

Challenges and Business Implications of IFRS 17

Prepared for CEO Focus Group 6th/2018
Demystifying IFRS 17 for General Insurers

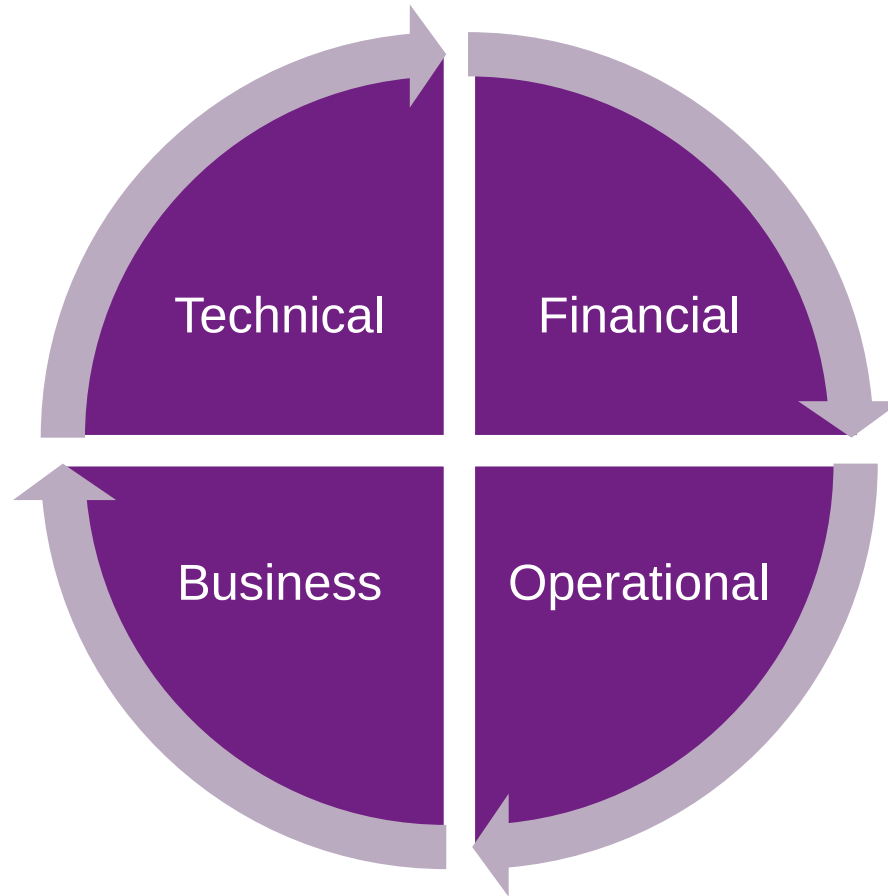
Jointly Organized by TGIA & WTW

14 November 2018



Overview: Key Aspects to Consider

The most important IFRS for insurers





IFRS 17 Framework

Current Balance Sheet Overview: Where does IFRS 17 fit?

The most important IFRS for insurers

IAS 38 *Intangible Assets*

IAS 18 *Revenue*

IFRS 4 *Insurance Contracts*

IAS 40 *Investment Property*

IAS 39 *Financial instruments:
Recognition and Measurement*

IAS 32: *Financial Instruments:
Presentation*

IFRS 7 *Financial Instruments:
Disclosures*

IAS 37 *Provision, Contingent
Liabilities and Contingent Assets*

**Intangible
Assets**

DAC

Property

**Financial
Instruments**

Cash

Assets

**Shareholder
Equity**

**Technical
Provisions**

Debt

**Other
Liabilities**

Liabilities

In 2014 standards finalised for:

- **IFRS 9** to replace IAS 39
- **IFRS 15** to replace IAS 18

In 2017 standards finalised for:

- **IFRS 17** to replace IFRS 4

IFRS 4 *Insurance Contracts*

IAS 39 *Financial instruments:
Recognition and Measurement*

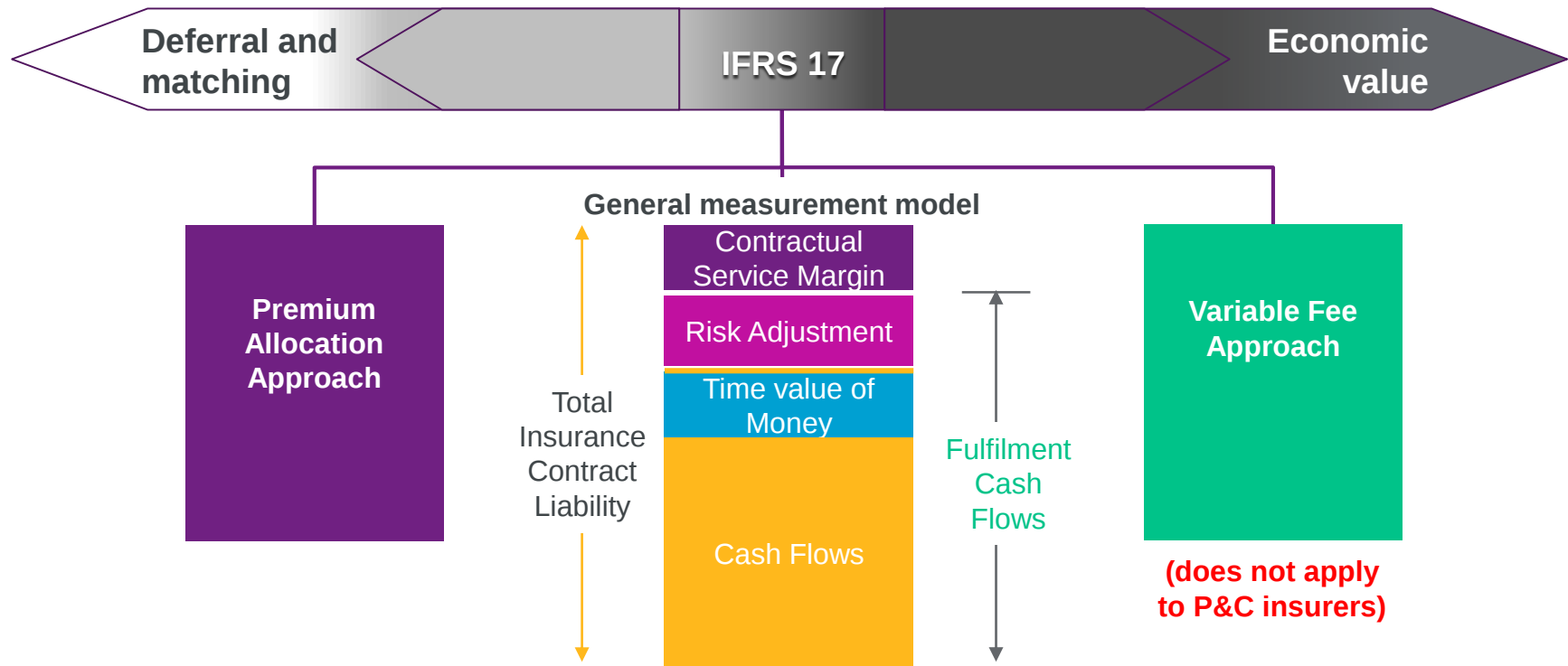
IAS 18 *Revenue*

IAS 37 *Provision, Contingent
Liabilities and Contingent Assets*

IAS 12 *Income Taxes*

IAS 19 *Employee Benefits*

IFRS 17 Hybrid Measurement Model



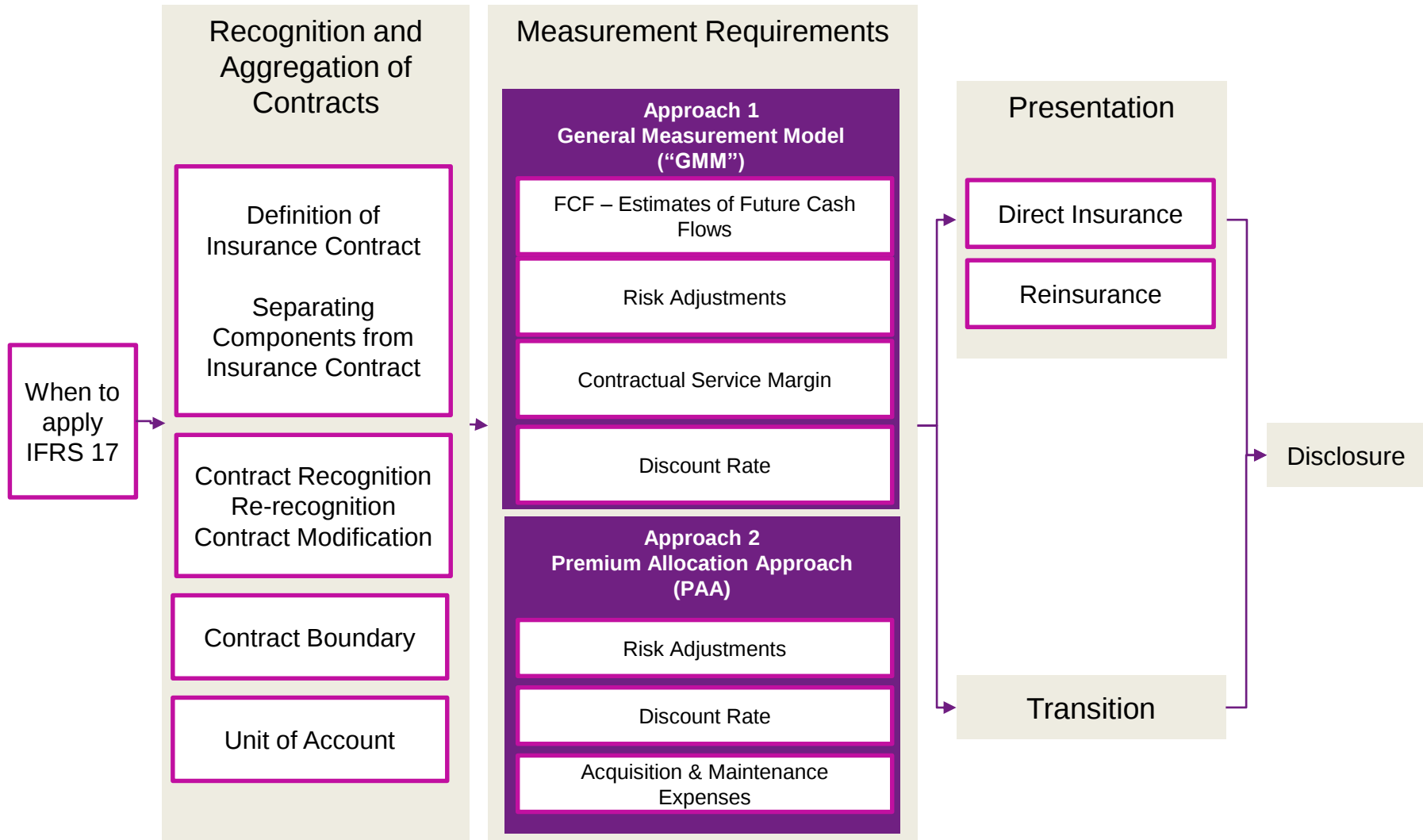
New IFRS 17 Income Statement

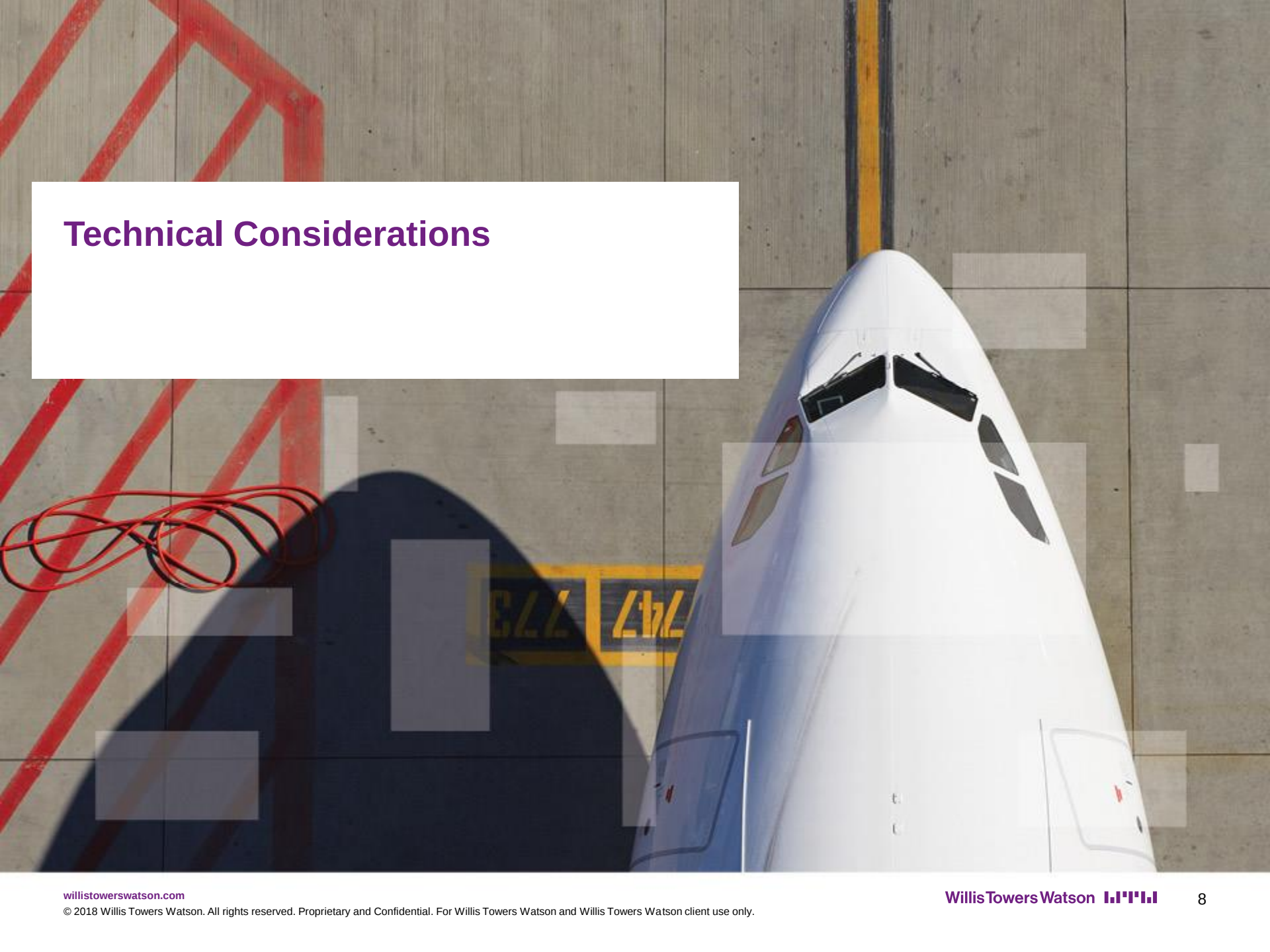
Statement of Comprehensive income	
	2021
Insurance contract revenue	x
Insurance service expenses	(x)
Insurance service result	x
Investment income	x
Insurance finance expense	(x)
Net financial result	X
Profit / Loss	x
Discount rate changes on insurance liability (optional)	X
Total comprehensive income	x

- Hybrid between sources of cash flow & surplus approaches – no premiums
- Insurance contract revenue and service expenses exclude any investment components
- Insurance finance expense is excluded from insurance service (underwriting) result
- OCI discount rate option appeals to countries currently on deferral and matching approach

Complexity

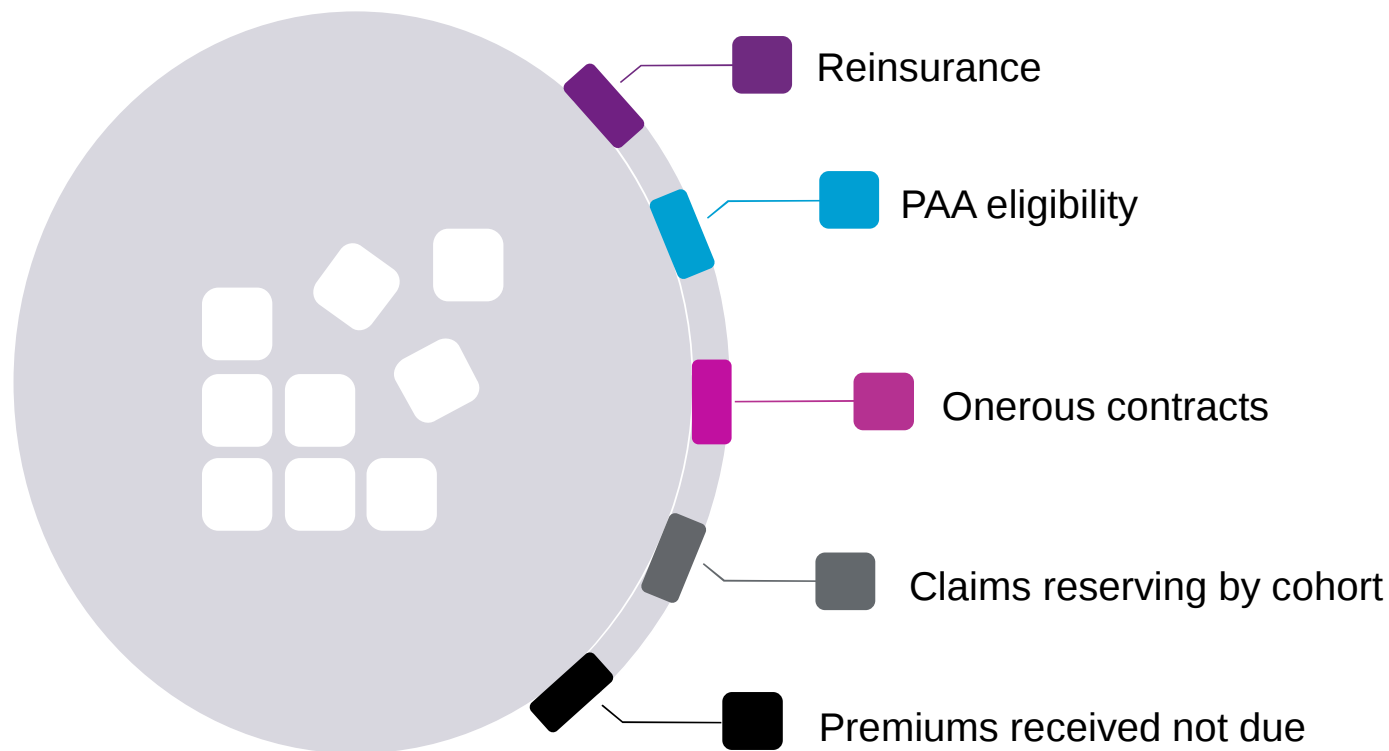
Key Focus Areas





Technical Considerations

IFRS 17 Technical Challenges – P&C specific



But is it simple for a traditional P&C insurer?

**General
Measurement Model
vs
Premium Allocation
Approach**

Level of Aggregation

**Identification of
Onerous Contracts**

**Recognition and
Contract Boundaries**

**Calculation of CSM
and Risk Adjustment**

Discount Rate

**Additional data
capture and
granularity**

**Allocation for
Changes in Discount
Rate
(OCI vs P&L)**

**Reserving under
IFRS 17**

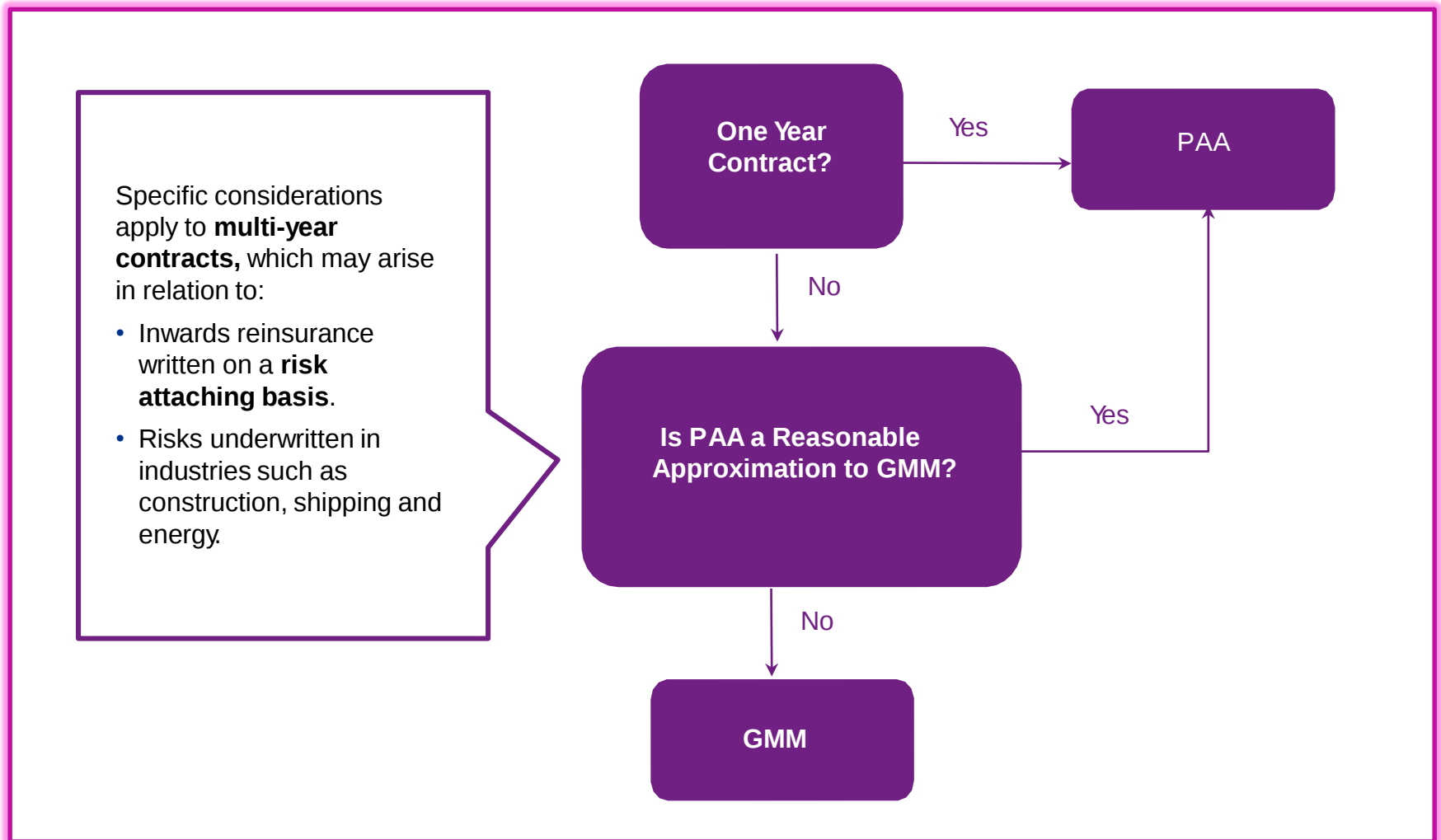
Reinsurance

**Presentation and
Additional
Disclosures**

Dividends, transition

Eligibility for PAA – Decision Tree between PAA vs GMM

Assess all lines to assess ability to adopt simplified PAA measurement approach



Operational Consideration

From theory to practice



Considerations

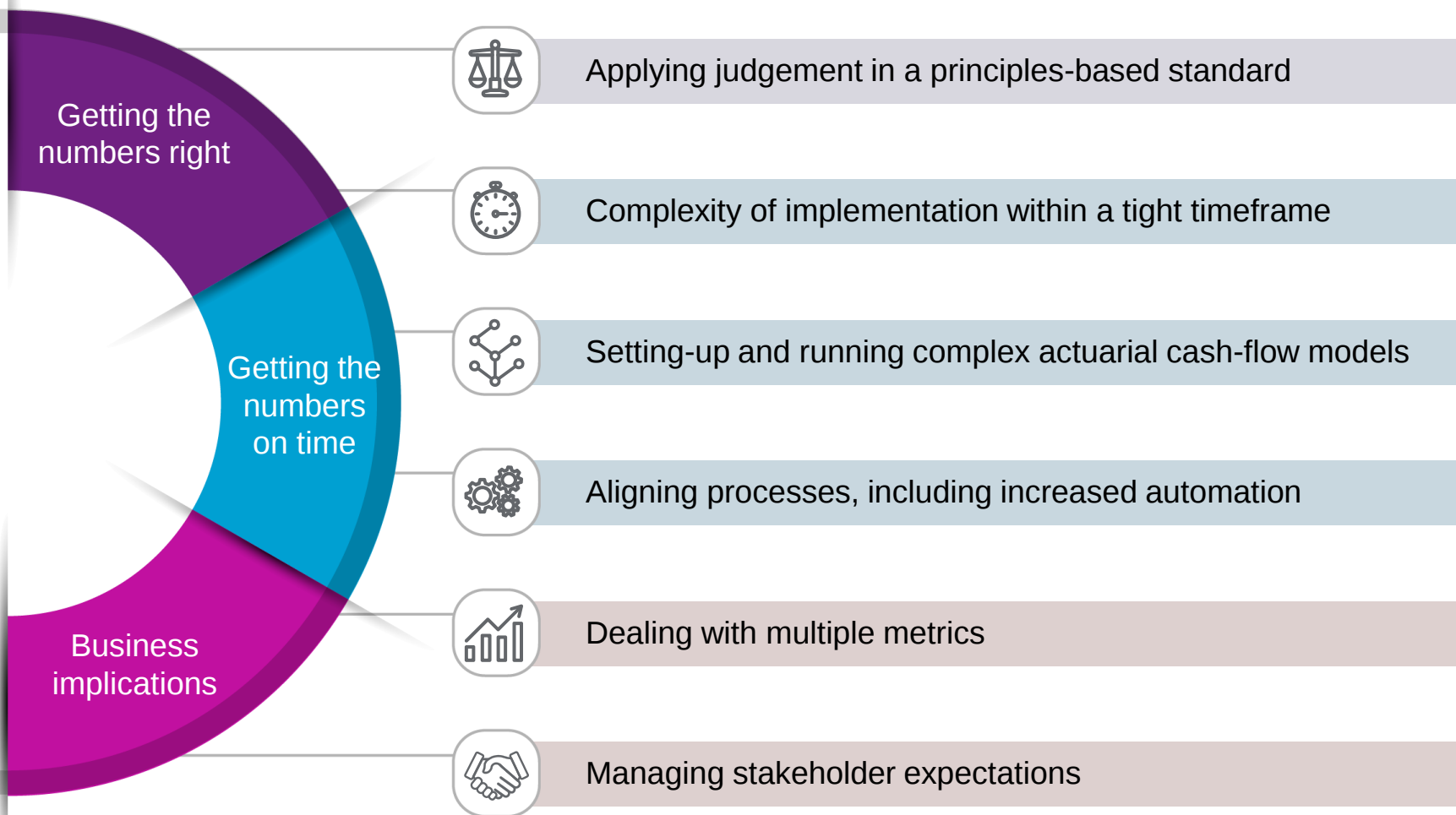
Why transition to IFRS 17 will not be without turbulence

1. Recognition of premiums/contracts
2. Definition of “portfolio”, segmentation and level of aggregation
3. Measuring onerous contracts:
4. Acquisition costs – attributable? Expense or defer?
5. Outstanding claims: when and how to discount?
6. Explicit risk adjustment to outstanding claims
7. Reinsurance – an explicit and separate calculation
8. Disclosures
9. Transition – retrospective view



Key implementation challenges

More than a compliance exercise



IFRS 17 – what are the key gaps?

IFRS 17 Key Requirements	Gap	Impact	Effort
Level of Aggregation			
1. Level of Aggregation – Unit of Account			
Identification of Onerous Contracts			
2. Onerous Contract Liability			
Measurement Models			
3. Measurement – General Measurement Model			
4. GMM – Contractual Service Margin			
5. GMM – Expected Cash Flows			
6. GMM – Discounting / Time Value of Money			
7. GMM – Risk Adjustment			
8. Measurement – Premium Allocation Approach			
9. Other Measurement Considerations			
Reinsurance Held			
10. Portfolio Transfer / Business Combination			
11. Reinsurance Contracts			
Identifying Scope of Insurance Contracts			
12. Scope and Unbundling			
13. Financial Instruments with DPFs			
Recognition and Contract Boundary			
14. Recognition / Derecognition			
Presentation and Disclosures			
15. Statement of Financial Position			
16. Statement of Comprehensive Income			
17. Disclosure – Amounts			
18. Disclosure – Judgements			
19. Disclosure – Risks			
Acquisition Costs			
20. Acquisition Costs			
Transition			
21. Transition			

Large Gap

Significant gap between current practice and IFRS 17 requirements. Fundamental to address this area

Medium Gap

Some ability to implement IFRS 17 requirements. Opportunity for further development exists

No Gap

Current practice is consistent with IFRS 17 requirements. Limited need for further development

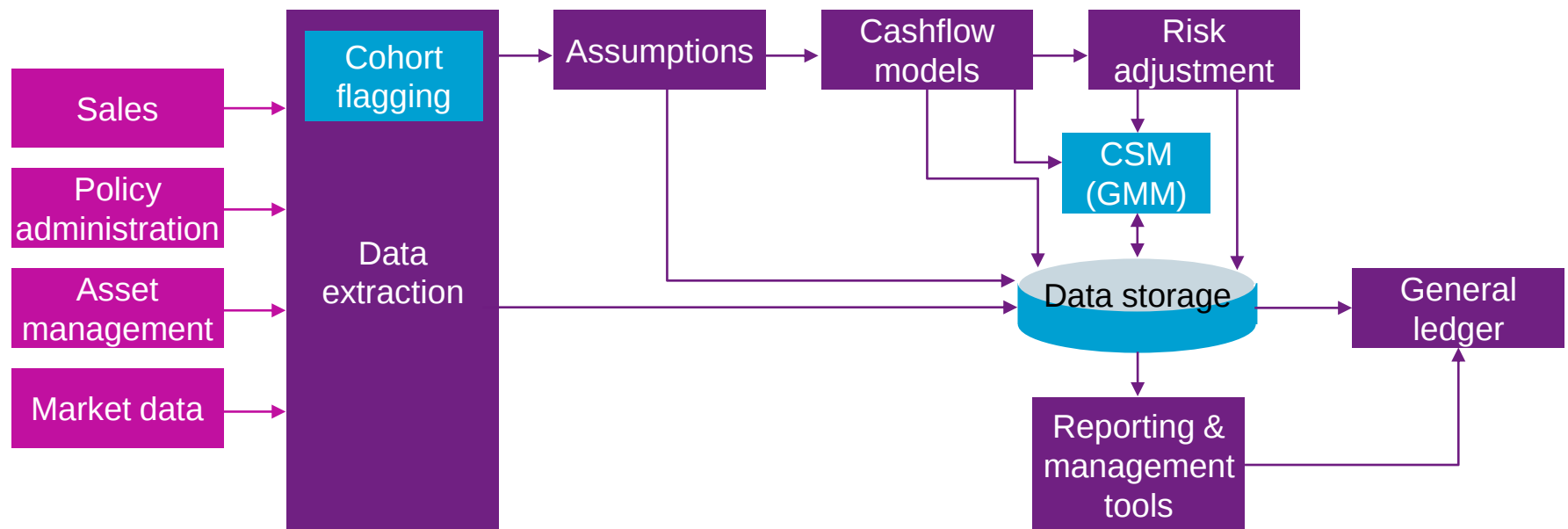
Vision

Industry current state	Industry future state
Information produced infrequently and in arrears	Real-time or near real-time processes
Processes triggered / run manually, using desktop and poorly governed solutions	Automated, controlled Enterprise software
Poor auditability and repeatability of processes	Full automatic auditability and repeatability
Fixed grids and / or some adoption of Cloud computing	Fully elastic compute resources
Software and hardware licenced from vendors on a static basis	Software and infrastructure available as service
Large and costly actuarial teams managing models and run processes	Significant reduction in cost with actuarial teams focused on value add work

Future State:

**Significant reduction in cost and operational risk
with actuarial teams focused on meaningful value-add work**

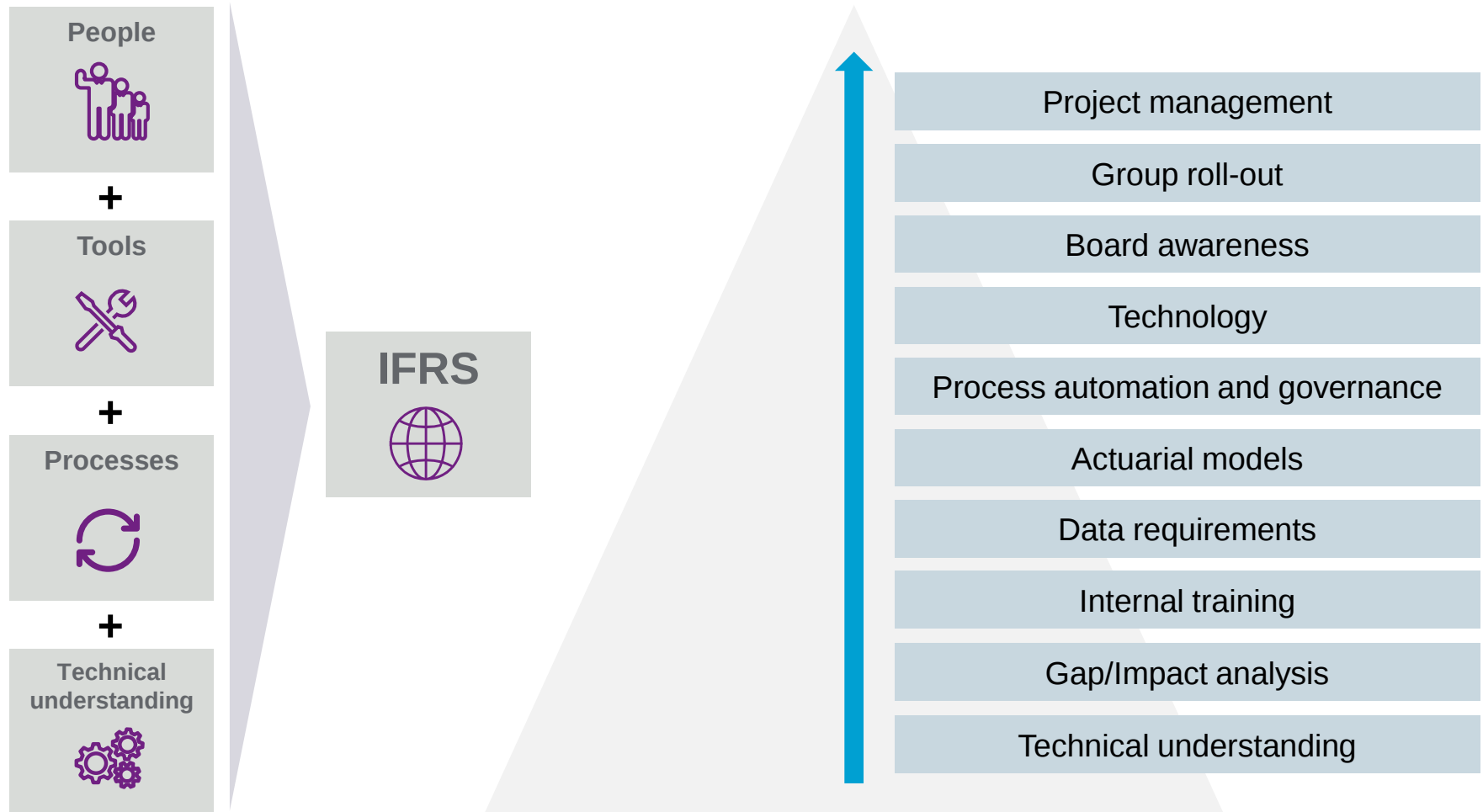
Example: the CSM engine



 Systems requiring change
  New systems required

Implementing IFRS 17 requires a holistic approach

The technical understanding of complex issues underpins the processes, tools and people change requirements



Business Implications

What does this mean to business



IFRS 17 Business Implications

Executive compensation



Impact on dividend paying capacity



Investor communication

- Intra IFRS 17
- Interaction with wider metrics
- Disclosure consultation



Use in decision making



Priority in implementation strategy



Other Considerations

- Product Strategy
- Reinsurance



Executive Compensation:

How is Compensation to be structured

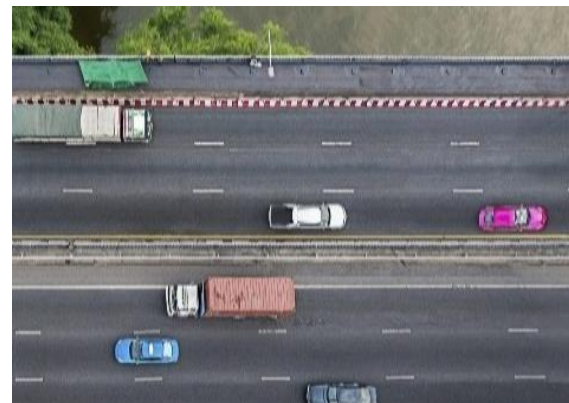


Mismatch in business planning

- Current vs IFRS 17 Financials

Performance Assessment

- Profit Emergence patterns
- Link performance to existing strategy



Compensation Restructure

- Link to drivers
- Re-education of key Stakeholders
- Equitable

Impact on dividend paying capacity:

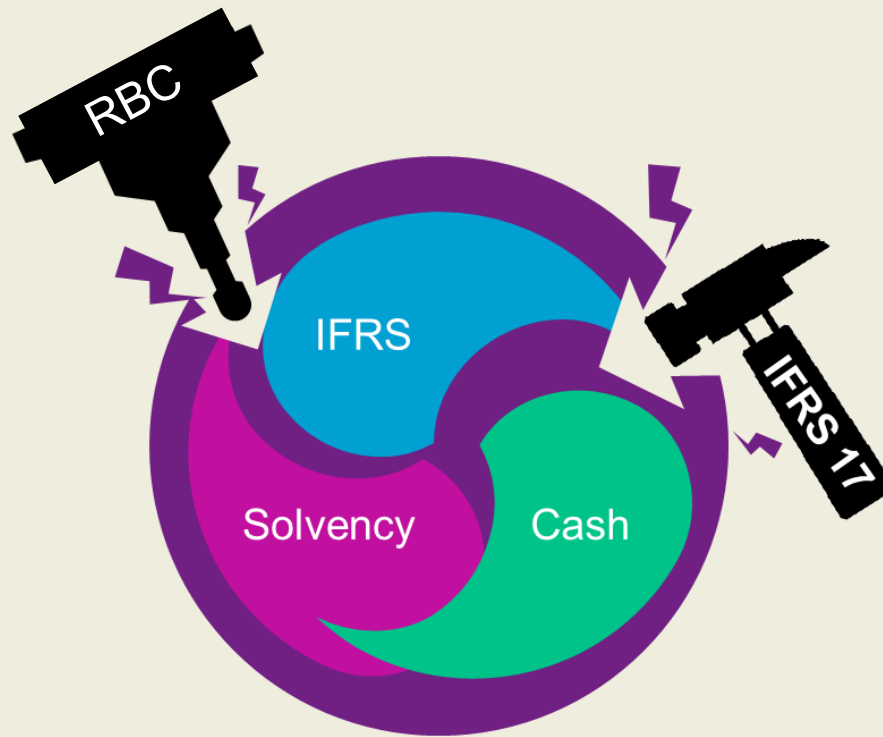
How will dividends be determined

Dividend Considerations

- Bound by solvency or capital requirements
- Also possibly restricted by retained earnings
- IFRS 17 may lead to restrictions in dividend paying capacity
- May be significantly different from existing practices

Investor communication:

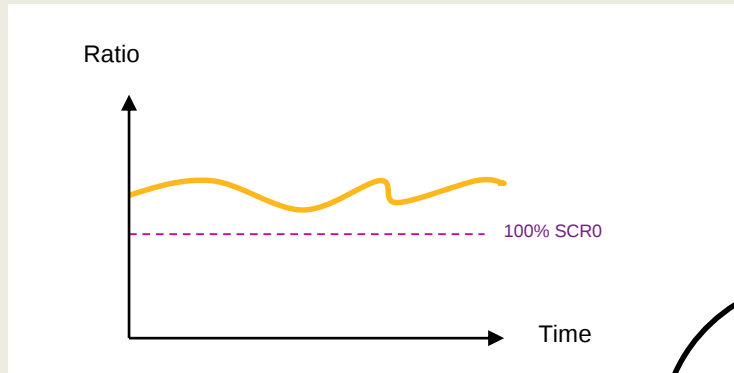
Increasingly complicated investor message



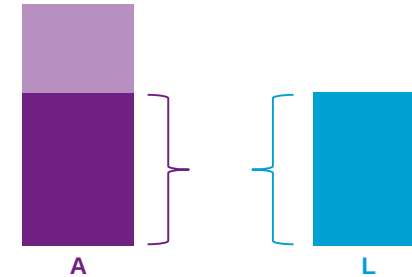
Use in decision making:

Which metric to manage to?

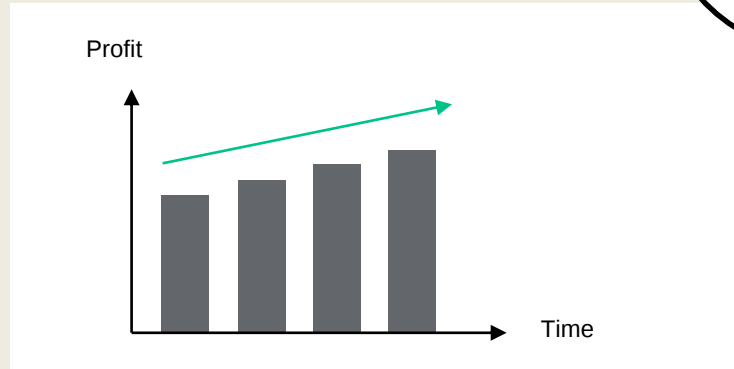
Capital Regime ratio



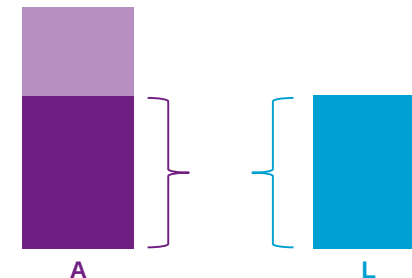
Capital Regime Balance Sheet



IFRS Profits



IFRS Equity / Value



Prioritizing implementation strategy:

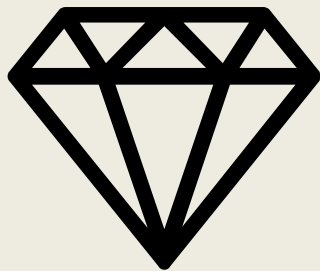
Business model affects optimal implementation

Business model?	Objective? Technical and financial implications?
Stable/mature direct writer	■ Demonstrate continued stable profits – use of OCI? ■ Retrospective transition? ■ Double declaration of past profits likely
Growing/new entrant	■ Demonstrate and reconcile IFRS new business impact with VNB ■ Possible dividend traps arising from low retained earnings ■ Slower emergence of profit than current?
Acquirer	■ Consistent reporting between past and future acquisitions ■ May encourage fair value approach to transition
Asset accumulator	■ Much of business may lie outside IFRS 17, hence impact limited
Composite	■ Dilemma: use of PAA or use of GMM throughout?

Other Considerations: *Product Strategy*

Repricing

- Reprice loss making or low margin products.
- Review and revise pricing where possible of onerous blocks
- What do you do with loss-making contracts once you have identified them?



Product Strategy Reassessment

- Review business mix
- Strategize around products or approaches which optimize profit emergence under IFRS 17
- Leverage reinsurance or revise RI strategy



Other Considerations: *Reinsurance*

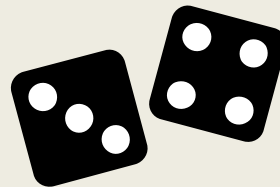
More scrutiny on reinsurer credit ratings

Insurers must include the risk of non-performance of a reinsurer in their projections of reinsurance cash flows.



Changes to prioritisation of reinsurance

IFRS 17 grouping may help insurers to decide what they reinsure, focusing just on the 'loss-making and 'might become loss-making' groups for example.



Review of insurers' reporting and pricing bases

IFRS 17 will require insurers to recognise the full loss on any unprofitable insurance business immediately.



IFRS 17 Business Implications

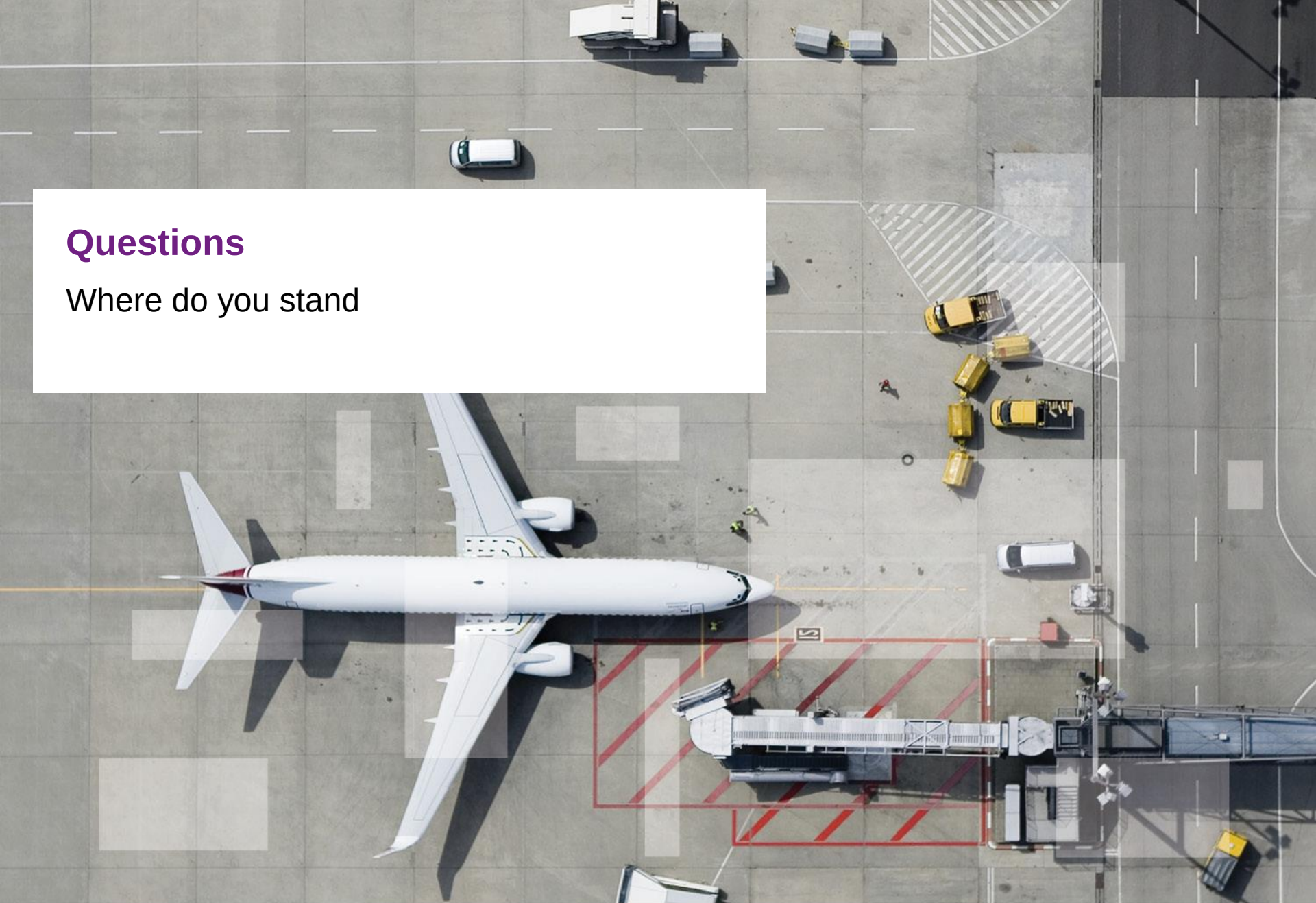
Other Considerations

- What will the impact be on your future revenue and profit streams?
- How much transparency will be provided by your disclosures?
- Do you continue writing business with no significant top- or bottom-line impact?
- Are your people engaged – from the CEO down?



Questions

Where do you stand



Q1. What sort of progress has your firm made in working out the business implications of IFRS 17?

1. Nil progress

2. Made a start, much more to do

3. Some internal views

4. Clear internal views

5. Moving already to embedding

Q2. What sort of budget and resources have you set aside to work and implement IFRS 17?

1.No budget in place

2. < 5 Million

3. 5 Million to 10 Million

4. 10 Million to 20 Million

5. > 20 Million

Q3. What approach are you considering in adoption of IFRS 17?

1.No change to current strategy and practices

2. Purely a compliance exercise – bare minimum of requirements without investing in new technology

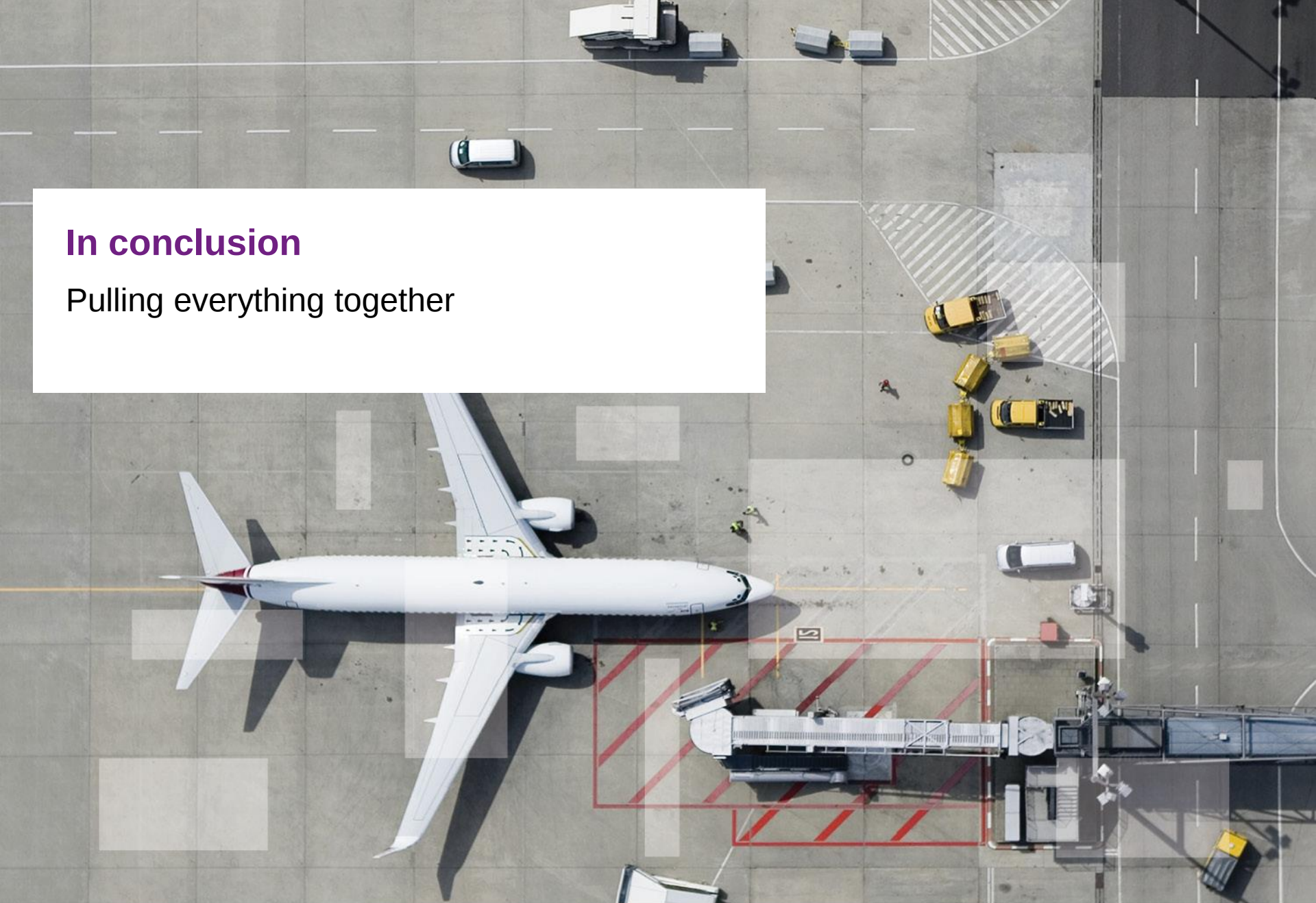
3. Focused on compliance with improvements in terms of financial Reporting with adoption of new technology

4. Mixture of enhanced strategy and financial reporting beyond the Minimum compliance requirements

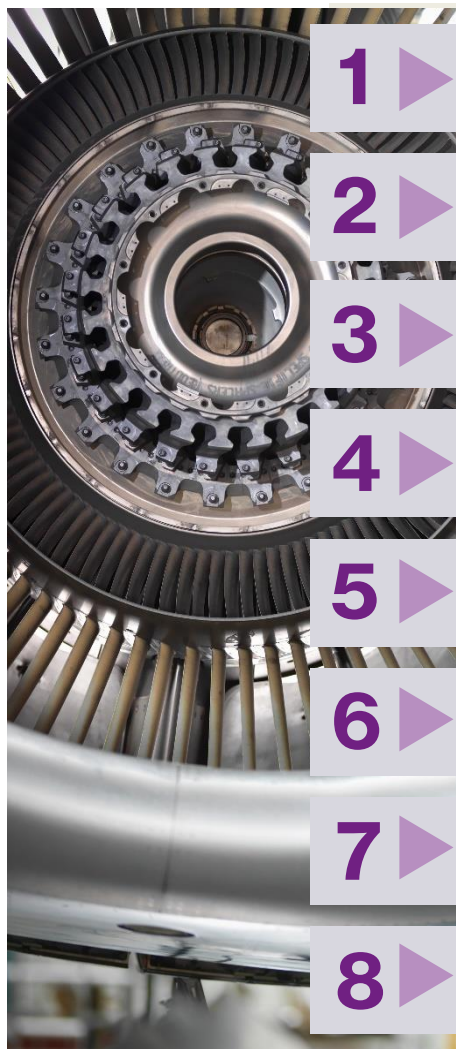
5. Full strategic optimization and financial transformation

In conclusion

Pulling everything together



IFRS 17 – why this time it is serious



1 ▶

IFRS 17 is a fundamental change in insurance accounting and reporting

2 ▶

Time is already running out!

3 ▶

The standard requires the use of judgement and the weighing-up of numerous options.

4 ▶

Top performers will look to use IFRS 17 to drive major changes in processes

5 ▶

As with all major transformations, people are key.

6 ▶

Leveraging existing tools is essential to reduce costs, as is focused project discipline

7 ▶

IFRS 17 will demand state-of-the-art modelling software, integrated into the overall project solution

8 ▶

Published IFRS figures will be the principal KPIs for shareholders, analysts and management



Implementation: critical success factors

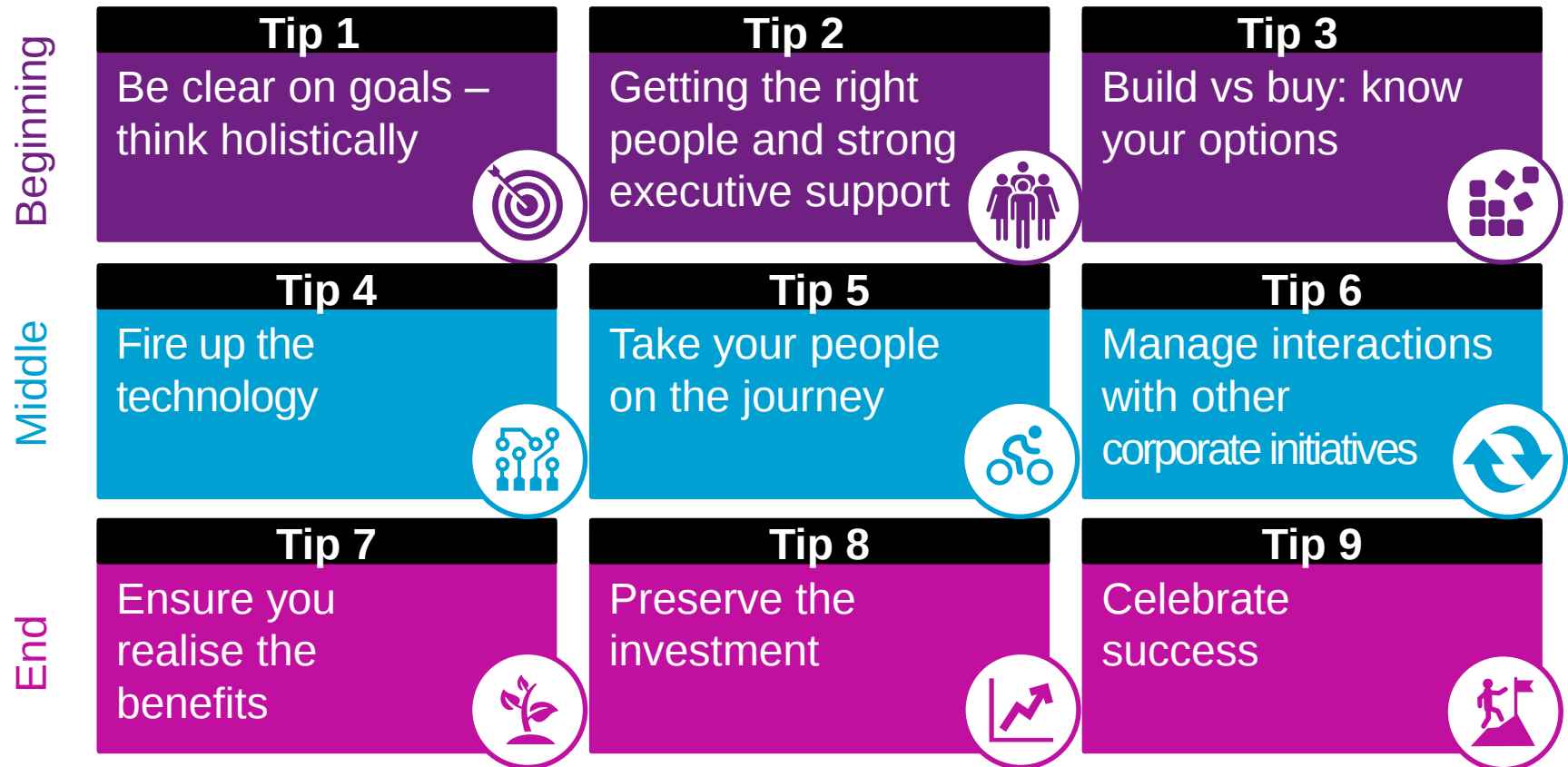
Steering a course through the storm



You will need a team that has the expertise and reach to captain, navigate, pilot, crew and power your journey to implementation

We Have Learned Many Valuable Lessons

Our practical experiences give us the know-how to be successful



Summary: Key factors for a successful IFRS 17 implementation

- Clear objectives
- Informed, efficient and effective governance
- Understand the business impact
- Stakeholder buy in to the programme
- Appropriate prioritisation and allocation of resources
- Accurate information and work quality
- Clear and state process, and roadmap to achieve
- Align to and complement other business objectives
- Consider early the business implications



What is your view of IFRS 17? How and when will you form one?



Reliances and Limitations

This presentation has been prepared by Willis Towers Watson for general information purposes only and does not constitute professional advice. The information, opinions and illustrations contained are derived from various sources and have not all necessarily been independently verified by Willis Towers Watson. The presentation is not intended to guide or determine any specific individual situation and persons should consult qualified professionals for appropriate professional advice before taking any specific actions. Neither the presenter, nor the presenter's employer, shall have any responsibility or liability to any person or entity with respect to damages alleged to have been caused directly or indirectly by the content of this presentation. If you require professional advice or require any further information, please contact your usual Willis Towers Watson representative.

