WHITE PAPER

# Insurers: Are You Ready for IFRS 17?

The January 2022 compliance deadline seems a long way out, but savvy insurers are acting now. Find out why, and the top 10 things to look for in an IFRS 17 solution.

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# Introduction

For many insurers, this accounting process will look familiar:

- Tools and processes vary for different lines of business.
- The needed data is stored in hundreds of files.
- Calculations are performed by multiple, undocumented spreadsheets, with little or no version control.
- Humans have to step in to help cobble together data from different channels.
- The process of preparing and presenting financial data is not manageable or traceable.
- The path from input data to P&L numbers is largely a black box.

In a simpler time, this patchwork was passable. But change is coming. New regulations will bring greater complexity to the accounting process for insurers, which will make semi-manual, legacy processes look like a house of cards and raise doubts about the validity of the final numbers on the P&L sheet.

That looming change, of course, is IFRS 17, the new International Financial Reporting Standard issued by the International Accounting Standards Board (IASB) in May 2017. It defines how accounting will be done by insurers in the more than 100 countries that adopted IFRS. IFRS 17 will replace IFRS 4 Phase II, which isn't a comprehensive international standard but rather a structure for grandfathering in the use of countries' national standards.

"If you look around the world, we see the use of myriad national standards, which are highly divergent and often a bit antiquated, so the quality of the information is often substandard and certainly not comparable," IASB Chairman Hans Hoogervorst told Accounting Today. "… The current practice is highly divergent and not of sufficient quality, so it was high time that we produced this standard."[1]

IFRS 17 will usher in a new era that puts insurers on a level footing internationally. For starters, the new standard:

- Defines clear and consistent rules that will increase the comparability of financial statements.
- Introduces new approaches for the valuation of insurance liabilities.
- Requires insurers to report on their business performance at a far more granular level.
- Brings new requirements concerning calculation and disclosure of financial measures.
- Requires calculation of some completely new measures.
- Limits the ability to offset onerous contracts against profitable ones.

This greater transparency will give analysts and investors more insight into a company's financial health than ever before. For most insurers, the transition to IFRS 17 will have a visible impact on financial statements and key performance indicators – and not in a good way.

1 Michael Cohn, "IASB releases insurance contracts standard," Accounting Today, May 17, 2017, https://www.accountingtoday.com/news/iasb-releases-insurance-contracts-standard

# Is Your Organization Ready for IFRS 17?

The final technical specifications were just released in May 2017, and the compliance deadline is now scheduled to be effective by January 2022. That sounds like a long time to get ready, but it really isn't. Savvy insurers are already acting, for several reasons.

- IFRS 17 will mean substantial changes for IT, finance, accounting and actuarial departments, primarily due to the demand for more detailed data and more frequent actuarial system runs. This kind of change management takes time.
- The P&L statement under IFRS 17 will be different from the current one and the Solvency II one. The significant differences between these logics will require new steps for data analysis and reconciliation.
- Since insurers need to get used to running the business according to new metrics and KPIs, a transition period – a parallel run of old and new accounting methods for one to two years – is recommended.
- Although the "go live" effective date is not until 2022, insurers will be expected to present comparative results in 2021. Since these results will be based on 2019 data, most of the implementation should already be done by that time.
- Even companies that are not required to adopt IFRS 17 standards might choose to do so, so they can present comparable information about their business and financial position – a growing expectation from investors.

The impact of IFRS 17 on finance and actuarial processes will depend on several factors, such as the current reporting basis, the complexity and maturity of the business, and whether it depends on a collection of legacy systems or has recently undergone a major finance IT transformation. For international insurance organizations that are accounting under generally accepted accounting principles (GAAP) – as is the case in the United States – the situation will be even more complicated because GAAP is a set of rules, conventions and procedures while the IFRS are principles based. A US-headquartered insurance group with business in IFRS countries, will need to support both these international standards in parallel. While efforts continue to bring together these two standards the differences mean that a coordinated application of both GAAP-related and IFRS-related standards will impact international insurers now and in the coming years, including the implementation of CECL in the US.

Whatever the organization's current readiness, it's not too early to consider how it will:

- Manage the increased granularity and complexity around accounting of insurance contracts.
- Deliver monthly run, consolidation and reporting with far more data in compressed time frames.
- Prepare, test, document and manage the underlying models that support the calculations.
- Provide rigor, governance and transparency for every step of the process.

The IFRS 17 accounting standard is designed to provide more transparent, comparable reporting on how insurance contracts affect an entity's financial performance and risk exposure, and how it earns profits or incurs losses through underwriting services and investing customer premiums.

Among Insurers getting a head start is global property/casualty and health/life reinsurer Gen Re, headquartered in Stamford, Conn. Gen Re is using SAS to create a comprehensive platform that covers all IFRS 17 requirements. "We were looking for a platform that we believed could help us comply with IFRS 17 but also which could potentially provide leverage for future global efficiencies," said Edward Nosenzo, North America Chief Financial Officer at Gen Re.

# Challenges in the Transition

As insurers move forward to prepare for January 2022 (original effective date of Jan 2021 was recommended to be changed by IASB in Nov 2019), they face challenges from several corners:

## Disparate systems and processes

One of the biggest challenges is that current accounting systems and actuarial tools are designed with traditional compliance in mind. They were created in isolation and have little or no integration capability. This threatens to cause significant problems as insurance companies seek to understand the full impact of the new standard.

In addition, many of these system integration points still rely on manual processes. This makes it difficult to scale and add the necessary layers of automation needed to deliver the speed, accuracy and visibility demanded by IFRS 17.

## Functional silos

Since many measures in new disclosure reports will be calculated based on comparing expected and actual cash flows, IFRS 17 calls for greater cohesion among diverse players in the process, such as:

- IT, which is responsible for uploading the data and checking data quality.
- Actuaries, who are responsible for IFRS 17 calculations and, in cooperation with accounting, for postings. There might also be cases where thematic actuaries will be responsible for some parts of business and a chief actuary will approve the overall values.
- Accountants, who are responsible for preparing the data set for the general ledger and, in cooperation with actuaries, for postings. There may also be an additional step of approval by a chief financial officer or comparable person.

What's needed is a common platform that provides common ground for these roles, and provides consistent data, processing and reporting for both financial and risk reporting.

## Overlapping compliance initiatives

For many companies, meeting IFRS 17 requirements by 2022 will overlap with Solvency II compliance efforts and make things even more difficult. Implementation synergies would minimize rework and costs. These companies need an information foundation that can support both compliance efforts and will be flexible and scalable to support similar, future regulations.

## Limited solution functionality

Most IFRS 17 solution vendors only support part of the compliance process. Insurers then must make heavy investments in acquiring and integrating multiple solutions. The resulting architecture is not well structured or easily traceable. Instead, insurers need a centrally managed solution that integrates all the stages of the compliance process, from data collection and management to calculations and allocations to reporting and governance.

Solvency II brought different functions – such as actuary, finance and accountancy – closer together, but IFRS 17 makes this integration even more important than before. Under the new regulations, most profit and loss comes from the actuary rather than from accountants, and this represents a significant change. Accountants will pull financial statements together, but it is the actuaries who will be playing a much more significant role in getting the numbers prepared.

## Processing bottlenecks

IFRS 17 involves a lot of new calculations, many to be performed on contract level of detail. Unless they have recently upgraded their data processing capabilities, insurance companies with large portfolios will struggle with data performance issues. Meeting the time windows for monthly runs will be a huge challenge. Insurers need the means to calculate all measures and analyze the results at the required detail with near-real-time speed.

## Process gaps

IFRS 17 adds new steps and interactions that will add complexity and require process changes and a better way to manage information flow among systems. An organization's actuarial and accounting functions will have to be fully integrated, with automated processes among them as illustrated in Figure 1.

Existing tools and systems will almost certainly lack the necessary flexibility to support the new standard without additional investment. Insurers will need to assess whether the IT infrastructure can meet the new requirements. There may be a temptation to respond by making a full-scale "rip and replace" of existing accounting systems and actuarial tools. However, this could be a costly mistake if the systems in place still provide significant operational effectiveness.

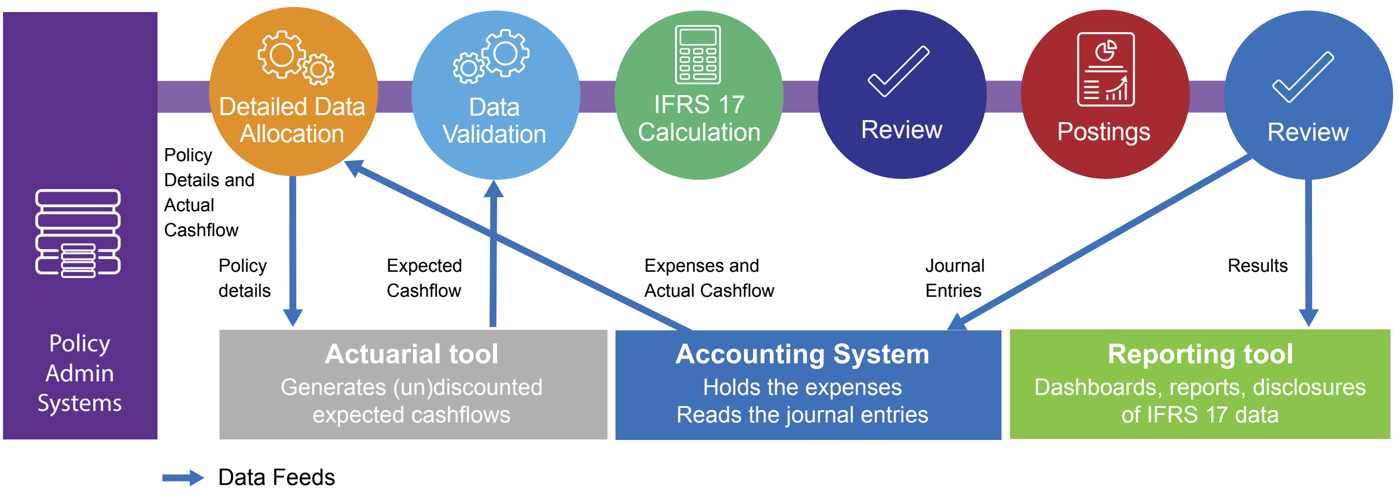


Figure 1: IFRS 17 high-level process

## Complex change management

The insurance market will need time to get used to the new measures and operate based on them. The sooner the IFRS 17-based numbers are available the better, but implementation will be a big undertaking. Insurers need a road map that defines the final architecture/process but gets there in incremental stages – adding data, quality rules and processes, models, validation and reconciliation rules, reports and more over time in a structured way.

Since IFRS 17 is based on principles rather than strict technical specifications, insurers might make various attempts to determine the best implementation for their lines of business, regions, etc. – which are subject to change in the future.

# Ten Things to Look for in an IFRS 17 Infrastructure

Some insurers are starting the march toward compliance by talking to advisory consultants. That's a great start, but these assessments typically focus on the business questions. "How will this new standard affect our financial results? How do we interpret IFRS 17 in the context of new business? If we are not mandated to adopt IFRS 17, should we migrate or continue with our present accounting practices?"

Before going too far down this path, organizations should also be assessing the technical aspects – the IT infrastructure and orchestration of data, systems and processes. "What data will we need that we don't have today? What changes will be required in our accounting and risk management architectures? Do we have the processing horsepower to meet reporting deadlines with much higher data volumes? What's the best to move forward?"

In answer to the last question, here's a quick view of the top 10 capabilities or attributes you should expect for your IFRS 17 information architecture.

## 1. A single, unified platform

Many solutions cover only part of the picture. Vendors of pure accounting solutions focus on preparing the structure of accounts, on the booking itself and on some reporting functionalities. Vendors of actuarial tools focus on valuation methodologies and some advanced model calculations. Technology-oriented vendors focus on data warehouses and support for reporting.

Few vendors support the end-to-end process and also provide the business logic. With one integrated, centrally managed, traceable platform, you could run the entire process for IFRS 17 – from source data to reporting – ensuring that all contributors and users are working in a consistent and well-managed framework.

## 2. Consistent data

A common platform helps ensure consistency of the data presented in new financial and risk reports and eases collaboration between actuaries and finance. However, in most cases, solution vendors focus either on capabilities related to risk or on capabilities related to finance – not both.

That separation makes sense to a degree, because there are differences. The scope of data required can be different, calculations follow different algorithms, the processes have unique steps, and reports present different measures. However, there is a broad common area of data, calculations and measures that should be reconciled. Furthermore, IFRS 17 brings risk elements into calculations and disclosure, so consistency between finance and risk is a must-have.

A single platform for risk and finance calculations and reporting ensures consistency in common data, enables comparability of data, and eases reconciliation of results. The result is closer collaboration among actuaries, risk managers and accounting staff around reporting of expected and actual cash flows and metrics.

## 3. High-performance processing

Most calculation tools available today will have severe performance issues when pressed to generate cash flows and perform calculations at the level of detail required by IFRS 17 – a real concern for making reporting deadlines. It's important to have a solution that can accelerate any of these calculations. For example, a high-performance processing engine could:

- Distribute a pool of active processing sessions among cores/servers for parallel processing.
- Automatically determine task dependencies and assign processing tasks to active sessions to run.
- Optimize assignment of processing tasks to sessions closer to where the data resides for efficiency.
- Find a previously calculated result (rather than repeat a computation) if the inputs have not changed.

Intelligent data processing capabilities on distributed computing platforms can dramatically reduce time to run the numbers. However, insurers might want to retain their existing actuarial engines as long as possible, provided they can seamlessly integrate those third-party technologies into the IFRS 17 reporting process.

Parallel execution and in-memory processing can accelerate required processes and calculations by orders of magnitude.

## 4. Traceability and auditability

Runaway spreadsheets and undocumented processes will soon become obsolete. IFRS 17 requires end-to-end accounting processes to be fully transparent and auditable for every controller.

When evaluating solutions, look for the ability to define processes as a flow of logical, documented steps. For example, a process could define specific pieces of calculations, detailing the roles involved, data sets used as inputs and the process outputs. Every step should be automatically documented as it occurs. The solution should store information about versions of each process, model and instance run. All manual changes to the data (configuration or results) should be stored along with related comments and attachments. This kind of governance ensures that processes are consistent, supportable and repeatable.

## 5. What-if capabilities

Look for the ability to define and run a process based on several different configurations, each representing a different set of assumptions. Users can verify how changing the assumptions (or scenarios) would influence the stated financial condition of the company.

This is critical for determining which final numbers to put into the P&L statement. If you haven't calculated different scenarios, you won't have alternatives from which to choose when defining the final numbers.

During the initial implementation, asking "what if" will also be useful to see what the final numbers on your portfolios will look like and to verify whether those numbers really are the right ones or what needs to be changed to get the correct numbers in the final financial reports. What-if capabilities are essential from the outset for refining models, identifying data issues and arriving at the most meaningful results.

## 6. Out-of-the-box structure with outside-the-box flexibility

Jump-start your implementation with a solution that offers prebuilt rules, models and templates with embedded business logic, such as:

- Dedicated configuration data.
- Models for the GMM – General Measurement Model (a.k.a. BBA – Building Block Approach), premium allocation approach (PAA), variable fee approach (VFA) and more.
- Predefined rule sets for validation, posting and reconciliation.
- Predefined report sets for IFRS 17 calculations and disclosure.

Then look outside the box for the flexibility to refine and customize. For example, an insurer may want to define custom sets of rules to assign/allocate the results of calculations to elements in the Structure of Accounts to be disclosed in the final reports. The rules may be different for different reporting periods – if the Structure of Accounts or the approach to it changes over time – or for entities in a different geography or type of business. Look for a solution that offers this level of flexibility.

## 7. Data quality and process quality management

The quality of data used for calculations and financial reporting is critical, whether it's input data or the intermediate results of calculations. Start with an insurance-specific data model that can load all the data required for IFRS 17. Beyond that, look for a solution that is both flexible and automated, one that:

- Enables users to define the data packages and data quality rules for various steps of the process.
- Monitors the delivery, completeness and quality of this data.
- Automatically triggers data quality and reconciliation rules at required states of the process.
- Can feed policy data into a wide variety of actuarial and reinsurance systems.

## 8. Advanced reporting with drill-down capabilities

In the early stages of operating under IFRS 17, everybody will have to get used to the new metrics and understand the reason (source) behind individual values. So, from the start it is important to have a set of properly designed, maximally informative reports.

This process is greatly simplified by starting with predefined financial reports that can be customized, and providing an interactive interface where users can drill down to the details and the source data used for calculating the final values. And of course, you'll want support for Microsoft Excel as well as web-based reports.

## 9. Incremental implementation

Transitioning from legacy GAAP accounting to IFRS 17 is a major undertaking. Insurers can reduce transition struggles and risk by evolving in phases. For instance, a company could start by upgrading less mature processes and models, and then move on to more advanced processes and target models that apply to the whole portfolio.

> "What-if" analysis – the ability to run different scenarios based on different assumptions – is a powerful tool for mitigating the higher volatility expected in P&L statements under IFRS 17.

Here's how this might look: The solution enables the insurer to define a template of the end-to-end process, then run calculations as instances of this template. You could start with a simpler process where just certain steps are implemented, such as basic validation rules, initial models created in Microsoft Excel or external tools, and preliminary versions of reports. Step by step, these basics are replaced with more mature versions. Look for a solution that supports this kind of incremental adoption.

### Validate before you leap

Validate the chosen implementation approach by performing a comprehensive proof-of-value exercise that assesses the process from end to end:

- Analyze input data.
- Test calculations and post entries.
- Evaluate downstream data.
- Measure data processing performance.
- Assess the hand-offs among functions and people involved.
- Ensure that the process is transparent and auditable.

### 10. Adaptable, extendable architecture

Like Solvency II, nobody expects IFRS 17 to be static. All regulations evolve and change. Businesses evolve and change. Look for an expandable and resilient infrastructure that will adapt to these realities. A flexible data and analytics architecture can resolve issues throughout the business while paving the way to add future functionality in a modular way.

## Synergies Between Solvency II and IFRS 17

Many insurers affected by IFRS 17 also have to comply with the 2009 Solvency II Directive, which went live on Jan. 1, 2016, and concerns the amount of capital European Union (EU) insurance companies must hold to reduce the risk of insolvency.

Although IFRS and Solvency II differ in the details (such as identification of contracts, level and approach to calculations, reported measures, responsibilities), the basic requirements regarding data, structures, auditability and traceability of processes and supporting systems are very similar. Both regulations call for a comprehensive approach using an integrated framework.

Many insurers have made significant investments to comply with Solvency II. These new systems and processes may need only little additional development to meet the requirements of IFRS 17. Considering Solvency II and IFRS 17 implementations jointly offers several benefits:

- Opportunities for wider transformation. Meeting Solvency II and IFRS 17 requires substantial change in the external reporting environment – a prime opportunity for insurers to transform the broader suite of management information across actuarial and finance functions. The business gains greater decision-making agility and responsiveness to opportunities and threats.

IFRS 17 brings new approaches for valuing insurance contracts and new metrics that describe company performance of the company – both changing the way reporting is done and how insurers will be evaluated.

Implement gradually – start with a less mature process and model set, and evolve to an advanced process and model set that applies to the whole portfolio of insurance liabilities.

- More effectiveness, lower cost. Implementing Solvency II and IFRS 17 in a coordinated fashion minimizes the amount of reworking on data, systems and processes. The joint approach reduces operating costs for data management and modeling, and makes actuarial and finance functions more effective.
- Smoother implementation. Both Solvency II and IFRS 17 call for a framework that supports both financial reporting and enterprise risk management in a sustainable way. The higher the level of integration between the two, the more effective (and cost-effective) each will be.

The last thing insurers need is to have to build an entirely new system from scratch, or build a solution based on a ledger that might not even exist when 2022 arrives. Select a technology platform that has the flexibility to support late-breaking process changes without disrupting what is being developed or already in place.

# If You Only Remember Three Things

## Think holistically

There are significant business benefits from choosing a unified platform that supports all IFRS 17 requirements. A single platform for risk and finance analytics and reporting ensures consistency in common data, enables comparability of data, and eases reconciliation of results. At the same time, it fosters closer collaboration among actuaries, risk managers and accounting staff.

Similarly, thinking about Solvency II and IFRS 17 in harmony can make both implementations more efficient and reduce redundant effort and operating costs, while opening up opportunities for broader transformation of information systems for the betterment of the business.

## Think layered, modular

A layered architecture provides a common foundation for multiple business functions. Modularity provides clear, logical delineation of functions and enables phased implementation.

The SAS solution for IFRS 17 is based on the SAS Infrastructure for Risk Management technical platform, which is also the foundation for other content packages, such as SAS offerings for firmwide risk for Solvency II, market risk management, underwriting risk management, stress testing, expected credit loss for IFRS 9 and others.

The IFRS 17 package itself is made up of discrete functional modules with embedded logic for data management, calculations, managing business rules and flows, reporting and process governance.

## Plan on being IFRS 17-ready well before 2022

IFRS 17 will mean substantial changes for finance and actuarial departments and their IT architectures. This implementation will take time and is best handled in increments.

Forward-thinking insurers will plan to complete their implementation projects long before 2022 to have enough time for extensive comparisons and testing before the compliance deadline. This testing period may entail parallel runs for one to two years to enable the insurer to adapt to new processes and to running the business by new IFRS 17 metrics.

## Start now to prepare for 2022

The primary objective of IFRS 17 is to provide more comparability of financial reports and insight into the reasons of change reflected in them. IFRS 17 implementation means making a long-term investment in a system that will be used for the next 10-15 years. It introduces new valuation approaches for insurance contracts and substantial changes in basic financial reports. Supporting this process requires new actuarial calculations, a new structure of accounts and key performance indicators that accounting and reporting systems must adapt to manage.

But the final impact will be much broader than that. IFRS 17 will have a significant impact on financial performance, operational processes, and data, requiring an integrated approach, based on an open and scalable platform. This should be designed to be able to manage both today's and possible future requirements of IFRS 17 and more. It's not too early to start moving toward this future.

# Learn More

SAS risk and finance solutions are used by more than 1,400 institutions worldwide. Learn more about IFRS 17 software at sas.com/IFRS17.

The SAS® solution for Solvency II is based on the very same analytical platform as the solution for IFRS 17. Functional modules and business logic sit on this common platform. This separation of platform from content modules means an insurer only must invest in the analytical platform once, then adds business components for Solvency II and for IFRS 17 on top of that platform.

To contact your local SAS office, please visit: sas.com/offices