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IFRS 17 Implementation Insights

Series 1 – Business Case and Project Planning for Asia

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Who is the audience of this paper?

The International Accounting Standards Board ("IASB") published IFRS 17 in May 2017, an update and replacement of the current standard, IFRS 4, on insurance contracts.

Effective for annual periods beginning on or after January 1, 2021, insurers will be required to bring additional transparency, granularity and comparability to the stakeholders according to the IFRS 17 requirements. This is specifically for life insurers expected to have fundamental impacts to how insurance companies measure the insurance contracts, and to disclosures, reporting and presentation of financial performance. In addition, it is for insurers who expect fundamental change to their Finance and Actuarial organizations to fulfill these requirements and beyond.

While the IASB's effective date is just over 3 years for insurers to implement the new requirements, a simulation and parallel run of the IFRS 17 production before the effective date would be desirable, which potentially pushes a "readiness date" as early as 1 January 2019. This leaves less than 2 years for insurers to prepare for the upcoming changes. This paper summaries our experience on developing business cases and implementing project planning in the past 6 – 9 months for the subject owners, project leaders and other stakeholders in the insurance space in Asia who are impacted by the implementation of IFRS 17.

Specifically, we will share our view on the system implications as it could for many insurers be the most budget and time consuming element on this journey.

IFRS 17 is global, why considerations in Asia are different?

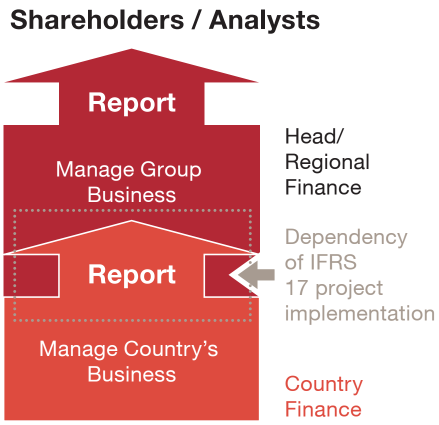
PwC estimates that significant spending by the insurance industry will be required as companies prepare to implement IFRS 17, especially for those insurance companies who plan to go beyond basic compliance into market reporting considerations and finance transformation. An estimated US$5 billion on accounting, actuarial modelling, and finance transformation initiatives is expected to be incurred worldwide.

The table below shows some differences in investments and programs for insurers in Asia to implement changes beyond accounting and compliance, but also to strengthen processes, actuarial modelling capabilities, and systems.

	Asian Operation
Business and Operation	• Fast growing. Scales of local businesses vary by countries. IFRS 17 implementation needs to be at a level of precision that takes into consideration future growth in business (i.e., relative materiality to the group) • Mostly country business units supported by group and/or regional offices
Regulations	• Evolving (e.g. C-ROSS in China, RBC 2 in Singapore, HK RBC currently being developed, etc.) • Multiple GAAPs and regulatory reporting requirements • Local statutory financial statements of business units in certain countries in Asia are publicly available • Implementation based on local materiality is required for the compliance of local IFRS 17 equivalent
Readiness for Implementation	• Some run on federated, legacy systems and spreadsheets • Do not necessarily have the infrastructure and process already streamlined because of Solvency II or other implementation • Do not currently in all instances and/or business units have the resources to deliver project

Asia is many times the growth engine of the overall insurance business. There is currently a lack of investment in finance transformation, but an increasing expectation from stakeholders for higher transparency and lower granularity of reports and analysis on performance of insurance and investment contracts, with or without IFRS 17.

Why Asia is not moving faster?



The clock has already started ticking. Given the scale and complexity of the changes required, the urgency to start the implementation has been the topic of conversation not only in Asia, but worldwide. While the Asian business is in the spotlight, why is IFRS 17 implementation not moving faster here?

One observation is that the head/group office of many insurers, which will determine the ultimate IFRS 17 requirements for group IFRS reporting, are not based in Asia. The decision on group reporting requirements and transition approach creates a dependency for the Asia implementation (i.e. Asia operations cannot decide on the scale of transformation needed particularly on fulfilling Finance Planning & Analysis ("FP&A") requirements and reconciliation for consistent market story). This imposes challenges on formulating a business case to justify expenses and management attention against other local business priorities.

On the other hand, given the variations and opportunities of the Asia operations, these attributes further lengthen the decision-making process of the group when deciding the group-wide IFRS 17 requirements (e.g. transition approach), which bring higher sensitivity and volatility to the financial performances of the Asia operations.

The inter-lock has generally slowed down the effort in Asia to get better prepared to implement the standard. Other challenges faced by insurers in Asia also include:

Business Priority	Talent Acquisition	System and Data
Finance and actuarial functions have much higher involvement in implementing digital and other transformational strategy. Finance and actuarial resources are already stretched with other inflight initiatives in place.	Lack of supply of talents with knowledge of Asia business and experience to drive major finance transformation such as Solvency II in Asia. Korea is just one example where all resources with relevant experience are "sold out".	Uncertainties on what system changes is required to provide proper control and efficient data acquisitions for reporting. Adoption of a "patched approach" in the past has created a back-log of system changes required to support IFRS 17.

The combined challenges of the requirement to inter-lock, competing business priorities, lack of available talent and under-invested infrastructure has made Asia implementation of IFRS 17 particularly challenging in the available time. However, we have observed that awareness and planning activities on IFRS 17 implementation have significantly increased over the past 3 months. Question is, what shall be done given the remaining time?

Where are we in Asia, in terms of the IFRS 17 implementation?

PwC has conducted a survey of some of the larger life insurers in Asia in mid-2017 to understand the status with reference to different stages of IFRS 17 implementation.

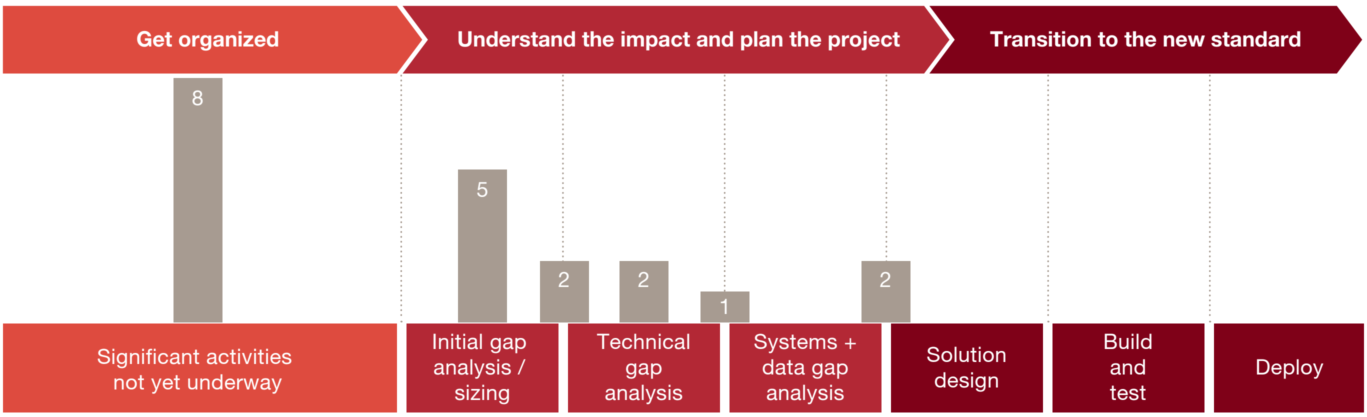


Figure: Distribution of the larger of life insurers in Asia in IFRS 17 implementation

	Observations
The Leaders	Large insurers with sizeable and growing business in Asia where IFRS 17 will be the group reporting standard and expected to be one of the primary bases of their market story; Initial budget is assigned to IFRS 17 implementation with some gap analysis performed; RFPs for advisory services on accounting, actuarial calculation, system implementation are issued.
The Majority	Significant number of insurers have started (or completed) assessment of the implication to the financials and operations by IFRS 17, with a usual starting point in some form of gap analysis.
The Laggards	Lagging for various reasons, (e.g. pending head/group office decisions and funding on IFRS 17 initiatives); IFRS 17 not being the primary performance indicators (e.g. US, Japan based companies). However, it is observed that many of the insurers in this category have a global finance transformation initiative in place for other purposes (e.g. cost reduction, fast closing, capital management, etc.).

What shall be done – Patch or transformative approach?

IFRS 17 brings a fundamental change in most insurer's accounting practices. For some insurers, it also introduces a more granular level of measurement, which requires a fundamental shift in the way data is collected, stored and analyzed, including the calculation of Contract Service Margin ("CSM"). It is not an uncommon discussion with insurers to focus on just developing calculation model (based on actuarial platform) to produce Best Estimate Liabilities ("BEL") and subsequently Risk Adjustment ("RA") and CSM and create a new manual IFRS 17 reporting process around it.

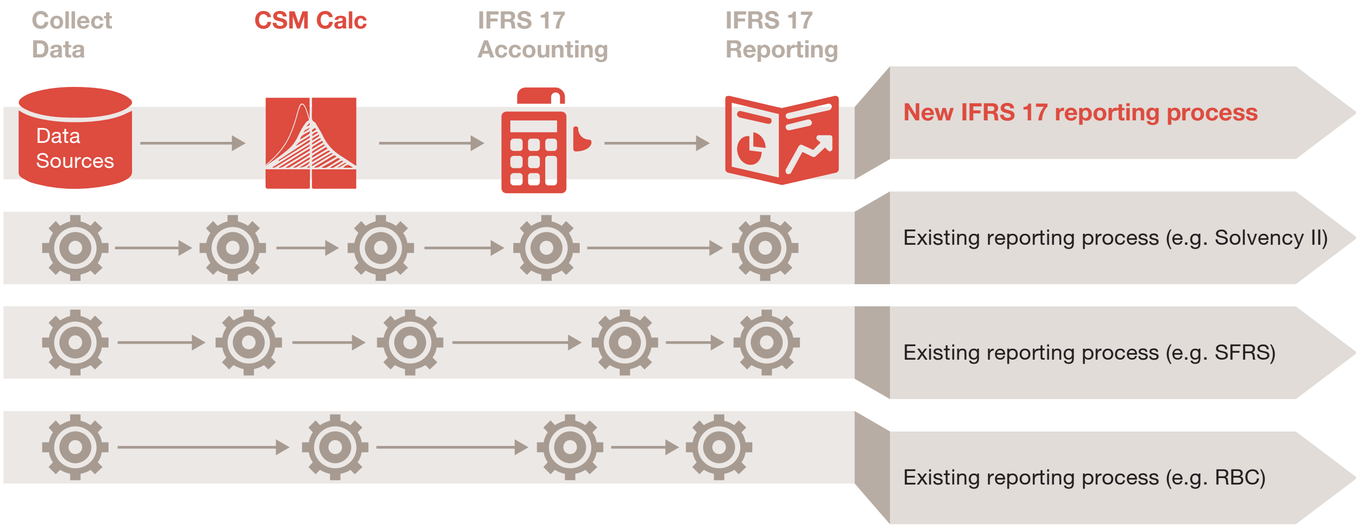


Illustration: A new, separate process to prepare financials based on IFRS 17 (i.e. the patching approach)

The "patching" approach has been widely adopted by insurers in Asia in the past in terms of system development, as it is often perceived as low cost and providing a quick fix. Given the significant and long-term changes that IFRS 17 introduces, additional controls and reconciliations are likely to be required between:

- Data acquisition and storage to ensure consistent data definition across data sources
- Actual-ised cash flow between actuarial models and general ledger/sub-ledger
- Policy choices and options to manage the profit and loss volatility, and the impact on the tax position (both on transition and ongoing tax profile)
- Transition approach, and decisions made around the CSM at transition will impact the profit emergence over subsequent years
- Reconciliation of market stories presented on different basis to manage market expectations before and after adoption. This is particular important as IFRS 17 reporting is expected to be more volatile compared to the current insurance standard and therefore requiring a more forward looking and predictive Finance function.

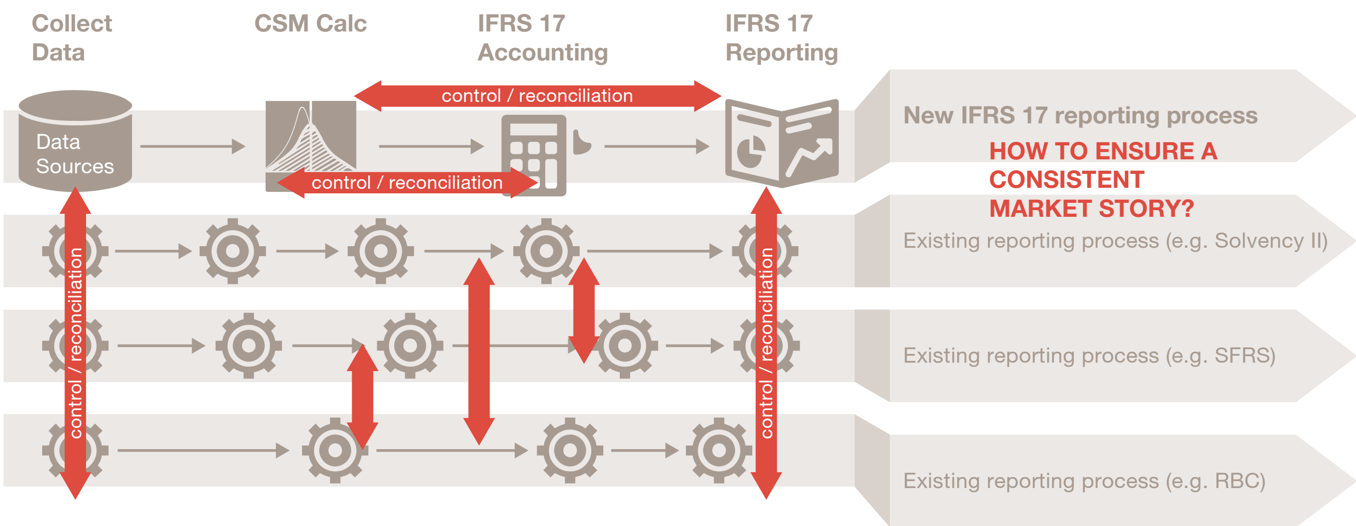


Illustration: Additional reconciliation points overlay with the new IFRS 17 reporting process

Over time, the layers of complexity and patches can become unmanageable, increase the total cost of reporting, and the risks will outweigh the short term low cost benefit.

Another drawback with a patched approach is that information to multiple stakeholders including management and investors may not be up to the expectations without significant rework or re-generation of the numbers to trace number back to calculation models and assumptions.

The evolving insurance regulatory framework in Asia (e.g Risk Based Capital regime in Singapore) will further increase the complexity and cost for future reporting if a patched approach is adopted.

An integrated finance transformation program with proper systems in place and infrastructure support will ultimately smoothen, if not speed up the reporting process and reduce the costs of financial reporting and analysis.

What are the "future proof" elements? How much will they cost?

With the aforementioned uncertainties, stepping back to look at a holistic view on how the insurers can reduce the long term risk and cost of implementing IFRS 17 and the time allowed for the implementation, we suggest to consider the following essential set of actions.

Considerations	"Future proof" essential set of actions
Data integration, storage and aggregation	• Explore options to supplement with more granular data to address the data requirements under IFRS 17
Actuarial models and risk applications	• Cash flow models which are in place will be recalibrated (if not redeveloped) according to the IFRS 17 requirements • A robust CSM calculation engine needs to be in place
Finance system	• Strengthen controls on accounting treatment/ posting logic in order to adopt additional requirements • Amend the Chart of Accounts ("CoA") for IFRS 17 and add new KPIs as needed • A new IFRS 17 ledger needs to be in place
Finance Planning & Analysis	• More granular details for analyzing and presenting business performance • A technical sub-ledger to share actuarial calculation assumptions and results in a finance presentable format, and to perform reconciliation

In addition to the talent acquisition and other challenges described in this paper, the largest line item on the IFRS 17 implementation budget will potentially be related to system implementation.

In most of our discussions, the implementation of the financial system infrastructure to support IFRS 17 is estimated to take around 12 to 18 months for a country business unit, and the time and cost will be driven mostly by the following elements:

- Complexity of the existing portfolio and number of inforce policies
- Gaps to reuse existing cash flow model for CSM calculation
- Granularity of data to support future FP&A requirements and reporting
- Number of reporting basis, ledgers and accounting rules
- Pre-existing data management infrastructure (e.g. policy data warehouse) that can be leveraged
- Existing resources that can be spared for the implementation (i.e. cost for back-fill)

While the implementation complexity and cost varies, we have developed an assessment matrix to assist our clients to plan and budget for the implementation, incorporating the "future-proof" essential set and consideration of major cost drivers.

Is there something plug-n-play ready to buy?

Unfortunately, we have yet to encounter an IFRS 17 solution in place where insurers can buy and install. There is currently no proven solution provider which can provide a complete end-to-end solution, nor a one-size-fits-all solution. There are 4 major trends in the solution vendor landscape that we observed:

1. Actuarial systems providers are extending their reach to include reporting and workflow
2. Traditional finance vendors are building insurance specific content into sub-ledgers and calculation engines
3. Several finance and actuarial vendors are collaborating to leverage each other's strengths
4. All vendors are making forays into the strategic enablement of their platform for example applying digital mobility, leveraging the cloud or utilizing information models

Leveraging our insurance experience on financial system implementations and vendor solutions; and a RFI on IFRS 17 vendor capability that we performed in early 2017, we have developed a perspective on the trends and comprehensiveness of the vendor solutions that may support the implementation of IFRS 17.

	Data Integration	Data Lake/ Large Dataset	Insurance Data Model	Capital/ Cash Flow Mgmt.	CSM Engine	Accounting Rules Engine	Technical Sub-Ledger	General Ledger/ COA	Consolidation & Disclosure	FP&A Support	Strategy	Context	What to do now
Act Later											Wait for Maturity	IFRS 17 specific components are being developed by multiple vendors. Not mature yet but likely become available given time	Assess target operating model options (e.g. process ownership, group vs local BU, etc.), determine close implications and overall solution architecture to "frame" the evaluation criteria of the components
											Identify Gaps and Optimise	Critical components that either exist in current infrastructure or tailored to the insurer. Unless major overhaul is planned, tweak / optimise existing setup are much cost effective	Reconfirm major financial system strategy and changes (e.g. revamp of GL system). Commence implementation planning to determine changes required, and critical path for implementation
											Do Not Wait and Start Early	Components less specific to IFRS 17, with mature vendor product and will be essential to support the future IFRS 17 reporting and finance transformation	Assess the existing capability and capacity to handle any extra work required for IFRS 17 transition and reporting; also the flexibility of existing infrastructure to support different reporting and analysis
Act Now											Act Now and Strategize	Components that are non IFRS 17 specific but essential. In-flight projects may be in place for other strategic initiatives (e.g. digitalization, customer centricity, etc.)	Perform implementation planning to assess the scope of work, timeline and data points to be covered in other in flight projects; Align with IT on standard toolsets and technologies

The above recommendation is derived from researching solutions from FIS, Milliman, WTW, SAP, Oracle, CCH Tagetik, Aptitude and SAS which either has significant presence in the Asia and/or actively participating in the IFRS 17 implementation discussions/RFPs.

A watch list of solutions and vendor, and a comprehensive research on solution functionality and comparison is developed for client sharing and discussions with PwC

What’s next?

To our targeted audience of this paper (i.e. IFRS 17/Financial Reporting subject owners and project leaders), we anticipate that the following are the up-coming, if not current, activities being undertaken.

Project Planning and Assumptions Validation	• Validation of key business and technical assumptions to understand the cost and time implication of implementing IFRS 17 • Training and resources gaps identification in Actuarial and Accounting functions to get the team up-to-speed on what is coming • Project planning and alignment, particularly with IT and other business priorities to make sure that procurement and system development effort/resources are lined up
Solution Evaluation and Proof-of-Concepts	• Business and solution architecture (e.g. CSM calculation and presentation in actuarial models vs accounting system) that determines future operating model • Assessment of financials to determine effort and approach for opening balance creation and other transition planning that requires management decisions • Buy vs. build evaluation of system components that need to be in place

Next in the series of our implementation insights Thought Leadership, we will discuss in details the vendor evaluation, implementation strategy, transition approach, auditor’s point-of-view and other considerations.

Where to go for further information?

Please contact us if you have any questions regarding this Thought Leadership, or if you would like to discuss specifics on IFRS 17 implementation.

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