

Whitepaper

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Getting IFRS 17 Implementation right

The worldwide implementation of IFRS 17 is likely to be one of the most disruptive changes to the insurance industry ever.

While it varies from one company to another, and also by region, the initial impact assessments of IFRS 17 by insurers are likely nearing completion. However, this global standard was designed to be principles-based and to apply to all types of insurance. This led to some confusion and challenges in the interpretation of the text and in translating it into practical terms. Significant practical challenges around data, systems and processes are to be expected.

Accounting and financial reporting standards have changed many times in the past. Why is IFRS 17 such a 'revolution' for the insurance industry?

IFRS 17 changes completely the way the insurance industry will report its numbers. At a fundamental level, the way that profits are calculated will change. Also the way that liabilities are calculated and presented will change, because of the addition of the CSM to a more familiar actuarial calculation of the PV of cash flows. The CSM is designed to reflect the remaining unearned profit on a group of contracts and potentially absorb the day 1 gain. That is a significant change in how insurers need to think of managing their profit through time.

Fully understanding the new measurement of profit, and what drives it, will take some time. Analysts will have more information available to review financial performance of a company, which increase pressure and competition. So, there is a lot at stake for insurance companies which need to pay close attention to the implementation of IFRS 17 and to the choices they make during this project. IFRS 17 will impact many departments and functions across organizations including product design, pricing, valuation, and finance. Understanding how to comply and the choice around the design of systems and processes to comply seems, to us, to be one of the major challenges.

Firms should not underestimate the resources that will be required to implement the required changes effectively and meet the deadline. These resources will likely become scarce as the project progresses.

How is Moody's Analytics helping insurance organizations to respond to the IFRS 17 accounting standard?

This new standard connects two worlds within insurance organizations that up until now had limited interactions: the actuarial and accounting departments. The new financial statements under IFRS 17 will require many more components than the actuarial reserves. As an example, the change in liabilities is mostly reflected in the income statement and traditional cash-based accounting determined the rest. Not so anymore under IFRS 17. Going forward, these two worlds will have to be bridged, and they will have to speak a common language.

Moody's Analytics has deep actuarial modeling expertise with an understanding of insurance company structures, data processing requirements, traditional accounting and regulatory reporting compliance, and evolving technology capabilities. We have been spending a significant amount of time over the past 18 months working to understand the problems in some depth. IFRS 17 is like the proverbial iceberg, in that there's a lot below the surface to understand.

We have worked hard at building solutions, and enriching our existing solutions, to address these challenges and to help our customers accelerate their IFRS 17 projects by delivering most of the functionalities out-of-the-box.

Moody's Analytics has a proven track record of providing award-winning solutions to the insurance industry, including our new IFRS 17 solution, comprised of:

- » An all-in-one, next-generation actuarial solution that can be deployed in the cloud for unmatched performance
- » An IFRS 17 solution that handles natively all the complexities around the IFRS 17 calculations – including reinsurance held, intragroup transaction, and corporate hierarchy – using inputs from life, health and P&C actuarial systems, and can generate posting files for financial systems
- » Scenario generation solutions for market-consistent valuations
- » Advisory capabilities, including research and modeling to address IFRS 17 issues

What is Moody's Analytics offering to ensure an efficient and effective implementation of IFRS 17?

The first beta version of our IFRS 17 solution described above was published in December 2017. This solution can accelerate clients' projects by providing, out-of-the-box sophisticated and flexible capabilities for IFRS 17 calculations and reporting. This calculation engine is available out of the box to pair with any actuarial system.

We don't just provide the software – we also provide related solutions. For example, we offer market calibration services for discount rate and liquidity premia, and we have the capability to do scenario analysis in a more advanced way than what the standard requires, as well as macro-economic scenarios.

Potential synergies between IFRS 9 with IFRS 17 seem to be an important factor of the implementation project. What is your recommendation for insurers?

Insurance companies traditionally do not have assets that are as complex or as exposed to credit risk as banks. So there could be a temptation to set aside IFRS 9 and focus purely on IFRS 17, which is going to be more demanding and disruptive for insurers. Resources for implementing either initiative will be limited. However, our experience implementing IFRS 9 solutions globally tells us that there are benefits to addressing both standards simultaneously, to avoid rework in the future. This is particularly true where the two standards intersect. For example, when looking at participating insurance contracts where components potentially need to be separated and accounted differently.

How can insurers leverage and protect existing Solvency II or actuarial investments for their transition to IFRS 17?

Solvency II imposed significant project costs on European insurers. As a result, firms will want to leverage their Solvency II infrastructure when implementing IFRS 17. While the nature of the information – such as present values or risk adjustments – may appear similar, IFRS 17 and Solvency II have been designed to achieve different goals and require different processes. IFRS 17 also requires actual transaction data, and different granularity of data, discount curve approach, and risk adjustment methodologies.

That being said, there are important elements that can be reused, at least partially. Firms may be able to use some of the actuarial solutions they put in place for Solvency II to calculate some of the IFRS 17 building blocks, but probably not all of them. They may also be able to use their existing data warehouses. Perhaps most significantly, firms can leverage their experience dealing with massive and pervasive projects. But in the end, insurers will need to develop and implement many new processes for IFRS 17.

New technologies can have an impact on the implementation of the new standard. How is Moody's Analytics responding to these potential technology requirements from their clients?

IFRS 17 is very demanding in terms of data volumes and performance. Indeed, the time window to produce the balance sheet and P&L is tight. IFRS 17 also introduces extensive new requirements for calculation, transfer, storage and aggregation of a vast amount of data. Insurance organizations often request – and we can provide – solutions in either in a public or internal

cloud. Some insurers are also interested in big data capabilities because of the large volume of data they have to process to produce IFRS 17 calculations. Moody's Analytics can also help with this challenge.

We believe that a technological shift is currently underway, and that, even if insurers are not fully ready for it, they will need to grapple with it in the coming years. As a technology provider, we want to help our clients embrace these new enablers and make this transition smoothly.

In conclusion, insurers need to consider taking a holistic approach to adopting the IFRS 17 standard, and ensure that the project has the right level of attention and resources. IFRS 17 will impact organizations at a strategic and a tactical level, and so getting the implementation right is crucial to mitigate both compliance and strategic risk.

To find out more about Moody's Analytics solutions for IFRS 17, visit moodyanalytics.com/IFRS17

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