

# 4<sup>th</sup> **INDONESIAN ACTUARIES SUMMIT 2019**

**"ACTUARY AND BUSINESS ETHICS"**



**NOVOTEL LAMPUNG, 28<sup>th</sup> -29<sup>th</sup> MARCH 2019**

# **4<sup>th</sup> INDONESIAN ACTUARIES SUMMIT 2019**

"ACTUARY AND BUSINESS ETHICS"

## **IFRS 17: Practical Issues**

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# IFRS 17

- A lot has been said about IFRS 17 theory
- Today we move from theory to practice and focus on some key aspects of IFRS 17!
- We focus on two areas today:
  - Actuarial Technical Modelling
  - IFRS 17 Implementation Considerations

IFRS 17: Practical Issues

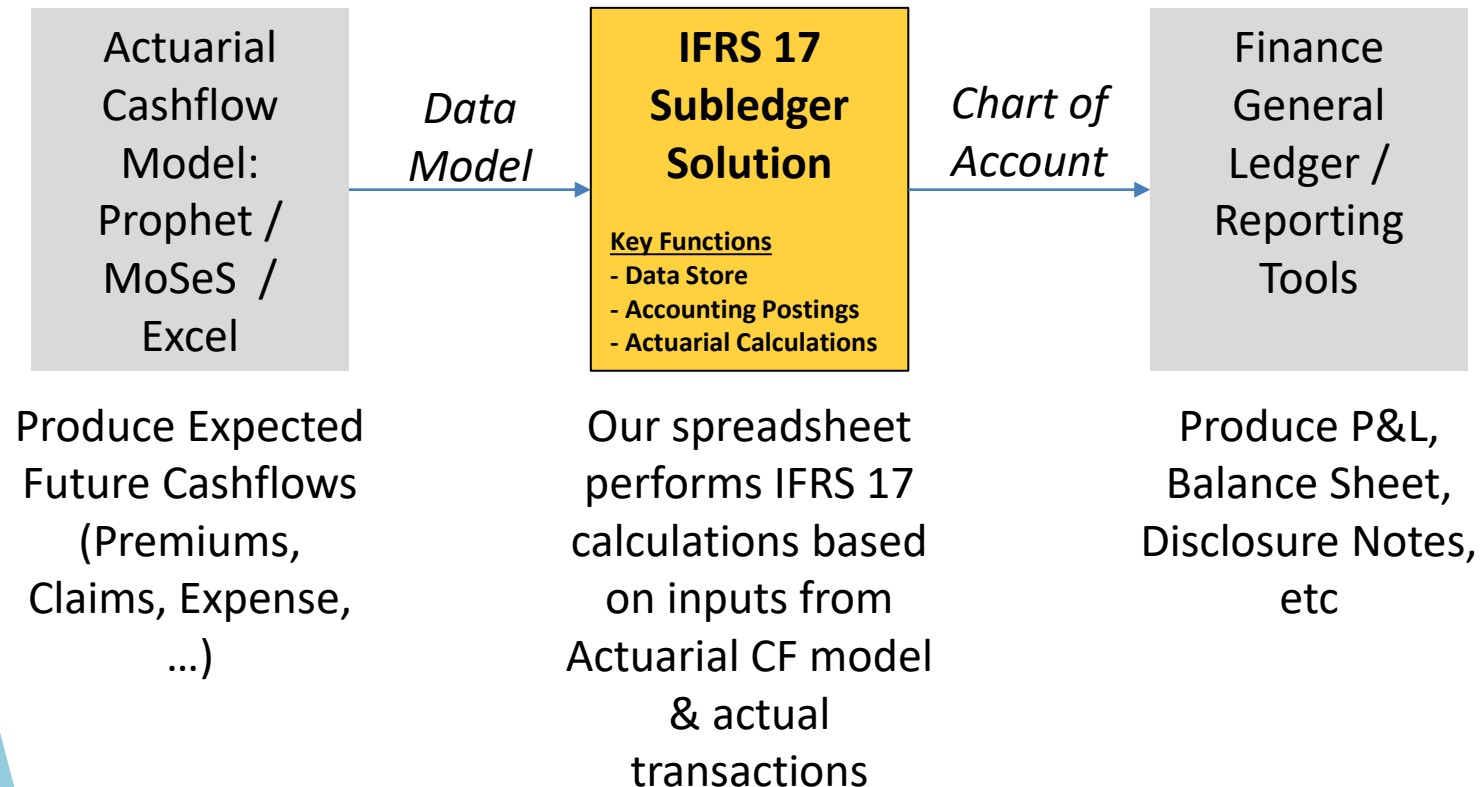
# **ACTUARIAL TECHNICAL MODELLING**

# Technical Modelling

- We will look at the modelling areas of IFRS 17, in particular at “initial recognition”
- We will start off with the pricing model discussed earlier
- We will consider the adjustments that must be made on current Cashflow projections to obtain IFRS 17 results at initial measurement ( $t=0$ )
- IFRS 17 is a significantly more complex topic – please refer to your advisors for more information

# Excel Model Structure

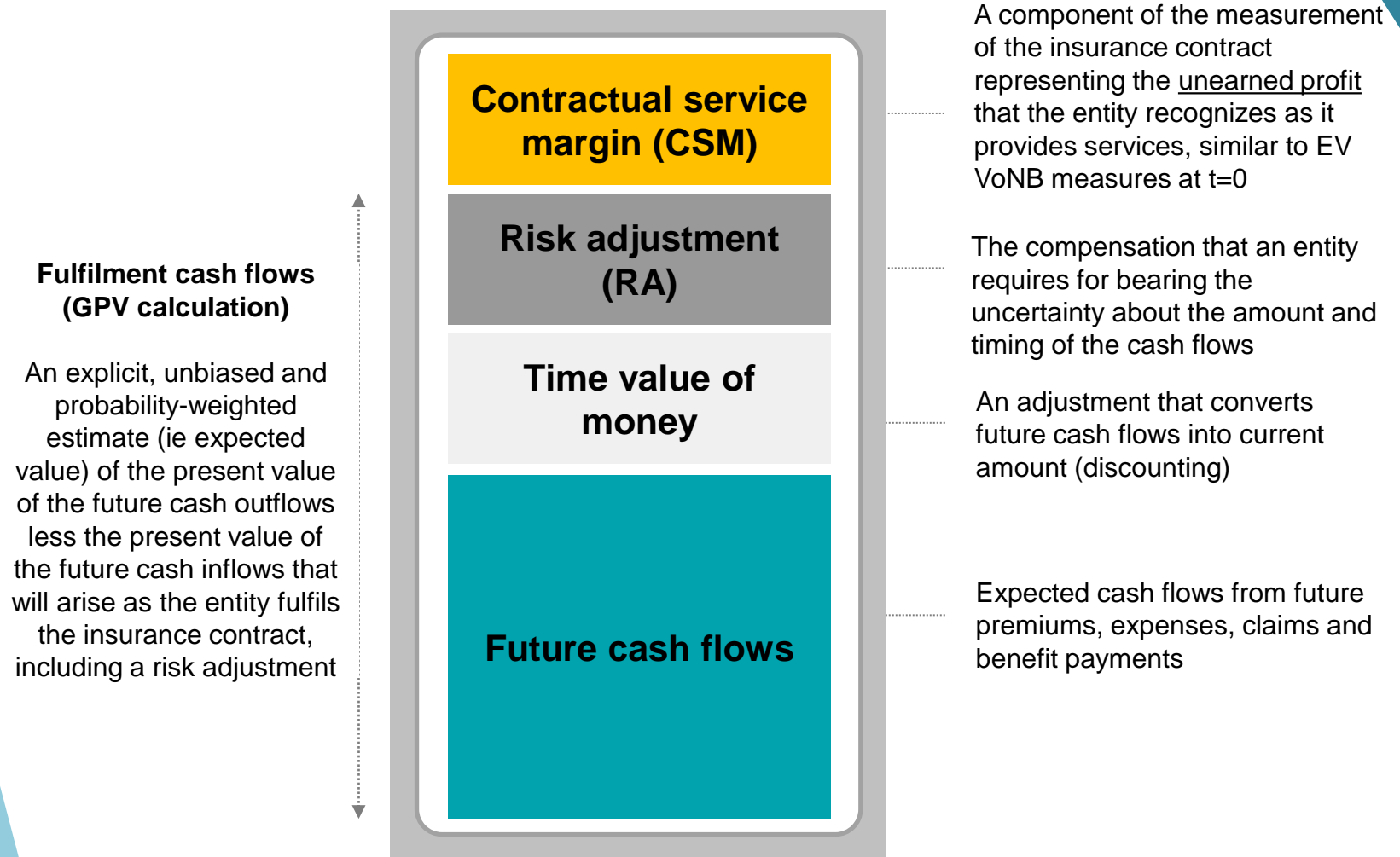
- The IFRS 17 excel spreadsheet shared is an extremely simplified model of how the subledger solution actuarial calculations will work:



# Key Changes from IFRS 4

- Reserving Model clearly defined (GMM, VFA, PAA)
- Profits: Deferral of  $t=0$  profits via “CSM”, and future release into profits
- Topline: “Insurance Revenue” is not Insurance Premiums
- Exclusion of “Investment Components” from revenue
- Level of Aggregation: Onerous vs Non Onerous
- More guidance on Discount Rates, Contract Boundaries, Expenses, etc
- Today we will look at each of this topics and how they can be modelled in Excel at  $t=0$  Initial Measurement (and assume Actual = Expected)

# General Model (“Building Blocks”)



# CSM

- ❑ At initial recognition, the CSM is defined as the negative of fulfilment cash flow, floored by zero.
- ❑ Purpose of recognizing initial CSM:
  - ❑ To eliminate any day 1 gains (if initial CSM is positive)
  - ❑ To represents the unearned profit that the entity recognizes as it provides services under the insurance contract
- ❑ If CSM is floored by zero at inception, the insurance contract is onerous. All loss making contracts should be recognized in P&L at inception.

- ❑ Subsequently, the roll-forward calculation of CSM is summarized as follows:

	CSM at the beginning of the reporting period
+	Accreted interest
+/-	Changes in the estimates of FCF
+/-	Changes in RA relating to future coverage
-	Amount recognised for services provided
=	CSM at the end of the reporting period

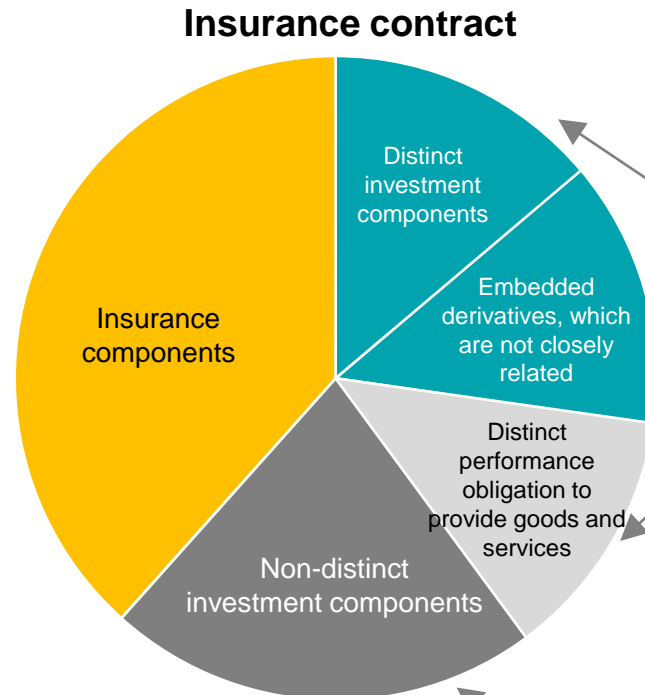
- ❑ Locked-in rate at the inception of contract is used for accreting interest.
- ❑ Changes in assumptions will impact CSM, not P&L
- ❑ “Coverage Units”: An entity should recognise the remaining contractual service margin in profit or loss over the coverage period in a systematic way that best reflects the remaining transfer of the services. For contracts with no participating features, the service represented by the CSM is insurance coverage (eg Sum Assured) provided on the basis of the passage of time. (Note: Potential change)

# Investment Components

For measurement purposes, an insurance contract is the cash flows remaining after separable non-insurance components are separated.

*IFRS 17.85 Insurance revenue and insurance service expenses presented in profit or loss shall exclude any investment components. An entity shall not present premium information in profit or loss if that information is inconsistent with paragraph 83.*

- Accounting under IFRS 17
- Accounting under IFRS 9
- Accounting under IFRS 15
- Accounting under IFRS 17, disaggregation for presentation



- Examples:
- Maturity Benefits
  - Surrender Values
  - UL Unit Funds
  - Universal Life Fund Balances

**IFRS 17 Appendix A Defined Terms:**  
**Investment component**  
 The amounts that an **insurance contract** requires the entity to repay to a **policyholder** even if an **insured event** does not occur.

*B31 Paragraph 11(b) requires an entity to separate a distinct investment component from the host insurance contract. An investment component is distinct if, and only if, both the following conditions are met:*

- (a) the investment component and the insurance component are not highly interrelated.
- (b) a contract with equivalent terms is sold, or could be sold, separately in the same market or the same jurisdiction, either by entities that issue insurance contracts or by other parties...

# Non Distinct Investment Components

Non Distinct Investment Components do not generate Insurance Revenue, but are instead disaggregated into the CSM

## Changes in the carrying amount of the contractual service margin for insurance contracts without direct participation features (paragraph 44)

B96 For insurance contracts without direct participation features, paragraph 44(c) requires an adjustment to the contractual service margin of a group of insurance contracts for changes in fulfilment cash flows that relate to future service. These changes comprise:

.....  
(c) differences between any **investment component** expected to become payable in the period and the actual investment component that becomes payable in the period, measured at the discount rates specified in paragraph B72(c); and

Example:

Unit Account Per Policy: \$600

Death Benefit Per Policy: \$1000

- DB Investment Component: \$600
- DB Insurance Component: \$400

Expected DB = \$50

- DB Investment Component: \$30
- DB: Insurance Component: \$20

Actual DB paid = \$40

- DB Investment Component: \$24
- DB: Insurance Component: \$16

Dr FCF	\$50
CR CSM – B96(c)	\$30
CR Insurance Revenue	\$20

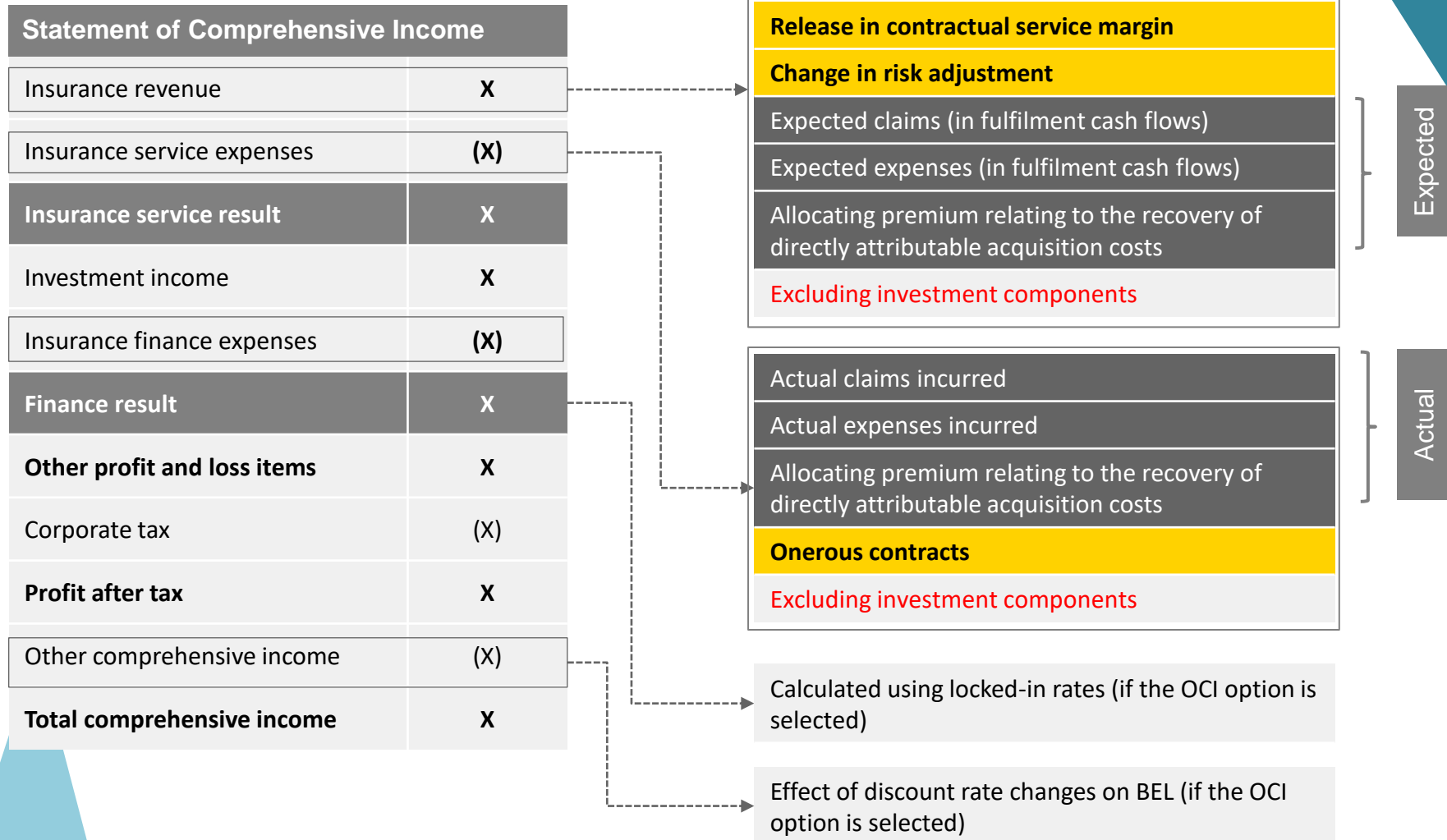
Dr CSM – B96(c)	\$24
Dr Insurance Expenses	\$16
CR Cash	\$40

This will result in:

P&L:  $\$20 - \$16 = \$4$  <--- insurance profit recognized in P&L

CSM:  $\$30 - \$24 = \$6$  <--- investment profit deferred in CSM

# Insurance Revenue



# Other Items to consider

- Level of Aggregation (Portfolio, Issue Year, Onerous)
- Discount Rate: Bottom Up vs Top Down
- Contract Boundaries
- Directly Attributable Expenses
- Etc – as you continue on your journey down IFRS 17, expect to learn more!

# Implications to Product Pricing

1

What is your IFRS17 product profitability?

- ▶ Pattern of profit emergence/release from CSM
- ▶ Onerous vs. non-onerous contracts. Credit Life products with cross-subsidy may be adversely affected.

2

How prepared are you for IFRS 17?

- ▶ Companies running under a S-II / MCEV type basis should be well prepared.
- ▶ The fundamentals of life insurance product (i.e. meets customer needs, priced soundly with proper risk management) would not change

3

How will your KPIs change?

- ▶ Will CSM replace EV VNB?
- ▶ Will the definition of “Insurance Revenue” encourage higher focus on Protection compared to Savings?

IFRS 17: Practical Issues

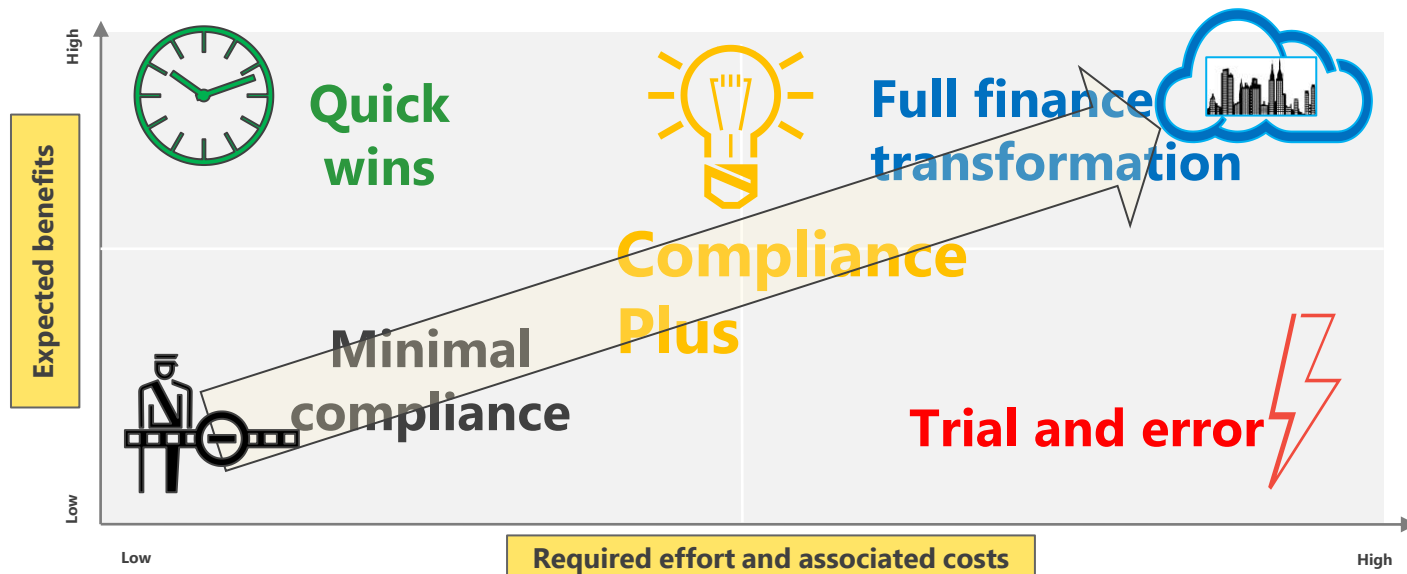
# **IMPLEMENTATION CONSIDERATIONS**

# How to approach the implementation of IFRS 17?

2018-2020 Implementation

2021- BAU

It is important to determine your **ambition level** before embarking on your IFRS 17 implementation ...



... so that you can derive the **expected benefits** from the pledged investments and resources!

# What are the key IFRS 17 requirements that a new end-to-end IFRS 17 System must be able to deliver?

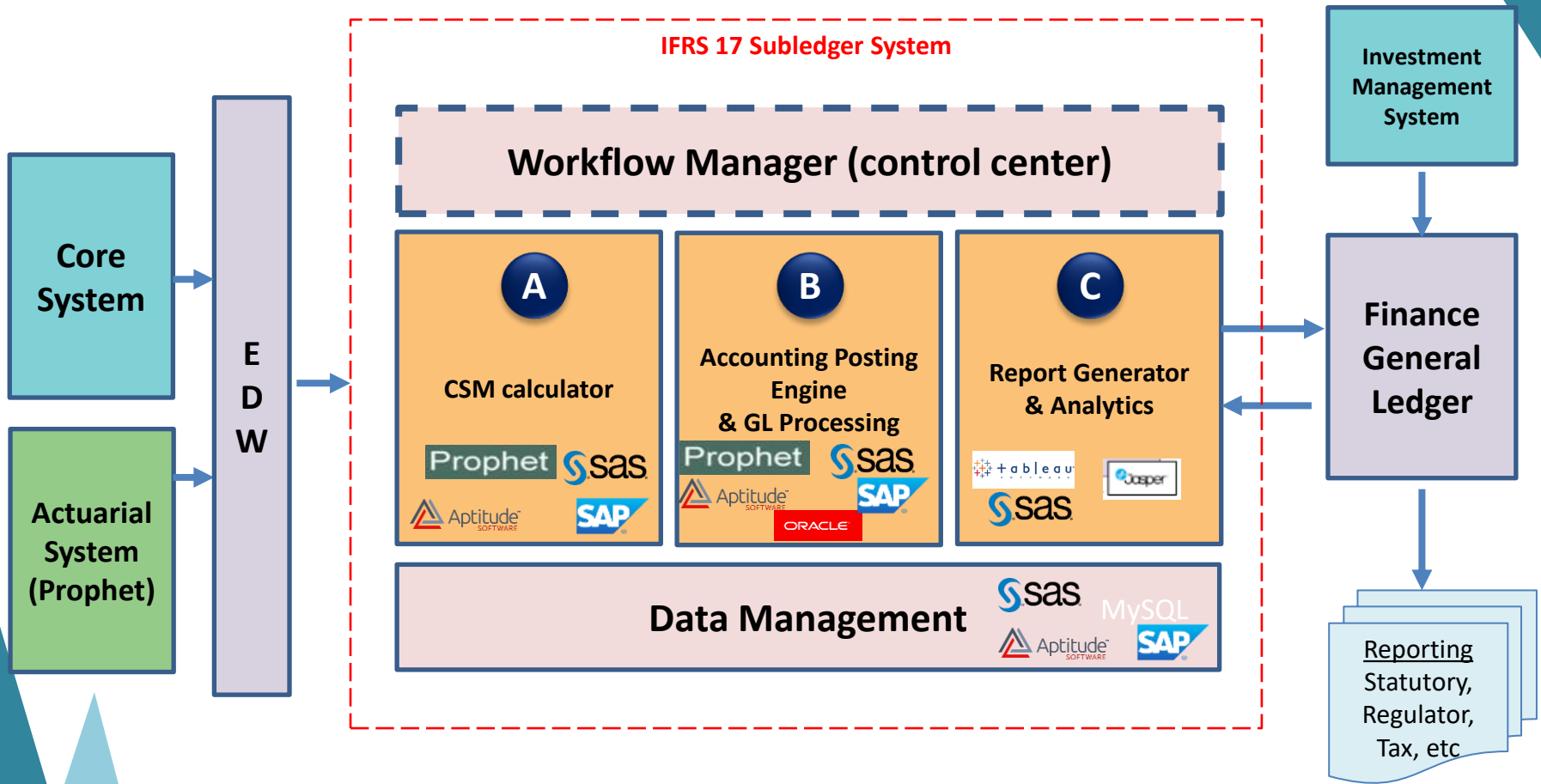
## **MUST-HAVE SYSTEM REQUIREMENTS (to be able to comply with new IFRS 17 standard):**

- ▶ Support data gathering/staging from multiple sources (Policy admin system, Actuarial system, Market data feeds, General Ledger, etc)
- ▶ Comes with built-in multi-dimensional IFRS 17 data model (part of integrated data warehouse solution)
- ▶ Must support data aggregation and grouping at cohort level (for contracts with similar risk profile, split by onerosity and not more than 12 months apart)
- ▶ Support cost allocation for directly attributable expenses (sourced from GL)
- ▶ Perform CSM Calculations (using both GM/BBA and VFA methods)
- ▶ Data storage for review/approval, disclosures and analytics
- ▶ Accommodate GL posting rules for all business transaction event types in accordance with IFRS 17 accounting policies
- ▶ Post the correct IFRS 17 double bookkeeping (Dt/Cr) journal entries in the GL system

## **OTHER OPTIONAL REQUIREMENTS (not driven by the new IFRS17 standard but by internal needs):**

- ▶ End-to-end workflow management tool (control center) with full audit trail
- ▶ Comply with internal control procedures and other SOPs
- ▶ Basic analytics & visualization capabilities
- ▶ Support both Cloud (private/public) and on-premise (host) processing
- ▶ Comply with relevant industry security standards
- ▶ Meet or exceed system performance criteria as per agreed SLA

# Data, Systems and Process Development – POV IFRS 17 target architecture



## CFO / CA Implementation Considerations

**1**

Do we have the necessary people (resources) to do the implementation?

**2**

How do we integrate the Sub Ledger (SL) solution with the General Ledger (GL) solution projects?

**3**

What trainings do we need to conduct while the system selection process is ongoing? Who should be a part of those trainings?

**4**

What are the implications of the new SL solution system on the closing process?

**5**

How do we prepare our technical infrastructure for the new SL solution system?

**6**

What is the control framework that the new SL solution system must abide by?

**7**

What do we need to do to prepare for the vendor team onboarding?  
(e.g logistic, laptops, access IDs)

# Recommended next steps

- Start your local IFRS 17 impact assessment project(s)
- Mobilize project resources and key stakeholders
- Conduct core team training (covering content and process)
- Perform gap analysis (using pre-populated structured templates)
- Conduct impact assessments (financial, products, systems and processes, people) to understand how IFRS17 will impact you
- Determine realistic implementation roadmap and budget (including Accountants, Actuaries, IT)
- Report findings to internal stakeholders (MT, Board, Group etc.)
- Discuss findings with external auditor and regulator(s)
- Seek approval for next phase (Design)
- Join in local professional discussions and contribute knowledge!

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