UNLOCKING IFRS 17

What do insurers need to think about now that IFRS 17 is effective?

IFRS 17 *Insurance Contracts* came into effect for reporting periods beginning on or after 1 January 2023. From our observations of the market, many have found the implementation challenging and information used to comply with the standard is not yet driving insurers' business decisions. In this paper we outline some key governance areas for IFRS 17, the impact on Key Performance Indicators (KPIs) and explore how insurers can set themselves up for future success.

IFRS 17 governance

To help think about the governance of IFRS 17 we have developed three areas of consideration – the three Rs:

Resources – IFRS 17 implementation has a significant impact on resourcing at a time when there is already an existing talent shortage. It's important for insurers to consider how they can address staffing needs and retain good people who understand the area, particularly if they are in contract roles. This will ensure that insurers can complete their implementation phase successfully and avoid passing the project to business-as-usual (BAU) in a mess.

Recalibration – there are many decisions that do affect the results under IFRS 17. The standard doesn't have an over-arching principle like IFRS 4 and there often isn't one single right answer. Think carefully about the right level of information and details to include. Sense check the initial results when they start emerging – what feels right and how do I communicate these new results? At this point there may be a need to recalibrate some of the decisions that can make it easier to operationalise processes and explain the results.

Remediation – while we are all sprinting to the finish line, it's also important to think about what happens after implementation particularly when the risks have surfaced and manual work-arounds continue to be relied upon by management. This is when you might want to think about what tweaks you can make to your finance and actuarial processes to avoid lengthy and risky month-end close timelines. We have heard of large insurers in Asia shifting from a month-end reporting schedule from T+5 days to T+22 days, which is clearly not sustainable and will need significant remediation to simplify and automate processes.

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JUNE 2023

What is the impact of IFRS 17 on KPIs?

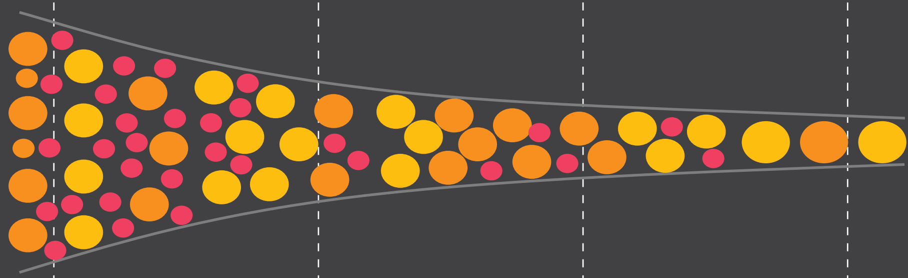
While IFRS 17 changes the timing of reported profit, it does not affect the underlying cash flow or expected dividend stream for insurers. However, what gets reported will have to be managed. Therefore it is useful to understand how IFRS 17 could affect commonly used KPIs within insurers.

The KPIs for insurers can be grouped into four main categories – business growth, profitability, value creation and distributable profit. Below we outline the main KPIs indicated by global insurers and our view on how local insurers might approach them.

	KPIs indicated by global insurers	What might local insurers do?
Business growth	• Insurance revenue • Contractual Service Margin (CSM) growth for life insurers • Gross Written Premium (GWP) for non-life insurers	Retain trusted measures such as GWP, new business and in-force Annual Premium Income growth measures. However, the availability of information may be subject to system constraints as premium revenue and GWP are no longer reported in the income statement.
Profitability	• Return on equity (ROE) • Combined ratio for non-life insurers • Insurance service result	Continue using a range of insurance service results or underlying profit options – differences in how these are calculated already exist. Where combined ratios are derived from income statement information, please note they would exclude non-directly attributable expenses and this is a change to current practice.
Value creation	• Embedded Value (EV) • IFRS 17 Volume of New Business (VONB) based on CSM • Equity + CSM net of tax	CSM is less relevant for annual renewable contracts because it considers the entire next year of renewals, in addition to new business. Life insurers are likely to keep traditional EV, VONB or other value measures as they factor in a long-term view of value inclusive of future renewals.
Distributable profits	• Net cash flow / generation • Dividends paid or expected • Regulatory capital (i.e. solvency)	IFRS 17 has no impact on cash generation, but dividends may be influenced by the new Interim Solvency Standard (ISS) issued by the Reserve Bank of New Zealand. Insurers should spend time understanding the impacts from the ISS, and should be mindful that there may be changes in the future for any unintended capital benefits.

A five stage framework for developing KPIs

STAGE 1 → **STAGE 2** → **STAGE 3** → **STAGE 4** → **STAGE 5**



STAGE 1 – Available metrics

Start with metrics included within your existing reporting packs (internal management, board reporting and external stakeholder reporting). Add any new IFRS 17 metrics that may be possible indicators of profitability, growth or value.

STAGE 2 – Relevance to the business

Filter based on whether the metrics remain relevant (based on your products and accounting decisions). While new business CSM is a popular KPI globally, it may not be relevant to you if you have a business dominated by annual renewable contracts.

STAGE 3 – Stakeholder usefulness

Filter out metrics that are difficult to understand or do not measure profitability, growth or value. For example, it may be useful to consider whether stakeholders will truly understand performance if you report metrics on a net of reinsurance basis as there will be accounting mismatches between direct and reinsurance contracts, which may lead to direct and reinsurance results being reported and analysed separately.

STAGE 4 – Practicability

Filter out metrics that cannot be derived easily from the new IFRS 17 compliant system. Many items that existed on the IFRS 4 income statement are no longer required under IFRS 17 (for example, gross written premium, net incurred claims) and may not be easily obtained from your new systems and processes.

STAGE 5 – Timeliness of information

Consider how to structure reports for metrics that may take much longer to produce each month. The implementation of IFRS 17 will likely impact reporting timelines and therefore it is important to strike the right balance between timeliness and completeness.

How can insurers set themselves up for future success?

IFRS 17 provides insurers an opportunity to further transform legacy systems and processes. Currently a significant amount of manual intervention is needed to complete reporting requirements which can be cumbersome and time consuming. Through enabling a greater use of technology and automation, processes could be streamlined and people freed up to focus on more value-added tasks leading to more cost effective ways of working.

Key points to consider include:

Remove transaction processing

- Transform your business from transactions to time-savers.
- Focus on less processing and analysis and more on value-added tasks.
- Embrace lean process redesign.
- Explore the use of process bots for repeatable tasks.
- Invest in AI and automation strategy (from end-to-end).

Transform finance to be a data function

- Build on existing cloud capabilities.
- Decentralise data ownership while still benefiting from shared infrastructure.
- Ensure effective data governance across all functions.
- Streamline accounting and reporting solutions (through the use of consistent information internally and externally to the regulator and the market).

Source capability through alternative delivery models

- Introduce shared services for non-core functions.
- Explore the possibility of third party service providers.

Lead with process, integrate with technology

- While technology is essential, remember it's really about people.

How can PwC help?

Our local insurance team provides a range of services to insurance companies from assurance services, accounting advice, actuarial services and finance transformation. Get in touch if you'd like to discuss the challenges you're facing.

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