IFRS 17 – CHALLENGES AND ZEB-SERVICE PROPOSAL

The implementation of IFRS 9 and IFRS 17 presents insurance companies with major challenges. The companies subject to IFRS are already working at full speed to structure the complex business and IT implementation requirements. The new IFRS 9 accounting standard which will generally come into force on January 1, 2018 already is going to introduce comprehensive new regulations for accounting financial instruments [1]. At the same time, IFRS 17 creates a standardized regulation for accounting insurance contracts for the first time. The publication of the final IFRS 17 accounting standards is expected in May 2017 [2]. The initial application is planned for key dates after December 31, 2020, whereas respective comparative figures have to be established already for the previous period in 2020 according to IFRS 17. The planned valuation methods pursuant to IFRS 17, such as the building block approach (BBA), the premium allocation approach (PAA) and the variable fee approach (VFA), represent a paradigm shift in the assessment of insurance contracts with the goal of increased comparability of annual financial statements and at the same time a more economic view on insurance contract regulations.

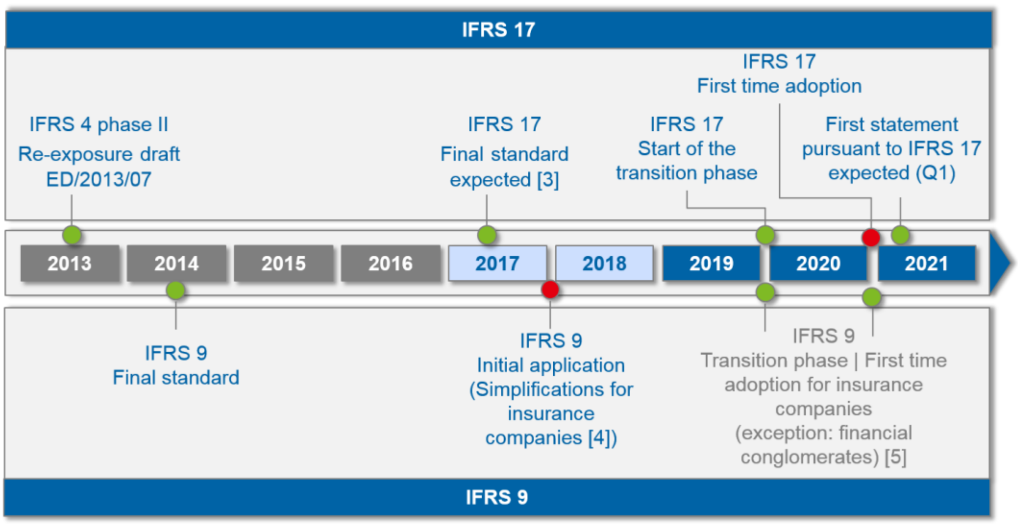

Figure 1: Overview of IFRS 9 and IFRS 17 schedule.

The implementation of IFRS 17 represents a major effort for the insurance industry that will tie up internal and external resources before initial application and beyond. An early examination of the requirements of the standards, the related challenges and the potential project risks is therefore highly sensible due to the tight implementation schedule.

Insurance companies will have to face the following main challenges during the implementation of IFRS 17:

- **New valuation models for identifying technical provisions.** The current exposure draft suggests three models for assessing technical provisions: the building block approach (BBA), the premium allocation approach (PAA) and the variable fee approach (VFA). Cash flow projections are required for applying these valuation models that have to be established and prepared by means of appropriate actuarial methods. A transfer of existing cash flow projections that have originally been set up for Solvency II is possible only to a limited extent due to different definitions of contract boundaries and required data granularities. In addition, yield curves have to be determined either following a bottom-up or top-down approach for an IFRS 17-compliant assessment. The existing risk model for identifying the risk margin has also to be reviewed with regard to compliance with IFRS 17. A transfer of Solvency II is not automatically possible.
- **Comprehensive reporting requirements (esp. for notes).** Insurance companies have to face increased reporting requirements for external regulatory reporting. Additional information has to be stated especially for the notes (the appendix), such as the composition of the technical provisions on the valuation key data, the development of the technical provisions in the reporting period, the selection of the valuation method, the assumptions and premises underneath the valuation model and estimations as well as the (scope of the) risks resulting from the insurance contracts.
- **Higher level of data granularity.** The future IFRS standard sets out different requirements for the granularity of the data involved. While cash flows projections and yield curves have to be provided on single contract level (or at least on an adequate sub-portfolio level), IFRS 17 focuses on a less granular portfolio level for the identification of contractual service margins. The standard setter did not however define the exact aggregation level. Thus, the IFRS-compliant and at the same time practicable structuring of the insurance business is essential for an efficient business/IT IFRS 17 target process (esp. within a fast close). Not least to prevent or mitigate comprehensive and elaborate adjustments to the previous systems by means of an intelligent structuring of the business.
- **New business and IT processes.** IFRS 17 entails fundamental changes for the cooperation between actuarial services, accounting and IT. At the same time, the area of scenario and analysis capability of results before posted in the main ledger assumes a new role in the annual financial statements process. These significantly increased requirements for data storage and processing necessitate a high level of automation of the processes.

As the leading management consultancy for financial services in Europe, zeb can provide comprehensive expertise in the implementation of regulatory requirements. In order to analyze the impact of the introduction of IFRS 17 on your company, zeb recommends the following approach within a first project stage and/or a pre-study of IFRS 17 as part of the IFRS 17 zeb.process model:

1.1 Common understanding of the major requirements and implications:	1.2 Deeper understanding of the requirements and implications:	2 Target IT architecture:	3 Project plan:
• Basics with respect to methods • Basics with respect to processes and structures (incl. simulation) • Differences between IFRS 17, local accounting and Solvency II • Notes	• Measurement methods: BBA, PAA, VFA, specifics for reinsurance (incl. data requirements) • Use Cases • Booking logic and posting records • Planning (over planning period comprising several years)	• Functional/technical architecture (as is) • Identification of necessary changes in the application environment • zeb reference model and functional modules • Developing rough functional/technical target IT architecture (alternatives)	• Developing a project plan: Main working packages, activities and responsibilities • Transition • Documenting specific requirements and open questions identified during the pre-study • Documenting all results from the pre-study

Figure 2: Main contents of a first project stage (IFRS 17 pre-study).

The first step is to develop a common understanding of the main requirements of the IFRS 17 standard and the challenges related with its implementation. Both the valuation models as well as the underlying zeb interpretations of an IFRS 17-compliant valuation and posting logic are presented, process requirements are discussed and the differences with existing accounting methods are revealed. The requirements and challenges are not only presented in theory but explained by means of practical zeb.use cases. Consequences, e.g. due to changed assumptions of IFRS 17 valuation models, can be directly understood and analyzed. A reference model developed by zeb identifies missing functionalities of the existing system landscape in a second step in order to elaborate an IT target architecture for your company that is compliant with the IFRS 17 requirements. Based on the findings of the upstream steps, an overall IFRS 17 implementation plan is set up in a third step which pools the identified task packages, reveals necessary resources and defines the schedule and respective responsibilities.

Benefit from our offer of a comprehensive range of services from “one hand”: we provide all aspects from an integrative business perspective and process support to the technical implementation. Solving your IFRS 17 issues with support from thought to action – that is what the team of zeb can offer you.

[1] The IASB allows insurance companies a prolonged implementation phase of IFRS 9 by the entry into force of IFRS 17 in order to prevent an accounting mismatch by the shifted entry into force of IFRS 9 and IFRS 17.

[2] See IASB homepage (http://www.ifrs.org/Current-Projects/IASB-Projects/Pages/IASB-Work-Plan.aspx).

[3] Acc. to IASB homepage (www.ifrs.org; April 2017).

[4] Acc. to IFRS 17 publication "Applying IFRS 9, Financial Instruments with IFRS 4, Insurance Contracts" (September 12, 2016).

[5] If deferral approach is applied.

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