Actuarial transformation: the route to IFRS17 smart compliance?

Presentation to Fagkomité Skade Reserving Seminar

28 May 2018

Agenda

1 **Overview of IFRS 17**

Background and overview of the new international accounting standard for insurance

2 **Implications on actuarial processes**

Overview of key changes to the actuarial processes and models

3 **How to approach IFRS 17 compliance**

Time to transform the actuarial function?

Overview of IFRS 17

IFRS 17 is the first truly international, comprehensive accounting Standard for insurance, replacing IFRS4 – an interim Standard that results in widely divergent practices

18 May 2017	2018	2019	2020	2021
IFRS 17 published	• Some entities begin implementation process • General questions • Contentious/specific implementation questions		Entities finalising implementation	Effective date of IFRS 17

The IASB aimed for IFRS 17 to bring:

- Consistent accounting for all insurance contracts (health, life and general insurance sectors and with other sectors)
- Updated information about obligations, risks and performance of insurance contracts
- Increased transparency in financial information reported by insurance companies

What IFRS 17 requires:

- A measurement model for insurance contracts which is based on:
  - expected future cash flows;
  - discounted to reflect time value of money; and
  - a risk adjustment to reflect the compensation the insurer requires to bear risk
- The expected profit in a contract is measured on day one and released over the coverage period
- Early recognition of potential loss making contracts
- Increased disclosure requirements

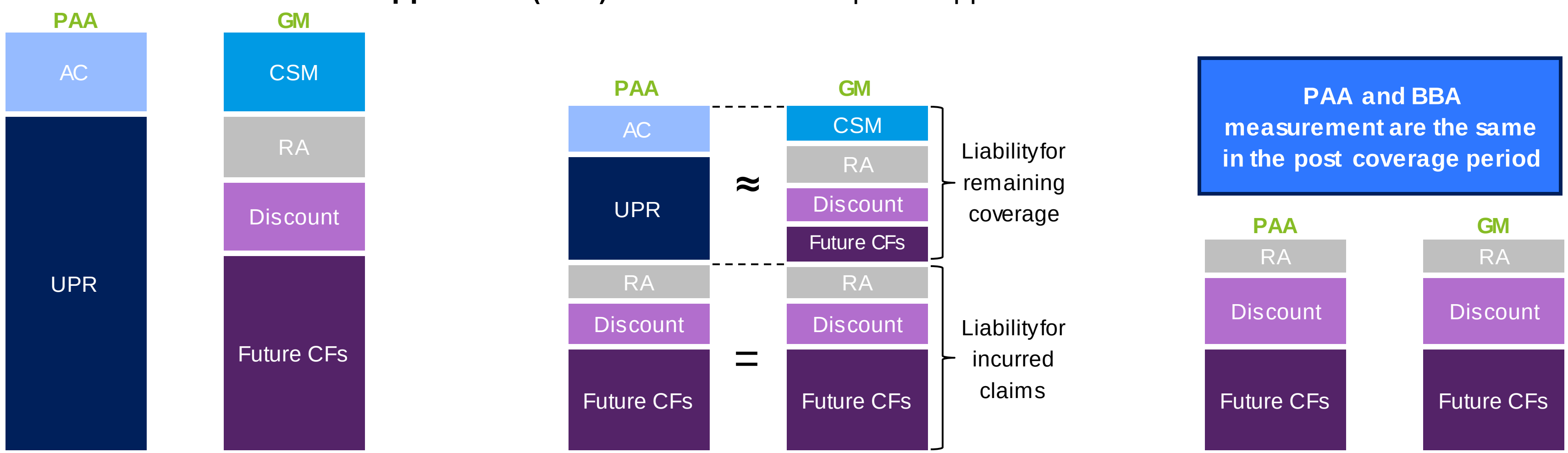
Impact of IFRS 17 on QBE:

- QBE entities required to apply IFRS 17 for Group reporting and locally if the standard is adopted locally
- The overall profit profile in a steady state is not expected to differ significantly; presentation and disclosure will differ from AASB 1023
- Whilst the simplified model is closer to AASB 1023 the results and balance sheet need to be prepared on a more granular basis and therefore require significant work to achieve compliance
- Adjustments expected on transition mainly related to recognition of onerous contracts and previous acquisitions

Measurement model overview

IFRS 17 introduces two measurement models:

1. **“General Model” (GM)** where unearned and earned coverage is all measured by considering discounted, risk-adjusted cash flows and profit is measured at inception by the Contractual Service Margin (CSM) which is earned out over the coverage period.
2. **“Premium Allocation Approach” (PAA)** which offers a simplified approach to measurement of unearned business.



Day 0 **Coverage Period** **Post Coverage (settlement period)**

Contracts are eligible for the simplified approach if:

- the coverage period is 12 months or less (*c90% of QBE’s business*); or
- if the entity reasonably expects it would produce a liability for remaining coverage for the group that would not **differ materially** from the one that would be produced under GM (*PAA eligibility testing indicates a large proportion of the remaining 10% will qualify for PAA – most likely exceptions being LMI in ANZO and Long term Life reinsurance business in QBE Re Belgium in EO*).

Overview of key areas of the standard for general insurers

Simplified approach (PAA) ★	Central estimate cash flows	Discounting/ inflation	Risk adjustment ★
Portfolios / onerous contracts ★	Contractual service margin (GM only)	Reinsurance measurement ★	Unbundling
Acquired portfolios ★	Expenses	Presentation and disclosure ★	Transition

Overview of key changes to the actuarial processes and models

These new actuarial calculation processes as well the increased complexity of existing processes could give rise to insurerst reviewing their global actuarial operating model and whether this could/should be delivered through a global solution (e.g. Global Actuarial Centre of Excellence) vs. separate local solutions. Below summarises the cumulative impact on actuarial models introduced by IFRS 17.

CSM calculations

Fulfilment Cashflows for BBA contracts

CSM calculation and unlocking (BBA contracts)

CSM calculation and unlocking (Acquired Bus.)

- Cashflow modelling required here will be on an inception cohort / UWY basis rather than AY basis, and will include unearned Fulfilment Cashflows.
- New computations that don't currently exist will need to be built to calculate CSM at inception and track the unwind to be posted at each subsequent reporting period.
- Model should also be able to handle outwards reinsurance, any CSMs resulting from acquisitions etc.

Onerous contracts charges

Onerous Contract charge valuation

- Cashflow modelling required here will also be on an inception cohort / UWY basis and include unearned Fulfilment Cashflows.
- Will need to calculate, post and unwind any loss component where a group of contracts are identified in the "facts and circumstances" test – determine onerous contract charge and track over time.

Test frameworks

Onerous Contract 'facts & circumstances' test

PAA eligibility model

- These requirements are for reporting / modelling tools which play back data primarily from local policy admin and planning tools.
- Consistent Group-wide policy will be critical.
- PAA eligibility model will require mechanism to model variability of assumptions for remaining coverage – how will Group influence how this is modelled / demonstrated?

New cash flow modelling

Discounting

Application of credit risk to Ceded cashflows

Ceded cash flows

Ceded risk adjustment

Intercompany

- Number of new requirements for cash flow models to cater for IFRS 17 requirements.
- Modelling ceded cashflows, applying allowance for credit risk and ceded risk adjustment.
- Increases complexity of current process, e.g. intercompany.

OCI option

Discounting at current and locked-in rates

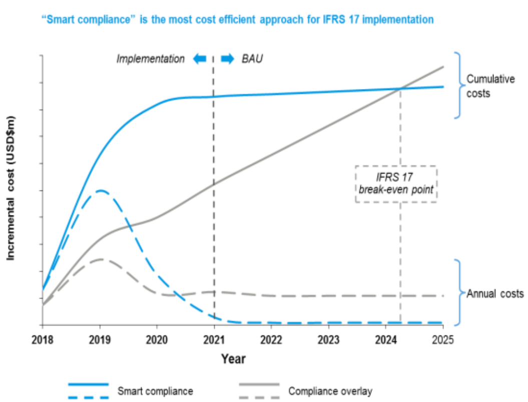
- Need a mechanism to discount on multiple bases and to analyse the difference resulting from discount rates changes over time (separate from changes in the cash flows).
- This would need to be incorporated into the discounting solution if QBE plan to take up this option.
- Currently discounting solutions would need significant re-work to cater for this.

QBE

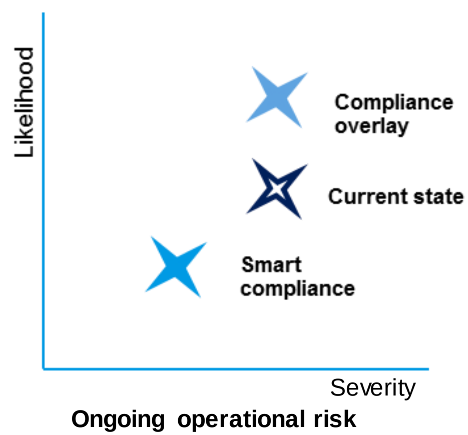
Approach to compliance

Could actuarial transformation as part of IFRS 17 agenda, lead to…

Lower cumulative costs?



Reduced operational risk?



and more...

- Better performance management?
- Better staff engagement?
- Better oversight and governance?
- Better consistency?