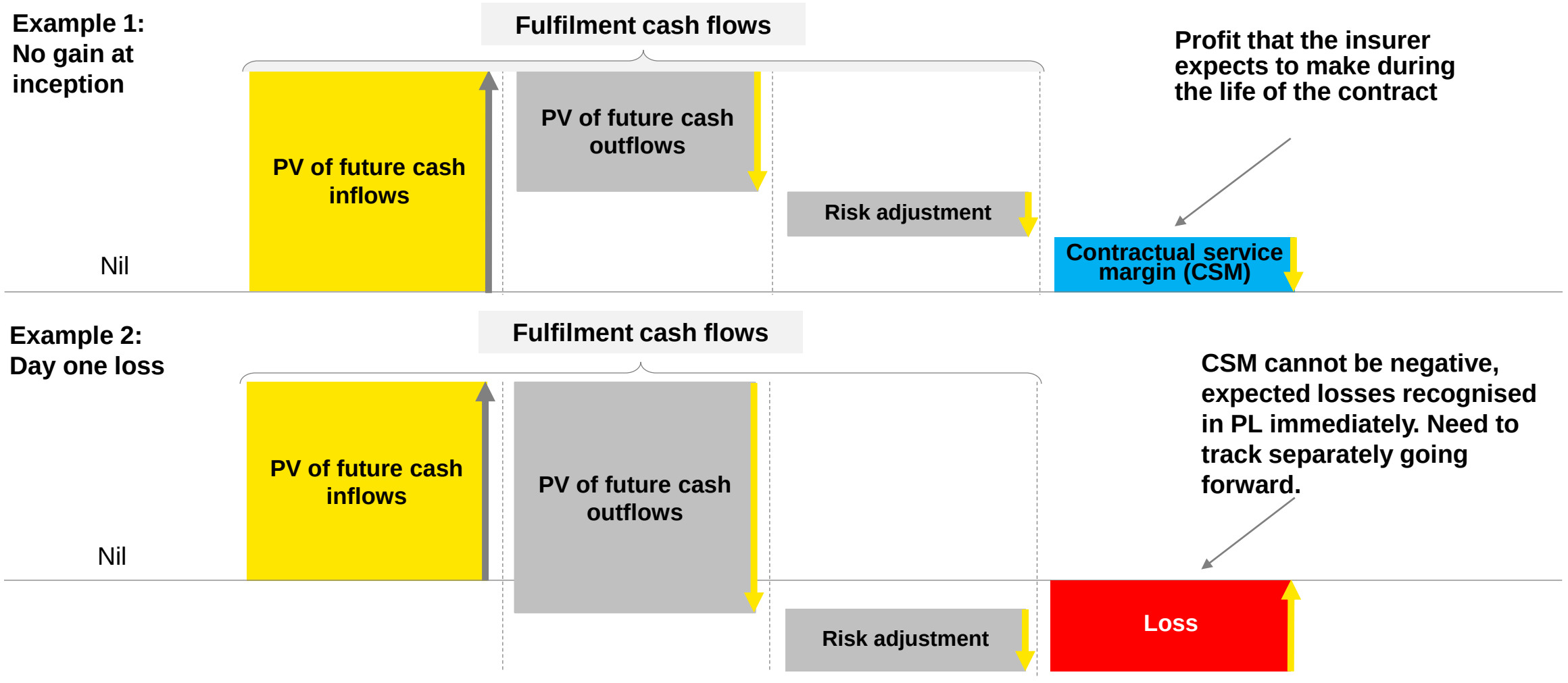


Section 2

Building block approach

Building block approach

Fulfilment cash flows

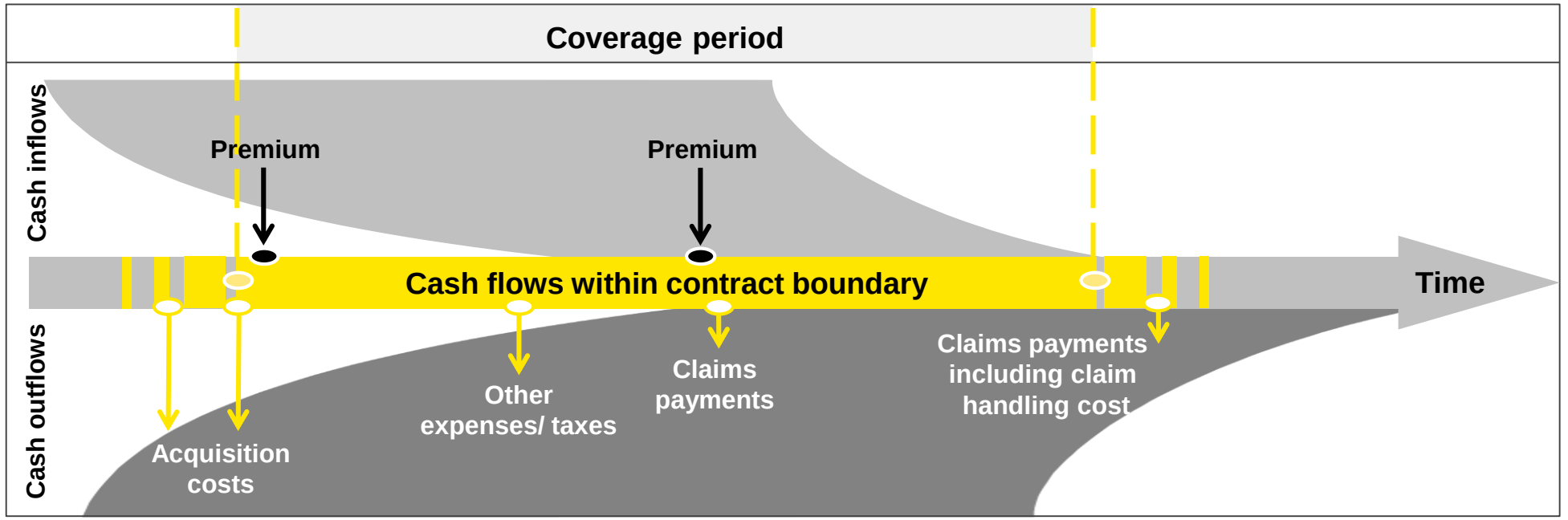


Building block approach

Fulfilment cash flows

- Contractual service margin
- Risk adjustment
- Time value of money
- **Future cash flows**

- The estimates of CFs used to determine the fulfilment CFs shall include all cash inflows and outflows that relate directly to the fulfilment of the portfolio of contracts:
  - Current and explicit (separate from discount rate and risk adjustment)
  - Market variables as consistent as possible with observable market prices
  - Incorporate all available information in an unbiased manner (including trends)
  - Include all CFs within contract boundary



Building block approach

Time value of money

Contractual service margin

Risk adjustment

Time value of money

Future cash flows

- Adjust the estimates of future cash flows for the time value of money using discount rates that:
  - Reflects characteristics of fulfilment cash flows
  - Consistent with observable market prices for instruments with cash flows that have consistent characteristics with insurance contract, e.g., with respect to timing, currency and liquidity
  - Adjust observed market prices to reflect the characteristics of the liability/ the factors that are relevant for the contracts, e.g., exclude irrelevant risks, estimate the rate beyond the period of observable data
  - Consistent with other estimates used to measure the insurance contract (e.g. inflation, discount rate for participating contracts)
- Top-down approach or bottom-up approach
- No need to discount cash flows which are expected to be paid or received in one year or less

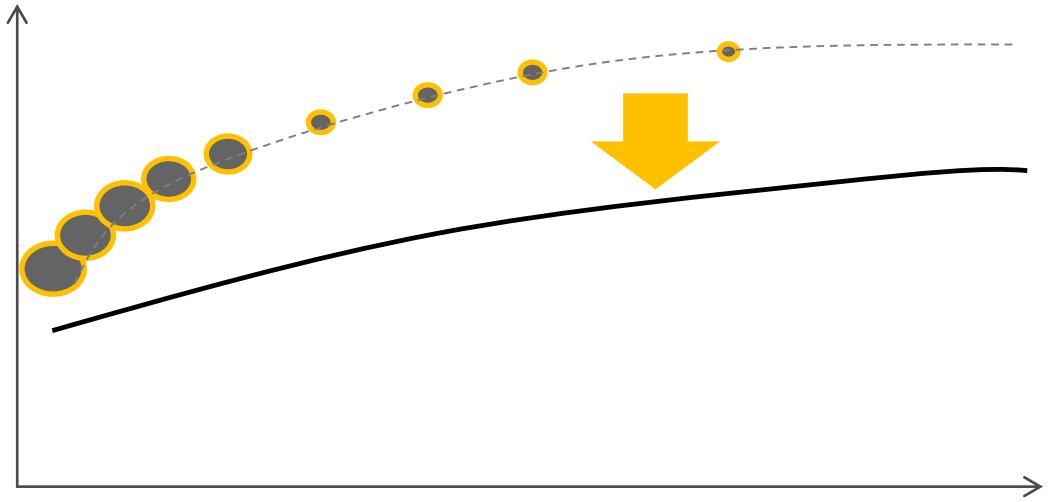
Building block approach

Time value of money

Top-down approach
Current market rates of returns:
either of own asset portfolio or a reference portfolio

Adjust for **risks that are not relevant to the insurance contract**, e.g., default risk, market risk

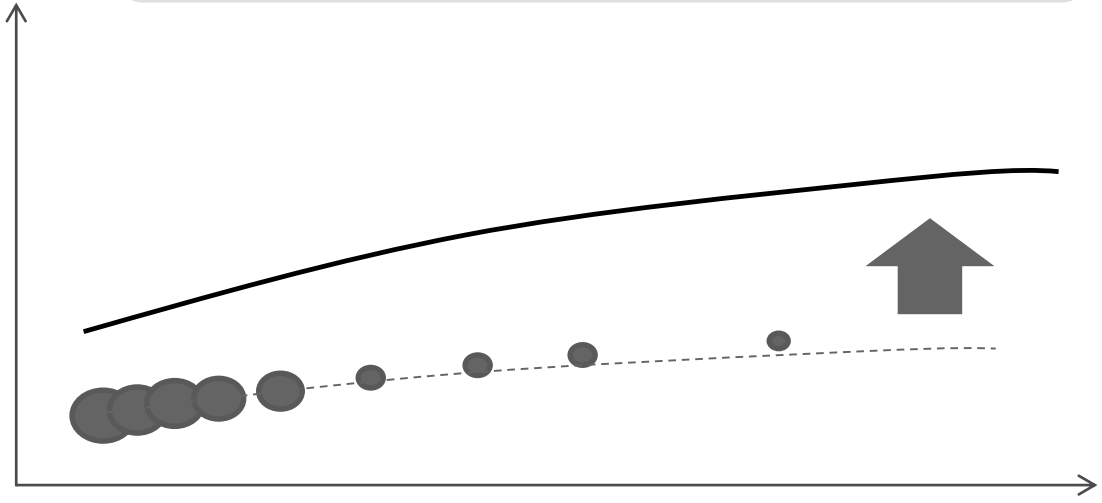
Adjust for **duration differences** if necessary
(No need to adjust for the difference due to liquidity)



Adjust for **other characteristics** of the insurance contracts if necessary

Illiquidity premium: Adjust for liquidity characteristics of the insurance contracts

Bottom-up approach
Risk-free yield curve with similar characteristics (e.g., duration, currency)



Building block approach

Risk adjustment

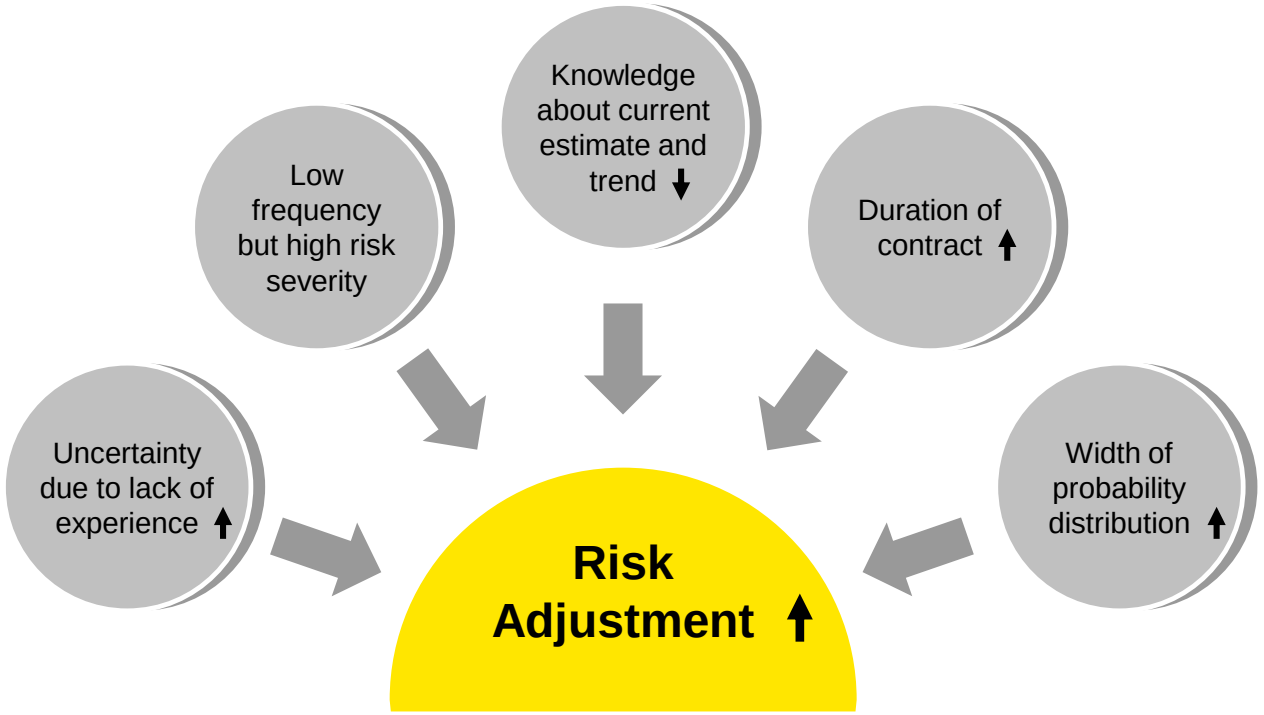
Contractual service margin

Risk adjustment

Time value of money

Future cash flows

- Compensation that an entity requires for bearing the uncertainty about the amount and timing of the cash flows that arise as the entity fulfils the insurance contract
- RA shall be included in the measurement in an explicit way (i.e. uncertainty should not be included in the future cash flows)
- No prescribed technique so different companies may use different techniques
- Disclosure on the confidence-level is required if the entity uses a technique other than the confidence level technique



Building block approach

Contractual service margin

Contractual service margin

Risk adjustment

Time value of money

Future cash flows

- At initial recognition, the CSM is defined as the negative of fulfilment cash flow, floored by zero.
- Purpose of recognizing a positive initial CSM:
  - To eliminate any day 1 gains (if initial CSM is positive)
  - To represents the unearned profit that the entity recognizes as it provides services under the insurance contract
- If CSM is floored by zero at inception, the insurance contract is onerous. All loss should be recognized in P&L at inception
- Objective of the standard is to:
  - Provide principles for the measurement of an individual insurance contract, but that in applying the standard an entity could aggregate insurance contracts provided that it meets that objective; and
  - Onerous contracts should not be aggregated with profit-making contracts

Contractual service margin

Contractual service margin

Risk adjustment

Time value of money

Future cash flows

- Subsequently, the roll-forward calculation of CSM is summarized as follows:

  CSM at the beginning of the reporting period

  \+ Accreted interest
  – Amount recognised for services provided in the period
  +/– Changes in the estimates of future cash flows
  +/– Changes in RA relating to future coverage

  = CSM at the end of the reporting period

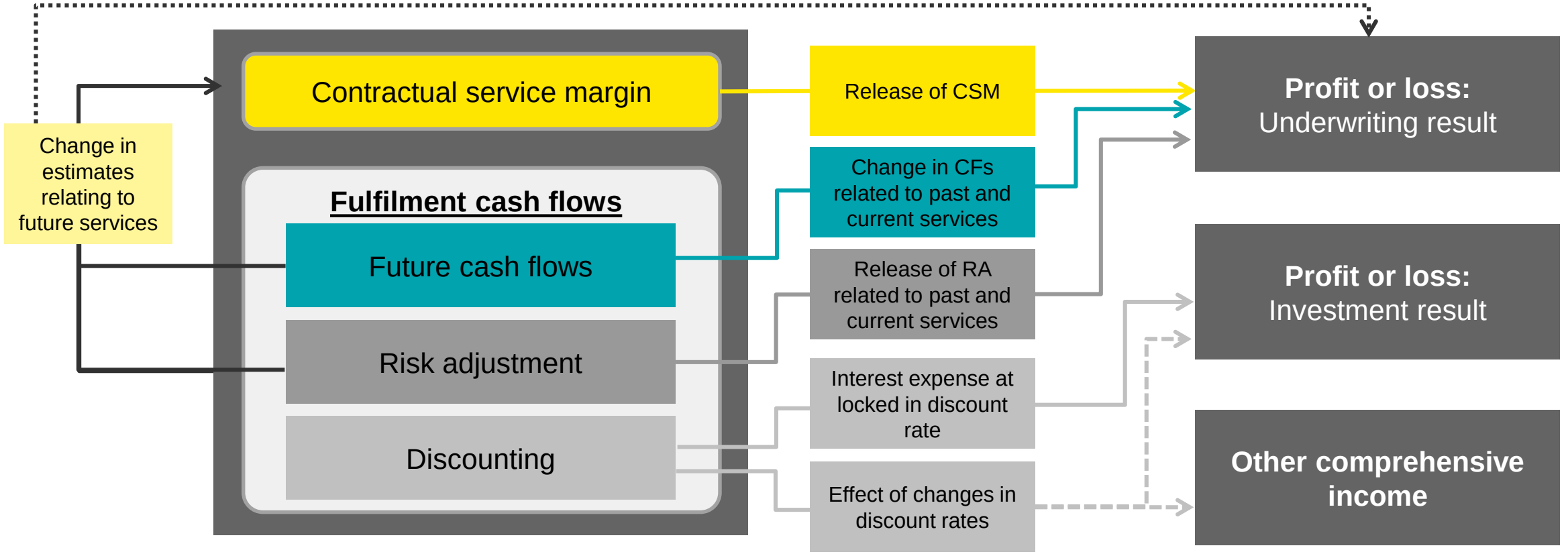
- Locked-in rate at the inception of contract is used for accreting interest.

- An entity should recognise the remaining contractual service margin in profit or loss over the coverage period in a systematic way that best reflects the remaining transfer of the services. For contracts with no participating features, the service represented by the contractual service margin is insurance coverage that:
  - is provided on the basis of the passage of time; and
  - reflects the expected number of contracts in force.

Building block approach

Subsequent measurement - overview

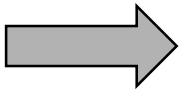
To disaggregate changes in the measurement of the insurance contracts in different line items of the financial statements, depending on the sources of the changes.



Building block approach

Case study

- Benefits
  - 2-year term
  - Single premium of BT1,000
  - Sum assured = BT3,000
- Assumption
  - 100 policies sold, with deferrable expenses incurred of BT10,000
  - Best estimate assumption: 10 claims each year
  - Risk adjustment (RA) = BT2,000
  - No other cash flows
- For simplicity, discount rate = 0%



- By applying the building block approach
  - At issue: Total cash flows = 100 * 1,000 – 10,000 – (10+10) * 3,000 – RA 2,000 = 28,000
- Therefore, CSM = 28,000
- Under these settings, the total IFRS 17 insurance liability at issue is:
  - Fulfillment cash outflows = (10+10) * 3,000 + RA 2,000 = 62,000
  - CSM = 28,000
  - Total IFRS 17 insurance liability = 62,000 + 28,000 = 90,000

Building block approach

Case study

Start of Year 1

Accounting entries:

			Dr	Cr
1.0	Dr	Est. future cashflow	30,000	
	Cr	CSM		28,000
	Cr	RA		2,000
	(Recognition of est. future cashflow [P - Cl - Co], RA and CSM)			
2.0	Dr	Cash	100,000	
	Cr	Est. future cashflow		100,000
	(Premium received)			
3.0	Dr	Est. future cashflow	10,000	
	Cr	Cash		10,000
	(Payment of deferrable expenses)			

Income statement:

Insurance contracts revenue	-
Incurred claims and expenses	-
Acquisition costs	-
Operating result	-
Investment income	-
Profit	-

Balance sheet:

Assets:	
Cash	90,000
Liabilities:	
Insurance contract liabilities:	
Fulfillment cashflow:	
Est. future cashflow	60,000
RA	2,000
CSM	28,000
	90,000
Equity:	
Profits	-
	90,000

Case study

- At the end of year 1,
  - There are 15 claims (as opposed to the 10 claims expected)
  - The Company re-estimates year 2 claims as 8 cases, down from 10 previously
  - The updated RA = 1,000
  - No other assumption changes

- Profit driver assumed to be based on no. of policies in-force:
  - The amortization factor = 28,000 / (90 + 80) = 164.7
  - Based on the remaining policies at end of year 1 (100 – 15), the CSM amortization = 85 * 164.7 = 14,000
  - However, there is also a favorable assumption change, where claims are reduced by (10-8) * 3,000 = 6,000
  - Therefore ending year 1 CSM = 28,000 – 14,000 + 6,000 = 20,000

- For end of year 1,
  - The updated future cash flows = 8 * 3,000 = 24,000

- Therefore total IFRS 17 insurance liability
  - Fulfillment cash flows = 24,000 + RA 1,000 = 25,000
  - CSM = 20,000
  - Total IFRS 17 insurance liability = 45,000

Case study

End of Year 1

Accounting entries:

			Dr	Cr
1.0	Dr	CSM	14,000	
	Dr	RA	1,000	
	Dr	Est. future cashflow (expected incurred claim)	30,000	
	Dr	Acquisition costs	5,000	
	Cr	Insurance contract revenue		50,000
	(Revenue recognition)			
2.0	Dr	Claims incurred	45,000	
	Cr	Cash		45,000
	(Claims recognition)			
3.0	Dr	Est. future cashflow	6,000	
	Cr	CSM		6,000
	(Recognition of impact of favorable change in future claims)			

Income statement:

Insurance contracts revenue	50,000
Incurred claims and expenses	(45,000)
Acquisition costs	(5,000)
Operating result	0
Investment income	-
Profit	0

Balance sheet:

Assets:	
Cash	45,000
Liabilities:	
Insurance contract liabilities:	
Fufillment cashflow:	
Est. future cashflow	24,000
RA	1,000
CSM	20,000
	45,000
Equity:	
Profits	0
	45,000

Building block approach

Case study

End of Year 2

Accounting entries:

			Dr	Cr
1.0	Dr	CSM	20,000	
	Dr	RA	1,000	
	Dr	Est. future cashflow (expected incurred claim)	24,000	
	Dr	Acquisition costs	5,000	
	Cr	Insurance contract revenue		50,000
	(Revenue recognition)			
2.0	Dr	Claims incurred	24,000	
	Cr	Cash		24,000
	(Claims recognition)			

Income statement:

Insurance contracts revenue	50,000
Incurred claims and expenses	(24,000)
Acquisition costs	(5,000)
Operating result	21,000
Investment income	-
Profit	21,000

Balance sheet:

Assets:	
Cash	21,000
Liabilities:	
Insurance contract liabilities:	
Fufillment cashflow:	
Est. future cashflow	-
RA	-
CSM	-
	-
Equity:	
Profits	21,000
	21,000

Case study

Comparison – Income Statement

	IFRS 17			
	Start of year 1	End of year 1	End of year 2	Total
Insurance contracts revenue	-	50,000	50,000	100,000
Incurred claims and exp.	-	(45,000)	(24,000)	(69,000)
Acquisition costs	-	(5,000)	(5,000)	(10,000)
Operating result	-	-	21,000	21,000
Investment income	-	-	-	-
Profit	**-**	**-**	**21,000**	**21,000**

	TFRS 4			
	Start of year 1	End of year 1	End of year 2	Total
Gross earned premiums	100,000	-	-	100,000
Premiums ceded to reinsurers	-	-	-	-
Net earned premiums	100,000	-	-	100,000
Investment income	-	-	-	-
Other revenue	-	-	-	-
Gross benefits and claims paid	-	(45,000)	(24,000)	(69,000)
Gross change in contract liabilities	(62,000)	37,000	25,000	-
Net benefits and claims	(62,000)	(8,000)	1,000	(69,000)
Fee and commission expenses	(10,000)	-	-	(10,000)
Management expenses	-	-	-	-
Other expenses	(10,000)	-	-	(10,000)
Profit	**28,000**	**(8,000)**	**1,000**	**21,000**

Case study

Comparison – Balance sheet

	IFRS 17			
	Start of year 1	End of year 1	End of year 2	Total
Asset:				
Cash	90,000	45,000	21,000	21,000
Liabilities:				
Insurance contract liabilities:				
Fulfillment cashflow:				
Est. future cashflow	60,000	24,000	-	-
RA	2,000	1,000	-	-
CSM	28,000	20,000	-	-
	90,000	45,000	-	-
Equity:				
Profits	-	-	21,000	21,000
	90,000	45,000	21,000	21,000

	TFRS 4			
	Start of year 1	End of year 1	End of year 2	Total
Asset:				
Cash	90,000	45,000	21,000	21,000
Liabilities:				
Insurance contract liabilities:				
Fulfillment cashflow:				
Est. future cashflow	60,000	24,000	-	-
RA	2,000	1,000	-	-
CSM	n/a	n/a	n/a	n/a
	62,000	25,000	-	-
Equity:				
Profits	28,000	20,000	21,000	21,000
	90,000	45,000	21,000	21,000

Section 3

Premium allocation approach

Premium allocation approach

Overview

Insurance contract liability split into:

Liability for remaining coverage (LFRC)
simplified approach based on allocation of premium (analogous to existing UPR, net of DAC and premium receivables)

Liability for incurred claims (LFIC)
(analogous to existing claim reserves)

Like Unearned Premium Reserve – but net of DAC and premium receivables

Like best estimate claim reserves – but expected value, discounted and probability weighted

Premium allocation approach

Example of LFRC after Initial Recognition

A group of contracts with Premium of 120 are issued at 1 Jan. Premium is paid on 31 Dec. Acquisition costs of 12 are incurred at inception. Revenue is earned evenly over the period. No claims are incurred. Debits/ asset balances are negative.

	Current accounting		IFRS 17 - PAA	
Start	UPR	120	Liability for remaining coverage (LFRC) (0-12)	(12)
	DAC	(12)	*[Equivalent to 120-12-120]*	
	Premium debtors	(120)		
	Cash	12	Cash	12
	Total	0	Total	0
Mid year	UPR	60	Liability for remaining coverage (LFRC) (-12-60+6)	(66)
	DAC	(6)	*[Equivalent to 60-6-120]*	
	Premium debtors	(120)		
	Cash	12	Cash	12
	Total	(54)	Total	(54)
End	UPR	0	Liability for remaining coverage (LFRC) (-66-60+6)	0
	DAC	0	*[Equivalent to 0-0-0]*	
	Premium debtors	0		
	Cash (-120+12)	(108)	Cash (-120+12)	(108)
	Total	(108)	Total	(108)

Premium allocation approach

Case study

Position	0	1	2	3	4	5	6	Total
Contract revenue	-	250	250	250	250	-	-	1,000
Release risk margin	-	-	-	-	-	-	-	-
Claims incurred	-	(150)	(150)	(150)	(150)	-	-	(600)
Acquisition costs (amortized)	-	(30)	(30)	(30)	(30)	-	-	(120)
Administration expenses	-	(20)	(20)	(20)	(20)	-	-	(80)
Underwriting result	-	50	50	50	50	-	-	200
Investment income	-	-	-	-	-	-	-	-
Interest on insurance liability (unwind of locked-in interest rate)	-	-	-	-	-	-	-	-
Net profit	-	50	50	50	50	-	-	200
Change in insurance contract liability	-	-	-	-	-	-	-	-
Fair value movements on FVOCI assets	-	-	-	-	-	-	-	-
Total comprehensive income	-	50	50	50	50	-	-	200

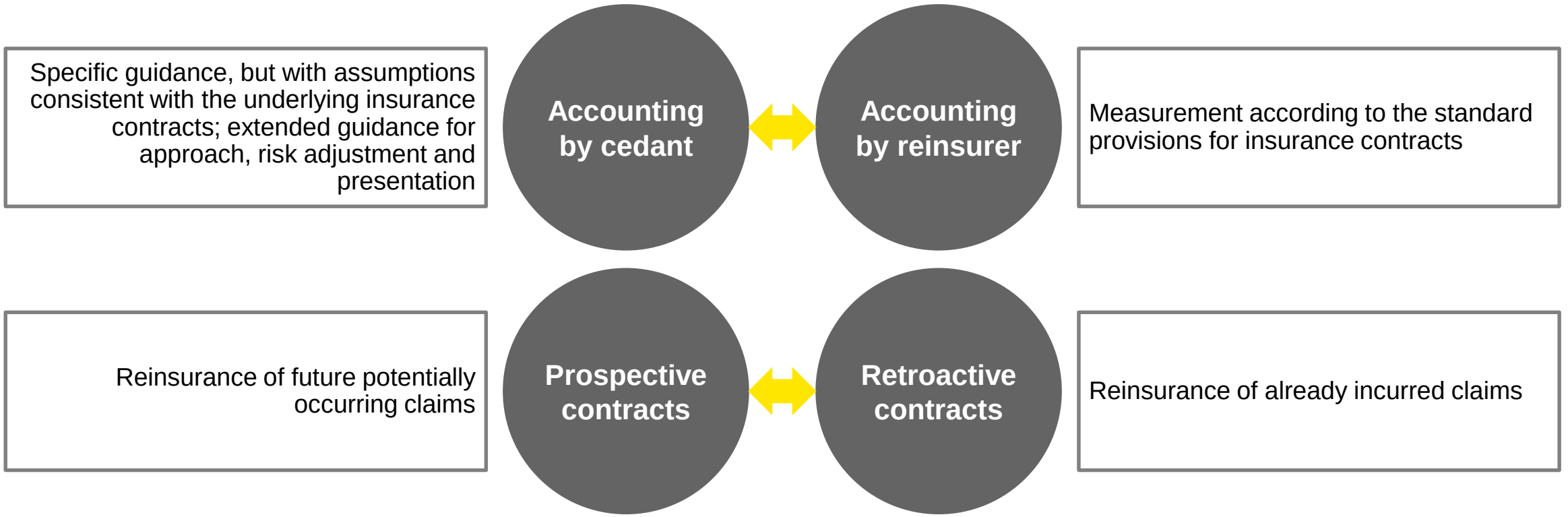
Position	0	1	2	3	4	5	6	Total
Invested assets	880	800	720	520	380	260	200	-
Insurance contract liabilities	880	750	620	370	180	60	-	-
- Liability for remaining coverage	880	660	440	220	-	-	-	-
- Liability for incurred claims	-	90	180	150	180	60	-	-
- Estimates for incurred claims	-	90	180	150	180	60	-	-
- Risk margin	-	-	-	-	-	-	-	-
Equity	880	800	720	520	380	260	200	-

Section 4

Reinsurance ceded

Reinsurance ceded

Overview of specific requirement



Reinsurance ceded

Summary of requirement

Largely follows the approach for direct assumed business, but with some specific considerations:

- Consistent assumptions in estimating future cash flows for RI contracts and that of underlying insurance contracts
- Allowance for non-performance by reinsurers within the future cash flows
- Risk adjustment – captures risk being transferred to the reinsurer (so difference between gross and net)
- CSM at initial recognition– captures net cost / net gain (unless retrospective coverage)
- Retrospective reinsurance arrangements
- The decision on whether PAA is applicable needs to be considered separately for the ceded reinsurance

Reinsurance ceded

Example

An entity enters into a 30 percent proportional reinsurance contract and, at the same time, issues corresponding underlying insurance contracts.

The reinsurance coverage does not relate to events that occurred before the purchase of the reinsurance contract.

The entity measures the corresponding **underlying insurance contract** at initial recognition as follows:

EPV of cash outflows	**900**
EPV of cash inflows	(1,000)
Risk adjustment	60
Fulfilment cash flows	(40)
Contractual service margin	40
Insurance contract at initial recognition (immediately before premium received)	-

The company pays a **single reinsurance premium** to the reinsurer (ceding commissions already deducted) of CU 300 (variant A) or CU 280 (variant B).

Reinsurance ceded

Solution

In relation to the reinsurance contracts held, the entity estimates the following:

- The EPV of cash inflows is CU270 = recovery of 30 percent of the EPV of cash outflows of CU900 for the underlying insurance contracts
- The risk adjustment is assumed to be CU18 = 30 percent of the risk adjustment of CU60 for the direct insurance contracts, since the entity expects that the reinsurance contract held reduces 30 percent of the risk
- The EPV of cash outflows = the single reinsurance premium paid to the reinsurer
  - In Example A: CU 300; and
  - In Example B: CU 280

Reinsurance ceded

Solution

Example A

EPV of cash inflows (recoveries)	270
EPV of cash outflows (premium ceded, net of ceding commission)	(300)
Risk adjustment	18
Fulfilment cash flows	(12)
Contractual service margin	12
Reinsurance contract at initial recognition	**-**

Example B

EPV of cash inflows (recoveries)	270
EPV of cash outflows (premium ceded, net of ceding commission)	(280)
Risk adjustment	18
Fulfilment cash flows	8
Contractual service margin	(8)
Reinsurance contract at initial recognition	**-**

Reinsurance ceded

Specific issues for reinsurance contracts

Consideration	Observation
Coverage period more than one year	A reinsurance contract might be written that only lasts one year but then provides coverage for the underlying exposure that runs for longer than one year. (e.g. risks attaching reinsurance)
Open ended renewal	Some reinsurance arrangements are written with an open ended renewal. However, a contract boundary needs to be set for such reinsurance arrangements.
Reinstatement premiums	Reinstatement premiums may be treated as claims rather than premiums if they relate to claims experience.
Ceding commission arrangements	Ceding commission may be treated as claims rather than premiums if they relate to claims experience.

Section 5

Presentation and disclosure

Presentation and disclosure

Statement of Comprehensive Income: A huge change from today

Statement of Comprehensive Income	
Insurance revenue	X
Insurance service expenses	(X)
Insurance service result	**X**
Investment income	X
Insurance finance expenses	(X)
Finance result	**X**
Other profit and loss items	**X**
Corporate tax	(X)
Profit after tax	**X**
Other comprehensive income	(X)
Total comprehensive income	**X**

- **Release in contractual service margin**
- **Change in risk adjustment**
- Expected claims (in fulfilment cash flows)
- Expected expenses (in fulfilment cash flows)
- Allocating premium relating to the recovery of directly attributable acquisition costs
- Excluding investment components

Expected

- Actual claims incurred
- Actual expenses incurred
- Allocating premium relating to the recovery of directly attributable acquisition costs
- **Onerous contracts**
- Excluding investment components

Actual

Calculated using locked-in rates (if the OCI option is selected)

Effect of discount rate changes on BEL (if the OCI option is selected)

Presentation and disclosure

How performance reporting will change: A comparison

TFRS 4
Net earned premiums
Interest, dividend and other investment income
Incurred claims and benefits
Change in provisions
Profit or loss

IFRS 17
Insurance revenue
Insurance services expense
Incurred claims and expense
Acquisition costs
Gain/loss from reinsurance
Insurance service result
Investment income
Insurance finance expense
Net financial result
Profit or loss
Discount rate changes on insurance liability (optional)
Total comprehensive income

Key Changes

- Insurance contract revenue excludes investment components
- Revenue and expense are recognised as earned or incurred
- Insurance finance expense is excluded from insurance service result and is presented (i) fully in P/L or (ii) in P/L and OCI, depending on accounting policy
- Written premiums disclosed in the notes

Presentation and disclosure

How will your balance sheet change

TFRS 4	IFRS 17
Assets	**Assets**
Reinsurance contract assets	Reinsurance contract assets
Deferred acquisition costs	Insurance contract assets
Premiums receivable	
Policy loans	
Liabilities	**Liabilities**
Insurance contracts liabilities	Insurance contracts liabilities
Unearned premiums	Reinsurance contracts liabilities
Claims payable	

Key changes for balance sheet

- IFRS 17 will requires **separate presentation** of insurance groups which are in a **net asset position** and those that are in a **net liability position**
- **BBA – Premium receivables from policyholders** will no longer be presented within the receivables line. This will instead be netted against the liability for remaining coverage for each group of contract and presented as part of insurance contract liabilities or assets (depending on whether the relevant group of contracts is in a liability or asset position). **PAA – Premium receivable** have to consider whether they still shown on balance sheet
- **Deferred acquisition costs** will no longer appear as a separate assets line item on the balance sheet. Instead they will be implicitly deferred through inclusion in the insurance contract liabilities (if directly attributable)
- **Reinsurance recoveries on insurance claims** will change in line with underlying inwards valuation basis, but will also require a charge for the expected credit risk.
- **Premium payable to reinsurers** will netted against the reinsurance contract assets for remaining coverage for each groups of contracts
- **Insurance liabilities** will change to follow the IFRS 17 measurement basis. If the eligibility criteria is met, insurers writing short-term contracts can adopt the premium allocation approach for the premium liability (similar to UPR). Measurement of the outstanding claims liability (estimate for incurred claims) will follow the BBA.

Disclosures: Purpose and type of information

In general

- **Purpose:**
  - Information concerning the **amount**, the **future development** and uncertainties of **cash flows** resulting from the insurance contracts
- **Qualitative and quantitative information concerning:**
  - Balance sheet and P/L items
  - Significant estimations and their changes
  - Type and extent of risks, including sensitivity analysis
- **Adequate aggregation level**
  - Contract type, product group
  - Geography
  - Reportable segment, as defined in TFRS 8
- **Transition** to income and expenses in P/L and to assets and liabilities in balance sheet in **tabular format**
- Information concerning **reinsurance assets**

Presentation and disclosure

Disclosures: Overview

Balance sheet and P/L items			
Development of B/S items during business year	Used valuation methods and inputs	Transition of booked premiums to insurance revenues	Interest curve for discounting

Type and extent of risks		
In general	**Insurance risks**	**Other risks**
Risk appetite	Risk exposure	Risk exposure
Risk management	Risk concentrations	Risk concentrations
Regulatory law	Claims settlement	Maturity analysis
	Sensitivity analysis	Sensitivity analysis concerning market risks

Disclosures: Detailed roll forwards – an example (illustrative)

	Liabilities for remaining coverage		Liabilities for incurred claims	Total
	Excluding onerous contracts component	Onerous contracts component		
Insurance contract liabilities 20X0	7,375	290	2,060	9,725
Insurance revenue	(1,608)			(1,608)
Insurance service expenses	15	(41)	1,000	973
Incurred claims and other expenses		*(11)*	*1,000*	*989*
Amortisation of insurance acquisition cash flows	*15*			*15*
Losses on onerous contracts and reversals of those losses		*(30)*		*(30)*
Changes to liabilities for incurred claims			-	-
Investment components	*(200)*	-	*200*	-
Insurance service result	(1,793)	(41)	1,200	(635)
Insurance finance expenses	488	17	76	582
Total changes in the statement of comprehensive income	(1,305)	(24)	1,276	(53)
Cash flows				
Premiums received	1,880			1,880
Claims and other expenses paid			(1,400)	(1,400)
Insurance acquisition cash flows	(19)			(19)
Total cash flows	1,861	-	(1,400)	461
Insurance contract liabilities 20X1	7,932	266	1,936	10,134

There are rounding differences in this table

Disclosures: Detailed roll forwards – an example (illustrative)

	Estimates of the present value of future cash flows	Risk adjustment	Contractual service margin	Total
Insurance contract liabilities 20X0	9,268	148	309	9,725
Changes that relate to current services	(330)	(36)	(238)	(604)
Contractual service margin recognised for services provided			*(238)*	*(238)*
Risk adjustment recognised for the risk expired		*(36)*		*(36)*
Experience adjustments	*(330)*			*(330)*
Changes that relate to future services	(672)	53	588	(30)
Contracts initially recognised in the period	*(325)*	*62*	*266*	*3*
Changes in estimates reflected in the contractual service margin	*(315)*	*(8)*	*323*	-
Changes in estimates resulting in onerous contract losses/(reversal)	*(32)*	*(1)*		*(33)*
Changes that relate to past services	-	-	-	-
Adjustments to liabilities for incurred claims	-	-		-
Insurance service result	(1,002)	18	350	(635)
Insurance finance expenses	569	-	12	582
Total changes in the statement of comprehensive income	(432)	18	362	(53)
Cash flows	461			461
Insurance contract liabilities 20X1	9,296	166	671	10,134

There are rounding differences in this table

Section 6

Transition

Transition

Overview

Decide transition method by group of contracts

Full retrospective approach

If impracticable

Modified retrospective approach **OR** **Fair value approach**

- Modifications available if necessary given reasonable and supportable information (*)
- Maximise the use of the information needed for full retrospective approach

(*) If no reasonable and supportable information available, use fair value approach

Estimating CSM on transition – Key requirements

Full retrospective approach

- Required when sufficient historical data exists and hindsight is not required

Modified retrospective approach

- When full retrospective approach is impracticable
- Not all historical information is available
- Several modifications are included (e.g. level of aggregation, cash flows, discount rates)
- Modifications to be applied to the extent 'reasonable and supportable information' is available

"Fair value-based approach"

- When full retrospective approach is impracticable
- No historical information about cash flows is available to calculate the CSM
- Insurance liability "calibrated" to fair value
- CSM is positive difference between fair value and fulfilment value

Section 7

Issues from a general insurance perspective

Issues from a general insurance perspective

Premium allocation requirements - reminder

Premium allocation approach (PAA)

To be treated as premium allocation approach rather than the building block approach the following criteria need to be met :

- The entity reasonably expects that doing so would produce a measurement of the liability for remaining coverage that would not differ materially from the building block approach or
- The coverage periods is one year or less

The condition is not met if:

- The contract includes an investment component
- At inception an entity expects significant variability during the period before a claim is incurred (this variability would be expected to increase the longer the coverage period)

Issues from a general insurance perspective

Which contracts don’t meet PAA requirements?

Premium allocation approach (PAA)

Examples of contracts which are typically longer than one year coverage period

- Construction contracts
- Bond contracts
- Extended warranty
- Long term fire contracts

Issues from a general insurance perspective

TFRS 4 technical provision calculations can provide many of the IFRS 17 figures – although not exactly the same …

	TFRS 4	IFRS 17
Cashflows	Best estimates (i.e. no margins). Overdue premium receivables and reinsurance receivables shown separately	Best estimates (i.e. no margins). Overdue premium receivables and reinsurance receivables included in technical provisions
Discounting	No discount rates	Flexibility on the insurer on how to determine discount rates
Risk adjustment / risk margin	Provision for Adverse Deviation (PAD) at 75% confidence level approach prescribed by RBC (Option)	Flexibility on the insurer on how to risk adjustment. Both gross and net of reinsurance risk adjustments are required
Contract boundaries	Include contracts once “bound”	Include contracts before inception if they are loss making

Issues from a general insurance perspective

Should I just assume everything is BBA?

Advantages	Disadvantages
Some contracts will be BBA, so treating all business as BBA means only one approach is used	Combined ratio metric is not as readily available
Can be seen as more directly building on TFRS 4 – only possible difference for balance sheet is adding in CSM	TFRS 4 requires a split between claim and premium provisions anyway – so already provides information to build on for liability for incurred claims
As most contracts have coverage period 1 year or less the tracking of the CSM becomes more straight forward	Tracking CSM over time is more complicated
For groups with life arms it is more comparable and allows everything to be treated in a similar way	For users of accounts the change to BBA is larger

Once the coverage is “earned” the results under both methods are exactly the same

Issues from a general insurance perspective

Impact on KPIs

Combined ratios

Will be changed

- Discounting (both claims and revenues)
- Need to decide whether to include risk adjustment or not
- Earned premiums replaced by revenue – similar but some changes (reinstatement premiums will now appear as a claims item)

Return on equity

Pattern of earning of profits will change

- Discounting
- Setting up and releasing of Risk Adjustment
- BBA contracts can earn profits slightly differently

Issues from a general insurance perspective

Onerous contracts and PAA

Defining onerous contracts is a key part of the standard for BBA. For PAA the requirements are slightly different:

Under PAA: “the entity shall assume no contracts in the portfolio are onerous at initial recognition, unless facts and circumstances indicate otherwise.”

How could this be interpreted?

- Lines of business which have been consistently loss making in the past
- Intentional writing of loss making business to gain market share
- Soft market creating loss making contracts
- There is no requirement to individually test each contract
- The effect of gender neutral pricing does not create onerous contracts

Issues from a general insurance perspective

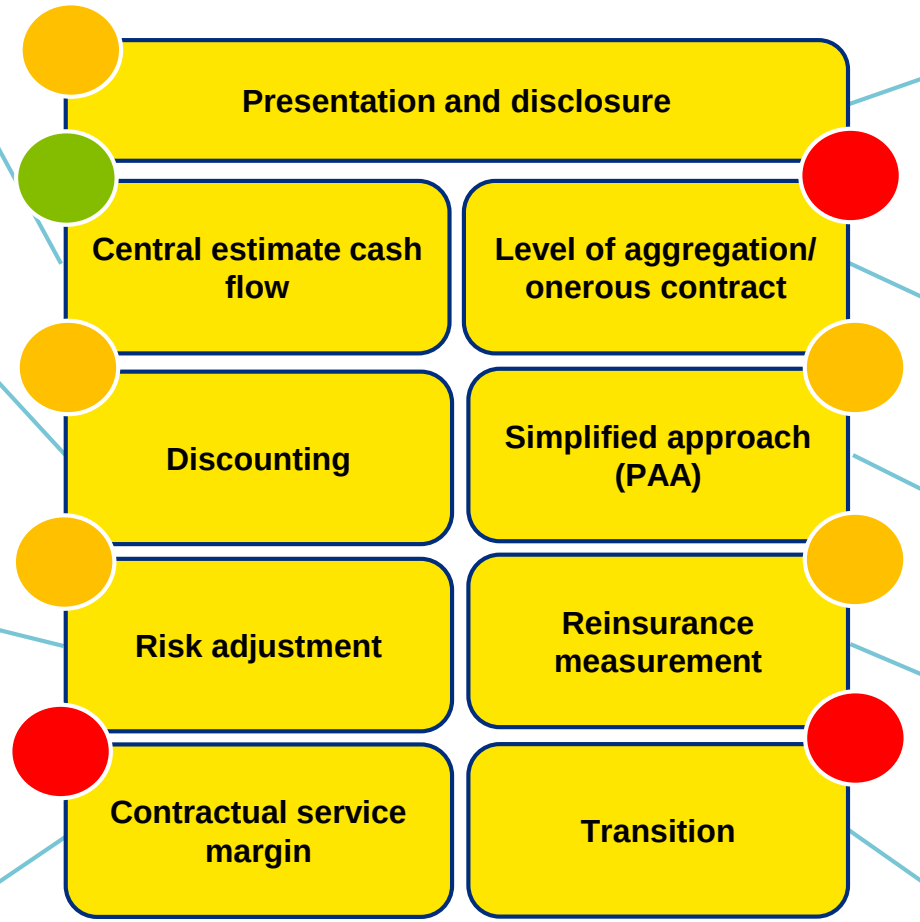
Summary

Best estimate is the current measure of claims liabilities under TFRS 4

Currently discount using risk free rates (not all). **OCI solution is new**. High operational cost to calculate OCI vs P&L split.

The **disclosure of the confidence interval** for risk adjustment is current practice. Allocation for onerous contracts and CSM determination introduces new level of granularity

CSM approach is complex and brings changes in assumptions about the future into the current period



Underwriting result and finance result will have a new presentation. New KPIs, strategy, incentives and education are required as well as system changes

Greater **granularity** in measuring and reporting onerous losses at inception

PAA likely to be the most frequently used measurement basis

Reinsurance mismatch between PAA and BBA between direct and reinsurance

Challenging but much of the required data expected to be available albeit at a more aggregated level

Section 8

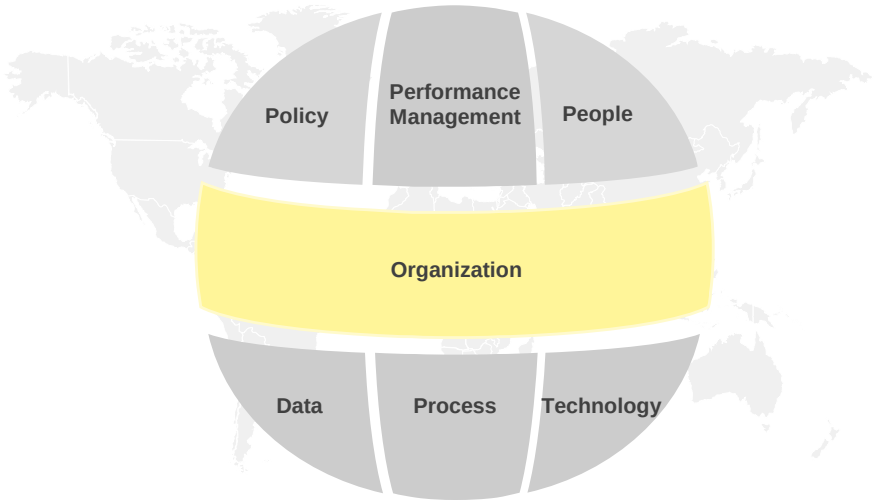
Operational implications

Operational implications

The big picture

1. Policy
- New accounting policies/procedures and control documentation
- IFRS 17 methodology guidance and reporting instructions
- GL Chart of Accounts changes and account mappings
- Assumptions setting (modelling)
- Investment policy changes (TFRS 9)

2. Performance Management
- Changes in MI reports and KPI's
- Planning, budgeting and forecasting processes need to be adjusted
- VBM, scorecards and incentive schemes



3. People
- Training
- Cross functional collaboration (especially for Finance & Risk)
- Project resourcing & budget
- Managing change fatigue

4. Organization
- Roles and responsibilities between Actuarial and Finance departments
- Technical Provisions Assumptions/ Expert Judgement Committee
- Impact on outsourcing contracts

5. Data
- Refinement, upgrading, conversion and migration of (complex) actuarial valuation models
- New financial reporting data requirements (input/output)
- Data reconciliations at different levels
- Data quality, storage and archiving
- Data security & controls
- Data governance and master data management

6. Processes
- Materiality concepts/guidelines
- Updating closing and reporting processes, planning processes, actuarial processes, risk management etc.
- Internal and external reporting templates including group reporting packages
- Internal controls and audit trail

7. Technology
- Core systems, investment system, actuarial systems, pricing systems, etc.
- Posting logic/engines
- General Ledger, consolidation and reporting systems
- System interfaces
- Current system capacities & capabilities (agile technology)
- New functionalities/features

Operational implications

Key lessons learnt so far

1. IFRS 17 is much more than an accounting change, it has a major impact on the entire organization (front-, middle- and back-office)

2. If you think the IFRS 17 standard is difficult, wait till you try to implement this in real life!

3. Don’t underestimate the amount of time it takes to find the required data to fulfil the extensive IFRS 17 primary financials and disclosure requirements

4. The biggest amount of work sits in the end-to-end Data, Systems & Process (DSP) changes – need to make sure IT does not become the bottleneck!

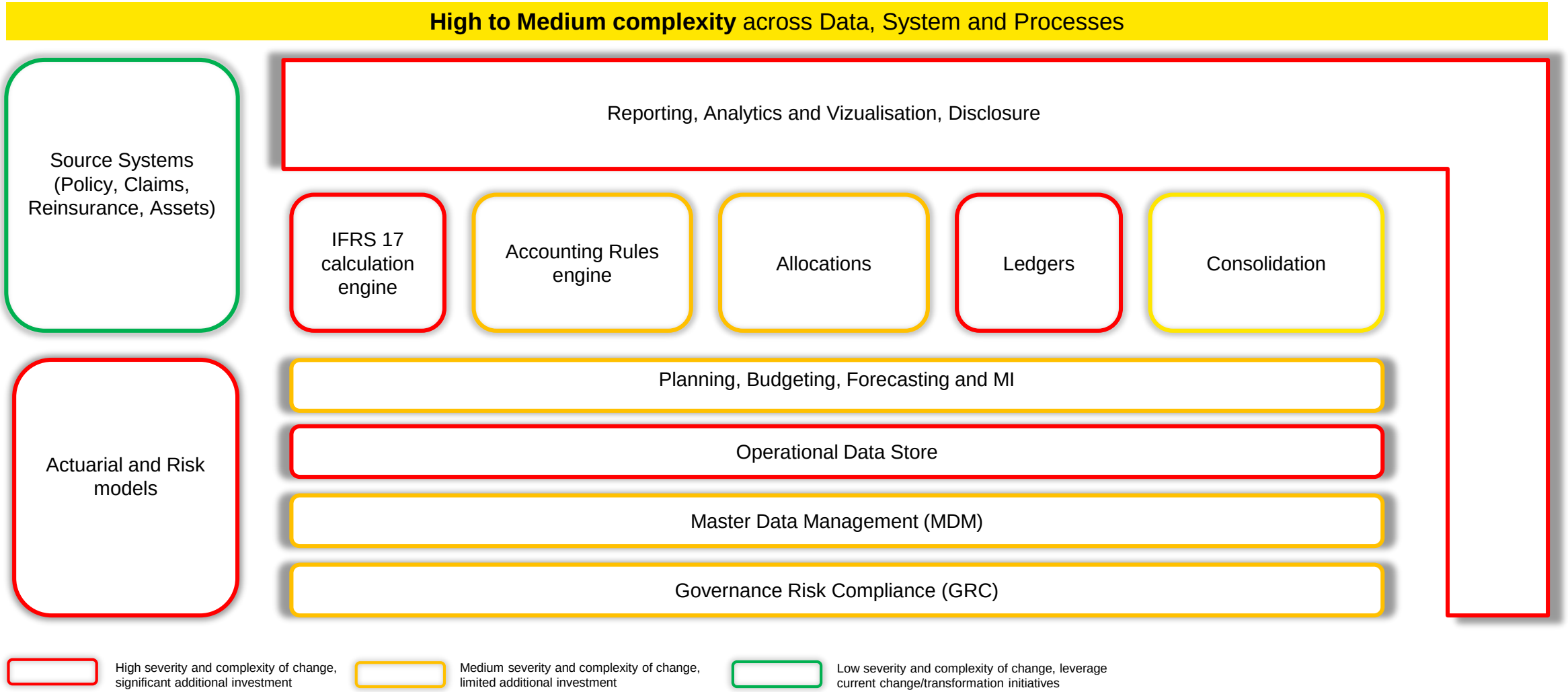
5. Follow a proven IFRS implementation methodology (with structured and centrally prepared input templates)

6. Important to emphasize both the content and process skills needed to get the job done (difficult to find people who master both skills equally well)

7. Need to appoint a separate **accounting lead** (IFRS 17 specialist), **actuarial lead** (financial & business impact models), **systems lead** (ERP/EPM) and **conversion project lead** (finance change specialist) to jointly manage the IFRS 17 conversion

Operational implications

Due consideration is required across the entire systems architecture



Operational implications

We recommend a phased approach to manage the timely implementation of IFRS 17

1 Perform current state assessment

- Do detailed gap analysis
- Perform financial and operational impact assessments
- Start with resource planning
- Educate key stakeholders

2017

2 Design desired state and develop new architecture

- New accounting policies and proforma financial statements
- Design desired system landscape
- Tackle issues identified during the operational impact assessment
- Design actuarial and finance target operating model
- Allocate people

2018

3 Implement new processes and systems

- Execute planned implementation
- Go live with new systems architecture
- Perform parallel runs
- Ensure wider business impact is managed appropriately
- Discuss issues with auditors/regulators
- Workshops and trainings

2019 - 2020

Operational implications

Recommended next steps (in 2018)

- ✓ Start your local IFRS 17 impact assessment project(s)
- ✓ Mobilize project resources & key stakeholders
- ✓ Conduct core team training (covering content & process)
- ✓ Perform gap analysis (using pre-populated structured templates)
- ✓ Conduct impact assessments (financial, products, systems & processes, people)
- ✓ Determine realistic implementation roadmap & budget (including IT)
- ✓ Report findings to internal stakeholders (MT, Board, Group etc)
- ✓ Discuss findings with external auditor and regulator(s)
- ✓ Seek approval for next phase (Design)

Operational implications

Our IFRS 17 thought leadership publications and reference tools

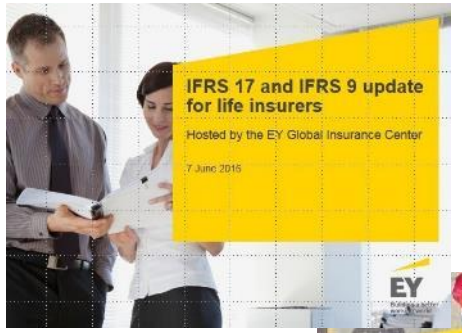
Thought leadership

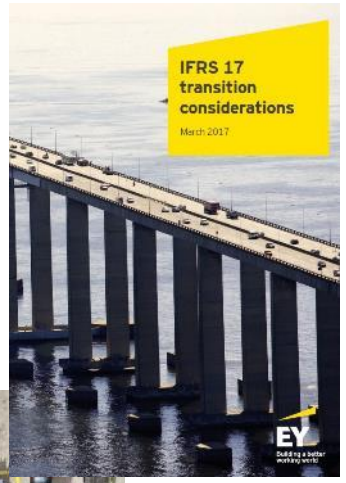
- IFRS 17 Insurance Accounting Alert (May 2017)
- IFRS 17 transition considerations (May 2017)
- IFRS 17 Insurance contracts: Ready, set … Implications for Hong Kong insurers (March 2017)
- IFRS 17: Shining a light into the value of insurers? (December 2016)
- IFRS 17: Illustrative example of life contract without participation features (June 2015)

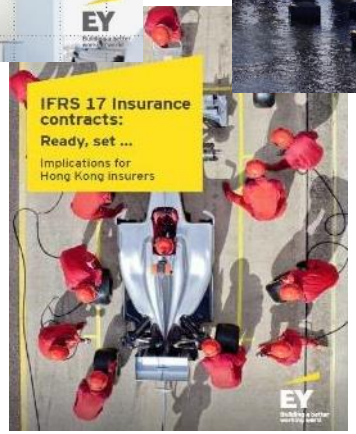
Reference tools

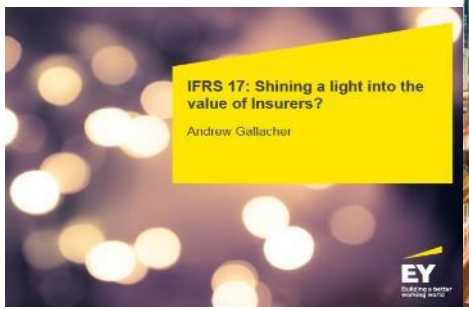
We regularly publish thought leadership on IFRS 17 providing valuable insights for your business.

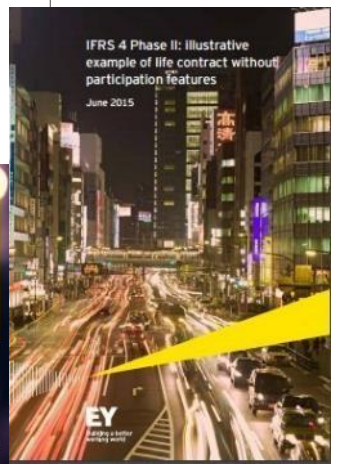
Visit us on http://www.ey.com/gl/en/industries/financial-services/insurance/ey-frac-accounting-change to read about our latest insights and view points.











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