IFRS 17 WHITEPAPER

The CFOs guide to achieving compliance

By Ross E. Chapman, Aptitude Software

An overview of finance's IFRS 17 requirements

- Chief Financial Officers are vested with chief actuarial officers to deliver IFRS 17 reporting accurately, on-time with controls and audit-ability
- Complying with IFRS 17 requires more than delivering Contractual Service Margin calculations
- IFRS 17 requires finance to harmonize data, processing and control across the entire systems environment
- In a post-IFRS 17 world, CFO's will be challenged to clearly explain the business strategy and results
- IFRS 17 offers an opportunity to improve finance's capabilities

IFRS 17 is arguably the biggest change to insurance accounting ever. The standard requires insurance CFOs to produce new financial reporting and will challenge their ability to explain the business clearly to investors, boards, regulators and other stakeholders.

The principles-based standard drives forward-looking estimates onto the balance sheet, placing finance teams under an even brighter 'audit spotlight' with the need for new controls and governance processes, extensive disclosures and the ability to substantiate reported results.

> *Throughout all of this we need to explain our results, how much cash are we getting from our operating businesses, how much are we able to pay out in dividend, how do we reflect growth, and how are we going to report these KPIs?*
> Group Financial Controller at Leading UK-based insurance company

While initially the focus was on the addition of a new required calculation, the Contractual Service Margin (CSM), insurers and advisories are realizing that correctly calculating the CSM over time is just one aspect of achieving IFRS 17 compliance. Finance teams now recognize the extent of the IFRS 17 challenge, which includes changes to financial accounting, reporting and governance.

Insurers IFRS 17 requirements now extend beyond where to home the CSM calculation, which can be done in either actuarial or finance systems. Finance teams that are at more advanced stages of their analysis are focussing on how to deliver the end-to-end IFRS 17 financial reporting process.

What are finance's IFRS 17 accounting requirements?

IFRS 17 compliance requires a series of financial accounting changes. First, insurers need to fit their entire book of business into new measurement models, to create and apply complex accounting posting rules over hundreds of contract types and product lifecycle events.

Second, finance need a new IFRS 17 Chart of Accounts and to produce extensive new disclosures, delivering IFRS 17 accounting quickly within the 'working day timetables' which (for finance) are more frequent (monthly) and typically more accelerated than other regulatory insurance reporting such as Solvency II.

FINANCE FUNCTIONAL REQUIREMENTS

- ☑ Apply IFRS 17 measurement models
- ☑ Create and manage posting rules,
- ☑ New chart of accounts (COA)
- ☑ IFRS 17 disclosures
- ☑ Closely manage the IFRS 17 transition
- ☑ Delivering reporting within 'working day' timetable

Finally, finance teams need to manage IFRS 17 transition closely, as new balances will drive profitability for years to come and will be under scrutiny from investors, regulators and tax authorities.

It is important to note that IFRS 17 reporting can not be delivered in isolation, as financial balances are invariably affected by many other GAAP reporting standards including IFRS 9, IFRS 15 and other rules such as those that dictate the application of fair value.

IFRS 17 will challenges CFO's abilities to explain business performance?

CEO's, investors and boards rely on CFO's and clear financial reporting to explain their business clearly to investors, boards, regulators and management teams. Many insurers expect IFRS 17 to result in more volatile results and the new standards may affect the ability of companies to pay dividends and even impact executive bonuses. In the IFRS 17 world, finance teams will have to focus on how all reporting processes across metrics will work together, including for things such as planning and forecasting.

> "*Whilst ultimate economic profits will not change, the emergence of those profits can change significantly. Both insurers and their analysts will need to assess the full impact in terms of telling the performance story of their companies.*"
>
> Alex Bertolotti, PWC

For the external audiences, the common language of IFRS 17 will reduce variation in reporting practices and place pressure on CFO's to be able to quickly and clearly explain financial results. Experience adjustments will have to be applied and explained, and accountants will have to understand how P&L changes can be attributed to changing assumptions such as interest rates.

CFO's will need to deliver comparative reporting starting in 2020, which will challenge CFO's to explain the variations between reporting bases. Consistency of treatment across the business will be under much higher scrutiny, and investors will expect CFO's to explain variations across multiple GAAPs and regulatory reporting regimes.

> *We should be able to produce a set of parallel books to let the users [of financial statements] make a judgment as to whether it is useful. But, that will be costly - you need to run parallel systems and be able to reconcile between bases.*

Comparative reporting will challenge CFO's for many years to come, with many insurers already hearing from tax authorities that they will want to see results presented using old and new models for up to 7 years, and managers wanting to continue non-IFRS 17-related KPIs for employee performance management processes.

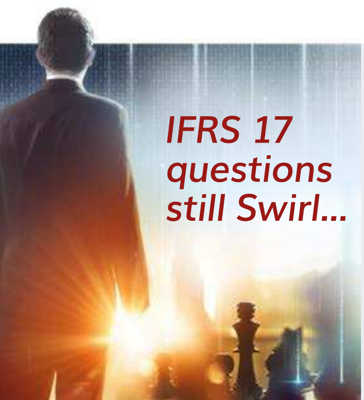
IFRS 17 financial controls and governance

Those insurance companies that have performed deeper analyses or completed proof-of-concepts have highlighted finance's need to harmonise data, processing and controls across actuarial, policy administration and finance systems, to create and manage IFRS 17 portfolios, and ultimately produce highly-controlled finance results.

Expected cashflows sourced from actuarial systems will form the basis of most IFRS 17 calculations. A lot of these numbers have been done by actuaries for many years, but insurers will need higher levels of comfort and greater control frameworks around the actuarial data sets. Ownership of these figures is driving actuarial and accounting teams much closer but ultimately finance will need to be able to deliver the controls around the end-to-end process. This goes well beyond the Contractual Service Margin (CSM) calculations.

For example, within the PAA model, evaluating onerous contracts requires links with pricing teams. Allocating costs to groups of contracts requires repeatable and auditable processes. For contracts of over one year in length, it will be necessary for finance to justify use of IFRS 17's secondary measurement models (PAA) to show that it produces similar results to the general measurement model. There needs to be policy and rules for applying coverage units and discount rates, especially when those parameters may differ to other regulator reporting frameworks such as Solvency II.

Whereas data for these judgments may source from actuarial, pricing or policy systems; finance's role is to manage the end-to-end process to deliver consistent, audit-able, results with the ability to quickly and clearly explain business performance to all stakeholders. Having the ability to drill-down into the provenance and transformation of underlying data will be a key success factor for insurance CFO's.



> *How are we going to link with the 'pricing guys' to understand whether a contract is onerous, when the info from pricing is not typically good enough to use in our finance systems? How will we allocate costs to groups of contracts? How are going to show that the Premium Allocation Approach is applicable as it produces similar results to the General Measurement Model? On the life-side, what are our rules for coverage units? How are we going to use discount rates, as it looks like it'll be different from what's in use for Solvency II? How do we deal with diversification? And where we hedge... how are we going to account for that in this new world?*
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> Lead technical accountant and member of the IFRS 17 Transition Resource Group

Looking to the future – incremental benefits for CFO's and the companies they serve

It is possibly premature for insurers to seek 'strategic benefits' from their IFRS 17 programmes when their routes to compliance are not yet defined. However, when defining finance requirements, insurance CFO's should consider potential future requirements and what strategic changes they expect to make to their architectures.

For example, it will be important for CFO's to consider whether they foresee the need for multiple different measurement models, as to support accounting for new business lines they may enter. Finance teams may want the ability to group contracts at the most granular level to more easily control and change how they manage IFRS 17 portfolios in the future and to support deeper analysis of results.

With these needs in mind, some insurers are already tying their IFRS 17 programmes into broader finance transformation objectives, with insurance CFO's wanting to gain a single chart-of-accounts across their business, support new business models and product lines, deliver cost reductions (through reduced manual processing), and build better financial data foundations to drive better insights into the business. These 'strategic' benefits come with an incremental cost, but provide finance with important capabilities to deliver value in a post-IFRS 17 world.

About Aptitude Software

Aptitude Software delivers specialist finance applications to equip insurance CFO's to fulfil their strategies and ambitions. Our software is used by leading insurance companies to deliver faster, relevant and integrated financial reporting; to underpin decision-making with aligned finance, risk and actuarial data foundations; and to achieve compliance with regulatory requirements efficiently.

About Aptitude Software's IFRS 17 Solution

The Aptitude IFRS 17 Solution enables insurance CFOs to comply with IFRS 17 requirements efficiently, with an end-to-end management of the IFRS 17 financial reporting process. Our specialist product approach fits into existing actuarial and financial reporting architecture to reduce cost and risk of change while enabling customers to leverage accounting best practices and the agility to address other financial reporting requirements.

The solution embeds IFRS 17 processes such as insurance contract portfolio management and P&L attribution; incorporates insurance data models and IFRS accounting templates; and leverages Aptitude Software's proven operational accounting platform.

The Aptitude solution is designed to enable insurers to exploit all IFRS 17 approaches including the Building Block Approach (BBA), Premium Allocation Approach (PAA) and the Variable Fee Approach (VFA), in line with what has been documented by regulators and in support of the requirements of leading international insurance companies.

For more information, visit **aptitudesoftware.com**
Call us on **+1 617 273 8289 (US)**, **+44 (0) 207 496 8100 (UK)**
or email **info@aptitudesoftware.com**

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