IFRS 17: What the industry thinks about implementation

The IFRS 17 accounting standard for insurance contracts is due to take effect in 2021, but some insurers are already complaining about the complexity it brings, and querying whether the benefit will outweigh the effort and investment in the project.

The potential headaches that IFRS 17 will cause were discussed at InsuranceERM's Data for ERM & Solvency II conference on 7 June. Ross Chapman, marketing director of software vendor Aptitude, asked a panel comprising life and general insurers, actuarial and accounting experts, to share their insights into the implementation challenges.


Jo Clube

Jo Clube, group technical accounting director, Aviva

What is different about IFRS 17?
IFRS 17 is going to fundamentally change how we measure and report our insurance contracts. The basic measurement model has the same building blocks as Solvency II, but overlays a performance mechanism to measure profit – that's where the complexity comes in.

The first big difference is the scope of IFRS 17: it's just your insurance contracts and participating investment contracts. Unit-linked products, where there's no insurance risk, will not be measured under IFRS 17.

IFRS 17 is much more principles-based. The standard says you should reflect the characteristics of the liability. There are no details, guidance or anything prescriptive about what the discount rate should be, so there could be a big difference with Solvency II numbers. Similarly with the risk adjustment.

Another difference is the contractual service margin – the profit that you expect to earn over the lifetime of a contract. That future profit, which you haven't earned yet, goes on your balance sheet as a liability, and then you earn over time as you deliver the service or the contract. There is a lot of complexity in that.

The great hope is that it will bring consistency to insurance reporting. But actually there are quite a lot of choices within the standard, such as around the discount rate and which variation of the model you use.

How will IFRS 17 affect tax?

In terms of tax, I think the UK is quite unique, as we use IFRS profits as the basis for tax, with no adjustments. So it's going to directly impact how much tax you pay.

For example, annuity contracts are currently recognising a lot of profit on day one. Those profits will have been taxed. In the IFRS 17 transition, we're going to have to reverse those profits and put them back on the balance sheet, then they will be recognised again in line with the IFRS 17 principles. We need to figure out with tax authorities how we deal with that transition, to make sure profits don't get taxed twice, or that profits on other profits don't escape tax.

Prashanth Ariyam

Prashanth Ariyam, UK

IFRS 17 audit lead, Deloitte

What's going to be the impact on profitability?

The impact on the income statement will be entity-specific and depend on a number of factors. Typically, the longer the duration of the product, the greater the impact.

If you are a life insurer and have annuity-type contracts, typically under the current IFRS you recognise big day-one profits. Some CFOs have said to me they recognise 80% of profits on day one. Under the IFRS 17, much of that profit will be deferred over the term of that policy, which could be 10, 15, 20 years.

For a with-profits contract, the impact could be the opposite. Under current IFRS, typically you recognise small profits over the life of the contract, with a big component at the end. Under IFRS 17, you accelerate that recognition for accounting purposes.

For general insurance, where typically the coverage is a 12-month policy, there is probably not a huge amount of difference. But in the 'expired portion', the claims reserve, we see some difference in profits: that's largely due to the choice around the discounting, the risk adjustment and some other technicalities.

Richard Olswang,

head of finance actuarial, Prudential

What makes IFRS 17 so complex?

Probably the two biggest areas of complexity are the unit of account and transition.

The unit of account is the level at which you can aggregate contracts. IFRS 17 is an individual contract standard, but it allows a degree of grouping. That grouping is very important, because profits are spread over the course of a contract, but if the contract is loss-making (onerous) then the loss is recognised on day one. If you group these together, you get a very different profit profile from accounting for them separately.

The level of aggregation is also

Richard Olswang

critical from an operational perspective, as it will have a big impact on systems and processes.

The other area is transition. When you first implement IFRS 17, you must have an opening balance sheet and the objective is to determine that as if it you had always applied that standard – effectively going back to when the business was written, calculating the contractual service margin and the day one profit at that time, and rolling it forward.

It's clearly difficult to do. There are alternatives, but that is a big area of complexity and will have a huge impact on the results. On day one of IFRS 17, all of the shareholder equity and profit will be driven by the transition balance sheet.

Looking at the solution architecture, is IFRS 17 just Solvency II with a CSM engine top of it?

It is a lot more than that. You can leverage a lot from the Solvency II investment, but there is more required on top. Start with the actuarial models that calculate the basic liabilities: you'll be able to use those, but IFRS 17 will inevitably use different assumptions and will require more granular output and it will require multiple runs. So, the models will need to be adapted and enhanced to be able to give all that output and do all those runs in a very short reporting timeframe.

There will need to be a process to leverage from the Solvency II risk margin to an IFRS 17 risk adjustment. The contractual service margin is new; that will require a completely new system to calculate it and data storage systems. Then there will be changes to general ledgers and financial consolidation systems.

What stage is the industry at in terms of preparations?
IFRS 17 has to be implemented by 1 January 2021. It sounds like a long way off, but you're going to have to start designing those systems fairly soon. But you can't do that until you decide on your accounting policy. That might not be a final accounting policy, but you need working assumptions to be able to specify the system changes.

Thomas Behar, chief actuary, CNP Assurances

What from the Solvency II implementation will be applicable to IFRS 17?
There are many things that we can reuse. I have eight here: first, all the work that we have done on improving data quality; second, the frameworks for managing assumptions; the third point is the model quality – we have worked hard to validate the results of the model, as we have done for data; fourth is the governance of data, assumptions and models; fifth is the process we have for developing models; the sixth point is the industrialisation of the models – we have streamlined the process of parameterisation; seventh is the IT infrastructure we have in place; eighth is all the links we have introduced between accounting and actuarial teams and the storing of calculations in new accounting systems.

We have spent a lot already, so the main difficulty for us today is to knock again at the door of the CEO and ask for money.

Thomas Behar