Pre-Empting Post Live Challenges

Gautham Subramanian takes a look at various considerations during the implementation journey of IFRS 17.

The year 2023 marks the D-day for IFRS 17 to be implemented globally. This being the biggest global change to the accounting standards in last couple of decades, the implementation journey has been full of obstacles and surprises for companies across the globe.

MARKET READINESS

The regulatory landscape has been a key factor to drive the market readiness of different members of the GCC. While KSA and Bahrain are in lead with multiple IFRS 17 Dry Runs performed for the year 2022, UAE and Qatar are following with completion of the Financial Impact Analysis as of 2020.

Oman, on the other hand, have just issued a timeline of 2024 to go live for IFRS 17 reporting, while Kuwait has not laid down any active requirements for IFRS 17.

The Saudi Central Bank, previously known as the Saudi Arabian Monetary Agency (SAMA) have been actively involved to monitor the IFRS 17 implementation. SAMA formed a Working Group with key stakeholders to develop and validate the financial reporting templates for IFRS 17. The Working Group is coming up with market wide recommendations for the findings of each dry run. The interim dry runs have been audited and final dry run is monitored to include audit feedback. This has been significantly helpful in making the market ready to go live for 2023-Q1 reporting. SAMA has also been pushing stakeholders including managers and boards to be trained on IFRS 17 concepts.

The UAE Central Bank (CBUAE), on the other hand, have only asked for Financial Impact Analysis once a year. CBUAE had provided their feedback on the 2020 Financial Impact Analysis towards the end of 2022-Q3. The market is not completely go-live ready, hence CBUAE has asked for parallel runs of IFRS 4 and IFRS 17 for the year 2023, to allow for time for companies to build knowledge internally, develop IFRS 17 solutions, assumptions and KPIs.

GO-LIVE CHALLENGES

Data and System are the two key challenges for the companies in the GCC markets. Other challenges faced are: Resource Planning, Setting up KPIs, Budgeting & Forecasting and Solvency & Capital Position.

DATA RECORDING

IFRS 17 requires more granular data and numbers to be calculated at the 'Group of Contracts' level instead of the Portfolio level under IFRS 4.

IFRS 17 requires the entity to provide specific reconciliations showing how the net carrying amounts of insurance contracts changed during the period as a result of changes in cash flows and income and expenses recognized in the statement(s) of financial performance.

Companies even for KSA are struggling with tracking the actual cash transactions as the current IT systems are not equipped to record transactions at Group of Contracts level. Hence many companies end up using approximations, specifically for allocating transactions to different Underwriting Years.

The IT systems for many companies even in the KSA market are not equipped for policy level data recording. A major challenge faced by many companies is recording of receivables and payables as data for most of the companies' is recorded on net basis from various distribution channels, while IFRS 17 requires them

GAUTHAM SUBRAMANIAN, SENIOR MANAGER- IFRS 17 PRACTICE LEAD, BADRI CONSULTANCY

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separately at gross basis. Also, Reinsurance data is not available for many companies.

SYSTEM CHALLENGES

Companies are using a wide range of different systems for Admin, Actuarial and Accounting which involves multiple parties and there is no standard approach being followed.

The lack of data requirement and system knowledge companies are heavily dependent on the implementation partners. This is causing delays in the implementation project and automation. Another challenge is the difficulty to apply company-wide rules, validation, aggregation and other considerations due to different requirements in head office versus regional offices. Many companies are more focused on software implementation rather than an accounting standard implementation. In addition, non-life companies issuing life products may need to change their systems due to more and heavier reporting requirements.

RESOURCE PLANNING

Due to change in reporting requirement, the company needs to re-examine the upstream and downstream impact on the processes. This includes month end close, reporting, control and governance, etc.

Another challenge is the shortage of persons with the necessary skillsets along with the risk of hiring resources that would be redundant post implementation

Consultants can be one solution to this challenge, but policies and methodologies are mostly prepared by internal staff.

KEY PERFORMANCE INDICATORS

Below are some KPIs which could be considered for IFRS 17 numbers:

» New Business Profitability = Contractual Service Margin for new business / Present Value of Expected Premium

» Profit Margin = Insurance Result / Insurance Revenue

» Return on Equity = Underlying Earnings / Average Shareholder's Equity (excl OCI)

» Return on Debt = Financial Debt / (Shareholder Equity (inc OCI) + CSM + Financial Debt)

BUDGETING AND FORECASTING

Impact on Equity is unknown for many companies. Budgeting and forecasting will depend upon how significant is the impact of transitioning to IFRS 17.

ACTUARIAL REQUIREMENTS

Historically, actuaries have modelled the reserves on an accident year basis. Under the IFRS 17 regime, the financials and disclosures are needed on an underwriting year basis. This leads to a challenge of allocating the reserves from an accident year basis to an underwriting year basis. While there is no 'correct' methodology for doing this allocation, different methodologies can produce different results. Even using the same methodology could produce volatile results from one quarter to another. It is imperative that actuaries consider modelling the reserves on an underwriting year basis over a medium to long term.

Another aspect affecting actuaries is modelling gross and reinsurance. Currently, the general practice is to model the gross and net of reinsurance for the same lines of business. For example, Motor as a line of business is modelled on a gross of reinsurance basis and net of reinsurance basis. Under IFRS 17, the financials and disclosures are required on gross and reinsurance basis. So, under the same example, if Motor has an excess of loss treaty, then Motor on a gross should be modelled and the excess of loss for Motor needs to be modelled. This again leads to a fundamental shift in the way reserving is currently performed.

SOLVENCY AND CAPITAL POSITION

Asset management is unaffected from the Solvency and Capital position. Regulators have not come up with new approach or formula to calculate the solvency and capital position of a company. The impact of this calculation is unknown and would vary depends upon how significant IFRS 4 and IFRS 17 differs.

EXPLAINING THE RESULTS

Currently most of the work for IFRS 17 has been done as dry runs of impact assessments which are all carried out with IFRS4 as a yardstick. Q1-2023 will be the first quarter in which the P&L will be structured on IFRS 17 basis and the results will need to be published on stock exchanges and explained to the Boards. We feel this is going to be one of the key challenges for management during this year. Interpretation of IFRS 4 numbers have become intuitive and it will be some time before which we develop the same level of intuition and understanding of the different aspects that impact IFRS 17 results. ❷