



Society of Actuaries in Ireland

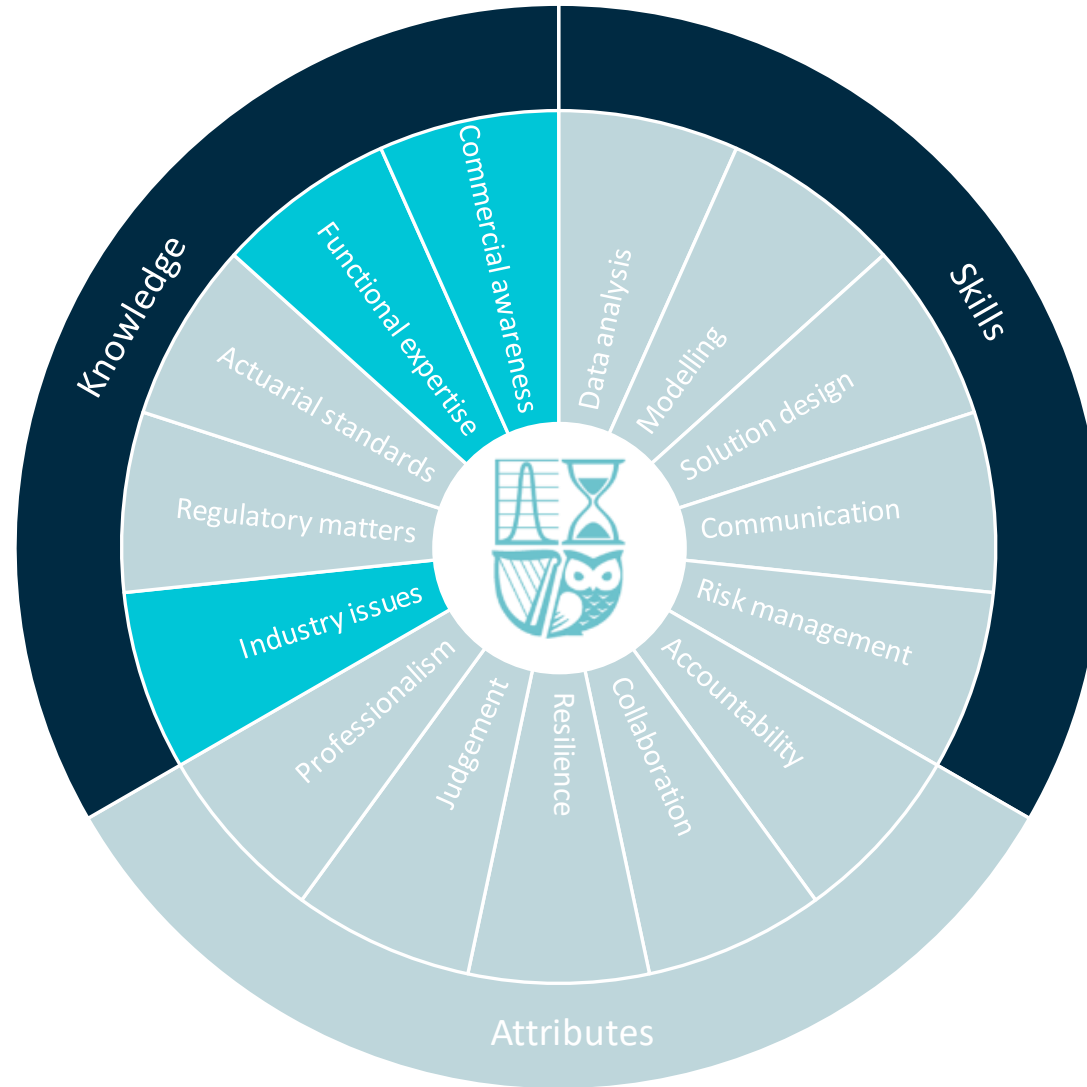
IFRS 17 transition balance sheet Issues and insights

September 2022

Disclaimer

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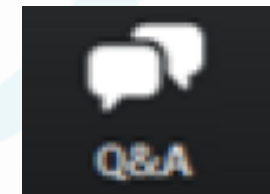
Competency Framework Wheel



Agenda

- Introduction
- Technical
- Other considerations
- Q&A – please submit questions as we go

Please use the Q&A function in Zoom



IFRS 17 working groups – current members

Life WG

Andrew Kay

Caroline Lynch

Ciara Fitzpatrick

David MacCurtain

Francis Furey

Frank O'Regan

Maaz Mushir

Miriam King

Niall Naughton (Chair)

Paraic Byrne

Non-life WG

Andy Smyth

Aoife O'Brien

Brian Walsh

Joanne Lonergan (Chair)

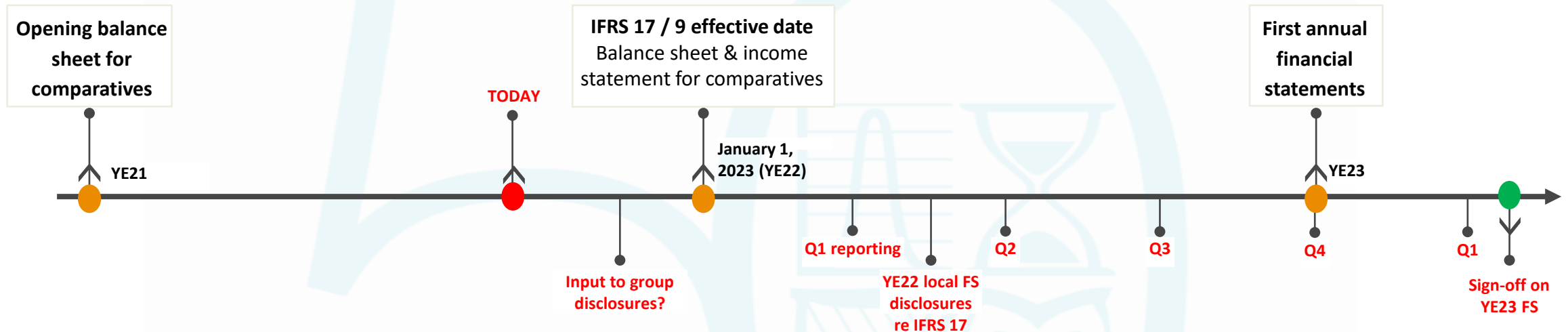
Working group activities

Event	Slides and podcast
Introduction	https://web.actuaries.ie/events/2018/10/introduction-ifrs17
GMM	https://web.actuaries.ie/events/2019/02/deeper-dive-ifrs17
VFA & PAA	https://web.actuaries.ie/events/2019/09/deeper-dive-ifrs-17-vfa-and-paa
Financial reporting emerging issues	https://web.actuaries.ie/events/2019/11/financial-reporting-emerging-issues
Reinsurance & transition	https://web.actuaries.ie/events/2020/02/webinar-deeper-dive-ifrs-17-reinsurance-and-transition
IFRS 17 Panel Discussion	https://web.actuaries.ie/events/2020/10/webinar-ifrs-17-panel-discussion
Presentation & disclosure; technology, systems & data	https://web.actuaries.ie/events/2021/06/webinar-deeper-dive-ifrs-17-presentation-disclosure-and-technology-systems-data
IFRS 17 member survey results	https://web.actuaries.ie/events/2021/11/webinar-ifrs-17-member-survey-results

Other

- SAI IFRS 17 webpage: <https://web.actuaries.ie/press-publications/ifrs-17-working-group>
 - Provides links to materials and publications

Timeline and recent developments



- IFRS IC:** On 15 June 2022, the IFRS Interpretations Committee (the IFRS IC) agreed to finalise the agenda decision related to the submission on transfer of insurance coverage under a group of annuity contracts. On the 13 September 2022 IFRS IC agreed to finalise the agenda decision in relation to multi-currency groups of insurance contracts. See:
 - <https://www.ifrs.org/projects/work-plan/profit-recognition-for-annuity-contracts-ifs-17/>
 - <https://www.ifrs.org/projects/work-plan/multi-currency-groups-of-insurance-contracts-ifs-17-and-ias-21/>
- EFRAG:** On 23 May EFRAG published its Final Letter on the IFRS Interpretations Committee's (IFRS IC's) Tentative Agenda Decision in the final phase of implementing IFRS 17 Insurance Contracts. See <https://www.efrag.org/News/Project-588/EFRAAGs-Final-Letter-on-the-IFRS-Interpretations-Committees-Tentative-Agenda-Decisions-in-the-final-phase-of-implementing-IFRS-17-Insurance-Contracts>
- ESMA:** In May ESMA issued the guidance on disclosures around IFRS 17, including in respect of 2022 interims and 2022 financial statements. See https://www.esma.europa.eu/sites/default/files/library/esma32-339-208_esma_public_statement_on_implementation_of_ifrs_17.pdf
- UKEB:** The UK Endorsement Board (UKEB) announced in May that it has approved the adoption of the IASB's IFRS 17 for use by UK companies. It is the first major standard adopted by the UKEB since the UKEB received delegated powers from the Business Secretary on 22 May 2021. See <https://www.endorsement-board.uk/endorsement-projects/ifrs-17>

Agenda detail

- Classification and level of aggregation (unit of account)
- Reinsurance
- Contract boundaries
- Expenses
- Discount rates
- PAA
- Models
- Transition approach
- Tax
- Risk adjustment
- Coverage units
- CSM
- Other considerations

Health warning: not exhaustive, example issues and insights only!

Our speakers

Frank O'Regan an Associate Director with Deloitte Ireland's Actuarial, Rewards & Analytics practice in Dublin. He has over 19 years' financial services experience and provides advice to insurers on a range of topics, including reserving, Solvency II and IFRS17.



David Mac Curtain has 20 years experience across a variety of (re)insurance areas and is an active member of the SAI. David leads Grant Thornton's Life Actuarial team in Dublin.



Paraic Byrne is Head of Actuarial Function at Monument Life Insurance in Dublin. He has over 15 years' experience working in reporting roles covering a wide array of lines of business and reporting bases.



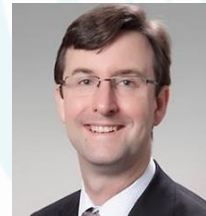
Andy Smyth is a Director with EY in Ireland, and has worked in consulting roles across Irish, Bermudan and London insurance markets. Andy leads the provision of Non-Life Actuarial Services to EY's Ireland-based clients, including international and domestic insurers & reinsurers.



Maaz Mushir is a self employed actuary who has significant experience in supporting IFRS 17 implementation for Life Companies. He is currently supporting Irish Life's IFRS 17 programme.



Francis Furey is a Principal Consultant with Finalyse where he leads out on the Finalyse Dublin practice. He is a subject matter expert in the areas of Financial Reporting (MCEV, IFRS17, US GAAP) and Prudential Regulation (Solvency II, BMA, ICS).



Andrew Kay is a Principal and Consulting Actuary in Milliman's Dublin office. He provides actuarial advice to insurers on range of topics including IFRS 17 and model validation, and is a member of Milliman's global IFRS 17 team.



Niall Naughton (Chair) is a Director and leads the life actuarial team in PwC Dublin. He has advised several clients on their IFRS 17 implementations. Niall is a member of the SAI life committee and chairs its Life Financial Reporting Working Group.

Classification & UoA

- “Grey area” products needing conclusive classifications
- Justification of distinct investment components/ contract combination
- Consideration of “significant insurance risk” transfer in scenarios where insurer is not at risk of making a loss.
- Differences to IFRS4 – reconsideration of approach:
 - Reclassification of insurance to investment products – contrary to prior IFRS4 classification
 - Removal of option to unbundle
- No longer paragraph re homogenous groups of small contracts
- IFRS17 “Portfolios” at transition
 - Fair Value transition – requirement for annual cohorts falls away
 - Profitability assessment conducted at transition.
- Operational challenges/ “hindsight” challenges on profitability assessment.

Reinsurance

- Management of allowance for future new business
 - Practical challenges of amendment of treaty dates to reporting quarters
- Onerous treaties now clearly identified
 - Management consideration of implication of new MI impact on metrics
 - Appropriate application/testing of Loss Recovery Component calculation in IFRS17 solution.
 - Consideration of % Loss Component or split of reinsured/non-reinsured cashflows for subsequent measurement.
 - Systematic and rational methods
- Impracticability challenge from auditors
 - Requirement to process extra historical reinsurance cashflow data

Contract Boundaries (1/2)

Judgmental

- Wide variety of considerations

Unit-linked: Difference vs SII

- Reasonably possible that longer CB than SII

Post-Contract Boundary Expense Approach

- Needs consideration; no alignment even for SII

Cashflows outside CB

- How capture – new group, or extend CB?

Insurance Acquisition Cashflows

- Asset if renewals post CB; test recoverability

Contract Boundaries (2/2)

Reinsurance BBNI

- CFs of anticipated new policies issued and ceded

PAA Eligibility

- Coverage period is important to PAA eligibility

SII EIOPA Guidelines

- Recent update (incl. unbundling & discernible effect on economics)

Practicalities

- Operational, KPI, etc

Expense assumptions & costs data (1/3)

Context

- Materiality - expenses have a significant PV quantum and are judgemental.
- Significant granularity required in expense assumptions e.g. by UoA.

Data granularity

- Therefore, significant granularity of cost data is required, with mapping to support assumptions needed, and robustness to support auditability.
- And in constructing retrospective view of costs/expenses, don't forget about manual reserves for expenses ...

Expense assumptions & costs data (2/3)

Attributability

- Substantial judgemental aspects exist in deciding on attributable versus non-attributable costs.

Projection

- For projection, the expense inflation assumption is important
- As is the projection method

Expense assumptions & costs data (3/3)

Risk Adjustment

- The risk adjustment methodology for expenses may commonly be an adaptation of SII (with justification of the final approach).

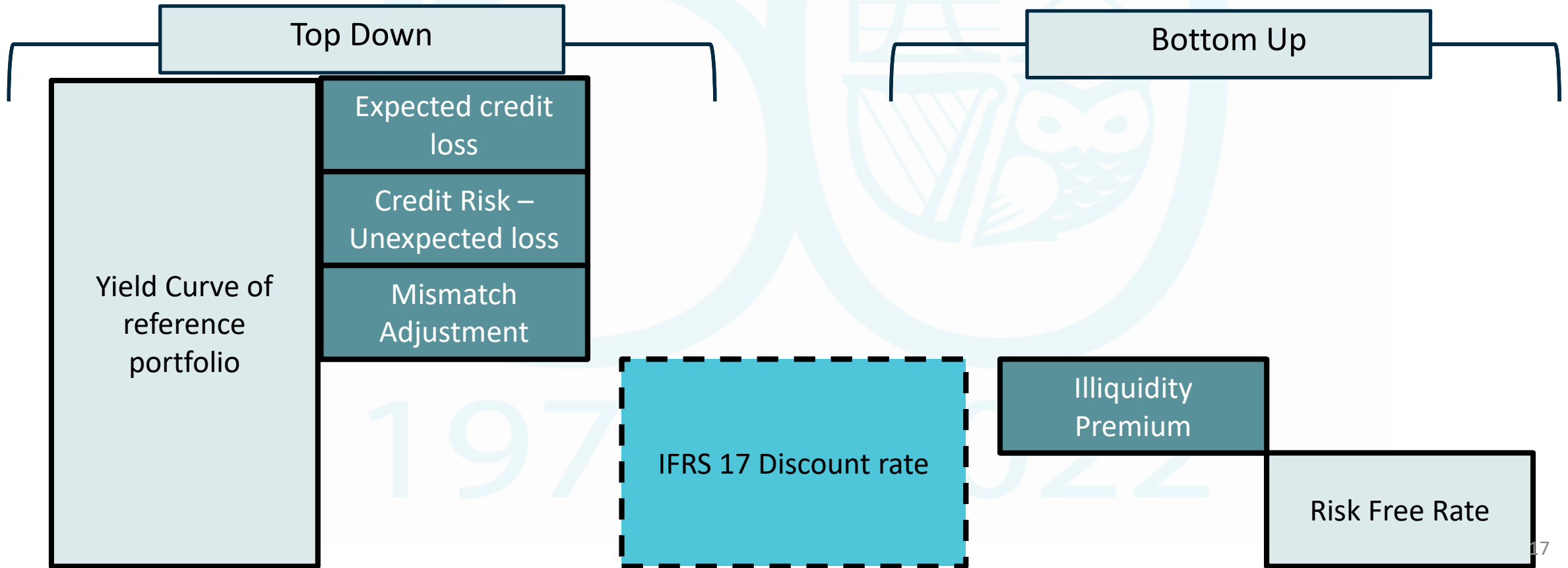
Other considerations

- Possible competing incentives in setting assumptions
- Whether higher costs arise due to operating in IFRS 17 environment

Discount Rates (1/3)

Standard requirements

- Reflect time value of money
- Consistent with observable market inputs
- Reflect characteristics of the liabilities



Discount Rates (2/3)

Bottom Up

- Choice of risk free curve not specified.
 - Government bonds?
 - Inter-bank swap rates?
- Adjustments to 'raw' curve
- Illiquidity premium: Must be appropriate to the liabilities

Top Down

- Yields on reference or actual portfolio of assets
- Flat rate Vs Curve
- Remove the components of credit risk
- Further adjustment for asset liability mismatches

Discount Rates (3/3)

Other Considerations

- Top Down != Bottom Up
- Impact on the Balance Sheet.
- Impact on emergence of Profit.
- Impact of volatility.

Premium Allocation Approach

Transition Approach

Relevant IFRS 17 Paragraph references: IFRS17 Para C3 to C5B

- Full Retrospective vs Modified Retrospective vs Fair Value
- SAI Survey in November 2021: FRA for 95% - 100% of the business
- Potential challenges: Onerous Contract testing, allocation of attributable acquisition expenses, risk adjustment

PAA Eligibility Assessment

Relevant IFRS 17 Paragraph references: IFRS17 Para C3 to C5B

- Relevant IFRS 17 Paragraph references: IFRS17 Para 53
- Methodology: comparison of PAA LfRC vs GMM LfRC
- Interpretation of “reasonably expects” and “not differ materially”. How are materiality thresholds defined?
- Frequency of reassessment: quantitative vs qualitative
- Assessment of coverage period and composition of the business
- Assumed vs Reinsurance

Premium Allocation Approach

Liability for Incurred Claims (how you get comfort)

Relevant IFRS 17 Paragraph references: IFRS17 Para 59 (b)

- Starting Point: IFRS4/Local GAAP reserves or Solvency II
- Any adjustments required to base IFRS4/Local GAAP reserves?
- “New” IFRS 17 assumptions
 1. Risk Adjustment assumption
 2. Claims handling assumption
 3. Discounting
- Other considerations:
 1. Definition of Actual vs Accruals
 2. Interest on Funds withheld
 3. Reinstatement Premiums
 4. Adverse Development Covers

Premium Allocation Approach

Liability for Remaining Coverage

Relevant IFRS 17 Paragraph references: IFRS17 Para 55

- IFRS 17 vs IFRS4/Local GAAP balances as a starting point – received vs receivable basis
- DAC: How should this be refined to meet IFRS 17 requirements:
 1. Classification of what is considered acquisition cost under IFRS17
 2. Expenses: amortisation of attributable expenses
- UPR and Premium receivables:
 1. Adjustment for premium related commissions, i.e. shift between DAC and UPR
 2. Reinstatement Premiums
- DAC Payable: DAC at Inception – DAC Paid – easily attainable balances?
- Loss Component
 1. OCT test for contracts as at Q4 2021
 2. Cashflow basis – earned vs paid. Basis for LRC risk adjustment.
 3. BBNI contracts
 4. Measure at IR and unwind vs remeasure at transition date

Measurement Models

Market practices in relation to PAA and VFA eligibility testing

- “Quantitative” vs “Qualitative” vs “No” assessments.

Performance of tests at date of initial recognition or date of transition.

- Requirements of the standard (IFRS 17.C9 and IFRS 17.C21).
- Factors influencing performance of assessments at date of initial recognition or date of transition.

Measurement Models

Different measurement models within same portfolios.

- Operational complexity.

Differences between group and local entity measurement.

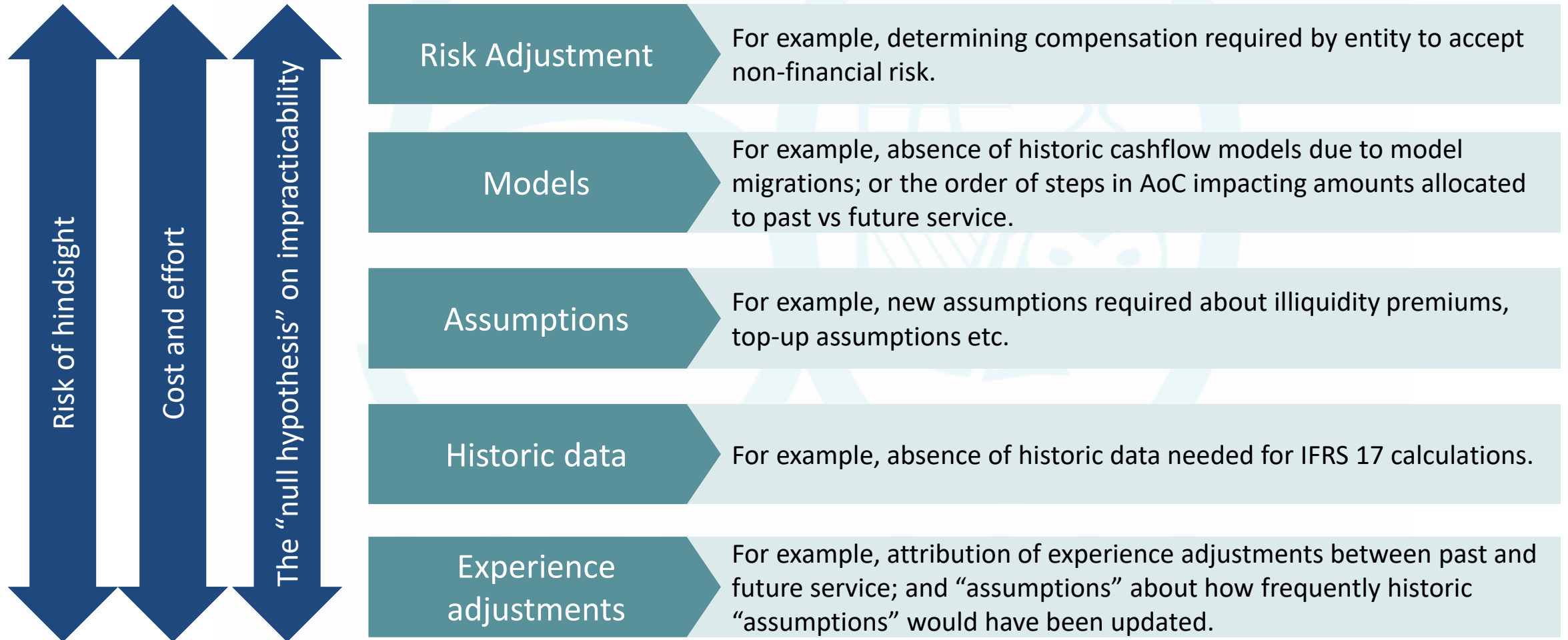
- Different dates of contract inception for Mergers and Acquisitions.
- Intra-group reinsurance
- With Profits considerations.

Transition approaches

- Factors influencing full retrospective approach vs modified retrospective vs fair value approach
 - Impacts on opening equity and CSM at transition;
 - Impacts on ROE;
 - Impacts on dividend paying capacity from interaction between cash emergence, IFRS profits and Solvency requirements;
 - Ability to unlock capital tied in “non-distributable” reserve (subject to conditions);
 - Operational considerations etc.....

And of course, what the standard has to say!

Transition approaches – causes of impracticability (illustrative)



Transition approaches – impracticability assessment

IAS 8.53

Hindsight should not be used when applying a new accounting policy to, or correcting amounts for, a prior period, either in making assumptions about what management's intentions would have been in a prior period or estimating the amounts recognised, measured or disclosed in a prior period. The fact that significant estimates are frequently required when amending comparative information presented for prior periods does not prevent reliable adjustment or correction of the comparative information.

IAS 8.5

.... For a particular prior period, it is impracticable to apply a change in an accounting policy retrospectively or to make a retrospective restatement to correct an error if... the retrospective application or retrospective restatement requires assumptions about what management's intent would have been in that period.

Transition approaches – other considerations

The further one goes back to apply the full retrospective approach, the greater the risk of producing accounting estimates that are of lesser quality due to use of hindsight involved in determining what accounting policy choices/methodologies would have been applied at the time insurance contracts were issued; or inaccurate, incomplete or inappropriate data used to calculate insurance contract liabilities.

The choice between full retrospective and modified retrospective can sometimes be a trade off between producing high quality accounting estimates and taking a very strict view on impracticability.



Transition approaches

- Factors influencing full retrospective approach vs modified retrospective vs fair value approach
 - Impacts on opening equity and CSM at transition;
 - Impacts on ROE;
 - Impacts on dividend paying capacity from interaction between cash emergence, IFRS profits and Solvency requirements;
 - Ability to unlock capital tied in “non-distributable” reserve (subject to conditions);
 - Operational considerations etc...

Taxation of opening equity restatements

- Deferral of tax liabilities over 5 years.
- Impact of loss in opening equity
 - Deferred Taxation;
 - Double taxation of same profits;
 - Impact of the “sunset clause” on taxes (N/A in Ireland).
- Implications on losses carried forward due to IAS 12 and question on what likely profits are

IFRS 9/17 Transition requirements

- Differences in IFRS 9/17 requirements for transition can lead to tax implications.
- Impact of December 2021 amendment to the IFRS 17 standard.

Solvency II considerations

- Knock on impacts of the IFRS 4 DTA/DTL for the SII DTA/DTL and LACDT.

Global developments

- Examples from UK, Canada, and Germany.
- Impact of BEPS 2.0 and the benefits of the OCI option.

Risk Adjustment

Intro

- The risk adjustment is the compensation that the entity requires for bearing the uncertainty about the amount and timing of the cash flows that arises from non-financial risk.

Areas of significant judgment and interpretation

- Approaches used for the calculation of the risk adjustment
- What is the target confidence level for the RA?
- How will you allocate RA to lower levels of granularity

Simplifications and approximations

- Are you determining your risk adjustment based on a one-year view vs. ultimate run-off?
- Will disclosures be a point estimate or a range?

Differences/alignment vs SII

- Comparison of risks covered: – IFRS17: only insurance, lapse and expense risk v SII - (all NH risks)
- Risk Margin versus Risk adjustment differences

Coverage Units (“CUs”)

- CU determines the proportion of the CSM to be released in the P&L for services provided in the period at a level of group of contracts. IFRS17 does not define quantity of benefits (and expected duration) – should reflect insurance benefits provided in each period.
- Examples of coverage units used
- IFRIC recent developments:
 - Quantity of the Benefits Provided under a Group of Annuity Contracts:
 - Services provided under Annuities contracts- also applicable to deferred annuities, income protection, pure endowments
- Areas of significant judgment and interpretation.
 - Possible methods for determining the quantity of benefits related to insurance coverage
 - Possible methods for weighting insurance contract services if there is more than one type of benefit
- Simplifications and approximations.
 - Reasonable proxies for determining the investment-return services provided under a group of insurance contracts
 - Reasonable proxies not allowed to determine coverage units

Intro

- The CSM represents the unearned profit under the group of contracts that relates to future service to be provided under the contracts. (IFRS 17 paragraph 38)

Areas of significant judgment and interpretation

- IFRIC tentative decision: Transfer of insurance coverage under a group of annuity contracts
- IFRIC tentative decision: Multi-currency groups of insurance contracts
- A key indicator for market deferred profit
- Potential volatility to P&L

Simplifications and approximations

- How will you account for the Bow Wave in VFA contracts

Other considerations

- Transition disclosures
- Role of “reporting actuary” post IFRS 17
- Wrap-up

Transition disclosures (1)

- Timing of first IFRS 17 disclosures
- **ESMA Statement** - Transparency on implementation of IFRS 17 (May 2022)
- ESMA highlights the need for companies to **provide relevant and comparable information in their 2022 financial statements** to enable users to assess the initial impact of IFRS 17, as required by IAS 8.
- Where the impact is expected to be significant, ESMA expects issuers to:
 - Provide information about the **significant policy choices** such as methods to calculate the **discount rate**, how the level of **aggregation** requirements will be applied;
 - **Disaggregate the expected impact** in a way that is useful to users of financial statements; and
 - **Explain the nature of the impacts** (on recognition, measurement and presentation)
- The full statement can be found here: www.esma.europa.eu

Transition disclosures (2)

- **Market updates**
 - Limited public disclosure so far. Expect listed groups to give investor guidance over the coming months.
 - Quantitative or Qualitative - will need to be audited
- **Other reporting considerations**
 - Information for Group reporting
 - Link with Solvency II
 - Will need to report your DTA in the balance sheet at Q1 2023
 - Also expecting an updated NST covering the P&L

Reporting Actuary?

- AAE discussion paper (2020) – proposed the role of Reporting Actuary for IFRS 17...responsible for **preparing and conducting the calculation of insurance liabilities for accounts purposes**
- ... prepare an **internal actuarial report** to the Board to support financial statements, covering at least the applied **methodology**, the **assumptions** used, the **data** used, identification of the **judgments** applied, the **results** including their **sensitivities** in relation to the valuation of insurance liabilities and any material **risks, uncertainties, limitations** and **recommendations**.
- **Actuarial standards and education**
 - ISAP 4 – non-binding model standard from the IAA
 - IAN 100 – educational note from the IAA
 - EAN - educational document from the AAE – builds on IAN 100
 - ASP PA 2 – General Actuarial Practice
- <https://web.actuaries.ie/other-guidance>

Possible topics include...

- Classification of contracts
- Unbundling
- Data
- Assumptions e.g. discount rate, expenses...
- Contract grouping / unit of account
- Profitability assessment
- Risk Adjustment
- Materiality
- Expert judgements / simplifications / limitations
- Sensitivities
- ...
- See SAI FRWG discussion paper for further information -
<https://web.actuaries.ie/events/2019/11/financial-reporting-emerging-issues>

- **Industry Readiness?**
 - Finalising Opening Balance Sheets
 - Board and Audit engagement
 - Working on Q1/Q2/Q3 reporting
 - IFRS 17 projections/budgets
 - Lots of work remaining e.g. systems, processes, governance
- **Next wave...**

Q&A

Please click on the **'Raise Hand'** icon
to ask a question aloud
and
wait to be unmuted

or

Use the **Q&A function** to ask a question

